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THE 1978 ECONOMIC REPORT OF THE PRESIDENT

HEARINGS

BEFORE THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

NINETY-FIFTH CONGRESS

SECOND SESSION

PART 1

JANUARY 31 AND FEBRUARY 1, 3, AND 6, 1978

Printed for the use of the Joint Economic Committee

U.S. GOVERNMENT PRINTING OFFICE

29-531 WASHINGTON : 1978

For sale by the Superintendent of Documents, U.S. Government Printing Office
Washington, D.C. 20402

Stock No. 052-070-04642-2

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THE 1978 ECONOMIC REPORT OF THE PRESIDENT

TUESDAY, JANUARY 31, 1978

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

The committee met, pursuant to notice, at 10 a.m., in room 345, Cannon House Office Building, Hon. Richard Bolling (chairman of the committee) presiding.

Present: Representatives Bolling, Moorhead, Brown of Ohio, Brown of Michigan, and Rousselot; and Senators Bentsen, McGovern, Javits, and Roth.

Also present: John R. Stark, executive director; Louis C. Krauthoff II, assistant director; Richard F. Kaufman, general counsel; G. Thomas Cator, Thomas F. Dernburg, Kent H. Hughes, L. Douglas Lee, Katie MacArthur, Deborah Norelli Matz, Philip McMartin, and George R. Tyler, professional staff members; Mark Borchelt, administrative assistant; and Charles H. Bradford, Stephen J. Entin, George D. Krumbhaar, Jr., and Mark R. Policinski, minority professional staff members.

OPENING STATEMENT OF REPRESENTATIVE BOLLING, CHAIRMAN

Representative BOLLING. The committee will be in order.

Today the Joint Economic Committee opens its annual hearings on the state of the American economy with Charles Schultze, Chairman of the Council of Economic Advisers.

It is a great pleasure to have Mr. Schultze with us once again.

The annual hearings will continue tomorrow with the focus on the problem of structural unemployment. Additional hearings have been set throughout February and early March. A schedule of future hearings is available on the press table.

Both the political and economic circumstances have changed considerably since Mr. Schultze appeared last before the committee. At the beginning of 1977 the Carter administration had just arrived. Despite an extremely limited amount of time available to them, the administration suggested a number of changes to what was basically a Ford budget and proposed a program for limited economic stimulus.

The committee itself appeared somewhat troubled. A bitter winter threatened to weaken an already indifferent recovery, but 1977 turned out to be a reasonably good year.

The United States met the target rate of growth set at the London Summit in May 1977. The employment grew by just over 4 million, an all-time record, unemployment continued to fall steadily throughout the year. For the fourth quarter 1977 the unemployment rate stood at 6.7 percent and in December dropped as low as 6.4 percent.

To the administration's credit, it has set realistic goals for 1978 and set policies on the right path. These good intentions are paving a road to continued growth and lower unemployment.

Yet I remain concerned about the course of the economy in 1978 and am a little more than apprehensive about the prospects for 1979. Despite the good news, Mr. Schultze is sure to be pressed on a wide range of economic issues. There appears to be a broad concensus that more stimulus is needed but not quite so much agreement on how to provide it. With an eye on declining cities and high levels of central-city unemployment, some of my colleagues are sure to press for additional spending rather than tax cuts.

The size and composition of the tax cut are sure to precipitate questions of adequacy and equity.

Monetary policy is the third part of the policy problem which we must consider. Of course, there is some uncertainty about the direction monetary policy will take under the guidance of Chairman designate Miller. But I do not think we should be shy about discussing the issue in forming our own recommendations. The analysis prepared by the JEC staff indicates that the President's proposed tax and expenditure mix could be substantially more stimulative if interest rates are kept at their 1977 average level rather than allowed to rise.

Inflation remains the unwanted guest at our economic banquet. To the President's credit, he has continued to emphasize the problem of inflation and presented us the outlines of an anti-inflation program. He has taken the right steps in attempting to fight inflation directly rather than through restrictive fiscal or monetary policies.

Many of us feel that much more must be attempted on the anti-inflation front.

The good news on employment is mitigated by the staggeringly high rates of unemployment among black teenagers and other groups. If Congress and the administration work closely, we will attack the problem of structural unemployment during 1977. The comprehensive youth bill and economic stimulus program for 1977 were both targeted on groups with higher than average rates of unemployment. The President's budget contains some additional moneys, proposed youth and public service employment, and a wealth of emphasis on incentive for private sector jobs, and still the Nation finds itself with millions and millions of people without work.

Despite, or perhaps because of, the strong performance of the domestic economy, the United States is faced with the prospect of a second record trade deficit and a depreciating dollar. In my view the emphasis is more a reflection of strength than weakness, but there remains a danger that the deficit will come and negate the course of domestic monetary policy.

Before I call on Mr. Schultze, I would like to call on several of the members.

Senator Javits.

Opening Statement of Senator Javits

Senator Javits. Thank you, Mr. Chairman. I would like to welcome Mr. Schultze and the wonderful expertise which he brings to our deliberations. I hope you will, as you testify, look ahead to our future. I am especially concerned about a number of the imperfections in this country's economic policy which I see, as being unbelievably serious.

Our chairman has mentioned one of these: Structural unemployment and the difficulty of youth to break into the employment circle with the necessary training and education that goes with it.

Second is the very alarming drop in productivity, causing considerable erosion of strength in our country. Unless we correct it, we will not go anywhere but deteriorate seriously as a nation.

A third problem area relates to our deep involvement in the LDC's, especially as we are not acquiring an adequate scope of markets to deal with the industrial production of our own country and of the OECD countries. The north-south dialog has fallen flat. I, myself, was a delegate to the last such meeting at the Kleber Conference Center in Paris. It's a discouraging picture.

In addition, our banks are heavily involved. I don't believe our banks have in any way been pigs, but the question of whether we can continue even to roll over these vast sums that have been loaned to the LDC's or whether the alternative will be an enormous monetary and credit crunch in the world is again a very prominent question with us.

Finally, we do not seem able to summon the political skill to deal with the OPEC situation which, if continued— and it doesn't seem to be ending—can really put us into a depression tailspin.

These are serious matters which we, as Members of Congress, share without any regard for party or theology or anything else.

You are a highly expert man in charge of this for our President and for our country, and I look forward to hearing you and other witnesses on these serious problems.

Thank you, Mr. Chairman.

Representative Bolling. Thank you, Senator Javits.

Now I would like to recognize the gentleman who, after a minor formality this afternoon in the excutive committee of this committee, will become the new vice chairman of the committee. It is a great pleasure to recognize Senator Bentsen.

Opening Statement of Senator Bentsen

Senator Bentsen. Thank you very much, Mr. Chairman.

It is hazardous to predict the outcome of elections but, assuming that it comes to pass ——

Senator Javits. We can guarantee this one.

Senator Bentsen [continuing]. I will be sitting in the chair of Hubert Humphrey, and I am well aware that no one takes the place of Hubert Humphrey, not in the JEC, the Senate, or the hearts of the American people. Hubert Humphrey left his mark, the indelible imprint of goodness, compassion, and opportunity. It is not an easy task to follow in the footsteps of the Senator from Minnesota, who established standards which are difficult to emulate. I think we owe it to Hubert to continue his work to help provide the freedom of opportunity that is essential to his vision of America and to our vision of America.

I believe that the American economy is fundamentally sound because it is rooted in a stable political order that invites broad citizen participation and because we have an economic system that enlists the industry, the ingenuity and the creativity of the American people through a system of incentives and awards.

Our economy has some very apparent problems. The chairman and Senator Javits have touched on them. I am deeply concerned. as they are, with structural unemployment. The idea we can have as much as 40 percent of the young people of our country who are in minorities and are unemployed—we can't put those folks on a ship; we can't icebox them. If we leave them out of the economic mainstream of this country, 2, 3, 4 years, they develop a life style to which I think we pay a long-term political, economic, and philosophical cost in this country of ours.

The other problem was touched on by Senator Javits—the loss of productivity in this country. It is time for the modernization of America, to try to see that this productive capacity that we have—and 83 or 84 percent of it—is being utilized.

The question is what kind of productive capacity are we talking about. Is it truly competitive productive capacity, and what can we do to encourage the private sector to modernize America and make it more competitive?

I want to see us direct our attention to these issues.

I think the economically disenfranchised people of this country lost a great, effective champion when Hubert Humphrey's voice was stilled. If Hubert were still with us, he would exhort us to rethink our old ideas and to reformulate old programs, leaving no stone unturned in our quest for a solution to this tragic problem. He would tell us we have an obligation, an economic, moral, and humanitarian obligation to foster opportunities that are important to those young people in the private sector and in the Government sector if necessary.

That is precisely what I think we are about to do.

Mr. Chairman, I look forward to working with you and members of this committee to help develop answers to economic problems faced by this Nation.

I am particularly anxious to see what can be done to open up our economic system to the millions of Americans who have had the door of opportunity closed in their faces.

Thank you, Mr. Chairman.

Representative Bolling. Thank you, Senator Bentsen.

It is a very real pleasure still to welcome to this committee a very old friend of mine from the House days when he served there, the very distinguished Senator, Senator McGovern.

Opening Statement of Senator McGovern

Senator McGovern. Thank you, Mr. Chairman. I am pleased to have the opportunity to participate in these hearings. It is difficult to express my deep sorrow about the circumstances of my appointment. Hubert was an old and dear friend whom we all will miss. He was a power for what is good on this committee. I am, however, honored to be his successor on this important committee.

I am not satisfied with the 1979 budget proposed by the President. I am concerned by its weak response to the needs of the nation's cities, its agriculture, its jobless, and its poor. The President, recognizing the need to stimulate the economy, has proposed a $25 billion tax cut—$7 billion of which will offset an increase in the social security tax and $6 billion of which will compensate for the increase in personal taxes due to inflation. It seems obvious to me that: (1) The economy requires more that the $12 billion net stimulus provided by the administration's tax package—which will result in only a 4.5 percent rate of economic growth in the GNP and a marginal decline in the unemployment rate to at most 6.2 percent in the fourth quarter of 1979; (2) it requires considerably more than the $7.8 billion increase in spending proposed by the President above what would have otherwise occurred; and (3) it requires a variety of new programs targeted to provide direct stimulative assistance to individuals and groups in need.

The most significant need in our Nation today is reducing the unemployment level. Beyond the unacceptable 6.4 percent rate of unemployment nationally, is the more dismal state of black employment. Black unemployment in December was still 12.5 percent and the rate for black youths, an incredible 37.3 percent—up from 34.8 percent 1 year ago. It seems apparent to me that the proposed tax cut will hardly make a dent in the lives of these individuals. If the intent of the tax cut is to address the high level of unemployment, a far more efficient approach would be to create jobs directly. In 1975, the CBO estimated that the gross cost per PSE job is about $8,000, while the gross per job created by a tax cut is about $25,000. Thus, using these figures, $13 billion of stimulus, if applied to PSE, for example, could create almost 1.5 million new jobs, but $13 billion in the form of a tax cut would result in only 480,000 new jobs.

We must stimulate the economy in the most direct manner—by providing people with meaningful jobs. For example, a major effort could be undertaken to upgrade, restore, and maintain the Nation's railbeds and tracks. The railroad industry contributed $22 billion in wages and services to our economy in 1974. Presently the state of our railroads is disastrous.

Our Nation's cities too need much more than the trickle down from a tax cut and slight increases in existing programs. They require a commitment—a dollars and cents commitment—to pump new life in to the old veins—to restore deteriorated facilities—to provide direct incentives for business to locate in the cities—to provide adequate city services—and, yes, to provide jobs for the Nation's unemployed who are concentrated in our cities.

This is the mandate before the administration. The tax cut is an ineffective alternative. It does not meet the needs of the people, of business, and of cities. It is a quick and easy method of appearing to deal with our problems. These are not quick and easy problems which can be elimated with a sweep of IRS wand. They are deep-rooted, long-term problems, which warrant specific programmatic efforts and funds to validate the commitment to their success. There are no bargains in this business—any wholesale approach to our most serious problems is seriously short-changing the American people.

Instead of a $25 billion tax cut, representing a small tax rebate to each taxpayer, I suggest a $25 billion job-creating investment to strengthen our economy and upgrade our society.

Such a public investment might be allocated roughly as follows:

(1) $12 billion for the cities of the Nation.

(2) $7 billion for agriculture and rural America including parity target guarantees.

(3) $6 billion to upgrade our national rail system.

Such a public investment would create new jobs, reverse the decline of our cities, strengthen farm income and the purchasing of farm families, and upgrade an energy saving national rail system.

Representative BOLLING. Thank you, Senator McGovern.

Representative MOORHEAD. Mr. Chairman, may I make an opening statement.

Representative BOLLING. Certainly.

OPENING STATEMENT OF REPRESENTATIVE MOORHEAD

Representative MOORHEAD. Mr. Chairman, Mr. Vice-Chairman to be, I want to welcome our old friend Charles Schultze here. It is always a pleasure to hear from the Chairman.

I hope, Mr. Chairman, that these hearings focus in particular on two aspects of the President's economic program; first, the fiscal policy, with the $25 billion tax cut, and the planned deficit which would result therefrom. I say that our problem in the Congress is complicated by the fact that in the normal process of tax-writing we make the net reduction much larger that the $25 billion mainly because many of the revenue-raising reforms are controversial. So I would hope that we would explore what is the safe outer limit of the deficit and hence the tax reduction for this year.

The second area is anti-inflationary policy. On its face it makes eminently good sense where we have momentum inflation to provide for deceleration, but the problem that remains is how it is going to work. Will it be ignored by the private sector? If so, then what do we do? I am less concerned about the leaning to controls because I don't believe the Congress would enact such controls, but I am concerned that it may be ignored.

I am suggesting you can strenghten your appeal by tying it to this tax reduction so that the typical wage earner realizes he is better off with the tax reduction and a lower rate of wage increase than he would otherwise have.

Thank you, Mr. Chairman.

Representative BOLLING. Mr. Brown, would you like to make a statement?

Representative BROWN of Ohio. Mr. Chairman, I suggest we have had enough overture. Let's go ahead with the ballet.

Representative BOLLING. Mr. Schultze.

STATEMENT OF HON. CHARLES L. SCHULTZE, CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS

Mr. SCHULTZE. Thank you, Mr. Chairman, Mr. Vice Chairman designate, if that is the appropiate term, members of the committee. I have a relatively lengthy statement, and in order to avoid taking up too much of your time, I will go through it skipping particular parts of it, but I just wanted to say in advance that there is no particular indication that anything I may not read out of the text I consider to be unimportant.

Hence, no particular conclusions are to be drawn as to the importance or unimportance of anything.

I am pleased to be here today to talk with the members of the Joint Economic Committee about the President's economic program for 1978 and 1979. That program is designed to maintain a strong economy over the next 2 years but also to build a foundation for continued progress over the longer term.

I know you are particularly interested in the overall dimensions of that program and how its pieces fit together and what the longer term policy considerations are that guided its formulation. I will try to pay particular attention to those points.

We start from the fact that the American economy today is basically healthy. We are making good progress in recovering from the trauma of earlier years when the Nation was hit in quick succession by double-digit inflation and a severe recession. Last year, as you know, our economy created a record number of new jobs and reduced the ranks of the unemployed by over 1 million people. The pace of activity appears to be moving well as we enter 1978.

Because the inflation was so great and the recession so deep, the progress we have made still leaves us short of full recovery. Substantial further progress is needed, and steps must be taken now if we expect to achieve our long-range economic goals.

Economic growth will slow in late 1978 and in 1979 unless we act to relieve the growing tax burden on consumers. Payroll taxes are rising sharply, and inflation is pushing individuals into higher tax brackets. Other sectors of the economy are not growing sufficiently to counterbalance this depressing effect on consumer spending. So tax reductions for individuals are therefore needed to maintain growth of consumer purchasing power and spending.

Business investment is not rising fast enough. More investment will create additional jobs for a growing labor force and increase our industrial capacity for the future. Business tax reductions are needed to provide the incentives for a faster expansion of investment and the capital stock and a better growth in productivity.

The Federal tax system is too complex and in many respects unfair. Reform of our tax laws is needed and can and should be combined with tax reduction this year.

Structural unemployment remains a major unsolved problem. Overall economic progress will help reduce the very high unemployment rates among youth and minorities. But these and other groups will not enjoy their fair share of the fruits of economic expansion and recovery unless their job opportunities are increased substantially. In addition to overall economic measures, we need to improve and expand our employment and training programs to address the specific employment problems of these groups.

Inflation is too high. We should take steps to prevent a worsening of inflationary pressures as the economy moves to higher levels of employment and production. And at the same time we must bend our efforts now toward reducing the present inflation.

These problems cannot be dealt with in a piecemeal fashion. Only with a coordinated effort to deal with all of them will we realize the potential that our national resources and the energy of the American people make possible.

Let me set the stage for an explanation of the President's proposals by reviewing briefly, and I mean very briefly, the major economic developments of the past year and the situation of the economy as we enter 1978.

The economy grew strongly last year. In the fourth quarter of 1977 the Nation's real gross national product in real terms stood 5¾ percent above its year-earlier level. More than 4 million jobs were created and by December the rate of unemployment had fallen to 6.4 percent, 1.4 percentage below its level 12 month earlier.

We are entering 1978 with good prospects for continued strong expansion for the near term. Growth will be spurred for a time by increased inventory investment, as businesses catch up with the unanticipated surge in consumer spending late last year. Moreover, the 1977 economic stimulus programs are still gathering strength and will encourage recovery through the first half of 1978.

But as we look further ahead, it is clear that unless steps are taken now to maintain economic growth, expansion is going to slow to an unacceptable pace and our efforts to reduce unemployment will be frustrated.

The most important development threatening sustained recovery is the increasing burden of taxes borne by the average taxpayer. Under present law, large increases in payroll taxes are coming into effect to finance the social security programs. Some of these added taxes were scheduled by law in 1973 social security amendments.

Additional increases were enacted last year and are essential to the continued health of the social security system, since without them the trust funds would soon be depleted. But the economic impact of these higher taxes cannot be ignored. Payroll taxes will rise by $7 to $7.5 billion in 1978 and again in 1979. An additional drag on consumer purchasing power will occur because inflation and real economic growth push taxpayers into higher brackets. Unless steps are taken to lower individual income taxes, Federal revenues over the next 2 years will be absorbing a significantly rising share of personal income.

Now, there are times when increased effective tax rates are needed to restrain an overheated economy. But that is not the case at present. On the contrary, growth in the private sector is not likely to be strong enough to overcome a substantial increase in the degree of fiscal restraint that would be emanating from the Federal budget, if we didn't take measures to arrest it.

Turning to the top of the next page, Mr. Chairman, and dealing now with other sectors of growth besides the consumer sector, the source of growth that would be most welcome in 1978 and 1979 would be a strong rise of business fixed investment. Over the past several years, the labor force in our country has grown very rapidly. Growth of the capital stock has not kept up. Productivity is therefore increasing very slowly. And although there is, at present, substantial idle capacity in our plants and factories, a faster growth of capacity will be needed to avoid inflationary bottlenecks in later years as we approch a high employment economy.

You note the table there and you will see that during the years from the mid 1960's to 1973, the stock of business capital grew at 4.4 percent a year and the labor force at slightly under 2 percent. In the last 3 years, given the recession, the stock of business capital has grown at less than 2 percent and the labor force has grown faster than 2 percent, and this has effects in both terms of productivity and the longer term outlook for availability of capacity when we get the unemployment rate down to lower levels.

During the course of an economic recovery, business plans for investment spending typically strengthen—as capacity utilization increases, profits improve, and the outlook for the long-term future brightens. There has been a significant improvement in the rate of investment over the past 2 years, but it wasn't sufficient.

In real terms, business fixed investment in the final quarter of 1977 was still 3 percent below its peak in 1974. Moreover, surveys of business plans for investment in new plant and equipment in 1978 suggest a rise this year but a rise that may fall somewhat short of last year's performance. And that's simply not good enough.

Given the absence of growing strength in these major sectors of the private economy, it would clearly be unwise to impose a major increase in the tax burden on the economy—but that is what would happen without the President's tax program. As a consequence, economic growth would slow. We estimate that if the President's tax program were not enacted, growth in 1979 would slow in a range of about 3¼ to 3¾ percent. For shorthand, we say 3.5 might be the best estimate of what might happen to economic growth.

The rate of unemployment would therefore stop declining, and it might begin rising again, because there would be insufficient absorbing of the labor force growth. We are still too far from full recovery to accept such a result, and the President's fiscal program for 1979 is designed to assure that it does not happen.

Now let me sketch out the program, and I know you are somewhat familiar with it, but the centerpiece of the administration's economic program for fiscal 1979 is the proposal for substantial tax reductions, integrated with recommendations for meaningful reform of the tax system. The elements of the program include:

1. Tax reductions of $24 billion for individuals combined with revenue-raising reforms of $7 billion. Tax reduction is achieved by substituting a $240 per capita credit for the existing $750 personal exemption and the general tax credit, and by reducing personal tax rates. The reduction in tax burden is greatest for low and middle-income taxpayers.

2. Business taxes are reduced by $8 billion. Tax reforms affecting businesses will raise about $2 billion in revenue, for a net business tax cut of about $6 billion. Tax cuts are provided through a substantial reduction in the corporate tax rate—the first since 1964—and through liberalization of the investment tax credit, the ITC. The investment tax credit is made permanent at 10 percent and for the first time is extended to include industrial and utility structures, as well as equipment to which it now applies. Furthermore, businesses will be permitted to use the investment tax credit to offset up to 90 percent of their tax liability, compared with the current 50 percent limit.

3. The Federal telephone excise tax, which under current law is now being gradually phased out, will be eliminated this year and the Federal unemployment insurance tax rate will be reduced to its pre-1977 level. The net tax reduction from these two provisions is $2 billion, which will be realized by consumers principally through lower prices.

These proposals do not include any provisions relating to the energy legislation now pending before the Congress. If, when finally enacted, the energy program does not include a full rebate to consumers of the net proceeds of the wellhead tax on oil, the President has indicated that he will seek additional personal tax reductions to return those funds to consumers.

In total, the President's program calls for tax reduction of $34 billion, partially offset by $9 billion in revenue-raising reforms. The two elements of reduction and reform go together. Without the tax reforms, the size of the tax reduction components of the program should be scaled back to the size proposed for the net tax reduction.

The reforms included in this package are achievable and desirable. They will make our tax system much more equitable by eliminating a variety of business deductions that have been greatly abused, by sharply curtailing tax shelters, and by strengthening the minimum tax. They also eliminate tax subsidies in the area of international business transactions whose public benefits do not justify the costs. And they will make the tax system simpler and easier to understand.

The amount of net tax reduction called for in the President's program has been scaled to the needs of our current economy and designed to promote a sustainable economic growth rate of 4.5 to 5 percent in 1978 and 1979. It will amount to 1.1 percent of the 1979 GNP. This is about half the size of the 1964-65 tax cut, but 60 percent larger than the tax cuts which went into effect in 1970 and 1972.

In the absence of those tax cuts, the share of personal income absorbed by Federal personal income taxes and by the contribution of employees and the self-employed to social security would rise from 14.3 percent in 1977 to about 15.1 percent in 1979. Under the President's proposals, however, the share of personal income absorbed by these taxes will not increase between 1977 and 1979. Looked at from a different perspective, the President's tax proposal will mean that total Federal tax revenues as a share of GNP will rise only slightly between 1977 and 1979, compared with the situation which would have led to a relatively large increase without the tax reduction. Thus, by reducing taxes, we will counter-balance the prospective drag on the economy from the rising tax burdens which would otherwise occur.

The second table in my prepared statement attempts to lay out those ratios for you.

One minor technical point—if you look at the personal tax ratio to personal income, you note that it drops from 14.3 to 14.1 percent. That assumes that the net proceeds of the wellhead tax are rebated. If that were not done, it would be about 14.4 instead of 14.1. They are approximately the same.

The size of the tax proposal, however, was not designed to achieve some particular ratio of tax revenues to income. It was formulated in concert with the President's expenditure recommendations, to keep the economy on a path of growth that will insure significant further progress in reducing unemployment during 1978 and 1979.

If the President's program is enacted, we expect both 1978 and 1979 to be years of good economic growth. The Nation's real output should increase each year by 4.5 to 5 percent—a rate that would make it possible to reduce the unemployment rate from 6.6 percent in the final quarter of 1977 to a range of 6 to 6¼ percent by the end of 1978, and to somewhere in the 5.5 to 6 percent range by the fourth quarter of 1979. We estimate that the tax package will create nearly 1 million additional jobs by the end of 1979.

Effects on the deficit: Achieving these results through tax reduction means, of course, that the 1979 Federal deficit will be larger than it otherwise would have been. The President's fiscal 1979 budget carries a deficit in the unified budget of $61 billion in that fiscal year, only slightly below that in 1978. Had the proposed tax reductions been forgone, however, the deficit would have been $15 to $20 billion less. But the price would have been a weaker economy, almost 1 million fewer jobs, a substantially higher unemployment rate, and less growth of investment and industrial capacity. That is far too high a price to pay.

The 1979 budget deficit is large, but it is not inflationary. We recognize fully that deficits in the Federal budget do cause inflation if they create excess demand. We see no danger of that during the next 2 years, since unemployment is still high and there is ample slack capacity in the manufacturing sector to permit further increases in real output without encountering bottlenecks.

We know, however, that the Federal budget must be brought into balance as rapidly as the developing strength of the economy permits. That is an essential principle of the President's long-range budgetary strategy, and our recommendations for fiscal 1979 are entirely consistent with it.

Long-range budget strategy: The President has stated on numerous occasions his intention to keep a tight rein on the growth of total Federal expenditures. The administration's 1979 budget reflects this commitment—Federal expenditures increase in real terms by less than 2 percent. Similar restraint will be shown in succeeding budgets. We intend to reduce gradually the share of the Nation's output devoted to Federal expenditures.

Budgetary restraint does not mean neglect of important social problems. The Federal Government should, and under this administration will, continue to meet the pressing needs of the Nation. Through careful budgetary management—using zero-based budgeting and multiyear planning—we can improve efficiency and select priorities carefully, thereby channeling budgetary resources to meet important social and other national needs. In the years ahead sustainable overall economic growth can be promoted by such an expenditure policy, coupled—when and as the need arises—with tax reductions.

At each step along the way, the benefits of tax reduction will have to be weighed against the costs of a larger deficit. We intend to move toward a balanced Federal budget. In a high employment economy, with strong growth in private demand, deficits must be avoided, since under those conditions they would create excess demand and generate inflationary pressures.

If the private economy grows very strongly between now and 1981, we can and will balance the budget that forecloses this possibility. If private economic growth appears to be insufficient in the future to achieve high employment, we are prepared to undertake additional fiscal measures to insure that our economic objectives are realized. In that event, the date for achieving a balanced budget would have to be deferred.

One obvious question comes immediately to mind in relating these budgetary principles to the 1979 budget. Why is it necessary so far into economic recovery to have a budget deficit of $61 billion? Under the economic conditions which prevailed in the 1960's or the early 1970's, this would not have been the case. But there are several characteristics of our present economy which make it very difficult to balance the Federal budget without sharply slowing economic growth. The difficulty stems in the main from developments affecting the budgets of State and local governments, and from the drain of income associated with our foreign trade in goods and services.

As I go through the next several pages, I call your attention to the fourth table in my prepared statement, which I am, in effect, talking to.

In the past, State and local governments in the aggregate typically ran small budgetary deficits. More recently, however, the aggregate budgets of State and local governments have been in sizable surplus. Last year, that surplus was nearly $30 billion, up from $18 billion in 1976 and $3 billion in 1970. Part of this growing surplus stems from the accumulation of moneys in pension funds for the 13 million employees of State and local governments, obviously a needed accumulation to pay those pensions.

Another part stems from efforts by some of these governmental units to put their financial houses in better order after the recession of 1974-75. Within the aggregate, of course, there are some governments whose fiscal positions are quite difficult, and a few where they are quite precarious.

However pleasant the overall surplus in State and local governments may be from the standpoint of many of those governments, they tend to restrain economic activity because they draw more out of the income stream in tax revenues than are put back by way of expenditures.

The current account deficit in our international transactions—nearly $18 billion in 1977—poses a similar problem. It also represents a drain on the stream of national income; it means that we are sending more dollars abroad through purchases of goods and services than are returning to our country to buy goods and services here.

The fourth table shows the current size of these drains on income, and how large they are compared with earlier years of high employment.

The aggregate surplus of State and local governments is likely to diminish somewhat in the next few years, but it will probably remain large for many years to come. Adjustment of our trade deficit will also take time. That deficit can be traced to two major factors: We are importing large amounts of oil at high prices, and our exports have been depressed by slow rates of economic growth abroad. Enactment of an effective energy program and improvement in the economic growth rates of other nations will contribute to a gradual reduction in our foreign deficit, but it can only occur gradually.

The State and local and the foreign sectors are, of course, not the only economic forces which determine the appropriate fiscal stance for the Federal Government. But the size and recent growth of the income drain form these two areas are large, and they must be taken into account in the formulation of Federal fiscal policy.

We cannot realistically expect that the unprecedented size of the income drain in the State and local and foreign sectors will automatically be counterbalanced by extremely strong spending propensities on the part of American businesses or consumers. Therefore, the Federal budget has to stand ready to provide a counterbalance, in order to maintain a healthy economy.

Let me turn, if I may, to the problem of structural unemployment.

Fiscal and monetary policies are the basic tools at our command for promoting healthy growth in the overall economy and reductions in unemployment. But even in periods of relative prosperity some groups of American workers continue to suffer high unemployment rates. The current recovery has bypassed some Americans. Blacks and members of other minority groups particularly face disproportionately high rates of unemployment; the 40-percent rate of unemployment among black youth is simply not tolerable. Unless the Government takes steps to bring all groups of citizens into the economic mainstream, we will be frustrated in our efforts to achieve tolerable levels of unemployment.

In the longer run, dealing with structural unemployment successfully also has important implications for controlling inflation. Typically, as our economy approaches high levels of employment, some labor markets tighten up much more that others. Unemployment rates for experienced adult workers drop to very low levels, while large unemployment still exists for other groups. Employers, however, still tend to expand their work force by trying to fill vacancies with workers from the groups with low unemployment, rather than turning to those with higher unemployment rates. As a consequence, inflationary pressures on wages and prices ensue, even though unemployment among some segments of the labor force is still very high. Employment and training programs that provide skills and open up job opportunities for disadvantaged groups of workers tend to reduce these inflationary pressures, and such measures are essential if we are to achieve both our objectives of price stability and our goal of high employment.

The task we face is difficult. We have already taken some important first steps, but much remains to be done.

In the 1977-78 stimulus package, which the Congress enacted early last year, the level of jobs under the public service employment program was increased from 310,000 to 725,000. PSE employment has grown substantially since last spring, and now totals about 600,000. The remaining increase to 725,000 will occur over the next few months. The program was also modified to target more carefully on the longer term and low-income unemployed. The President is proposing to continue this program at the 725,000 job level in 1979.

The current public service jobs program is principally countercyclical in nature, and will be stepped down gradually after 1979 as the overall unemployment rate declines. A more permanent program, designed to provide work for 1.2 to 1.4 million persons, is part of the President's proposed overhaul of the Nation's tangled welfare system. This program is aimed at offering work, rather than cash welfare, to those of the Nation's poor who are able to work. The 1979 budget includes a request for a 50,000-job program to demonstrate the feasibility of this particular approach.

Special programs for young people were authorized under the Youth Employment and Demonstration Projects Act enacted by the Congress in 1977. These projects are aimed at testing a number of alternative approaches to combine work experience and training for young people. In the 1979 budget, we are requesting funding for 166,000 slots in the YEDPA programs and also funds to increase the Job Corps.

For most workers, the long-term answer to job opportunities must be in the private sector. More than five out of six new jobs will come from that sector. It is in the private sector that the greatest opportunities exist for job training, for advancement, and for meaningful lifetime careers. It is important, therefore, that we find effective ways to channel those who ordinarily would go jobless into private sector employment.

Later this year, the administration will send the Congress proposals to encourage the creation in the private sector of jobs for the structurally unemployed and particularly for the young. Details of this program are under active development at the present time and will be sent to the Congress shortly. The 1979 budget includes $400 million for this new initiative.

Now to turn to the problem of inflation. Another critical problem with which we must deal more effectively is inflation. During the period immediately ahead, there will still be some slack in the economy, and the likelihood of an increase in the rate of inflation is low. As the economy approaches higher levels of employment in 1980 and 1981, however, the risks increase that the rate of inflation will begin to move up. A significant worsening of inflation would undermine the confidence of consumers and business firms, causing them to cut back on purchases and investments. Moreover, we would be inhibited from taking the fiscal and monetary steps necessary to reduce the rate of unemployment further. Progress against inflation is thus absolutely essential to reducing unemployment.

The inflation problem that we face today has two distinct aspects. We need, on the one hand, to pursue policies that will avoid a worsening of inflation as we regain high employment in years out around the turn of the decade. And we must take steps now to begin unwinding from the high rate of inflation that we have inherited from the past.

Efforts to reduce the current inflation rate will encounter difficult problems. There is much that Government can do to contribute to lower inflation. A modest step—the proposed reduction in excise and unemployment insurance taxes that will contribute directly to lower prices and costs—is incorporated in the President's tax program.

The Government also can bring into line its own actions that raise costs and prices. A top priority of this administration is to reduce the adverse impact on costs and prices of Government regulatory actions. We have moved already to cut back significantly the sheer number of regulations, and to pare the paperwork burden imposed by regulatory agencies. We are establishing new procedures that will encourage regulatory agencies to seek out and apply the most cost-effective approach to accomplishing our regulatory objectives. The President has established under the chairmanship of the CEA Chairman an interagency committee to review the adequacy of economic analysis of major regulations. Government can in this way make a direct contribution to reducing the cost-rising effects of its own actions.

However, such actions alone will not be sufficient to make dramatic progress against inflation. For the past 3 years, the rate of inflation has persisted in the general range of 6 to 6.5 percent. There have been temporary fluctuations in the inflation rate, due to movements in food prices and fuel prices, but the underlying rate of price increase has neither accelerated nor slowed significantly throughout the recovery. Recent experience suggests that the rate of inflation is increasingly unresponsive to widespread unemployment and idle capacity that we have had during the past 3 years.

The inflation we have inherited from the past is built in to the process of setting wages and prices. Businesses raise prices to compensate for past and expected wage increases because they expect consumers to pay the higher prices they charge. Workers, seeing prices rising and expecting more inflation in the future, push for higher wage settlements. This process cannot be brought to halt by Government decree; nor can it be eliminated through the action of any one group of workers or business firms. If the rate of inflation is to be brought down from its current plateau, we must all work at the job together.

Over the past several months, the administration has examined closely a wide array of alternatives for dealing with the inflation problem.

Several approaches were rejected virtually from the outset. We cannot, for example, sit back and do nothing. Inaction could mean the eventual reemergence of bottlenecks and wage pressures that would lead to a worsening of inflation. Mandatory wage and price controls are not the answer. They do not effectively stop inflation, and the severe distortions, inefficiencies, and inequities they cause are unacceptable, particularly in the current climate. They are likely to reduce the rate of growth in investment, which in the long run we also need to control inflation.

We also have rejected policies of slow growth. We cannot wring the inflation out of the economy through high unemployment and economic slack. Such policies have only a limited impact on the kind of inflation we face, and then only at unacceptably high cost in human suffering and lost output. Moreover, by discouraging business firms from commitments to increase capacity, slow rates of growth may lead to inflationary problems later on, when high employment finally is approached.

A number of innovative ideas to reduce inflation through the tax system have been given serious consideration. Some of these proposals would give tax reductions to workers in return for restraint in annual wage increases. Others would tax wage increases above a specified level or use general revenue sharing as a means of encouraging State and local governments to reduce their own sales taxes which also have a direct effect on inflation.

All of these plans, however, are subject to major questions with regard to administrative feasibility, economic impact, and political acceptability. It would therefore be highly imprudent to propose introducing any of them before subjecting them to a much wider discussion and a more complete evaluation with respect to their economic effectiveness, administrative feasibility, and social equity. On the other hand, the momentum of inflation is so great and the consequences of either allowing it to continue or trying to wring it out with excessively slow growth are so large that they should not be dismissed out of hand. Further economic evaluation and a much broader debate would be very healthy, whatever its outcome.

After reviewing a long list of policy options, the President has concluded that the most appropriate step we can take at this time is to embark on a program of voluntary restraint in the setting of wages and prices. He has set forth a reasonable standard of behavior for gradually reducing inflation. Over the next year, labor and management in each industry have been asked to reduce rates of increase in wages and prices to below what they were on average in the prior 2 years.

This is a flexible and a fair proposal. It recognizes that there will be some cases in which the profit margins have been badly lagging, and that there are some groups whose wages have not risen as rapidly as others. In those cases, deceleration may be more difficult to achieve, and in some circumstances, may not be possible at all. By the same token, those businesses and groups of workers that have done better than average recently should contribute more to the overall deceleration.

To carry out this program, the administration will initiate discussions with officials and representatives of firms and unions well in advance of decisions on price increases or the opening of wage negotiations. This is not a program that requires prenotification of wage or price decisions or Government interference with the normal process of collective bargaining. But we will seek, through discussions that focus on conditions in major industries, to impress upon both workers and businesses the public's interest in wage and price restraint.

We fully recognize that this program will meet some skepticism. Given the nature of the current inflation, it is clear that no individual business or group of workers can afford to take the steps necessary to solve the inflation problem unless he is convinced that others will go along. Inflation poses a problem in which the interests of individuals coincide in the long run with the public interest. If the program succeeds in accomplishing a gradual reduction in inflation, and we can't stop it overnight, we will all be better off. Money wages will grow less rapidly but real wages will continue to expand because prices will also rise more slowly. Profits will continue to rise and to provide adequate incentives. Our chances of sustaining economic growth will be improved, and the risk of new inflation reduced.

Mr. Chairman, I don't want to downplay at all the importance of the international economy, and I have a section in my testimony devoted to that. But in order to give the members chances for questions, let me simply skip to that and the last paragraph.

Along with other nations in the world we are dealing with some stubborn problems. But I might interject, on balance, taking unemployment and inflation into account, we have done better than most. We have done virtually better than anyone if you take both measures into account. But all of the nations face stubborn problems. Problems of inflation simultaneously occuring with unemployment. Problems of structural unemployment. Problems of imbalances in our trade. These problems are not going to be solved overnight. But the American economy is remarkably resilient. It will respond to carefully designed economic policies that address both short and long-run needs. The President's economic program meets that criterion. I believe it is essential to the continued healthy growth of the American economy, and I urge your favorable consideration and prompt action upon the President's proposals.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Schultze, together with an appendix, follows:]

PREPARED STATEMENT OF HON. CHARLES L. SCHULTZE

I am pleased at this opportunity to discuss with the members of the Joint Economic today the President's economic program for 1978 and 1979. That program is designed to maintain a strong economy over the next two years and to build the foundation for continued progress over the longer term.

As you know, the President delivered his *Economic Report* to the Congress on January 20, and yesterday the Council of Economic Advisers published its own Annual Report. In my testimony today, I would like to summarize the economic situation and outlook as we see it, and discuss how the Administration's economic program meets the needs of the country.

In know that you are particularly interested in the overall dimensions of that program, how its pieces fit together, and what are the longer-term policy considerations that guided its formulation. I shall pay particular attention to those points.

THE MAJOR TASKS OF ECONOMIC POLICY

The American economy today is basically healthy. We are making good progress in recovering from the trauma of earlier years, when the nation was hit, in quick succession, by double-digit inflation and severe recession. Last year, our economy created a record number of new jobs and reduced the ranks of the unemployed by over one million people. The pace of activity, moreover, is moving well as we enter 1978.

Because the inflation was so great and the recession so deep, the progress we have made still leaves us short of full recovery. Substantial further progress is needed, and steps must be taken now if we expect to achieve our long-range economic goals.

Economic growth will slow in late 1978 and in 1979 unless we act to relieve the growing tax burden on consumers. Payroll taxes are rising sharply, and inflation is pushing individuals into higher tax brackets. Other sectors of the economy are not growing sufficiently to counterbalance this depressing effect on consumer spending. Tax reductions for individuals are therefore needed to maintain growth of consumer purchasing power and spending.

Business investment is not rising fast enough. More investment will create additional jobs for a growing labor force and increase our industrial capacity for the future. Business tax reductions are needed to provide the incentives for a faster expansion of investment and the capital stock.

The Federal tax system is too complex and in many respects unfair. Reform of our tax laws is needed and should be combined with tax reduction this year.

Structural unemployment remains a major unsolved problem. Overall economic progress will help reduce the very high unemployment rates among youth and minorities. But these and other groups will not enjoy their fair share of the fruits of economic expansion unless their job opportunities are increased substantially. In addition to overall economic measures, we need to improve and expand our employment and training programs to address their specific employment problems.

Inflation is too high. We must take steps to prevent a worsening of inflationary pressures as the economy moves to higher levels of employment and production. And we must bend our efforts now toward reducing the present inflation.

These problems cannot be dealt with in a piecemeal fashion. Only with a coordinated effort to deal with all of them will we realize the potential that our national resources and the energy of the American people make possible.

THE ECONOMIC SETTING

Let me set the stage for an explanation of the President's proposals by reviewing briefly the major economic developments of the past year and the situation of the economy as we enter 1978.

The economy grew strongly last year. In the fourth quarter of 1977, the nation's real Gross National Product stood 5¾ percent above its year-earlier level. More than 4 million jobs were created in 1977—the largest employment increase of any single year. By December, the rate of unemployment had fallen to 6.4 percent, 1.4 percentage below its level 12 months earlier.

The benefits of growth were impressive. On a per capita basis the real after-tax income of Americans rose almost 5 percent over the four quarters of 1977. The rate of capacity utilization in manufacturing increased, and corporate profits rose by 9½ percent for the year.

The course of the expansion during 1977 was uneven. Output rose strongly early in the year, as businesses sought to rebuild depleted inventories, and unemployment declined sharply. When consumer spending slowed in the spring and summer months, retailers reduced their orders and manufacturers cut back on the rate of production and also their hiring. By year end, however, the pace of activity had begun to pick up again, led by a vigorous rise in consumer spending, and the economic stimulus program proposed by the President and enacted by the Congress earlier in the year.

We are entering 1978 with good prospects for continued strong expansion for the near term. Growth will be spurred for a time by increased inventory investment, as businesses catch up with the unanticipated surge in consumer spending late last year. Moreover, the 1977 stimulus programs are still gathering strength and will encourage recovery through the first half of 1978.

As we look further ahead, however, it is clear that unless steps are taken now to maintain economic growth, expansion will slow to an unacceptable pace. Our efforts to reduce unemployment will be frustrated.

The most important development threatening sustained recovery is the increasing burden of taxes borne by the average taxpayer. Under present law, large increases in payroll taxes are coming into effect to finance the social security programs. Some of these added taxes were scheduled by law in the

1973 social security amendments. Additional increases were enacted last year and are essential to the continued health of the social security system, since without them the trust funds would soon be depleted. But the economic impact of these higher taxes cannot be ignored. Payroll taxes will rise by $7 to $7½ billion in 1978 and again in 1979. An additional drag on consumer purchasing power will occur because inflation and real economic growth push taxpayers into higher brackets. Unless steps are taken to lower individual income taxes, Federal revenues over the next two years will be absorbing a significantly rising share of personal income.

There are times, of course, when increased effective tax rates are needed to restrain an overheated economy. But that is not the case at present. On the contrary, growth in the private sector is not likely to be strong enough to overcome a substantial increase in the degree of fiscal restraint that would be emanating from the Federal budget.

For example, consumer spending will probably rise in 1978 and 1979 by somewhat less than the increase in after-tax incomes. Americans are now saving about 5¾ percent of their income after taxes—a lower rate than has prevailed for most of the past decade. The saving rate could easily increase somewhat in the near future. Consumer purchases cannot be expected to serve as the driving force for economic expansion, as they did early in the recovery.

Similarly, housing construction, which has risen very strongly since early 1975, will not continue to provide a major source of thrust to economic expansion. Backlogs of demand have been reduced, and financial markets have tightened somewhat. We do not expect housing construction to decline significantly over the next two years, but it is unlikely to show a substantial increase.

The foreign sector has been a major dampening factor on growth in our economy over the past two years. Last year, the U.S. current account deficit increased dramatically—to about $18 billion—due largely to a surge in oil imports. Other imports also rose strongly, but our exports showed little growth. Economic expansion abroad is likely to improve somewhat in 1978, increasing the demand for U.S. exports, and the dollar volume of our oil imports will probably remain about unchanged this year. Our overall current account deficit, therefore, should not increase signficantly further. But we cannot, unfortunately, expect it to diminish materially either.

The source of growth that would be most welcome in 1978 and 1979 would be a strong rise of business fixed investment. Over the past several years, the labor force in our country has grown very rapidly. Growth of the capital stock has not kept up. Productivity is therefore increasing very slowly. And although there is, at present, substantial idle capacity in our plants and factories, a faster growth of capacity will be needed to avoid inflationary bottlenecks in later years as we approach a high employment economy.[1]

AVERAGE ANNUAL GROWTH IN THE STOCK OF BUSINESS FIXED CAPITAL AND THE PRIVATE LABOR FORCE

[Percent per year]

	1965–73	1973–76
Business capital stock	4.4	1.9
Labor force	1.9	2.3

During the course of an economic recovery, business plans for investment spending typically strengthen—as capacity utilization increases, profits improve, and the outlook for the long-term future brightens. There *has* been a significant improvement in the rate of investment over the past two years, but it is not sufficient. In real terms, business fixed investment in the final quarter of 1977 was still 3 percent below its peak in 1974. Moreover, surveys of business plans for investment in new plant and equipment in 1978 suggest a rise this year that may fall somewhat short of last year's performance. This is simply not good enough.

[1] Appendix 1 briefly discusses the problem of capacity utilization as the economy approaches high employment.

Given the absence of growing strength in these major sectors of the private economy, it would clearly be unwise to impose a major increase in the tax burden on the economy—but that is what would happen without the President's tax program. As a consequence, economic growth would slow. We estimate that if the President's tax program were not enacted, growth in 1979 would be in a range of about 3¼ to 3¾ percent. The rate of unemployment would therefore stop declining, and it might begin rising again. We are still too far from full recovery to accept such a result, and the President's fiscal program for 1979 is designed to assure that it does not happen.

THE ADMINISTRATION'S FISCAL PROGRAM

The centerpiece of the Administration's economic program for fiscal 1979 is the proposal for substantial tax reductions, integrated with recommendations for meaningful reform of the tax system. The elements of the program include:

1. Tax reductions of $24 billion for *individuals* combined with revenue-raising reforms of $7 billion. Tax reduction is achieved by substituting a $240 per capita credit for the existing $750 personal exemption and the general tax credit, and by reducing personal tax rates. The reduction in tax burden is greatest for low and middle-income taxpayers.
2. *Business* taxes are reduced to $8 billion. Tax reforms affecting businesses will raise $2 billion in revenue, for a net business tax cut of about $6 billion. Tax cuts are provided through a substantial reduction in the corporate tax rate—the first since 1964—and through liberalization of the investment tax credit (ITC). The ITC is made permanent at 10 percent, and for the first time is extended to include industrial and utility structures, as well as equipment. Furthermore, businesses will be permitted to use the ITC to offset up to 90 percent of their tax liability, compared with the current 50 percent limit.
3. The Federal *telephone excise tax*, which under current law is now being gradually phased out, will be eliminated this year and the *Federal unemployment insurance tax* rate will be reduced to its pre-1977 level. The net tax reduction from these two provisions is $2 billion, which will be realized by consumers principally through lower prices.

These proposals do not include any provision relating to the energy legislation now pending before the Congress. If, when finally enacted, the energy program does not include a full rebate to consumers of the net proceeds of the wellhead tax on oil, the President has indicated that he will seek additional personal tax reductions to return those funds to consumers.

In total the President's program calls for tax reduction of $34 billion, partially offset by $9 billion in revenue-raising reforms. The two elements of reduction and reform go together. Without the tax reforms, the size of the tax reduction components of the program should be scaled back.

The reforms included in this package are achievable and desirable. They will make our tax system much more equitable by eliminating a variety of business deductions that have been greatly abused, by sharply curtailing tax shelters, and by strengthening the minimum tax. They also eliminate tax subsidies in the area of international business transactions whose public benefits do not justify the costs. And they will make the tax system simpler and easier to understand.

The amount of net tax reduction called for in the President's program has been scaled to the needs of our current economy, and designed to promote a sustainable economic growth rate of 4½ to 5 percent in 1978 and 1979. It will amount to 1.1 percent of the 1979 GNP. This is about half the size of the 1964–65 tax cut, but 60 percent larger than the tax cuts which went into effect in 1970 and 1972.

In the absence of the tax cuts, the share of personal income absorbed by Federal personal income taxes and the contribution of employees and the self-employed to social security would rise from 14.3 percent in 1977 to about 15.1 percent in 1979. Under the President's proposals, however, the share of personal income absorbed by these taxes will not increase between 1977 and 1979. Looked at from a different perspective, the President's tax proposal will mean that total Federal tax revenues as a share of GNP will rise only slightly between 1977 and 1979. Thus, by reducing taxes, we will counterbalance the prospective drag on the economy from the rising tax burdens which would otherwise occur.

RATIO OF TAXES TO PERSONAL INCOME AND GNP, CALENDAR YEARS 1977-79

[In percent]

	1977	1978	1979
Ratio of personal taxes plus employee and self-employed social security taxes to personal income:			
With tax cut	14.3	14.3	14.1
Without tax cut	14.3	14.5	15.1
Ratio of total Federal revenues to GNP:			
With tax cut	19.3	20.1	20.0
Without tax cut	19.8	20.4	21.2

The size of the tax proposal was not designed to achieve any particular ratio of tax revenues to income, however. Rather, it was formulated in concert with the President's expenditure recommendations, to keep the economy on a path of growth that will ensure significant further progress in reducing unemployment during 1978 and 1979.

A full appraisal of the contribution of the Administration's proposals to the performance of the economy must take into account both the expenditure and revenue sides of the budget. One simple, but useful, measure of the overall degree of fiscal impact is the deficit in the high-employment budget. In this budget, the estimates of spending and revenues are those that would occur if the economy were at high employment. This budget thus abstracts from the increased spending and reduced tax revenues that result automatically when the economy is not at high employment. As a result, the discretionary elements in the budget stand out clearly. The movements in the high-employment budget, as measured in the national income and product accounts are shown below for calendar years 1977 through 1979.

[In billions of dollars]

	1977	1978	1979
High employment deficit	−18	−27	−23

With the President's program, the high employment budget deficit would increase significantly in 1978. In 1979, it would decline somewhat, but remain $5 billion higher than in 1978. Thus, the Administration's overall budgetary program adds modestly to the degree of fiscal stimulus between 1977 and 1979.

If the President's program is enacted, we expect both 1978 and 1979 to be years of good economic growth. The nation's real output should increase each year by 4½ to 5 percent—a rate that would make it possible to reduce the unemployment rate from 6.6 percent in the final quarter of 1977 to a range of 6 to 6¼ percent by the end of 1978, and to somewhere in the 5½ to 6 percent range by the fourth quarter of 1979. We estimate that the tax package will create nearly one million additional jobs by the end of 1979.

The economic effects of this tax proposal, if enacted, will begin to show up in the latter part of 1978. Some additional stimulus to consumption should occur promptly in the last quarter of the year, as tax reductions are reflected in take-home pay. From the final quarter of 1978 to the same period in 1979, real personal consumption expenditures should rise at close to a 5 percent annual rate.

This strong and sustained growth in consumer markets should encourage businesses to augment investment plans in 1978 and 1979. The tax incentives proposed by the President should also encourage a step up of investment plans. The extension of the ITC to investment in structures will be made retroactive to January 1, 1978, and some effects may begin to be felt before final enactment of the tax proposals. Prospective reductions in the corporate tax rate, meanwhile, will increase the expected returns on investment and, once enacted, help to finance needed investments through greater cash flow. We expect business investment in real terms to strengthen during the course of 1978 and to rise by about 8 to 9 percent in 1979 if this program is put in place.

EFFECTS ON THE DEFICIT

Achieving these results through tax reduction means, of course, that the 1979 Federal deficit will be larger than it otherwise could have been. The President's fiscal 1979 budget carries a deficit of $61 billion in that fiscal year, only slightly below that in 1978. Had the proposed tax reductions been foregone, however, the deficit would have been $15 to $20 billion less. But the price would have been a weaker economy, almost a million fewer jobs, a substantially higher unemployment rate, and less growth of investment and industrial capacity. That is far too high a price to pay.

The 1979 budget deficit is large, but it is not inflationary. We recognize fully that deficits in the Federal budget do cause inflation if they create excess demand. We see no danger of that during the next two years, since unemployment is still high and there is ample slack capacity in the manufacturing sector to permit further increases in real output without encountering bottlenecks.

We know, however, that the Federal budget must be brought into balance as rapidly as the developing strength of the economy permits. That is an essential principle of the President's long-range budgetary strategy, and our recommendations for fiscal 1979 are entirely consistent with it.

LONG-RANGE BUDGET STRATEGY

The President has stated on numerous occasions his intention to keep a tight rein on the growth of total Federal expenditures. The Administration's 1979 budget reflects this commitment—Federal expenditures increase in real terms by less than 2 percent. Similar restraint will be shown in succeeding budgets. We intend to reduce gradually the share of the Nation's output devoted to Federal expenditures.

Budgetary restraint does not mean neglect of important social problems. The Federal Government should, and under this Administration will, continue to meet the pressing needs of the Nation. Through careful budgetary management—using zero-based budgeting and multi-year planning—we can improve efficiency and select priorities more carefully, thereby channeling budgetary resources to meet important social and other national needs. In the years ahead, sustainable economic growth can be promoted by such an expenditure policy, coupled—when and as the need arises—with tax reductions.

At each step along the way, the benefit of tax reduction will have to be weighed against the costs of a larger deficit. We intended to move toward a balanced Federal budget. In a high employment economy, with strong growth in private demand, deficits must be avoided; since under those conitions they would create excess demand and generate inflationary pressures.

If the private economy grows very strongly between now and 1981, we can and will balance the budget by then. No decisions have been made in the 1979 budget that foreclose this possibility. If private economic growth appears to be insufficient in the future to achieve high employment, however, we are prepared to undertake additional fiscal measures to ensure that our economic objectives are realized. In that event, the date for achieving a balanced budget would have to be deferred.

One obvious question comes immediately to mind in relating these budgetary principles to the 1979 budget. Why is it necessary so far into economic recovery to have a budget deficit of $61 billion? Under the economic conditions which prevailed in the 1960s or the early 1970s this would not have been the case. But there are several characteristics of our present economy which make it very difficult to balance the Federal budget without sharply slowing economic growth. The difficulty stems, in the main, from developments affecting the budgets of State and local governments and from the drain of income associated with our foreign trade in goods and services.

In the past, State and local governments in the aggregate typically ran small budgetary deficits. More recently, however, the aggregate budgets of State and local governments have been in sizable surplus. Last year, that surplus was nearly $30 billion, up from $18 billion in 1976 and $3 billion in 1970. Part of this growing surplus stems from the accumulation of monies in pension funds for the 13 million employees of State and local governments; another part stems from efforts by some of these governmental units to put their financial houses in better order after the recession of 1974–75. Within the aggregate, of course, there are some governments whose fiscal positions are quite difficult.

However pleasant the overall surplus may be from the standpoint of many State and municipal governments, they tend to restrain economic activity—because they draw more out of the income stream in tax revenues than are put back by way of expenditures.

The current account deficit in our international transactions—nearly $18 billion in 1977—poses a similar problem. It also represents a drain on the stream of national income; it means that we are sending more dollars abroad through purchases of goods and services than are returning to our country to buy goods and services here.

The table below shows the current size of these drains on income, and how large they are compared with earlier yaars of high employment:[2]

[In billions of dollars]

	1955-56	1965-66	1972-73	1977
State and local surplus	-1.1	0.2	13.4	29.2
Foreign sector	-.7	-2.9	5.2	19.1
Total	-1.8	-2.8	18.5	48.3
Federal surplus or deficit (-)	5.2	-.6	-12.0	-49.6

The aggregate surplus of State and local governments is likely to diminish somewhat in the next few years but it will probably remain large for many years to come. Adjustment of our trade deficit will also take time. That deficit can be traced to two major factors: we are importing large amounts of oil at high prices, and our exports have been depressed by slow rates of economic growth abroad. Enactment of an effective energy program, and improvement in the economic growth rates of other nations, will contribute to a gradual reduction in our foreign deficit; it can only occur gradually.

The State and local foreign sectors are, of course not the only economic forces which determine the appropriate fiscal stance for the Federal Government. But the size and recent growth of the income drain from these two areas are large and they must be taken into account in the formulation of Federal fiscal policy.

We cannot realistically expect that the unprecedented size of the income drain in the State and local and foreign sectors will automatically be counterbalanced by extremely strong spending propensities on the part of American businesses or consumers. Therefore, the Federal budget must stand ready to provide a counterbaalnce, in order to maintain a healthy economy.

STRUCTURAL UNEMPLOYMENT

Fiscal and monetary policies are the basic tools at our command for promoting healthy growth in the overall economy and reductions in unemployment. But even in periods of relative prosperity some groups of American workers continue to suffer high unemployment rates. The current recovery has bypassed some Americans. Blacks and members of other minority groups particularly face disproportionately high rates of unemployment; the 40 percent rate of unemployment among black youth is simply not tolerable. Unless the government takes steps to bring all groups of citizens into the economic mainstream, we will be frustrated in our efforts to achieve tolerable levels of unemployment.

A nation that prides itself on human rights cannot ignore a structural unemployment problem of the magnitude we face in the United States. The human and social costs are much too large. The economic costs are also substantial. If we can give those individuals who otherwise would be unemployed the training and experience they need to become productive workers, and open up job opportunities for them, the nation's potential to produce would be greatly enhanced. Millions of Americans out of work amount to an enormous waste of valuable resources.

[2] Data are from the Department of Commerce national income accounts.

In the longer run, dealing with structural unemployment successfully also has important implications for controlling inflation. Typically, as our economy approaches high levels of employment, some labor markets tighten up much more than others. Unemployment rates for experienced adult workers drop to very low levels, while large unemployment still exists for other groups. Employers, however, still tend to expand their work force by trying to fill vacancies with workers from the groups with low unemployment, rather than turning to those with higher unemployment rates. As a consequence, inflationary pressures on wages and prices ensue, even though unemployment among some segments of the labor force is still very high. Employment and training programs that provide skills and open up job opportunities for disadvantaged groups of workers tend to reduce these inflationary pressures, and are essential if we are to achieve both our objective of price stability and our goal of high employment.

The task we face is a difficult one. We have already taken some important first steps, but much remains to be done.

In the 1977–78 stimulus package, the level of jobs under the Public Service Employment program was increased from 310,000 to 725,000. PSE employment has grown substantially since last spring, and now totals about 600,000. The remaining increase to 725,000 will occur over the next few months. The program was also modified to target it more carefully on the longer-term and low-income unemployed. The President is proposing to continue this program at the 725,000 job level in 1979.

The current public service jobs program is principally countercyclical in nature, and will be stepped down gradully after 1979 as the overall unemployment rate declines. A more permanent program, designed to provide work for 1.2 to 1.4 million persons, is part of the President's proposed overhaul of the nation's tangled welfare system. This program is aimed at offering work, rather than cash welfare, to those of the nation's poor who are able to work. The 1979 budget includes a request for a 50,000-job program to demonstrate the feasibility of the Program for Better Jobs and Incomes proposals.

Special programs for young people were authorized under the Youth Employment and Demonstration Projects Act enacted by the Congress in 1977. These projects are aimed at testing a number of alternative approaches to combine work experience and training for young people. In the 1979 budget, we are requesting funding for 166,000 slots in the YEDPA programs, and to increase the Job Corps.

For most workers, the long-term answer to job opportunities must be in the private sector. Five out of six new jobs will come from that sector. It is in the private sector that the greatest opportunities exist for job training, for advancement, and for meaningful life-time careers. It is important, therefore, that we find effective ways to channel those who ordinarily would go jobless into private sector employment. Later this year, the Administration will send to the Congress proposals to encourage the creation in the private sector of jobs for the structurally unemployed, and particularly for the young. Details of this program are under active development at the present time and will be sent to the Congress shortly. The 1979 budget includes $400 million for this new initiative.

REDUCING THE RATE OF INFLATION

Another critical problem with which we must deal more effectively is inflation. During the period immediately ahead, there will still be some slack in the economy, and the likelihood of an increase in the rate of inflation is low. As the economy approaches high levels of employment in 1980 and 1981, however, the risks increase that the rate of inflation will begin to move up. A significant worsening of inflation would undermine the confidence of consumers and businesses, causing them to cut back on purchases and investments. Moreover, we would be inhibited from taking the fiscal and monetary steps necessary to reduce the rate of unemployment. Progress against inflation is thus absolutely essential to reducing unemployment.

The inflation problem that we face today has two distinct aspects. We need, on the one hand, to pursue policies that will avoid a worsening of inflation as we regain high employment. And we must take steps now to begin unwinding from the high rate of inflation that we have inherited from the past.

The government can, by following prudent fiscal and monetary policies, ensure that inflationary pressures are not increased due to excess aggregate demand when the economy returns to high employment. During the period from 1965 to 1969, inflationary pressures were intensified by continuation of deficit spending in a high-employment economy. Overly expansive monetary and fiscal policies also contributed to inflation during 1972, when a worldwide boom developed that put serious pressures on the basic resources of industrialized economies. With sound management of the budget and the economy, we can avoid such excesses in the future.

A second important step is to ensure that industrial capacity expands rapidly enough to prevent shortages and bottlenecks in individual industries as overall demand reaches higher levels. The President's economic program for 1979 recognizes this fact. It will encourage investment by promoting continued expansion of markets for the output of new plant and equipment, and by offering specific incentives to increased investment.

Third, a successful attack on the structural sources of unemployment also is essential to reduce the chances of higher inflation rates in the future. That fact, too, is recognized in the Administration's budget proposals for fiscal 1979.

Efforts to reduce the current inflation rate will encounter difficult problems. There is much that government can do to contribute to lower inflation. A modest step—the proposed reduction in excise and unemployment insurance taxes that will contribute directly to lower prices and costs—is incorporated in the President's tax program.

The government also can bring into line its own actions that raise costs and prices. A top priority of this Administration is to reduce the adverse impact on costs and prices of government regulatory actions. We have moved already to cut back significantly the sheer number of regulations, and to pare the paperwork burden imposed by regulatory agencies. We are establishing new procedures that will encourage regulatory agencies to seek out and apply the most cost-effective approach to accomplishing our regulatory objectives. The President has established under my chairmanship an interagency committee to review the adequacy of economic analysis of major regulations. Government can in this way make a direct contribution to reducing the cost-rising effects of its own actions.

However, such actions alone will not be sufficient to make dramatic progress against inflation. For the past three years, the rate of inflation has persisted in the general range of 6 to 6½ percent. There have been temporary fluctuations in the inflation rate, due to movements in food prices and fuel prices, but the underlying rate of price increase has neither accelerated nor slowed throughout the recovery. Recent experience suggests that the rate of inflation is increasingly unresponsive to widespread unemployment and idle capacity.

The inflation we have inherited from the past is built-in to the process of setting wages and prices. Businesses raise prices to compensate for past and expected wage increases, because they expect consumers to pay the higher prices they charge. Workers, seeing prices rising and expecting more inflation in the future, push for higher wage settlements. This process cannot be brought to a halt by government decree; nor can it be eliminated through the action of any one group of workers or businesses. If the rate of inflation is to be brought down from its current plateau, we must all work at the job together.

Over the past several months, the Administration has examined closely a wide array of alternatives for dealing with the inflation problem.

Several approaches were rejected virtually from the outset. We cannot, for example, sit back and do nothing. Inaction could mean eventual reemergence of bottlenecks and wage pressures that could lead to a worsening of inflation. Mandatory wage and price controls are not the answer. They do not effectively stop inflation, and the severe distortions, inefficiencies, and inequities they cause are unacceptable.

We also have rejected policies of slow growth. We cannot wring the inflation out of the economy through high unemployment and economic slack. Such policies have only a limited impact on the kind of inflation we face, and then only at unacceptably high cost in human suffering and lost output. Moreover, by discouraging businesses from commitments to increase capacity, slow rates of growth may lead to inflationary problems later on, when high employment finally is approached.

A number of innovative ideas to reduce inflation through the tax system were given serious consideration. Some of these proposals would give tax reductions to workers in return for restraint in annual wage increases. Others would tax wage increases above a specified level, or use general revenue sharing as a means of encouraging State and local governments to reduce sales taxes.

All of these plans, however, are subject to major questions with regard to administrative feasibility, economic impact and political acceptability. It would therefore be highly imprudent to propose introducing any of them before subjecting them to a much wider discussion and a more complete evaluation with respect to their economic effectiveness, administrative feasibility, and social equity. On the other hand, the momentum of inflation is so great and the consequences of either allowing it to continue or trying to wring it out with excessively slow growth are so large that they should not be dismissed out of hand. Further economic evaluation and a much broader public debate would be very healthy, whatever its outcome.

After reviewing a long list of policy options, the President has concluded that the most appropriate step we can take at this time is to embark on a program of voluntary restraint in the setting of wages and prices. He has set forth a reasonable standard of behavior for gradually reducing inflation. Over the next year, labor and management in each industry have been asked to reduce rates of increase in wages and prices to below what they were on average in the prior two years.

This is a flexible and fair proposal. It recognizes that there will be some cases in which the profit margins have been badly lagging, and that there are some groups whose wages have not risen as rapidly as others. In those cases, deceleration may be more difficult to achieve, and in some circumstances, may not be possible at all. By the same token, those businesses and groups of workers that have done better than average recently should contribute more to the overall deceleration of inflation.

To implement this program, the Administration will initiate discussions with officials and representatives of firms and unions well in advance of decisions on price increases or the opening of wage negotiations. This is *not* a program that requires prenotification of wage or price decisions; nor will the government attempt to interfere with the normal process of collective bargaining. But we will seek, through discussions that focus on conditions in the public's interest in wage and price restraint.

We fully recognize that this program will meet some skepticism. Given the nature of the current inflation, it is clear that no individual business or group of workers can afford to take steps to solve the inflation problem unless he is convinced that others will go along. Inflation poses a problem in which the interests of individuals coincide in the long run with the public interest. If the program succeeds in accomplishing a gradual reduction in inflation, we will all be better off. Money wages will grow less rapidly—but real wages will continue to expand because prices will also rise more slowly. Profits will continue to rise and to provide adequate incentives. Our chances of sustaining economic growth will be improved and the risk of new inflation reduced.

THE INTERNATIONAL ECONOMY

The problems which the American economy faces, and toward which the resolution of which the President's economic program is addressed, are not unique to our nation.

Throughout the world, in both industrial and developing countries, governments are struggling with the existence of inflation side-by-side with widespread unemployment.

Outside the United States economic recovery faltered in 1977. Unemployment is high and rising in most industrial countries abroad. The quadrupling of world oil prices in 1973–74, that contributed so much to the world-wide acceleration of inflation and the global recession, is still troubling the world economy through its effect on the balance of payments of oil-importing countries. And because they were so severe, the economic disruptions of several years ago still cast a shadow over current economic events, as their memory affects the attitudes of businessmen and consumers.

Continued economic recovery is critical to the health of the world economy. Growth in the U.S. economy—the largest and strongest in the world—is essential to that recovery. It is also important that other strong nations join with us to promote growth in their own economies. World recovery cannot proceed if nations rely upon exports as the principal source of economic expansion.

The problem of imbalances in international payments will also require concerted action. Because of the surpluses of oil-exporting countries, many nations have sizeable deficits. Some industrial countries are also running large and persistent surpluses, thus increasing the pressures on countries in deficit.

Reduction of these imbalances will demand several parallel steps. To begin with each individual country must ensure that its own policies help relieve the strains. The United States must do its part. In 1977 we had a current account deficit of $18 billion. The large rise in oil imports was a major factor in producing this result. We can take a most constructive step toward correcting this deficit by moving quickly to put a National Energy Plan in place.

Our 1977 trade deficit also stemmed from our better economic performance. Slow growth abroad held down our exports while expansion at home raised the demand for imports. The appropriate response to these developments is not a halt in U.S. recovery—that would seriously worsen the economic problems of the world. It is important, however, that in our recovery we encourage a faster growth in business investment, to improve productivity growth, provide adequate industrial capacity, and combat inflation, thereby enhancing our competitive position in world trade.

Countries in surplus should also do their part. Balance of payments surpluses in some countries have contributed to the economic stagnation among their trading partners. Where their own economies have slack, it is appropriate for nations in surplus to stimulate the growth of domestic demand—thereby increasing their imports and improving the prospects for growth in deficit countries. In some countries, lifting restraint on imports from abroad and reducing excessive government efforts to promote exports would be useful. After consultations with the United States, the Japanese have indicated they will take a series of steps toward reducing their large surplus.

During 1977 the U.S. dollar fell in value against several key currencies. The decline in the dollar's value has occurred primarily against the currencies of those nations that have large trade and payments surpluses, and was not surprising in view of our large payments deficit and their surpluses. Late in 1977, however, movements in our exchange rate became both disorderly and excessively rapid. The United States reaffirmed its intention to step in when conditions in exchange markets become disorderly and to work in close cooperation with our friends abroad in this effort.

Under the flexible exchange rate system basic economic forces must continue to be the fundamental determinant of the value of currencies. However, we will not permit speculative activities in currency markets to disrupt our economy or those of our trading partners. We recognize fully our obligation in this regard, and we have taken steps to fulfill it.

Although substantial progress can be made toward a balanced world economy, some imbalances will persist for a substantial period of time. Financing requirements will remain large while adjustments occur. The private markets can and will continue to channel the bulk of the financing from surplus to deficit countries. But it is essential that adequate official financing also be available, in case of need, to encourage countries with severe payments problems to adopt orderly and responsible corrective measures. To meet this critical need the United States has strongly supported a proposal to strengthen the International Monetary Fund by the establishment of a new Supplementary Financing Facility.

Along with other nations, we are dealing with some stubborn problems. They will not be solved overnight. But ours is a remarkably resilient economy. It will respond to carefully designed economic policies that address both short-run and long-run needs. The President's economic program meets that criterion. I believe it is essential to the continued healthy growth of the American economy, and I urge your favorable consideration and prompt action upon the President's proposals.

Appendix 1

Capacity Utilization Through 1981

To reach an unemployment rate of approximately 5 per cent by the end of 1981, GNP would have to grow by about 4.8 percent a year. A rough indication of the rise in manufacturing capacity utilization that may accompany the projected real GNP growth of 4.8 percent per year between 1977 and 1981 can be obtained by observing the capacity utilization growth experienced in 1962–68, when real output grew steadily at above-trend rates, and real investment grew more rapidly than real output. If the relation between real GNP growth and capacity utilization in 1962–68 is matched in 1977–81, an annual 4.8 percent growth in real GNP would raise the manufacturing capacity utilization rate by 1.5 percentage points a year. By 1981 the utilization rate would reach 89 percent, slightly above 1973 but less than the 1966 level. In view of the current capacity utilization differences among industries and particularly the current large unused capacity in materials industries, such an outcome should be consistent with the avoidance of inflation stemming from capacity shortages. If, on the other hand, investment and capacity growth proceed at a significantly lower rate, capacity utilization would rise to levels previously associated with inflation.

Representative BOLLING. Thank you, very much.

We will proceed under the 10 minute rule because of the number of members present.

Senator BENTSEN. Thank you, Mr. Chairman.

Senator Bentsen.

Mr. Schultze, your statement on the economy and the President's proposals appear to have a steady-on-course theme. You are trying to walk a very tight economic tightrope. I do think you are going to have to have some pretty bold innovative things to break through the problem of structural unemployment.

I recall reading your Godkin series some 3 or 4 years ago, in which you talked about pursuing public objectives by incentives and rewards.

I am particularly and intensely concerned about the structural unemployed. I do hope as you work toward those incentives, subsidies, tax incentives—whatever they may be—in the private sector, that you won't just develop a regional solution.

There is an awful lot of publicity about New York and some of the other areas with high unemployment, but structural unemployment is just as much a problem in south Texas as it is in New York. It must be kept in mind that we need national solutions to this problem.

I would like to disgress a moment from your testimony to ask you about some of the alarming reports I have read about hot spots on coal supplies that may be developing. Nationally we appear to have substantial supplies but from what I read in the paper we can look to States like Ohio and Illinois, perhaps, running out of electricity in the next 40 or 50 days.

Of course, this is complicated by the weather. What, if anything, is the administration doing to try to end the strike?

Mr. SCHULTZE. I don't know the specific details. The administration through the Federal Mediation Service has been closely involved in this; they are No. 1 in the way the Mediation Service usually is.

With respect to the coal supplies, it is my understanding in these areas it is a combination of both the supplies and stocks which actually still are—there are spot problems but they are still fairly sizable, and a transportation problem in part due to the recent cold weather.

At the present time, however, the last review I saw indicated that there are still sufficient supplies; the Federal Government is proceeding to reduce—I want to make sure I am correct—to be sure it has actually reduced or is strongly considering reducing—I believe it has actually done so—the power consumption that the gaseous diffusion plant chews up. It is about 4,000 megawatts of power. That should provide some relief.

Senator BENTSEN. How much longer can this strike go on before we see substantial laying off of employees?

Mr. SCHULTZE. I cannot give you a specific answer to that, Senator. It clearly can go on for sometime, then there presumably would have to be some interruptions which maybe in terms of the number of hours a plant can operate but I don't have a time on that.

I think at the moment, however, that does not appear to be in the prospect. I cannot give you a number of days or number of weeks, rather. It would vary from place to place.

Senator BENTSEN. Some of the reports out of Ohio and Pennsylvania and Illinois would lead one to think that we are facing it now.

Mr. SCHULTZE. It is my information, Senator, that we are not now, that we could if it continued for a good bit longer but I don't have a time on that.

Senator BENTSEN. On the energy question, we now import about 8.7 million barrels of oil a day. Your budget document states that the President's energy plan will bring about increased coal utilization and energy conservation and will cut oil imports to 6½ million barrels a day by 1985.

On the other hand, we have the Library of Congress report saying our oil imports will be at 12 million barrels per day by 1985, 12 million barrels as opposed to the administration's projections of 6½ million barrels.

We see the National Coal Association circulating a paper indicating that the administration's plan to double coal production could not be met without significant easing of environmental restrictions or regulations.

Now, last spring, the CIA issued a report indicating our oil imports could go as high as 15 million barrels per day by 1985, and thereby precipitating or bringing about a worldwide energy shortage.

I see that petroleum demand in 1977 surpassed the level in 1973, despite a 500-percent increase in prices.

My question is, Who is right? Is the CIA right or the Library of Congress; is the administration's assessment still a correct one that we can cut oil imports to 6½ million barrels by 1985?

Do you still feel confident of that?

Mr. SCHULTZE. Obviously, it is difficult to feel confident of predicting anything 8 years out into the future.

Second, the administration projections of 6 million barrels a day were based upon its original national energy program and I must confess I do not since we don't have an outcome yet. I don't have any projections of what the changes that have been made or are likely to be made would do to that.

On the other hand, my recollection of the CIA analysis was that it did not take into account the national energy plan, that is, that imports would not be 15 million barrels a day with the national energy program.

So "confident" is a difficult word to use, but in terms of the best estimate that one could make given the original national energy program, that ballpark seems about right.

The measures won't have an impact overnight. It does take time. In the case of coal conversion, that is not something that will happen overnight. It is going to take time and you will not see those kinds of reductions for a while.

But, give it 8 years to work and the combination of conservation measures and production measures should get us into that ballpark, subject to the proviso, of course, that I cannot speak to what finally comes out when it is enacted.

Senator BENTSEN. On our balance of payment problem, how much improvement do you see coming about by the agreement to accelerate their growth by our interested trading partners? Do you see a positive result there, an improvement, and if so, do you have an estimate of it?

Mr. SCHULTZE. I don't have an estimate. As you know, the Japanese Government has recently undertaken major stimulative measures aimed at their own target of a 7-percent growth rate which would be a substantial increase over what will apparently happen this year, which is near 5; and what would clearly have happened next year without any such measures. Whether they will make the 7 percent yet or not, I cannot tell, but they have taken some major actions.

The rate of growth in OECD countries outside of the United States has been something like 2.5 percent this year, 1977 over 1976, and if you look at the pattern during the year, it has been flat since about April. Given what is likely to happen in other countries and measures that have been taken, that rate of growth during the year 1978 should pick up. But it is still going to be a relatively moderate rate of growth; that is, from 2.5 percent it might pick up to the 3½ neighborhood, maybe a little more.

In the case of the Japanese, it would be significantly more. That will help. We do not have an explicit estimate of how much that will do, but those growth estimates are built into our own economic forecasts for the year. So that, yes, there will be some pickup in the rate of growth; no, that pickup will not be dramatic as far as we now know except, perhaps, with the case of the Japanese.

Senator BENTSEN. Mr. Schultze, I can understand the concern and great difficulty in getting a handle on wages and prices in trying to find an approach to inflation that works. This one that the administration is talking about looks to me like prejawboning if I would try to give it a title.

How can you forestall either labor or management anticipating that this won't work and developing the attitude that they better get theirs while they can because tougher measures will be forthcoming?

How can you forestall that?

Mr. SCHULTZE. I am not sure there is any way I can guarantee that. I can point to several things.

First, we have some past history in that in those cases where the Federal Government has attempted to deal with some sort of volunteer measures on wage and prices, it has not put in wage and price controls.

On the other hand where Government, that particular 8 year period where the Government came in and said we are not going to do anything volunteer at all, then wage and price controls were put on.

So it seems to me, any reading of past history and any reading of the President's firm intentions would indicate that this is not a program which would be followed by wage and price control.

Senator BENTSEN. Let me ask you about a column in the Washington Star yesterday. It said the administration is going to call for tighter self-restraint by labor and by industry; is there any truth to that?

Mr. SCHULTZE. That was a complete misinterpretation, Senator. What we would be asking for is an equal degree of deceleration in wages and prices. However, there will be obvious difficulties among particular sectors.

For example, in the case of prices, a deceleration in food prices will particularly help so that you will tend to get more in food and less in other sectors.

We have to take into account what is happening to payroll taxes in all of this. So when you look, begin to look at all the details, obviously, it is not uniform, but with respect to wages and prices, we are asking and we would be expecting for the same degree of restraint in both cases.

Senator BENTSEN. Good luck.

Mr. SCHULTZE. Thank you, sir, we will need it.

Senator BENTSEN. Thank you, Mr. Chairman.

Representative BOLLING. Congressman Brown.

Representative BROWN of Ohio. Mr. Chairman, thank you very much.

Mr. Schultze, I have always been a little bit of a Charlie Schultze fan. And I have been quoting you for the past year or so in this area of energy that I have been married to.

So far, it has been an entirely sterile marriage, I should say. I want to do a little quoting with you now, if I can, from your book, "The Public Use of Private Incentives."

You state on page 80 and I quote, "The world is not full of sharp corners and discontinuities."

By that statement I believe that you meant that prices and taxes do not have one threshold level at which they suddenly affect behavior or production. The relationship is smooth, gradual, and general.

For example, the higher the tax we might put on pollution, the more pollution we would get rid of; or the higher the price of coal, the more we turn to deeper and more costly coal deposits for mining.

I have a little chart over here, chart 1, which I guess is that kind of economic graph.

You said in the book, "An efficient situation demands that costs be balanced against gains in each case, taking into account the common characteristic that gradually rising costs buy gradually increasing gains—in pollution control, oil production, or industrial safety."

Yet, when it comes to natural gas, which the energy conference is now hung up over, the administration has implied that chart 2 looks like this, the one now being set up; that prices rising from $1.45 to $1.75 produce a great deal more natural gas, but that not a single cubic foot more in the way of gas is available at any price above $1.75.

Now, to my way of thinking, that is a sharp corner and sort of flies in the face of what your book told me, this one about what——

Mr. SCHULTZE. If I might say, my recollection is that without wanting to, by that corner, I suspect what it is is a curve that gets gradually steeper. I think the book said the world isn't full of sharp corners. It didn't mean there weren't a few.

Representative BROWN of Ohio. Well, you can understand that when the Energy and Power Subcommittee analyzed——

Mr. SCHULTZE. At least I hope that is what I said. Go ahead.

Representative BROWN of Ohio. You can understand that when my subcommittee analyzed the numbers of the administration paper, "Estimates of Produce Revenues and Consumer Costs Under Decontrol," we found that penny by penny from $1.45 to $1.75, the Energy Policy and Planning people were assuming a 1.5-percent increase in gas production for every 1-percent increase in prices.

And, therefore, that 22-percent price increase which the administration would allow, would produce a 33-percent increase in gas compared with continued Federal Power Commission proposals.

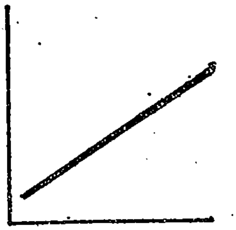
That means that the administration assumed a price elasticity of supply of 1.5, which is far higher than even the most optimistic advocates of deregulation would ever hope for. But, then, a strange thing happened. At $1.75, the price response comes crashing down to zero. We just don't get it anymore.

At $1.73 and $1.74, the elasticity is 1.5; at $1.76, it is suddenly zero. Chart 3 looks like this, and I think that is a discontinuity.

[The charts referred to follow:]

chart 1

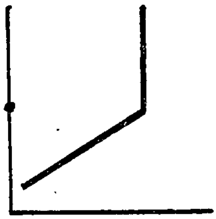
price $



quantity

chart 2

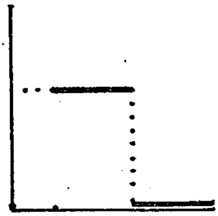
price $
1.75



quantity

chart 3

elasticity
1.8



0
1.45 1.75 price $

Representative BROWN of Ohio. With numbers like these in support of the President's energy bill, I think it is no wonder that the Energy and Power Subcommittee voted for deregulation and that the Senate concurred a little later.

You see, I have read your book, even if the administration hasn't, and, frankly, I believe that what you say in the book is right. "There is no fixed amount of oil or coal or copper available in the ground; rather, as we gradually exhaust the better deposits, the costs of extracting additional resources steadily rise." Again, I quote from the book.

You said in your book, and this is the other one that I have had a chance to look at, "Higher Oil Prices and the World Economy," on page 67, that "a reasonable solution to this problem of conflicting objectives might be to provide for a gradual rise in controlled prices toward parity with imported oil. Particular fossil fuel deposits are exploited over a large number of years. Similarly, changes in the consumption of energy are often associated with long-term investment decisions. As a consequence, it is long-term expectations about prices, rather than immediate price levels, that influence decisions concerning supply and demand. Removing uncertainties, by agreement on a policy of gradual decontrol announced in advance, would raise a long-term price expectations while significantly reducing the associated short-run demand management problems."

You were talking about oil in that paragraph, but you also referred generally to fossil fuels, and I am talking about gas now because that is our current problem.

Mr. Schultze, suppose the House-Senate Energy Conference succeeds in groping its way toward a policy of gradual decontrol of new natural gas. Suppose the time horizon is 5 years or less. It takes about 5 years to bring in new offshore wells and about 2 years to bring in onshore gas wells. Suppose the price increase—that is, the real price increase—were somewhere between 7 and 9 percent per year in real terms. Would you suggest, if we did that, that the President veto such a compromise or that he sign the bill in the national interest?

Mr. SCHULTZE. I cannot answer that until as far as I am concerned I would see it. So that I simply cannot give you an answer of what I would recommend or wouldn't recommend to a hypothetical situation.

Let me note one point with respect to your corner; I am not familiar with that particular estimate, but it is my recollection that the national energy program which the President proposed would allow for higher prices, for very high cost gas in tight or very deep formulations; and I think if you crank that in so that what you are talking about here is essentially the response not taking into account the additional high cost gas which would have a higher price.

I don't know what the curve would look like when you did that. But I think that corner is partly because that didn't take into account those exceptions.

Representative BROWN of Ohio. Well, this is what they did for conventional sources of natural gas. You are right.

Mr. SCHULTZE. As you go——

Representative BROWN of Ohio. The other sources of natural gas were handled somewhat differently. But for the conventional gas supplies—and I think, perhaps, that is what you have reference to in your book—it does bring about those sharp corners and discontinuities which I think are patently illogical.

Frankly, I think that is why the CBO, and the Office of Technology Assessment, GAO, the committee, and those who dealt with this had some trouble with the backup data behind the President's new energy plan.

My guess is that the plan was not thoroughly run by the Council of Economic Advisers before it was put together.

Mr. SCHULTZE. As I say, I think if you put it all together, you will find there is a curve, although a steep curve, as you put in the higher cost sources.

Representative BROWN of Ohio. Let me speak again to the elasticity question. We studied it, Representative Stockman and I, and we assumed lower price elasticities, being more conservative, perhaps, of somewhere between 0.35 and 0.7. And we found we would have 25 trillion cubic feet of additional natural gas between now and 1980, if natural gas is deregulated. We also assumed that the cost of replacing that 25 trillion cubic feet of gas with imported oil at $2.40 equivalency, or LNG at 4.5, or 4.08 for synthetics, or electricity at $11, would mean between now and 1990 we would have a considerable saving if we got natural gas rather than the substitute fuels.

Would you concur with that?

Mr. SCHULTZE. Well, I concur with it only in the sense that I have to take into account in this area the whole energy relationship of intrastate to interstate, the transfer of rents that you get when you are dealing with small incremental amounts of gas coming on for this, and, therefore, in terms of those particular numbers, I cannot really answer the question, Mr. Brown.

Representative BROWN of Ohio. Well, let me go to another question.

In the other book, "Higher Oil Prices and the World Economy," you recommend tax cuts to get the economy moving in the face of higher OPEC prices plus phased decontrol of oil prices to promote conservation, production, and efficient allocation in the free market.

Mr. SCHULTZE. In the case of—excuse me.

Representative BROWN of Ohio. In the President's energy plan, new new oil receives the world price. Old oil is brought up to the world price through added taxes supposedly offset by tax breaks for some consumers—although the tax cuts proposed by the administration are not nearly enough to offset all the energy and other taxes that have been proposed, enacted or raised by inflation, as you pointed out in your testimony.

In the case of natural gas, these same arguments for efficiency and comsumption, production, and allocation, it seems to me, also apply. Supposedly, under the energy plan, extending price controls on gas to the intrastate market, which you just mentioned, will redress part of the allocation problem by moving more gas to the interstate market. However, the plan would still have price ceilings, and a shortage area will still be unable in an emergency to bid a higher price to attract gas from a gas-consuming area in relative surplus.

Now, a free price would normally take on the role of sending gas to where it is most productive and most needed. Without a free price, how does the administration propose to divide up our limited gas supplies after controls are put on intrastate gas?

How much GNP annually will we still lose because of inefficient allocation under the new energy plan, such as we had last winter in Ohio when we lost about 1.5 billion in our State with almost 750,000 people out of work for several weeks?

Mr. SCHULTZE. But in that kind of a situation, where you are dealing with emergencies, Mr. Brown, the use of the price system to allocate in those very short terms can give you incredible prices for very small results.

Over a long term it is one thing but the——

Representative BROWN of Ohio. We paid incredible prices in that $4.08 for synthetic fuel.

Mr. SCHULTZE. But it could go, Lord knows, where when you get into the emergency circumstances. The market is a good allocator, but the market has its limits; for example, go back to the embargo.

In theory, we could have allocated that shortage by simply letting price do it. Lord knows, what that would have done. In the long run, it is one thing to rely on prices. But in the short run, to try to let prices allocate in an emergency situation is something we don't do and virtually no country I know of does when you are dealing with an emergency. That is quite a different kind of situation for the long run.

You get unknowns, your prices can run way up.

Representative BROWN of Ohio. We have a policy on oil which the administration seems dedicated not to follow on natural gas. I think, frankly, that is a tragedy. As I said for openers, I am a Schultze fan in this regard. I have been quoting from this book for my colleagues so that they might be encouraged to follow the same approach.

Mr. SCHULTZE. As you know, the administration is moving in that direction. In the case of oil, in effect, we do get domestic prices up to world oil prices. But it is not the kind of thing——

Representative BROWN of Ohio. For consumers?

Mr. SCHULTZE. Yes.

Representative BROWN of Ohio. But not for producers.

Mr. SCHULTZE. Not for producers except on, in effect, except on new oil where it counts in terms of getting additional oil supplies. What you don't want to do is transfer huge amounts of rents that are unnecessary to get your increased oil supplies.

We are allowing very substantial prices, it will be the highest price in the world, for new new oil so we are allowing that where it counts to get it. And the final point on the pricing system is obviously a—I agree as a general proposition, that is what you ought to move to but for emergency allocation, it doesn't work very well.

Representative BROWN of Ohio. My time is up, Mr. Chairman.

Representative BOLLING. Congressman Moorhead.

Representative MOORHEAD. Thank you, very much.

Thank you, Mr. Schultze, for your statement.

I notice in your prepared statement you point out several times that inflation moves the wage earner up into a higher tax bracket and, hence, his real income is reduced.

I have introduced legislation to help us solve that problem by indexing the personal exemption and the standard deduction. Before I pose the question, Mr. Chairman, I would like to ask unanimous consent to insert in the record an article from today's Washington Post entitled "Indexation: An Idea Whose Time Has Come."

[The article referred to follows:]

[From the Washington Post, Jan. 31, 1978]

INDEXATION: AN IDEA WHOSE TIME HAS COME

(By Robert J. Samuelson[1])

Tax indexation is an idea whose time has come—and this year is going to prove it.

Though indexation sounds complicated, it actually is simple. It means that the government automatically corrects the income tax system to prevent infla-

[1] Samuelson regularly writes about economic affairs for The National Journal, from which this article is reprinted.

tion from kicking taxpayers into higher and higher brackets. Assume, for example, that inflation raises a family's income 10 percent. It goes into a higher tax bracket, and its tax rate increases even though its "real" income hasn't. Without indexation, Congress must pass a major tax "cut" every few years to prevent this invisible tax increase.

That's precisely what has been happening. Assuming a tax package passes in 1978, Congress will have approved major tax reduction bills in three of the past four years. So long as inflation persists at a 5 percent to 6 percent annual rate, the cycle will continue.

The defects of this system are now becoming increasingly clear.

Most important, it's fundamentally dishonest. It confuses the average citizen and, indeed, possibly the average congressman. It puts the nation's highest officials, starting with the president, in the foolish and ultimately self-defeating position of pushing half-truths on the public. They promise tax reductions, but in the main, all they are doing is repealing automatic tax increases.

Average taxes, as a percentage of personal income, are declining largely against what they would have been, not what they were. Even if President Carter's program passes as proposed the average tax level is estimated to be higher in 1979 than in seven out of the past 10 years, as the following table indicates. It shows federal income taxes as a percentage of personal income since 1969:

	Percent		*Percent*
1969	11.6	1975	9.9
1970	10.5	1976	10.2
1971	9.9	1977	10.1
1972	9.9	1978 [1]	10.3
1973	10.3	1979 [1]	10.5
1974	10.7		

[1] Estimated.

Bombarded from Washington with propaganda about the beneficience of tax cuts and confronted with a largely static tax bill, the average taxpayer sooner or later is bound to react in anger and disillusionment.

A second flaw of the current system is that it hampers economic policy and increases the likelihood of an economic downturn or recession. In the days when inflation crept along at an annual rate of 1 percent to 3 percent, the dynamics of the income tax system were thought to represent a helpful "automatic stabilizer." If inflation increased, incomes would rise and, consequently, so would the tax bite. That would reduce consumer spending, the economy would slow, and inflationary pressures would abate. This was a comforting notion.

Unfortunately, it does not sit well with reality. As the past few years have demonstrated vividly, inflation has an independent momentum. Through powerful unions, oligopolistic companies, government fiat and social custom—the idea that everybody should stay "even"—inflation gets perpetuated, checked only feebly by weak constraints.

In this climate, the "automatic stabilizer" simply puts the economy on its backside—or threatens to do so—with a mild impact on inflation. There is then a rush to pass a tax cut to revive the economy.

The outlook for 1978 illustrates the risks. Many economists worry that the economy may slow down in the second half of the year, in part because the rising tax bite will curb consumer spending. But the administration doesn't think it can possibly get its tax cut passed before Oct. 1. So Carter's economists are forced to bite their nails and hope that the timing turns out right.

A final defect of the existing anarchic approach is that it constitutes a cruel and unusual punishment of congressmen. This, of course, contradicts the conventional wisdom that politicians like nothing better than approving tax cuts and then basking in the ensuing public approval. Many congressmen may have once embraced this simple logic, but, by now, a more complicated reality is forcefully asserting itself.

That reality is that Congress stirs up as much grief as gratitude when it acts on a major tax bill. Every interest group that feels entitled to some new tax break, or simply wants to protect an existing benefit, makes a pilgrimage to Capitol Hill. Any congressman is bound to disappoint some of these petitioners. And the more big tax bills there are, the greater the opportunity for offense.

Moreover, on the other side of the political ledger, public gratitude for tax reductions is increasingly tempered by the realization that they largely represent a holding action against inflation. The political arithmetic of this process is not especially favorable. The more the cycle of phantom tax cuts occurs, the worse the arithmetic will become. Ultimately, Congress is bound to search for an exit.

Indexation would minimize its problems. Although adjusting corporate and business taxes for inflation is difficult, the necessary alterations for the personal tax present no insuperable technical problems. Tax rates, deductions, exemptions and credits can automatically be changed to reflect inflation.

Indexation wouldn't—and shouldn't—exempt Congress from the necessity of changing the tax laws. There are fundamental political and social problems that will not conveniently vanish. As social security taxes rise (reflecting the program's higher costs), should Congress let the total federal tax bite increase, or should it cut some existing spending? Should the tax system be used more aggressively to promote income redistribution or, on the other hand, investment?

Regardless of what it does, Congress will have a difficult time permanently evading these issues. But, already overburdened by complicated problems that it only dimly understands, it does not need to create added uncertainties by having to fiddle with tax rates every 18 months.

Representative BOLLING. Without objection, the article has been introduced into the record.

Representative MOORHEAD. Then I would ask Mr. Schultze if the administration has any position with respect to indexing.

Mr. SCHULTZE. I find myself in a position of disagreeing with my good friend, Bill Moorhead.

Mr. Congressman, in essence, once you start down the indexing trail you have massive problems in making it fair and equitable. You can index some things but it is virtually impossible to index others without a complexity that would stagger anybody.

Representative MOORHEAD. I want to assure you I am not talking about overall indexing.

Mr. SCHULTZE. But my point is that once you get into it, you are indexing for some items and not for others and you get into a redistribution of the tax system that you are not aware of when you first do it.

If you are just indexing exemptions, for example, and standard deductions, all the other things in the Code are not you gradually begin to twist the distribution of that tax system around.

The second point is, given the problems we do have with inflation, it seems to me it is useful to have a tax system, it has its disadvantages, also, but it is useful to have a tax system where the Government can make a decision to let average tax rates rise if needed to choke off an overheated economy but then also make a decision to reduce them if it isn't needed.

Let me say it another way. I think everyone in this room realizes how difficult it is politically to raise taxes when that is necessary.

Now you happen to have a system that when you get into inflation gives you additional taxes. It turns out we don't want them now but there might come a time when we do. It is easier to let it automatically happen and simply make a decision not to cut than it is to make a decision to raise.

So, even if one could devise a perfect indexing system, and it would be very difficult, then there would be the political question as to whether or not you really want to get yourself in that position.

That is why in most things we tend to agree, but on this one I am sorry to say I will have to take an exception.

Representative MOORHEAD. You have discussed the administration's anti-inflation program of talking to businesses and unions and I note on page 110 of the annual report that you discuss the fact that other governments have in effect tied tax reductions to agreements with unions, for example, to moderate their wage settlements.

Can you give us any description of how these programs have worked particularly in other countries?

Mr. SCHULTZE. Well, really, the key case is the British. They did it on two different years running and I cannot get them separated in my own mind. But fundamentally, there was a case with the British in which they have had wage rate increases running 20, 25, 30 percent, prices at 25 percent and in some case 20; profits have been squeezed virtually to zero.

They needed not only to reduce wages and prices, they also had to reduce the rate of wage increase more than prices. In effect, they made a bargain with a fairly centralized union structure for a tax cut in return for a substantial hold down in the rate of wage increase.

In their case, they were just on the brink of disaster, I mean they were not running 6-percent price increases, they were running 25.

Second, they had a centralized union structure covering a much higher proportion of the work force than we do, as a consequence of which the combination of looking over the edge and the nature of their institutions made this possible.

We have looked at this and it just does not—again, I don't want to dismiss anything out of hand as I said—it certainly did not appear in the case of the kind of system we have where this might be done.

For example, what the British did not do was to have a law which explicitly tied the tax cut to a particular group of workers who decided whether or not to get this wage increase. They had a general bargain between the Government and the unions—then everybody got the tax cut.

Some proposals have been made in this country to have a tax cut which explicitly goes only to those who agree to reduce their wage increase below a certain amount. That poses all sorts of problems, both economically and in our environment.

In their circumstances and in their institutional environment, it turned out to work, all things considered, quite well. We have different circumstances and a different environment.

Representative MOORHEAD. Mr. Schultze, the table in your prepared statement about the business capital stock is a very dramatic demonstration of probably the weakest part of our recovery.

Does the Council have any opinion as to why the increase in business capital stock has been slow, compared to earlier recoveries?

Mr. SCHULTZE. Yes, sir. As a matter of fact, when I gather my own council members and staff around me we have at least eight opinions, four of which are contradictory. I exaggerate, but, yes, we have discussed this among ourselves and looked at all the research we could get our hands on.

There is no single answer to it. Let me just point one or two things out.

In the first place, what you see in that table on the right-hand side, part of it, right-hand column, comes about in any recession. That is, in the recession you tend to get a much bigger drop in investment than you do in labor force growth. It is just more dramatic this time.

The second point, if you look at what has been happening to investment, is that investment in equipment has been rising relatively well. There is some question as to whether it has been rising as much as you would normally expect or not, but it has been rising relatively well. It is investment in long-lived plants, new, large new construction, that has been very, very weak.

Now that suggests, although it doesn't prove, that one of the reasons is that firms are somewhat more reluctant than they used to be to make very long-term commitments. The equipment normally has a much shorter life, the payoff is much quicker. That has been progressing relatively well.

It is the investment in long-lived equipment that suggests a reluctance to make long-term commitments. That is one of the reasons why we have suggested the corporate tax cut include liberalizing of the investment tax credit, and extension to utility and industrial structures to which it does not now apply.

My own judgement is that some of this is really the remnants, the hangover of the trauma that everybody went through, business firms in particular, in 1973, 1974, 1975, and 1976, with double-digit inflation and the worst recession in 40 years.

That is bound to shake confidence in the future. I believe it is recovering, but it has got a long way to go.

Representative MOORHEAD. Thank you. You talk about the cost-effective approach to accomplishing regulatory objectives. Are you getting cooperation from the independent regulatory agencies as opposed to agencies in the executive branch?

Mr. SCHULTZE. At the present time we really have—in the terms of setting priorities—a bifurcated approach if you want. In the case of the economic regulation of the independent agencies, we have been heavily concentrating on trying to get regulatory reform through legislation, and our major effort last year and through the early part of this year will be on airline deregulation.

In the case of the agencies, this is not a 100-percent right, but the so-called independent agencies are the ones who kind of regulate for economic reasons, trucking, railroads, airlines, whereas, the agencies within the Federal Government are usually the ones who deal with such matters as social purposes, environment, worker health and safety; and, yes, it is normal—we are getting cooperation.

It is, of course, the normal perfectly proper business in Government that people have different objectives, and the whole secret of Government is to try to influence and reconcile them so I cannot say that this comes about and that we are proceeding with no argument. There are a lot, but we think it is our function to come down heavily on the economic consequences, realizing that at the same time the very legitimate concerns for other directions of agencies' policies involved.

So, yes; there is cooperation, but I cannot suggest to you that it is without a lot of argument back and forth, discussions, meetings, and so forth.

Representative MOORHEAD. Mr. Schultze, the President has proposed phasing out the Domestic International Sales Corporation, the tax deferral designed to promote exports and investment at home.

Does administration have any plans to propose other ways to promote exports?

Mr. SCHULTZE. Well, there is an expansion of the—I cannot, unfortunately, recall the numbers here—between 1977 and 1979, the 2-year year period in question, there is a substantial expansion in Export-Import Bank authority, and loans, et cetera.

Secondly, there is a major effort with Japanese in particular as a result of the consultation that went on recently. The Department of Commerce is setting up and giving very high priority to a trade facilitation committee through the United States and Japanese to make it easier for American importers into Japan to crack that market, if you will.

That is a major effort. There are two particular ones in the case of the Export-Import Bank and the American-Japanese trade facilitation agreement.

There are, of course, the other measures where the Japanese Government has announced its undertaking as a result of these consultations that will help in the area of citrus, beef, and a number of others.

Finally, of course, in the long run, what is important is our own competitiveness in years where we think the increase in investment to get higher productivity gains—not right away—but will over the long run prove very important.

Representative MOORHEAD. Thank you, Mr. Chairman. My time has expired.

Representative BOLLING. Senator Roth.

Senator ROTH. Thank you, Mr. Chairman.

Mr. Schultze, I would like to express the same sentiments that Representative Brown did. I am an admirer of yours, and I agree with much of what you say in your statement today as far as goals and objectives are concerned.

The thing that bothers me is that I don't see that the medicine or proposals really provide the cure for the economy.

You make the statement that as we look further ahead, it is clear that unless steps are taken now to maintain economic growth, expansion will slow to an unacceptable pace and our efforts to reduce unemployment will be frustrated.

"The most important development threatening sustained recovery is the increasing burden of taxes borne by the average taxpayer."

I can pretty much agree with that statement, Mr. Schultze, but I don't see that we are doing much about it.

As far as the so-called tax cut which the administration has said should be about $25 billion, there is a question in my mind how much of an impact that will have on a $2 trillion economy. But, basically, this tax cut does not even return to the economy what we are taking out of it in the way of higher taxes if you consider, one, the social security taxes; and two, the effect of inflation. Would you agree with that?

Mr. SCHULTZE. No, sir if you might—at least I don't agree with what I think is the purport of it.

Let me make the point and direct your attention to one of the tables in my prepared statement. It is true that we did not size the tax cut to achieve any particular ratio of taxes to income but rather one that would give us the 4½ to 5 percent growth.

Now, it turns out, if you look at the table, the best overall way to measure the burden is the ratio of taxes to income. You can look at total taxes which were 19.8 percent of your gross national product in 1977, calendar year; and with the President's proposal would be virtually the same.

It goes to 20. But virtually the same in 1979. That is, we believe we have a healthy economy, we don't want to let that tax burden grow as it would without the President's cut from 19.8 percent to 21.2.

But, on the other hand, with the measures that the President has proposed, and that does include, of course, the fact that in 1978 we will still be getting some of the advantage of the 1977 tax cut which was passed; that ratio virtually stays the same. It does creep up by two-tenths percentage point.

In the normal recovery that ratio arises fairly significantly. Here it is flat or virtually flat, not quite but virtually flat. That, is seems to us, is about the best measure of what we are doing. It is not—excuse me.

Senator ROTH. Well, I had the Joint Committee on Taxation make a study of the overall effects of the President's tax cut and according to their figures, if you consider the effect of social security, inflation, and House proposed energy taxes, which, as I understand, the White House is still espousing; that means that during the next five years we are going to take out of this economy about $70 billion after the President's tax cut.

If you forget for the moment the energy taxes, even on that basis you are taking out of the economy $20 billion during the next 5 years. So it seems to me that there is a serious question, I think economists will agree as to whether this particular tax cut will have any major stimulative effect.

But in some ways, what bothers me just as much, if not more, is the second thing I quoted from your statement, and that is the effect on the average taxpayer.

Now, I am very sympathetic to what you do on the low end of the economic scale, but your tax cuts wash out pretty rapidly as you go up.

I would ask you this question, have you or the administration made a study as to the impact of the social security taxes—the impact of inflation on taxes as people are pushed into higher tax brackets plus the energy taxes, not only at the $10,000 or $15,000 income level, which I think is very important, but on those making 20, 25, and even $30,000?

Mr. SCHULTZE. Well, sir, first with respect to the overall burden we talked about that; with respect to the individuals we have not done that income class by income class.

What you will find under this program, Mr. Roth——

Senator ROTH. May I just interrupt there because in your prepared statement you say the impact on the average taxpayer is causing the drag on the economy, if I understand your statement.

Mr. SCHULTZE. That is correct, sir.

Senator ROTH. That is your comment. So, isn't it very important that we know exactly what is going to happen all the way up the scale, all the way up? The other day, a representative before my subcommittee, a witness from Taxation With Representation, said, and I don't know whether this quote is accurate or not, "You have a third of the population earning $10,000 and less, a third in the $10,000 to $20,000 group and a third at $20,000 and higher."

Are we just forgetting, ignoring those that make $20,000 or higher or do we think these people are rich?

Mr. SCHULTZE. No, sir, we do not. There are tax reductions all up and down the scale. It is true, however, that the reductions are somewhat tilted.

Senator ROTH. Somewhat tilted?

Mr. SCHULTZE. In the favor of the middle to the lower.

Senator ROTH. What do you call "middle?"

Mr. SCHULTZE. I think——

Senator ROTH. Do you think $20,000 is rich?

Mr. SCHULTZE. No, not at all. I think the median is now about what, $15,000. The median is about $15,000 so $20,000 is obviously not rich.

Senator ROTH. There are reports out which say that a family of four in an urban area must have at least an income of $25,000 to have an average or reasonable standard of living.

What will be the impact on a person making $20,000 or $25,000, if you take social security increases, if you take the impact of inflation, plus the proposals on energy.

It seems to me that it is essential, and I would respectfully—yes, Mr. Schultze.

Mr. SCHULTZE. Well, go ahead and finish. I didn't want to interrupt.

Senator ROTH. I thought you wanted to comment. Go ahead.

Mr. SCHULTZE. Again, as I indicated, the average tax burden will be roughly unchanged, No. 1.

No. 2, when you look at the actual tax reductions we are proposing relative to the social security tax increases that would occur, remembering that they are paying for future benefits, you still get a reduction well up the line.

No. 3, for those who are getting the largest social security tax increase, it is those where the wage base goes up. But that wage base increase also entitles people to higher social security benefits in the future. So there is an offset there. Now, how those offsets work out income class by income class when one takes into account the impact of the higher retirement benefits later in the future, and the present value of those versus inflation, I admit I do not know.

I do not know on the average we are offsetting it. I do know the average tax burden is not going to rise. I do know with respect to offsetting the social security tax increases, even though some bring higher benefits, we are offsetting them well up the line.

Senator ROTH. I think that in all candor, the administration proposal is soaking the middle class. We are doing nothing to help people making $20,000–$25,000.

If you take the effect of all these factors, a high percentage of taxpayers—and there are different figures, I have seen some that say 43 percent, some much higher—are going to be paying much higher taxes in the years ahead.

What bothers me is that these are the people who are the ones responsible for savings and the capital formation which we need to get more investment and jobs in the private sector.

I am told, Mr. Chairman, that my 10 minutes have gone by. But I would request that either this committee or the administration make an indepth study as to what is the impact in every income level of the social security taxes, of the effect of inflation during the next 5 years, of the effect of energy taxes, because I think we ought to know what we are doing to people at these different levels of income.

I happen to agree that we ought to get the sort of size relief being proposed at the low end. The problem I have is that we are not doing anything for some of the most hard working, energetic Americans—the middle class—and that bothers me.

Thank you, Mr. Chairman.

Representative BOLLING. Senator McGovern.

Senator MCGOVERN. Mr. Chairman, let me just say, first of all, how pleased I am to become a member of this committee. This is my first hearing as a member of the committee. I regard it as an honor to be a part of this important part of the congressional business.

It goes without saying that I regret the sad circumstances that made this appointment possible. Hubert Humphrey was a special friend of mine for some 25 years. I had the privilege of living next door to him in Chevy Chase for 10 of those years and we rode together in a cab almost daily, so I think I can appreciate the fact that nobody is going to replace the powerful voice that he exercised during his years in the Congress and on this committee.

Mr. Schultze, what I would like to do is just open with an obser-vataion about the economy and kind of an alternative to what you are proposing, what the administration is proposing; and, then, give you a chance to react to it.

I don't think the $25 billion tax cut is going to do a good job in meeting the problem of unemployment, meeting the urgent problems in the cities, addressing the problems of these farmers who have flocked into the Capital the last couple of months, to say nothing of the problems of the poor who cannot get here.

As your testimony points out, the net stimulus is only about $12 billion. You lose roughly $7 billion in the Social Security tax increase, and another $6 billion is wiped out by the inflationary impact on the tax structure, so we end up not with a $25 billion cut but with a $12 billion cut, and it doesn't seem to me that it is targeted on the central problems of the country that I have just mentioned.

I think that it would be much more effective if we invested $25 billion in the public funds targeted on these major problem areas.

One possibility, and it is a rough one, could be to allocate $12 billion of that for urban programs above and beyond what the administration is now proposing.

I think the Conference of Mayors meeting here in Washington last week recommended a $11.3 billion increase in the cities beyond what the administration proposed. Half of that, perhaps, would be in the form of public service jobs.

It is my understanding that you can create those jobs, according to the Congressional Budget Office, for about $8,000 each in tax expenditure, whereas to create the same job throughout the indirect stimulus of the tax code would take about $25,000.

So you get about three times as many jobs for the same public investment with the moneys directly invested in job creation as you do working it through the tax structure.

Now in addition to that $12 billion for the cities, one might consider the possibility of a $7 billion increase in the rural sector, a substantial part of that in underwriting parity target returns to the farmers; and the third area might be an investment of some $6 billion upgrading the rail system of the country for a total of $25 billion.

It just seems to me that taxpayers, unemployed workers, city residents, farmers, everybody would be better off with that kind of a use of the $25 billion than they would in hoping that somehow a reduction of that level into the tax system will work its way through the economy in such a way as to provide the stimulus that you want.

I wonder if you would react to that. There may be a better formula for allocating the funds than I've outlined here, but it is really the argument of the public investment versus this tax cut. I think Senator Roth is trying to develop the line that it will not help a great many taxpayers anyway.

Certainly, it won't help the farmer who has no income because the farm returns are too low. It is not going to help the poor that don't pay taxes.

It is questionable to me how it addresses these other thoughts. I wonder if you would comment on that general line of reasoning.

Mr. SCHULTZE. Well, a number of things, Senator.

First, with respect to—let me go at it one by one if I might—without these tax reductions, the average tax burden would rise significantly on account of what is happening through inflation and Social Security.

Now, it is true, it is possible to take that $25 billion and instead of reducing taxes, let the tax rate rise and use those funds for other purposes.

In the long run, however, we don't think that that would give us the kind of a sustainable economy that would end up doing what both of us want. Let's look at public service employment:

With respect to the major public service employment programs, the administration has increased them. It came in at 300,000 and raised the number to about 700,000 jobs. That is just the regular programs. If you look at public service employment and the work experience including the youth programs, we are up to over 1 million already.

In the long run those are not the kinds of jobs which are going to move people into the productive career improving part of the economy. What we need to do is find ways on one hand to direct employment in addition to the public service, to direct employment into the private sector because that is where the major jobs are, that is where the long-run good is.

Not all of them——

Senator McGOVERN. Even if I granted you that point, why couldn't you arrive at that same goal, that same objective more effectively if you made a direct investment in the private sector either in the form of job subsidies or guarantees, rather than hoping that a tax cut would come out in that way?

Mr. SCHULTZE. It isn't just a question of "hoping." There is every evidence from past history that it does work. You may recall the period in which we got by far the greatest reductions in poverty, the greatest reductions in unemployment among minorities, was precisely during the sixties when the economy as a whole was growing at about a 5-percent rate, helped very substantially by a tax reduction.

That sets the underpinning for whatever you want to do elsewhere. Without that underpinning, the other programs won't work.

Now, we want to support that. We are coming up to the Congress sometime shortly with a program to provide incentives for private employers to hire from the disadvantaged. It is necessarily modest at first until we get better experience with it but we are going to do that.

What I am saying is that in the long run you have got to get the investment, you have got to get the private economy moving up if you want to get people—even those who are going through public service employment—ultimately put into these jobs.

Public service employment is not a lifetime career for people and we want to have a place where they can move out to in the private job sector. You want not simply to use those funds to create more public service employment.

Senator McGOVERN. Mr. Schultze, you state in your prepared statement that the President's proposed welfare reform envisions creation of 1.2 to 1.4 million eligible persons who would move out of the welfare stucture into jobs.

If the Congress does not act this year on welfare reform, what alternative do you have in mind to achieve those additional jobs that you are talking about in the range of 1.2 to 1.4 million?

Mr. SCHULTZE. Senator, those jobs are part of that welfare reform package. We believe the Congress will enact them. Essentially they are due to come in in 1981 as the other public service jobs phase down. We hope the Congress will enact welfare reform this year but if it enacts it next year, the program is still there.

At this stage I don't have an alternative recommendation except to urge the Congress to act on the President's recommendations. We have not in fact looked at alternatives because it is very clear in the game and we see no reason to believe that the Congress won't ultimately enact these.

Senator McGOVERN. If I have time I would like to ask one more question.

In your prepared statement, you assert that the aggregate budgets of the State and local governments have been in sizable surplus. Last year that surplus was nearly $30 billion.

Isn't it a fact though that that surplus is confined to, with very few States, primarily Caliornia and Texas, and we still have a very serious fiscal crisis, financial crisis in the Nation's cities of the Northeast and elsewhere?

Mr. SCHULTZE. As I indicated in my testimony, that is correct. The fact that it isn't confined to just a few States but nevertheless there are areas that have significant problems. We realize that.

On the other hand, from the point of view of making Federal budgetary policy you have to realize that the budget in total of all governments isn't in deficit $60 billion, because you have a Federal offset by State and local—therefore that statement is not meant to read as though there are not some particularly relatively slow growing or declining older cities where there are not serious finanical problems.

Senator McGOVERN. Thank you, Mr. Chairman.

Representative BOLLING. Senator Javits.

Senator JAVITS. Mr. Chairman, it is my fault to have missed my turn, and I would like to ask if my colleagues would like to precede me or if I should continue.

Representative ROUSSELOT. Fine. Go ahead.

Representative BROWN of Michigan. Sure.

Senator JAVITS. Thank you, gentlemen.

Thank you, Mr. Chairman.

Mr. Schultze. I think we have to face the fact that we have deficits—budgetary deficits, payments deficits, trade deficit—and consider whether there ought to be any tax cut at all.

This, I think, is a very serious question for our country, especially as we face more deficits in 1979, 1980, and 1981. It just doesn't seem to me that we are going anywhere. We gave ourselves a shot in the arm in 1977, which didn't seem to deal effectively with our employment problem.

Now we will give ourselves another shot in the arm in 1978, if it passes as the President wishes, for a net of some $27 billion.

Now you say, and I read your prepared statement very carefully, that unless we pass the tax cut—I don't know whether you mean precisely that or just put some of that kind of money in the spending stream—it is going to cost us a growth of at least 1 percentage point in the growth rate.

First, you say we won't have a growth rate of much more than 3¾ percent. Then you say it will cost us 1 million jobs, but from what we see of the expectation for the aggregate figures on unemployment, they do not seem to me as coming down significantly.

I assume that the 1 million jobs you mentioned will be added employment—an ongoing phenomenon—to take up the fact that women and many others are entering into the economic stream.

Therefore, I raise this basic question for you: Given the options of a tax cut or no tax cut at all, in view of the fear over the economic situation in which we find ourselves with the U.S. dollar very soft, with apparently no way—notwithstanding the GAO recommendations—of cracking the OPEC riddle which is taking—skimming, as they say in Las Vegas—off the top at least $30 billion to $35 billion—probably $40 billion because normally we had about a $5 billion problem.

You know how sympathetic I am to lowering taxes for the poor and everyone; I don't have to convince you of my bona fides on that. Don't we have to take another look at the fundamental proposition?

Let me give you another factor which deeply worries me. At the beginning of our discussion, we mentioned productivity. You and I have a common concern; you know I have no accusations; we are partners. Your analysis in the economic report on the reduction in productivity shows that the real deficiency is accountable to lack of business spending; the American economic machine is getting more obsolescent, and we know that to be a fact. It is falling behind Germany, falling behind Japan, and probably falling behind a great many other countries, especially in specialized lines.

Therefore, in view of the whole picture, might we not be braver if we said:

> Sorry, no tax cut even with the social security, even with inflation? We simply have to turn the other way. We have to take this terrible medicine or the whole world is going to go to hell, and we are going to lead it.

Mr. SCHULTZE. First, Senator, it seems to me about the worst thing we could do for the rest of the world, a country of our size and our importance, is to let our economic growth and our investment slide.

Yes; the rest of the world does have problems with payment imbalances, and if we should reduce our rate of growth below what is already a moderate ambition, growing 4½ to 5 percent because of that payment deficit and because of the large oil imports and try to save oil by keeping growth low, the impact back on the rest of the world on protectionism, on social systems in which unemployment outside the United States tends to be growing and the strongest country in the world cuts back and says, "To heck with it, we cannot do it;" it seems to me that is the worst thing we can do for the rest of the world both economically and in the long run politically.

The pressure on the Italians, the French, and other countries where there are particular political difficulties would be very, very severe.

So, from the best of my knowledge, with maybe a few exceptions and even that I doubt, we are not being pressed by our foreign friends to reduce our rate of growth, whatever they are pressing us to do that they are not pressing us to do.

There may be a few exceptions but they are really few.

The second proposition, investment, productivity.

There are two things involved—there are a lot of things involved but two big ones I would like to point out that both of us are aware of.

One, we are proposing to reduce business taxes. Precisely in order to speed up investment. But a reduction in business taxes with the low rate of growth in the economy and in markets is surely not going to produce the kind of investment we need.

One of the reasons precisely why we are in trouble with respect to productivity is the low investment and part of that in turn is the fact that during the recession investment just plummeted.

Therefore, in terms of both the world's long run and our own long run interestingly with respect to productivity, not a rapid burst but a sustainable and moderate growth of 4½—5 percent in general, is, I believe, in the interests of our country and the rest of the world for both of those reasons as well as others.

Senator JAVITS. I am glad to hear your rationale although I may not agree. I have grave doubts about the tax cut, et al. I shall do my utmost to resolve them and to make a strong case for whichever way I resolve them. I am deeply concerned about the tax cut, especially in view of history, because the best that can be said is that it worked in the 1960's with Kennedy and in a different frame of reference.

Since that time, a tax cut seems to have had only temporary effects.

Mr. SCHULTZE. Could I add one point?

Senator JAVITS. Please.

Mr. SCHULTZE. It is natural for all of us, precisely because in our different functions we are dealing with problems, to forget that with all our problems we have made some progress. The rate of unemployment touched 9 percent in the depths of the recession; a year ago, December 1976, it was 7.8 percent. It is down to 6.4, an important—by no means sole, but an important part of the reason for that is that the Congress did enact in 1975, and again in 1977, some tax reductions as well as some other economic programs.

They have not been 100-percent successful. Economic growth last year in the United States was 5.75 percent yearend to yearend, so that it has not been an unsuccessful approach even though we are still left with problems. There is no question about it.

Senator JAVITS. Mr. Schultze, I can understand your feeling, but my feeling is that even the cyclical recovery has had to be sustained by material tax cuts.

Mr. SCHULTZE. That is right, yes, sir.

Senator JAVITS. These tax cuts disable us from leveling out the cyclical recovery because they disable us from making the investments necessary to give us a more stable economy. Right now, with all respect, you are going to have this tax cut. It is probably inevitable. Whether it is shaped the way Senator Roth wants it, or whether it is shaped the way you or I want it, or the way Danforth and I may want it, it is probably going to happen. We are facing another world economic turndown in 1979 or 1980—freely predicted—as a result of OPEC oil and the debts of the LDC's, which are practically making them stand still in terms of development because of the debt service including amortization. I am concerned that we are not supplying the funds for investment.

I would like to ask you my next question which is a positive and a negative one:

We all agree that the OPEC drain is fantastic, and that it is one of the worst things that has happened to the economy of the world.

Now that the GAO has produced a study and has advised that we can do a lot about this problem, economically and politically, my question—and that is on the drain side—is, What is the administration's plan?

On the positive side, the LDC's, which now owe about $170 billion, are struggling with debt service (and I am talking about the nonoil LDC's), and we know that the market base for the OECD countries is too small. This is best shown by the fact that everybody drops dead because Japan has a $15 billion surplus, which—in the $2 trillion economy like ours—ought to be meaningless, but everything stops.

We have to acquire broader markets. On the positive side, in view of the fact that the north-south dialog is at a dead standstill, what is the administration's program to acquire broader markets for all of us—not only for the United States but also for all these economies? A plan is what these countries are looking for.

Do I make those clear, Mr. Schultze?

Mr. SCHULTZE. Yes, sir.

Senator JAVITS. Thank you.

Mr. SCHULTZE. I hope my answers are as clear. They probably won't be, but——

Senator JAVITS. Finally, I wish to reiterate that there is no sense of opposition. We are in this in exactly the same boat.

Mr. SCHULTZE. I understand. Let me start backward.

In the first place, it is impossible to have growing markets without growing economies. That is No. 1.

All nations in the world cannot grow by relying on exports. We have in terms of our own economic policy, and in recent months in terms of our dialog with the Japanese particularly, stressed that very much.

We believe that in terms of making it possible for nations to make adjustments in their balance of payments, and therefore to be able to grow somewhat more rapidly, that rapid implementation of the Witteveen facility is very important. Although it is a little farther down the road, significant increases in the seventh quota increase for the IMF are important, these financing devices.

All of these, we believe, are very important in maintaining world growth, maintaining as much as possible in a very difficult situation with smooth adjustment of balance-of-payments situations so that other nations are not constrained so much by that.

With respect to the LDC, I must confess here is an area where I don't feel myself particularly expert, but it is my impression that actually they have done a better job, with some exceptions, and there are some critical exceptions I realize—but in general have done a better job, all things considered, than many of the OECD nations in making adjustments to this world. Their deficits have been reduced. They were very hard-hit by our recession, but their deficits have been reduced. They do have some debt srevice problems, but they are also growing rather rapidly.

If you look at the Asian nations, while I don't have the numbers in my head, they are generally doing quite well and I am not singing of a Pollyanna because there are very great difficulties, but in one sense they have done better than the industrial countries in taking the steps and making the adjustments needed to continue their economic growth.

A combination, therefore, of our own relationships in urging with our partners with respect to growth, particularly with respect to the Japanese, in recent months, providing reasonable facilities to finance balance of payments adjustments and keeping our own growth going at a reasonable pace, it seems to me, are the biggest elements we can do in this.

With respect to the OPEC drain problem, I am not familiar except in a cursory way with the GAO study. I am familiar in a cursory way with it. As you know, we put a lot of effort in and we believe that it has paid off so far, to insure there was no price increase this year in the meetings of OPEC. That will help.

Finally, we believe, particularly in the long run, although admittedly not in the immediate run, that passage of an effective energy program will make a big difference. In fact, it will make a critical difference.

Those are the key elements of what we are dealing with.

Senator JAVITS. Mr. Schultze, I have finished with the questioning. I would like to urge the President and the administration to study carefully the GAO report. We have to show some political muscle, or they will ruin us all—OPEC and ourselves. For the 10 years ahead we cannot stand to have this kind of a deficit, which is about $500 billion skimmed right off the top—completely uneconomic. The GAO made some remarkably fine suggestions as to what we can do.

Thank you, Mr. Schultze. I want to thank my colleagues for their indulgence. Thank you, Mr. Chairman.

Representative BOLLING. Congressman Rousselot.

Representative ROUSSELOT. Thank you, Mr. Chairman.

Mr. Schultze, we have enjoyed your testimony today. I appreciate your stressing several times that the administration position is that the long-term permanent jobs basically have to come in the private sector. You have a recognition of that fact and your effort is to try to stimulate that portion of the economy that creates the jobs. A couple of times there have been references today to the tax cuts that occurred in 1963, actually called for by Kennedy in 1963 and put in place in 1964, and that the result was very substantial economic stimulus.

Those were marginal tax cuts across the board both for personal and corporate taxes?

Mr. SCHULTZE. Yes.

Representative ROUSSELOT. Now my question is, why haven't you used that same formula again? You have jiggered a little bit with reductions on personal income taxes. Why didn't you use that same formula again since you have referred to it as successful, and many of us feel it was very successful? Why didn't you use that same formula with the across-the-board cut again?

Mr. SCHULTZE. Because we thought we would end up with a much fairer tax system, particularly by going the route of shifting the exemption to the $240 credit.

Representative ROUSSELOT. But as Senator Roth has pointed out, because you have jiggered it, you make it biased against the middle-income-class-earning people who are the people you want to stimulate to participate in saving and investing, and our middle class has really moved—when you take the fact that the wife now works, too—into the income area of $16,000 to $25,000. Don't we really want to stimulate them, too, as President Kennedy did——

Mr. SCHULTZE. That is correct.

Representative ROUSSELOT [continuing]. Even though at that time it was a low-income bracket?

Mr. SCHULTZE. Pardon.

Representative ROUSSELOT. Even though at that time it was a lower income bracket.

Mr. SCHULTZE. There are rate cuts. The rate cuts are, in fact, heaviest in that general area. It does more than offset and up a good ways the social security tax increase. You have——

Representative ROUSSELOT. That is where we are in disagreement. I don't think you catch those people, say, $20,000 to $30,000, they are not going to have the benefit of a tax cut and the encouragement to save and invest, et cetera, to the same degree as the Kennedy tax cut.

Mr. SCHULTZE. To the same degree that is true, but the major reason for that—or a major reason for that—is the fact that the increase in social security taxes came not in sole part, but in significant part from an increase in the wage base.

Representative ROUSSELOT. I understand that.

Mr. SCHULTZE. In turn, the point I would try to put across is that is a bit like paying for a fringe benefit, that there is a significant increase in retirement benefits which come about because of that increase in the wage base, only half of which the person pays, the other half is the employer's payment.

Representative ROUSSELOT. But the consumer pays for the rest of it.

Mr. SCHULTZE. But that is spread evenly. You are quite right, it does, but that is spread evenly, not to that particular group.

The next point: You have to take into account, although I don't have a chart on incidences, that the reduction in corporate taxes insofar as it affects profits and dividends will, in turn, you know, it percolates down and the lower down you go, the smaller the effect, but it does percolate down to those groups. That is the first corporate rate cut since 1964 and that should have a major impact on those people even though you don't see it in the burden tables because they show only the individual tax.

Representative ROUSSELOT. I don't think some of us would disagree with that. The point that the corporate tax will have——

Mr. SCHULTZE. It doesn't happen overnight.

Representative ROUSSELOT. No; it sure doesn't.

Mr. SCHULTZE. You know, economists are not fully in agreement with each other on the real burden of the tax, the corporate tax, who pays it, so you don't have a burden table that shows it.

Representative ROUSSELOT. Or when you feel the impact in investment, equipment, and jobs and all the rest.

The President has said over and over, and I think you have said, that his proposed tax cut of $25 billion will produce approximately 1 million jobs. What are the calculations you used to arrive at that?

Mr. SCHULTZE. The number, the more precise numbers, precise in the sense of giving it to you to decimal points, is that our estimates are that the GNP by the fourth quarter of 1979 will be 1.7 percent higher than it would have been without the tax cut.

That, in turn, in the fourth quarter of 1979 will produce approximately 900,000 jobs and by the first quarter of 1980 you are up to virtually 1 million jobs.

Representative ROUSSELOT. The emphasis is on 1 million.

Mr. SCHULTZE. Nearly 1 million, and by a quarter later it is 1 million, by the first quarter of 1980.

Representative ROUSSELOT. As the quarter goes on, the impact of the tax cut on increasing employment keeps accelerating?

Mr. SCHULTZE. Not forever. It levels off, but you get to the middle of 1980 before it is leveled off.

Representative ROUSSELOT. Middle of 1980?

Mr. SCHULTZE. That is roughly correct, yes, sir, about the middle of 1980 before that levels off. That is my recollection.

Representative ROUSSELOT. Now, is most of that job production in the private sector?

Mr. SCHULTZE. Yes, sir. In fact—well, I don't want to——

Representative ROUSSELOT. All of it, isn't it?

Mr. SCHULTZE. Well, as far as I know all of that particular calculation, all of it is. We have some increases in——

Representative ROUSSELOT. I realize a lot of this is done by economic projections on econometric models. So if you maybe had a tax cut like my chairman suggested—$30 to $40 billion—wouldn't that accelerate the job picture even more, and also housing starts and personal income, savings and all of the things that you commented we need? Why not make it a $30 billion tax cut or $40 billion?

Mr. SCHULTZE. I think you have to look at the question in terms of, you know, if $25 billion is good, why isn't $50 billion twice as good? Why isn't $75 billion three times as good? What we want is substantial rate of growth.

Representative ROUSSELOT. Jobs, growth, and economic stimulus.

Mr. SCHULTZE. But over the long term, what you don't want to do is overdo it so you get an unsustained rate, an inventory buildup which gives you a turndown again, if you grow too fast particularly under current circumstances, you have that problem to worry about.

Second, the deficit in fiscal 1978 is going to be $61 billion.

Representative ROUSSELOT. But as we both know, in the Kennedy tax cut the projected deficit did not occur. The revenues to the Federal Government accelerated far better than predictions from the bureaucracy indicated.

Mr. SCHULTZE. I don't remember that.

Representative ROUSSELOT. I am sure you are familiar with it; they predicted an add-on deficit of something like $30 billion and actually the revenues accelerated by $54 billion over a 2-year period.

Mr. SCHULTZE. If you look at it from point to point, of course the revenues will accelerate because even without the tax cut, you would get some growth.

Representative ROUSSELOT. You are broadening the base, expanding employment and investment and all the rest.

Mr. SCHULTZE. Nevertheless you will not cut the deficit in 1979 by cutting taxes more. Now you won't lose the full amount of the additional tax reduction, but you will raise that deficit.

Representative ROUSSELOT. The reason I ask these questions is because your calculations on jobs creation and feedback effects of tax cuts are not really included in the budget report; you do not say how you arrived at them. So I hope you will look at our chairman's suggestions for a $30 to $40 billion tax cut and what your projections would be as to employment, housing, all of the things that we claim we are stimulating by Government action.

Mr. SCHULTZE. It is impossible, Mr. Rousselot, to say—the 24.5 is a magic number, but you know we did not pull it off the wall. It was designed to keep us going at a 4.5- or 5-percent rate of growth. A larger tax cut could have gotten more immediately—you would have risked on housing if you pushed the deficit too high. You would have risked it in terms of disintermediation and impact on funds. You would risk an excessive rate of the other accumulations and a turndown if you wanted it immediately. If you wanted to keep this going, sustainable and noninflationary, we felt that to be the amount.

There is no magic to that number, as I said.

Representative ROUSSELOT. I hope you look at the chairman's suggestion and I am not trying to put him on the spot, because I am sure he has his own reasons and would prefer that he be able to explain it himself rather than have me use him as a crutch. But when you take the econometric—you do use econometric model work for your projections, don't you?

Mr. SCHULTZE. We use them, but not mechanically, yes, sir. We use a lot of them.

Representative ROUSSELOT. You subscribe to them?

Mr. SCHULTZE. Yes, sir.

Representative ROUSSELOT. How many do you use?

Mr. SCHULTZE. The three major ones are DRI, Wharton, and we do use the BEA, Bureau of Economic Affairs.

Representative ROUSSELOT. Those are the three?

Mr. SCHULTZE. The three major ones.

Representative ROUSSELOT. So your projections utilize their econometric models as part of your background, is that correct?

Mr. SCHULTZE. That is correct. Then we, in turn, take those and—we don't just rely on them mechanically, but we apply our judgment, look at comparisons among them, a lot of things.

Representative ROUSSELOT. Have you ever tried projecting the tax cuts across the board instead of just targeting them primarily for those below $20,000 in income?

Mr. SCHULTZE. In terms of the overall economic performance——

Representative ROUSSELOT. In respect to housing, investment, savings, all the rest?

Mr. SCHULTZE. It should make relatively little difference within that framework, relatively little difference. The marginal propensity to spend are not all that different.

Representative ROUSSELOT. My time is expiring, but since the Wall Street Journal made quite a point on January 24, of criticizing the administrations accounting procedures in the budget, I would like your response. It seems that by labeling some things "refunds" you avoid calling them "outlays." So I would appreciate it if you could in writing comment on the Wall Street Journal editorial of January 24, because I don't want to take the time from my chairman.

They say President Carter's official 1979 budget has had at least one interesting innovation. He found a new way to make outlays disappear. It is done by converting an outlay into a refund.

In the Careter budget the money the Government proposes to collect from crude oil producers through a wellhead tax and distribute to heating oil consumers is described as a refund instead of an outlay——

Mr. SCHULTZE. But it was a refund.

Representative ROUSSELOT [continuing]. When it really is an expense.

Mr. SCHULTZE. Well, you know, that just never struck me as budget magic any more than what we are doing is offsetting the social security tax increases with a tax cut and calling that expenditures. These refunds would be principally—not all—through the tax system.

Representative ROUSSELOT. Well then, they go on to say——

Mr. SCHULTZE. They reduce taxes.

Representative ROUSSELOT. To carry that logic to an extreme, just think what you could do in the social security system if you called the payments refunds.

Mr. SCHULTZE. I see.

Representative ROUSSELOT. And if we are going to have a new category called refunds instead of outlays on the Budget Committee, we are going to have a problem.

Mr. SCHULTZE. The only thing I can point out to you is they are literally tax cuts.

Representative BOLLING. Congressman Brown.

Representative BROWN of Michigan. Thank you, Mr. Chairman.

What bothers me is that it appears that the tax cut proposal—and I have not examined it carefully, I will be the first to admit—does two things: It appears to offset somewhat the disadvantage caused by social security taxes, possibly energy taxes, et cetera; and, if anything, it does something on the demand side but does nothing on the supply side except to the extent that there may be a trickle down from the 4-percent reduction in the corporate income tax.

Why this bothers me is because, first of all, the middle-income person is one who, in my estimation, makes $20,000 or $25,000—in that area—and I would wager that a substantial portion of our productivity increase is in this group to the exent that it is labor attributed. By and large, our productivity today, I think, is a result of capital as much as it is a result of labor.

To the extent that it is attributable to anybody in the labor force, it is attributable to those skilled in the $20,000 to $25,000 bracket. Now, what do we do with them taxwise?

First of all, we increase social security taxes. Everybody gets the raise, but will many of these people be paying on a business in excess of what they paid on before?

Mr. SCHULTZE. Yes.

Representative BROWN of Michigan. So they get whacked there. When they get to another bracket as you inflate earnings, your income tax program presently means that they are moving progressively up to areas where the magical rates apply and you are zapping them. Therefore, because they are the ones that, if there is an improvment in productivity which keeps out inflation, get zapped and probably their productivity as well, there will be less incentive for productivity.

Therefore, it seems to me that the tax cut primarily goes to those who make less than $20,000 or $25,000, the ones from the productivity standpoint contribute the least, and on whom the income tax impacts the least. When we look to see that the base is going to be almost double in 5 years for the social security tax and that a person with no real earnings increase is going to be jumping up into different brackets from the social security standpoint because the base will increase, and he will be jumping to the upper brackets from the income tax standpoint, it seems to me that we are just not really directing the attention in the tax system where it should be directed.

Mr. SCHULTZE. Well, again, offsetting the social security taxes, that goes all the way up through the $100,000 group. Obviously within that there will be differences, but if you do it income class by income class, it more than offsets, although it is very little in the $50,000 to $100,000 class.

Second, as I indicated earlier to Mr. Rousselot, you have to remember that the increase in the wage base is the equivalent of getting a higher pension, because that raises individual entitlements to the retirement.

Representative BROWN of Michigan. Isn't it being advocated that we don't have benefits track contributions?

Mr. SCHULTZE. They don't track completely at all. All I am saying is that—it does increase the benefits, yes, it does track. It just doesn't track proportionally 1 to 1.

Representative BROWN of Michigan. Therefore, once again you are impacting more on those because they don't track. Down at the bottom level, they track pretty much.

Mr. SCHULTZE. Oh, but the social security system does that. All I am saying is that when you look at the distributions of who gets what, you are right, that the tax is particularly loaded, in terms of the percentage reductions at lower levels. On the other hand, if you then take into account that a large part of the social security tax increase was the base increase which is going to entitle individuals to a higher pension, then you have to take that into the calculation in terms of what the net impact on people is.

Now, translating a future pension into a present equivalent tax reduction I don't have, but it is significant and has to be taken into account.

Representative BROWN of Michigan. Thank you very much, Mr. Schultze.

Representative ROUSSELOT. Briefly, if I may correct my figures, Mr. Chairman, the table on page 74, in the 1977 Joint Economic Committee Report——

Representative BOLLING. Go ahead.

Representative ROUSSELOT [continuing]. In relating to the Kennedy tax cut, the revenue losses estimated for a 4-year period, 1964 to 1968, by the Treasury was $89 billion. That is how much we were going to lose. We actually gained $54 billion. That was on the basis of what the estimates were of the Treasury as impacting, what they reached against the Kennedy tax.

So my point is that over the 4-year period we more than recouped for the potential loss of revenue because of the tax cuts, $54 billion in gain.

Mr. SCHULTZE. Just one quick point. Some of that $54 billion would have been there anyway.

Representative ROUSSELOT. OK. fine.

Mr. SCHULTZE. Normal growth would have occurred. You just got faster growth.

Representative ROUSSELOT. My point is that I still believe the chairman's estimates of a $30 to $40 billion cut would not create that much add-on deficit. As a matter of fact, all the signs, I think, point the exact other way on the basis of historical perspective.

[The table referred to follows:]

TABLE I-3.—EFFECT OF 1962-64 TAX CUTS ON REVENUES, 1963-68

[In billions of dollars]

	1963	1964	1965	1966	1967	1968	Total
Revenue losses estimated in 1963 by U.S. Treasury	2.4	5.2	13.3	20	23.7	24.4	89
Actual revenue gains	7.0	6.0	4.0	14	19.0	4.0	54
Difference in estimates	9.4	11.2	17.3	34	42.7	28.4	143

Source: U.S. Department of the Treasury.

Representative BOLLING. Mr. Schultze, you are a man of stamina. It has been a long and very interesting conversation. I know your schedule and I know mine. I am still going to ask a few questions on monetary policy and hopefully get some lunch before the next commitment.

It seems to me that the gap in the discussion has been on monetary policy. I want to approach it from the point of view of the gap and also from the point of view of the possible, even probable, enactment of the Humphrey-Hawkins bill, which would require the Fed to come in with some public plans as to what it intended to do, not in detail, but generally. I am sure you are fully aware of that.

First, I am curious as to what your view was of the adequacy of monetary policy in 1977. Would you comment on the monetary policy as it affected the other factors that you have to deal with as chairman of the Council, the monetary policy of 1977?

Mr. SCHULTZE. Well, not to suggest necessarily I would have done it all the same way, but it does turn out that during the year I think the area that people were most worried about was the impact of rising short-term rates on residential construction as they affected—as they worked through the system. That is where monetary policy has its first impact.

As it turns out, we got and are continuing to get a very good increase in housing construction.

Second, it also turns out that except in very past years that long-term rates moved up very little, even though short-term rates did.

I think as one looks out to the future, one does have to worry about the potentiality with significant further increases in interest rates of what happens to housing, via the thrifts; and, third, what happens to long-term rates and, therefore, private investment.

But insofar as what has happened to date, as I say, without necessarily wanting to say I would have done it exactly the same way, I don't see any significant slowing of economic recovery on that account. I think what one wants to look at is the future and what room there is left before some of these things do happen.

Representative BOLLING. Well, in order to make the assumptions that you articulated in your report, you must have assumed something about monetary aggregates in growth of M–1 and M–2.

Could you tell us what the assumptions were?

Mr. SCHULTZE. Well, in general terms essentially what we are assuming—and I am searching for the right adjective—something like a supportive monetary policy in the sense that the rates of growth of 4.5 to 5 percent in the real GNP and something in the neighborhood of 11 percent in nominal GNP would in a sense be supported by or would be accommodated or made possible by monetary policy.

We don't believe there is any conflict in the objective of a responsible monetary policy and the achievement of those goals.

Now, with respect to specific monetary aggregate increases, that is going to depend very heavily on what is going to happen to velocity. Velocity has been changing, as you know, quite rapidly in recent periods and so, therefore, there is no use in my saying there is any one number on the monetary aggregate growths which will do that.

We think, on the other hand, that Federal Reserve policy can, in effect, make possible those rates of economic growth over the next 2 years without losing sight at all of the need to control inflation.

Representative BOLLING. Where does that leave us then on the prospects on interest rates?

Mr. SCHULTZE. In terms of prospects on interest rates, again I do not want to get into the business of publicly forecasting interest rates. What I guess I can say is that these economic growth rates that I have indicated, there is no one nice, neat interest rate that makes it possible or doesn't. It isn't that close at all, but presumably could be accomplished then if you had maybe a little bit of an upcreep in short rates as you normally get in cyclical expansion, but significant increases in rates, particularly long-term rates, would make it very difficult to get this kind of growth.

Representative BOLLING. The staff of the JEC has prepared a memorandum examining some policy alternatives to the President's proposals. Without objection, I will place the memorandum in the record at this point.

[The memorandum referred to follows:]

[Memorandum of the Joint Economic Committee, Jan. 30, 1978]

To: Members of the Joint Economic Committee.
From: John Stark, Executive Director.
Subject: Attached Memorandum on Fiscal Policy and the Budget.

The attached memorandum was prepared to provide members with materials that will assist in evaluating the Administration's economic program. The memo consists of three sections:

Section I describes the consensus forecast for 1978 and 1979 and provides a frame of reference for evaluating the adequacy of the Administration's economic program.

Section II provides a capsule summary of the main ingredients of President Carter's budget for Fiscal Year 1979.

Section III shows the economic effects of alternative macroeconomic strategies. Included are a larger tax cut than proposed by the President, a larger expenditure increase than recommended, and a more rapid rate of monetary growth than is presently anticipated by forecasters.

The analysis was prepared by Tom Dernburg and Doug Lee of the Committee staff.

Monetary-Fiscal Policy Alternatives for 1978 and 1979

The current economic expansion has shown itself to be considerably stronger than we had supposed it to be a few months ago. Talk of a "growth recession" in 1978 has all but disappeared and there is general consensus that the expansion has another year of life left in it. On a year over year basis, real Gross National Product (GNP) rose 4.9 percent; the unemployment rate fell from 7.7 percent to 7.0 percent and prices as measured by the implicit price deflator for GNP rose 5.6 percent. Because the economy was very weak at the end of 1976, fourth quarter over fourth quarter comparisons paint an even stronger picture of economic performance in 1977. Such a comparison reveals real GNP growth of 5.7 percent and a reduction in the unemployment rate of 1.3 percentage points from 7.9 percent in the fourth quarter of 1976 to 6.6 percent in the fourth quarter of 1977. Unfortunately, inflation also moved at a more rapid pace as shown by the rise in the GNP deflator of 5.9 percent since the last quarter of 1976. Nevertheless, and although inflation remains far too rapid for comfort, there is little indication at this time that the inflation rate is in serious danger of accelerating.

Forecasters of economic activity have had little difficulty in arriving at a consensus for 1978. The anticipated rate of real economic growth will be only 4.5 percent. This is strong enough to avoid a growth recession but not enough to reduce unemployment by more than 0.3 or 0.4 percentage points to the 6.6–6.7 percent range in 1979. In anticipation of the continuation of 8 to 9 percent upward wage adjustments, unit labor costs will continue to rise at roughly 6 percent and the inflation rate is apt to be in that neighborhood.

Table 1 shows selected economic indicators for 1977 and compares these with the forecasted values for 1978 and 1979 of the Data Resources (DRI) model. The DRI results are representative of the mid-range of present forecasts. The staff simulations of the effects of alternative policies that are reported subsequently were also obtained by use of the DRI model.

It is very important to note that the DRI forecast—and this is true of nearly all other current forecasts—has built into it expectations with respect to President Carter's budget. Specifically, unified budget outlays of roughly $500 billion were assumed, and it was also assumed that taxes will be reduced by $25 billion effective October 1, 1978, in a ratio of two to one between persons and corporations. These expectations have conformed very closely to the President's recommendations.

Without the tax reduction the economy would be very weak at the end of 1978, and even with the tax reduction a marked slowdown is expected in 1979. This expectation suggests that the Administration budget for FY 1979 is not sufficiently stimulative to reach the unemployment target of 4¾ percent for 1981 that the Administration has enunciated or the 4 percent for 1983 that is specified by the Humphrey-Hawkins bill. At the same time the failure to grow at a rate sufficient to meet these targets will mean the continuation of an ample supply of un- or underutilized productive resources, and this should permit more expansionary policies to be adopted without the threat that such policies will add substantially to inflation.

TABLE 1.—SELECTED ECONOMIC INDICATORS [1]

[Calendar years]

	Actual 1977	Forecast 1978	Forecast 1979
GNP	1,890.4	2,096.3	2,305.3
Rate of growth of GNP	10.8	10.9	10.0
Implicit price deflator for GNP (1972=100)	141.32	149.95	158.37
Rate of growth of GNP deflator	5.6	6.1	5.6
GNP in 1972 prices	1,337.6	1,398.0	1,455.6
Rate of growth on real GNP	4.9	4.5	4.1
Unemployment Rate [2]	7.0	6.6	6.4
Rate of growth of money supply (M_1)	7.4	5.8	6.4
Treasury bill rate (3 mo)	5.27	6.38	5.9

[1] All growth rates are year over year rates except for M_1 which is a 4th quarter over 4th quarter rate.

[2] The unemployment rates were level-adjusted to reflect the lower than anticipated unemployment rate of the 4th quarter of 1977.

The next section of this memorandum provides a capsule summary of the Administration's major budget proposals. Thereafter the results of the staff's simulations of alternative monetary and fiscal policy combinations are presented and discussed.

PRESIDENT CARTER'S BUDGET FOR FISCAL YEAR 1979

President Carter's first Budget has been characterized by the press as "lean and tight." The $500 billion outlay level proposed by the President leaves little room for new programs or proposals. Nevertheless, the budget represents a major break with the budget philosophies of Presidents Nixon and Ford. Instead of drastic cuts in domestic spending programs, President Carter provides small increases. Defense spending is also increased. On the tax side the budget contains a modest tax reduction proposal designed to offset fiscal drag and sustain economic expansion. This contrasts with President Ford's efforts to use tax reduction as an inducement to lower Federal spending and to reduce the relative size of the Federal sector. Instead of concentrating on the philosophy of government's role in the economy, the budget focuses on practical issues such as the amount of stimulus needed to sustain economic expansion. Congress, for its part, must consider whether the proposals are adequate for their intended purpose.

A major innovation in the 1979 budget is the way in which the budget proposals are presented. For the first time the budget shows a current services level of outlays that can be compared with the President's policy recommendations. For example, one can see that in FY 1979 it would cost $492.4 billion to maintain the same level of services as provided in 1978, and that the President has proposed spending an additional $7.8 billion in FY 1979. This new form of presentation has long been advocated by the JEC which began, in 1973, to publish its own current services estimates.

Table 2 shows a comparison of the current service outlay estimates with the Administration proposals. As can be seen in the Table, the only significant changes occur in national defense (+$1.0 billion) and energy (+$2.0 billion). Of the remaining $4.8 billion increase, about $3 billion is needed to adjust the non-automatically inflation indexed programs, and $1.7 billion is designated as an allowance for contingencies. Therefore, of the President's $7.8 billion increase above the current services level, the only real spending increases are in the defense and energy areas.

TABLE 2.—CURRENT SERVICES OUTLAYS BY FUNCTION

[In billions of dollars]

	1977 actual	Current services: 1978 estimate	Current services: 1979 estimate	1979 administration proposals
National defense	97.5	107.7	116.8	117.8
International affairs	4.8	6.7	7.4	7.7
General science, space, and technology	4.7	4.8	5.1	5.1
Energy	4.2	7.5	7.6	9.6
Natural resources and environment	10.0	11.7	12.0	12.2
Agriculture	5.5	9.0	5.5	5.4
Commerce and housing credit	(1)	3.5	3.1	3.0
Transportation	14.6	16.3	17.1	17.4
Community and regional development	6.3	9.5	8.5	8.7
Education, training, employment, and social services	21.0	26.9	29.4	30.4
Health	38.8	44.3	50.3	49.7
Income security	137.0	147.5	159.2	160.0
Veterans benefits and services	18.0	18.9	18.9	19.3
Administration of justice	3.6	4.0	4.1	4.2
General government	3.4	4.1	4.2	4.3
General purpose fiscal assistance	9.5	9.9	9.5	9.6
Interest	38.1	43.8	48.7	49.0
Allowances:				
Civilian pay raises			1.1	1.1
Contingencies				1.7
Undistributed offsetting receipts:				
Employer share, employee retirement	−4.5	−5.0	−5.2	−5.2
Interest received by trust funds	−8.1	−8.6	−9.1	−9.1
Rents and royalties on the Outer Continental Shelf	−2.4	−2.0	−1.8	−1.8
Total outlays	401.9	460.4	492.4	500.2

[1] $50 million or less.

The Administration estimates that receipts would be $463.8 billion in the absence of any changes in tax policy. After deducting the proposed tax cut, receipts would total $439.6 billion. In our judgment the estimate of $463.8 billion is excessive and a level of $460 billion would be more consistent with the Administration's own economic assumptions.

The appropriate size of the tax reduction that is generally believed to be necessary will be a topic of lively debate. Much of the tax reduction seems necessary merely to offset other tax increases. As shown subsequently, the fiscal drag that arises from social insurance tax increases and from the progressivity of the personal income tax will be about $15 billion in 1978, and an additional and even larger drag can be expected in 1979. Thus social insurance and personal income taxes produce enough drag in 1978 to eat up two-thirds of the stimulative effect of the President's proposed tax reduction. And this calculation does not include the energy tax proposals which ,although they have little budgetary effect as proposed by the President, may prove to have significant effects in the forms that emerge from the Congress.

The 1979 budget continues some of the positive changes that were initiated in the 1978 budget presentation. The budget shows fairly detailed estimates for 1980, and it gives much more information than in the past about the five-year budgetary picture. President Carter does not repeat President Ford's recommendation that many off-budget items be included in the budget totals.

Table 3 shows 1979 outlays compared with estimates for 1978. The large decline shown for agriculture reflects the reduced price support payments which result from large set-aside requirements. The decline in commerce and housing credit are the consequence of large receipts (counted as negative outlays) of the Federal Deposit Insurance Corporation and a substantial sale of mortgage paper by the Federal Home Loan Bank Board. The declines shown for community and regional development are spread throughout this function and cover such areas as disaster relief, community block grants, and local public works projects. The large increases—both absolutely and in percentage terms—are for income security, energy, and national defense.

The President's proposals will cause many taxpayers to avail themselves of the standard deduction rather than to itemize deductions. Tax rates will be lower. Both factors will cause tax expenditures to fall in many categories.

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According to the Administration's estimates, tax expenditures will fall by some $15 billion.

TABLE 3.—1978 AND 1979 OUTLAY PROJECTIONS

[In billions of dollars]

	1978	1979	Dollar change	Percent change
National defense	107.6	117.8	10.2	9.5
International affairs	6.7	7.7	.9	14.0
General science, space, and technology	4.8	5.1	.3	6.7
Energy	7.8	9.6	1.8	22.9
National resources and environment	12.1	12.2	.1	.8
Agriculture	9.1	5.4	−3.7	−40.3
Commerce housing credit	3.5	3.0	−.6	−15.8
Transportation	16.3	17.4	1.1	6.7
Community and regional development	9.7	8.7	−1.0	−10.5
Education, training, employment, and social services	27.5	30.4	3.0	10.7
Health	44.3	49.7	5.4	12.2
Income security	147.6	160.0	12.4	8.4
Veterans benefits	18.9	19.3	.3	1.8
Administration of justice	4.0	4.2	.2	4.8
General government	4.1	4.3	.2	4.5
Revenue sharing and general fiscal assistance	9.9	9.6	−.2	−2.3
Interest	43.8	49.0	5.2	11.8
Allowances and contingencies		2.8	2.8	
Undistributed offsetting receipts	−15.6	−16.0	−.4	2.6
Total	462.2	500.2	38.0	8.2

The full employment budget deficit is projected by the Administration to increase from $10 billion in 1977 to $32 billion in 1978 and to $37 billion in 1979. This implies that fiscal policy in 1978 is quite stimulative relative to 1977, but that only a tiny amount of additional stimulus is proposed for 1979 despite the inclusion in the budget of a proposed tax reduction of about $25 billion. The JEC staff has made its own calculations of the full employment budget deficit. These estimates show the full employment deficit increasing to $28 billion in 1978 and to $32 billion in 1979. The conclusions are the same: The 1978 budget is stimulative relative to 1977, but there is very little additional stimulus in 1979. If the economy weakens in late 1978, President Carter's proposals will prove inadequate unless they are accompanied by a sharply more expansionary monetary policy. The simulations reported in the next section show the importance of more stimulative monetary policy and they also show the economic effects of some alternative budgetary strategies.

ALTERNATIVE FISCAL AND MONETARY POLICIES

(1) *Expansionary Monetary Policies*

The Administration has been painfully silent about monetary policy. The *Economic Report of the President* barely mentions the subject, and nowhere is there to be found any indication of a desirable rate of monetary growth, a desirable path for interest rates, or the relationship between monetary policy and the performance of the economy. Recent policy actions, moreover, are not encouraging. The decision to raise the Federal Reserve's rediscount rate to 6½ percent was an attempt to shore up the international value of the dollar at the expense of the kinds of monetary and credit conditions that would support the growth of the domestic economy. Such use of monetary policy for international objectives has long been opposed by the Joint Economic Committee and it is to be hoped that the Committee will strongly insist on reversal of the unfortunate present retrogression of monetary policy.

The need for more stimulative monetary policy is evident from the persistent failure of capital spending to revive to prosperity levels and to the growing fear that financial disintermediation may interfere with the continued strength of the residential building industry. Moreover, under the President's budget proposals, the economy will receive no additional stimulus from fiscal policy until late 1978. Lessening the danger of a slowdown prior to that time could be effected by a more generous rate of monetary growth than is anticipated by present forecasts.

Although the nominal quantity of money (M_1) grew more rapidly in 1977 than in any year since 1972, this 7.4 percent growth rate appears to be regarded by most forecasters as having been unintentionally high, and, as can be seen in Table 1, DRI's expectation is that it will decline to rates of 5.8 and 6.4 percent in 1978 and 1979 respectively. It may also be noted that the 5.8 percent growth rate in 1978 is not sufficient to finance the projected 10.9 percent growth of nominal GNP without a rise in short term interest rates of more than 100 basis points.

Under present and prospective economic conditions a rise in interest rates is harmful and undesirable. It is the likelihood of such a rise that is perhaps the most important factor making for the meager 4.5 percent and 4.1 percent real growth rates forecasted for 1978 and 1979 respectively.

The results of the first staff simulation are reported in Table 4. This simulation assumes that the rate of monetary growth is stepped up in a way that reduces the 3 month Treasury bill rate of its 1977 average of 5.3 percent and that holds the bill rate at that level throughout 1979. The fiscal policy assumptions are the same as in the basic forecast.

TABLE 4.—SIMULATION RESULTS: RAISING THE RATE OF MONETARY GROWTH TO LOWER THE TREASURY BILL RATE TO 5.3 PERCENT

	1978	1979
Levels:		
GNP	2,106.6	2,344.5
Difference from forecast	10.3	39.5
GNP in 1972 prices	1,404.1	1,476.0
Difference from forecast	6.1	20.4
Implicit price deflator for GNP	150.0	158.8
Difference from forecast	.1	.5
Unemployment rate	6.45	5.90
Difference from forecast	−.10	−.50
Treasury bill rate	5.27	5.28
Difference from forecast	−1.12	−.63
Budget deficit (NIA basis)	45.4	36.5
Difference from forecast	−3.7	−13.4
Difference from forecast:		
Nonresidential fixed investment	+1.1	+7.4
Residential construction	+4.2	+13.5
Net exports of goods and services	+.2	−2.1
Growth rates:		
Money supply (M_1)	6.9	8.2
Difference from forecast	1.1	1.8
GNP	11.4	11.3
Difference from forecast	.5	1.3
GNP in 1972 prices	5.0	5.1
Difference from forecast	.5	1.0
Implicit price deflator for GNP	6.1	5.9
Difference from forecast	0	.3

As can be observed in Table 4 attainment of the interest rate target requires that the rate of M^1 growth be stepped up by 1.1 and 1.8 percentage points in 1978 and 1979 respectively. The results are gratifying. Since monetary policy affects the economy with a considerable lag, there is little effect in 1978 even though our simulation assumes an immediate increase in the rate of monetary growth. Thus in 1978 nominal and real GNP increase only $10.3 billion and $6.1 billion respectively and there is virtually no change in the inflation rate or in the unemployment rate.

The main effects of a faster rate of monetary growth begun immediately will be in 1979 when the economy will most need support. Relative to the concensus forecast GNP will be $40 billion higher, the real growth rate will be a full percentage point higher, and the unemployment rate will be one half of one percentage point lower. Thus a somewhat more rapid—though hardly excessive—rate of monetary growth can eliminate all risk of recession in 1979, and can contribute some 500,000 additional jobs in that year.

The greater strength shown by the economy as the consequence of more rapid monetary expansion is mainly in the investment sector. The simulation indicates that non residential fixed investment may be $7 billion higher in 1979 and that home-building may rise by more than $13 billion. In view of our lingering fears over the behavior of investment, it seems clear that a more generous monetary policy should be high on our list of policy priorities.

Unlike stimulative fiscal policies expansionary monetary policy reduces the Federal budget deficit. As shown in Table 4, the deficit may be reduced by from $10 to $15 billion by a monetary policy that does no more than bring short-term interest rates back to their 1977 average. The stronger economy will generate additional revenues from all taxes—personal, businss, social insurance, and indirect—and it will reduce outlays for unemployment compensation and welfare. Meanwhile the lower interest rates will reduce the interest cost of financing the national debt.

It is true, of course, that the inflation rate will rise somewhat. But this will happen as the consequence of all expansionary policies, and the simulation results indicate that the rise will be modest because the economy continues to have underutilized capital and labor at its disposal so that the danger of generating excessive demand is quite minimal. Moreover, since expansionary monetary policy tends to augment the investment share of GNP, whereas expansionary fiscal policies augment the government and/or consumption shares, expansionary monetary policies will yield productivity gains that will help to moderate inflation in the future.

(2) An Additional $15 Billion Tax Reduction

President Carter has recommended a net tax reduction of $25 billion to be made effective October 1, 1978. Because a tax reduction of this magnitude will not sustain growth at an acceptable rate in 1979, there are many who believe that a more substantial tax reduction is desirable. The Chamber of Commerce, for example, is recommending a reduction of $40 billion. Our next staff simulation examines the consequences of such a policy. It is assumed in this simulation that the two to one ratio of relief for persons and corporations is maintained.

The $25 billion tax reduction may be inadequate because of the tax increases that will take place automatically in 1978. For example, if social insurance taxes were to rise by the same 10.9 percent as the forecasted rise in nominal GNP for 1978, the taxes would increase by $13.0 billion. However, the forecasted increase is $18.7 billion, the extra increase of $5.7 billion being attributable to the fact that both the social security tax rate and base rose at the beginning of 1978, and to the fact that the minimum taxable Federal base for unemployment insurance increased from $4,200 to $6,000, thereby raising Federal taxes on employers, and forcing many states to raise their unemployment payroll taxes.

Because of the progressivity of the personal income tax, this tax tends to rise automatically by an amount equal to 1.5 to 1.6 times the percentage rise in personal income. If income taxes were proportional, they would rise by $18.6 billion in 1978. But because of the progressivity factor they will rise by $28.8 billion. The difference of $10.2 billion between the two figures is the fiscal drag attributable to the personal income tax. Added to the $5.7 billion disproportionate social insurance tax increase, this amounts to a net fiscal drag from these two sources of about $16 billion, and this wipes out about two-thirds of the stimulus that would be provided by a $25 billion tax reduction.

Table 5 shows the economic effects of adding $15 billion to the President's proposed $25 billion tax reduction. Because the reduction does not take place until October 1, 1978, there is virtually no effect this year. In 1979 both nominal and real GNP are higher by about one half as much as the increase achieved by the monetary policies of the earlier simulations. The reduction in the unemployment rate and the rise in the inflation rate are reduced accordingly.

The simulation was conducted without any attempt to accompany the fiscal expansion with an accommodative monetary policy. Evidently, however, an additional tax reduction of $15 billion is so tiny that it fails to put any upward pressure on interest rates and it therefore produces no crowding out of investment spending.

One-third of the tax relief is granted to business. This, combined with stronger product demand unimpeded by higher interest rates, raises non-residential fixed investment by $3.5 billion, or about one-half the amount of the first simulation. However, the less favorable monetary conditions implied by this simulation limit the rise in residential construction to a very modest increase. As usual, the bulk of the strength that results from the additional tax cut is in the consumption sector. More expansionary monetary policy, on the other hand, would have mainly stimulated the lagging capital spending sector and thereby set the basis for more rapid subsequent production advances.

TABLE 5.—SIMULATION RESULTS: $40 BILLION TAX REDUCTION

	1978	1979
Levels:		
GNP	2,097.5	2,323.7
Difference from forecast	1.2	18.4
GNP in 1972 prices	1,398.8	1,466.1
Difference from forecast	.8	10.5
Implicit price deflator for GNP	149.9	158.5
Difference from forecast	0	.1
Unemployment rate	6.6	6.2
Difference from forecast	.0	–.2
Treasury bill rate	6.38	5.90
Difference from forecast	0	0
Budget deficit (NIA basis)	53.4	66.0
Difference from forecast	+4.3	+16.1
Difference from forecast:		
Nonresidential fixed investment	+.1	+3.5
Residential construction	+.1	+1.7
Net exports of goods and services	0	–1.5
Growth rates:		
Money supply (M_1)	5.9	6.4
Difference from forecast	+.1	0
GNP	11.0	10.8
Difference from forecast	+.1	+.8
GNP in 1972 prices	4.6	4.8
Difference from forecast	+.1	+.7
Implicit price deflator for GNP	6.1	5.7
Difference from forecast	0	+.1

It should be noted, finally, that the additional tax reduction adds substantially to the Federal deficit whereas the expansionary monetary policy reduces the deficit. This is not a decisive advantage of monetary policy in all instances, but it is a factor that should be kept in mind.

(3) An Increase in Federal Outlays of $7.5 Billion Above President Carter's Recommendation

Those who prefer expanded expenditures to tax reduction as a means of providing fiscal stimulus have been put at a disadvantage by the persistence, throughout FY 1977, of a $15 billion expenditure shortfall. However, recent indications are that this shortfall has been eliminated and that FY 1978 outlays are now on target with respect to timing. This has two important consequences. First, it means the economy is currently in the process of receiving some welcome stimulus and may be stronger than expected in early 1978. Second, it means that additional outlays can be approved without danger that such action will merely add to the magnitude of the shortfall.

Nevertheless, it is not easy to find ways of spending more money both quickly and constructively. The staff has estimated that Congress may be able to add about $7.5 billion to FY 1979 outlays, but that any more than that would be difficult to spend in non-wasteful ways without major program initiatives. Our assumption is that $1 billion could be usefully put into each of the following categories—Energy, National Defense, CETA, General Purpose Fiscal Assistance, and Housing, that $2 billion could be added to outlays for Health and Education, and that $0.5 billion in fiscal relief could be granted to urban governments. For NIA purposes we put $2 billion into Federal Purchases, $1 billion into subsidies, and $4.5 billion into grants to State and local governments.

The economic effects of this $7.5 bililon increase in Federal expenditures are reported in Table 6. Since Federal grants will be reflected in State and local purchases, the impact on GNP and unemployment per dollar of budget cost is greater for the present mix of increased Federal outlays than for tax reduction. On the other hand, because the assumed tax reduction provided business tax relief, the effect on investment of that policy was more powerful than the increase in Government expenditure.

The expenditure expansion clearly helps the economy in 1979. The real growth rate is raised by 0.5 percentage points and unemployment drops to 6.2 percent

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of the labor force. The risk of a growth recession is therefore greatly reduced by this modest addition to the budget. Finally, because the GNP impact per dollar of outlay is greater than for tax reduction, the positive feedback to the Treasury is considerably higher and the policy therefore adds considerably less to the Fedeal deficit than would be the case if additional tax reduction were the chosen alternative.

TABLE 6.—SIMULATION RESULTS: INCREASED FEDERAL SPENDING BY $7.5 BILLION IN FISCAL YEAR 1979

	1978	1979
Levels:		
GNP	2,098.2	2,317.9
Difference from forecast	+1.9	+12.6
GNP in 1972 prices	1,399.2	1,463.1
Difference from forecast	+1.3	+7.6
Implicit price deflator for GNP	149.9	158.4
Difference from forecast	0	0
Unemployment rate	6.6	6.2
Difference from forecast	0	-.2
Treasury bill rate	6.38	5.94
Difference from forecast	0	+.04
Budget deficit (NIA basis)	50.3	53.1
Difference from forecast	+1.2	+3.2
Difference from forecast:		
Nonresidential fixed investment	+.1	+1.1
Residential construction	+.1	+.5
Net exports of goods and services	0	+1.3
Growth rates:		
Money supply (M_1)	5.9	6.5
Difference from forecast	+.1	+.1
GNP	11.0	10.5
Difference from forecast	+.1	.5
GNP in 1972 prices	4.6	4.6
Difference from forecast	+.1	+.5
Implicit price deflator for GNP	6.1	5.7
Difference from forecast	0	+.1

CONCLUSIONS

(1) President Carter's proposed $25 billion tax reduction is an appropriate measure of fiscal policy provided that it is supplemented by other policies. Without this tax reduction the economy would be extremely weak in late 1978 and a growth recession would be very likely in 1979.

Because of very heavy fiscal drag, the weakness of investment, and the weakness of the foreign sector, the $25 billion tax reduction will sustain growth in 1979 at the very meager rate currently forecasted to be only 4.1 percent in real terms. Supplementary policies are therefore needed.

(2) The most promising supplementary policy would be an immediate and continuing rise in the rate of monetary growth. By reducing interest rates this will stimulate capital spending and ensure the continuation of strong performance by the home-building industry. This, in turn, will provide higher GNP and more jobs in the short run, and faster productivity growth and less inflation in the long run. Unlike the tax reduction and the expenditure increase, expansion through monetary policy reduces the budget deficit.

The only possible disadvantage to more expansionary monetary policy is that the reduction in short-term interest rates implied by the policy will cause short-term capital to flow to higher yield financial markets abroad. This will reduce the demand for the dollar and possibly cause its value to fall relative to other currencies. Whether or not this is a gain or a loss is open to serious dispute.

Those who wring their hands over the "integrity" of the dollar complain that the rising costs of imports will add to domestic inflation. Those who believe that the dollar should fall in value in response to our massive trade deficit believe that the higher cost of imports is desirable because it will lead to the substitution of domestic production and employment for imports and that it will also encourage exports. Such analysts therefore welcome declining interest rates not only because this encourages capital spending but also because it tends to improve our balance of trade and thereby stimulates our economy.

(3) Tax reduction in excess of the President's $25 billion proposal would not be inappropriate, nor would additional expenditure expansion. Both policies would provide insurance against a slump in 1979. These policies are, however, inferior to expansion through monetary policy because they have less of an impact on capital spending and because they raise the budget deficit whereas the expansionary monetary policy lowers it.

(4) In view of the consensus forecast, an optimal policy might combine the President's $25 billion tax reduction with an additional $7.5 billion rise in Federal outlays, and it would combine both of these policies with an expansionary monetary policy that seeks to reduce short-term interest rates to their 1977 average. This combination of policies would raise the real growth rate for 1979 by 1.5 percentage points, and it would reduce the unemployment rate to 5.7 percent. Such a policy combination would not be dangerously inflationary. It would however, put the economy on the track of the Humphrey-Hawkins recovery path.

Representative BOLLING. One of these alternatives, the President's fiscal policy for expansion of monetary policy, produced a significantly stronger economy in 1978 and 1979 than we would otherwise anticipate. Monetary policy assumed in this analysis was to maintain interest rates at their average level for 1977.

Would you comment on the appropriateness of such a fiscal monetary mix?

Mr. SCHULTZE. Well, my recollection is that that would give you Treasury bill rates of something like 5.75, somewhere between 5.25 and 5.5 percent, compared to the current 6.75. It seems to me that as recovery goes on, to try to have a monetary policy which holds the bill rate below the rate of inflation, that is a negative real rate of return over the long pull, and that is a policy that would be very difficult to pursue.

I don't know what it would mean with respect to the monetary aggregate, but it is likely to mean a very, very large increase.

Representative BOLLING. Well, that leads me to the last question I will ask, and it is a complicated one.

What is going to be the effect of that provision in the Humphrey-Hawkins bill? What kind of a product are we going to get out of the Fed when we try to put together in a somewhat, I suppose, wiser fashion or more informed fashion what we ought to be doing fiscally? What kind of information can we expect to get from the Fed under the new chairman-designate if this committee ends up charged to deal with these things—including monetary policy?

Mr. SCHULTZE. Mr. Chairman, without at all wanting to be cavalier about this, the Humphrey-Hawkins bill is written in terms of the relationship between the Congress and the Federal Reserve and does not run through the administration and, therefore, I suggest that an appropriate person to ask this question of, would be the new Chairman of the Federal Reserve, not the Chairman of the Council of Economic Advisers.

Representative BOLLING. I know when I have been had, Charlie. That closes the hearing.

[Whereupon, at 12:39 p.m., the committee recessed, to reconvene at 9:30 a.m., Wednesday, February 1, 1978.]

THE 1978 ECONOMIC REPORT OF THE PRESIDENT

WEDNESDAY, FEBRUARY 1, 1978

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

The committee met, pursuant to recess, at 9:40 a.m., in room 345, Cannon House Office Building, Hon. Richard Bolling (chairman of the committe) presiding.

Present: Representatives Bolling, Reuss, Brown of Ohio, and Rousselot; and Senators McGovern and Javits.

Also present: John R. Stark, executive director; Louis C. Krauthoff II, assistant director; G. Thomas Cator, L. Douglas Lee, Katie MacArthur, Deborah Norelli Matz, and Philip McMartin, professional staff members; Mark Borchelt, administrative assistant; and Charles H. Bradford, Stephen J. Entin, George D. Krumbhaar, Jr., and Mark R. Policinski, minority professional staff members.

OPENING STATEMENT OF REPRESENTATIVE BOLLING, CHAIRMAN

Representative BOLLING. The committee will be in order. We are going to start, despite the fact that one of our witnesses is unavoidably detained for a while, but is expected shortly.

It is now a universally accepted premise that a growth economy is impossible without a program to effectively and adequately respond to our structural unemployment problem. I think it is universally accepted by those who have studied the problem. By this I mean that programs to provide jobs for the disadvantaged worker to acquire the skills to meet the labor market demands and thus gain for themselves the opportunity to form useful, productive workers at decent wages.

This can be done through work and training programs aimed at present and anticipated needs of the existing private and public sector employers and by programs designed to establish and expand private enterprise with new job opportunities for the depressed and urban areas which are the center of structural unemployment.

Unless Government successfully meets this problem, our Nation faces the prospect of the disruption in the continuing economic recovery, accompanied by a tightening labor market, resulting in an intolerable situation while millions of workers are made unemployed.

Under these conditions, we will, in all likelihood, find ourselves heading into another recession, and with all the circumstances with which we are all painfully familiar. The fact is that significant reductions are being increasingly projected. The JEC staff committee studied the long-term economic growth, and it does portend some relief of structural unemployment, but not nearly enough to be a solution.

The need to address this problem remains. Seen in this perspective, our Nation does not enjoy the dubious choice of economic recovery while allowing 8 to 9 million unemployed and underemployed to marginally exist on transfer programs of one kind or another. Unless Government successfully develops and implements an approach to dealing with this level of unemployment, full employment will remain beyond our grasp, Government, in complete cooperation with the private sector and with the various elements that have bearing on this market.

The point is confirmed that employment has increased by 4.1 million jobs, nearly that last year, the greatest increase in our history while joblessness is not diminishing, and has remained intolerable in the areas of concentration of unemployment.

It is my hope that our witnesses this morning will provide the committee with fresh insight on what must be seen as a crucially important problem. Specifically, I have asked the witnesses to tell us what is right and what is wrong with existing employment and job training programs, how they can be improved, and what new approaches are needed to answer this problem.

In respect to the latter, I look forward to the possible creation of new and expanded partnerships between the private sector and government, to provide a much broader response to the job creation employment and training needs.

Before I proceed to the witnesses, I would like to comment that I can remember some years ago when a rather well-known-in-his-time Republican, Tom Curtis, from St. Louis, was trying to explain to the members of this committee and the staff that one of the major problems we had was structural unemployment. He was greeted generally with laughter. It took a very long time and the fact became more and more clear before it was understood that he was right, that macroeconomics is not going to solve all of the problems of unemployment.

I think it is an illustration of the rigidity that people have in viewing economic solutions. It is a rigidity which, I think, has been extremely counterproductive. I know less about the rural areas, but the situation today in the cities—and Tom Curtis came from an urban area—is the most destructive thing that I have known as an adult, barring, of course, the long and tragic delay in the Nation dealing with the problems of civil rights.

We are creating not a generation but a part of a generation of people often, perhaps most often, black, brown, or other minorities, who have absolutely no hope in this society. They see no prospect of ever having a job. They see no hope of ever having anything like a career. It is an enormously dangerous kind of situation for us to have tolerated for this long.

I am delighted that you can be here, all of you. Mr. Burns, John L. Burns, is the vice chairman of the Research and Policy Committee for the Committee for Economic Development. Mr. Burns is accompanied by Mr. Frank Schiff, who is vice president and chief economist of the CED. Mr. Burns has a remarkably distinguished career, both in business and public service, and of course, is involved with an organization that I have long admired, because of its major contribution to the employment act a long, long time ago.

We also have Ms. Beatrice Reubens, of Columbia University. We have, in a few minutes—we hope we will have Prof. Michael Wiseman, of the University of California at Berkeley.

We are glad to have you. Mr. Burns, will you proceed as you wish.

STATEMENT OF JOHN L. BURNS, VICE CHAIRMAN, RESEARCH AND POLICY COMMITTEE, COMMITTEE FOR ECONOMIC DEVELOPMENT, ACCOMPANIED BY FRANK W. SCHIFF, VICE PRESIDENT AND CHIEF ECONOMIST

Mr. Burns. Thank you, Mr. Chairman and distinguished members of the committee. My name is John L. Burns. I am currently president of the John L. Burns & Co. and also of the Boys' Clubs of America. Previously, I have been president of RCA and chairman of City Services.

I appreciate the opportunity to appear before you today in my capacity as vice chairman of the Research and Policy Committee of the Committee for Economic Development (CED) and as chairman of the subcommittee that developed the newly issued CED policy statement, "Jobs for the Hard-to-Employ: New Directions for a Public-Service Partnership." Accompanying me is Mr. Frank W. Schiff, vice president and chief economist of CED and project director for the policy statement.

My main task this morning will be to present the highlights of our new policy statement. Copies of the statement have been distributed to each of you, together with a companion volume, which we consider very important, of case studies of effective private sector programs that are now in operation.

These case studies are based on a special survey we made of our own trustee companies. They bring together in one volume a set of success stories involving about 80 private firms and organizations. You can get an impression of the wide range of firms and activities covered simply by referring to the table of contents at the very beginning of the volume. I think it is fair to say that many of the members will find interesting situations in their own States which could be expanded.

The focus of our policy statement is on providing adequate training and job opportunities for those groups that are especially hard hit by high or prolonged unemployment, even in relatively good times: The young, the disadvantaged—particularly blacks living in inner cities—and older workers. We believe that finding a solution to this problem is of critical importance if this country is to achieve its longer term goal of high employment without inflation.

In studying this issue, we reached a number of other broad conclusions. One is that unemployment and underemployment are enormously wasteful and costly for our economy, and that the steps to overcome these problems which we propose are not merely good social policy but also good business.

Second, we feel strongly that public policy should place more stress on ways to put people to work than on paying them for not working.

Third, while we recognize that there is an important direct role for government in promoting employment, we feel that far more emphasis than in the past should be placed on involving the private sector—both profit and nonprofit—in efforts to provide jobs for the hard-to-employ. This is underlined by the fact that the private sector accounts for four out of five jobs in our economy. Fourth, this effort must not involve only large firms. Many of the added job opportunities need to be found in small firms and businesses and particularly in the expanding service sector, where small firms are so important.

It is often forgotten that half the jobs in this country are in firms with a hundred employees or less and that about three-quarters of the jobs are in firms with fewer than 500 employees.

Of course, no single program can by itself be expected to eliminate structural unemployment. What is needed is an integrated strategy that involves a wide range of public and private actions. That strategy must, among other things, include appropriate fiscal and monetary policies to foster a healthy growth of total demand; measures to render the economy more efficient, encourage productive investment, and otherwise reduce inflationary cost pressures; and steps to bring added job opportunities to the urban areas where many of the hardest-to-employ are concentrated.

CED has dealt with these elements of the strategy in various earlier statements and is examining other aspects in its current studies.

The statement I am discussing today focuses on another key element of the strategy; namely, direct measures to deal with structural unemployment and, particularly, the role that increased public-private cooperation can play in that connection. Our principal concern has been to identify aproaches that will work. A central theme of our statement is that the key to increasing the private sector role in this field lies not so much in developing brand new techniques. Rather, it calls for mobilizing much more active and widespread business, Government, and community support for the kind of activities that are already being successfully carried out by various individual firms and communities, as demonstrated in our case studies. Among the principal recommendations in the policy statement are the following:

First, we call for much wider dissemination of information about existing private sector programs that work. Our case studies are already contributing to this process, but we believe there is need for a permanent information clearing house regarding such efforts. With better information, the chances will be greatly enhanced that constructive programs that now operate on a small scale can be replilated much more wisely.

I think, again, if you scan through the attached document accompanying this statement, you get quite a few examples.

Second, we urge a concerted effort by the top business leadership, both nationally and at the community level, to provide new impetus for an effective private-public partnership for aiding the hard-to-employ. This effort needs to be paralleled by clearer and more unified direction of Federal manpower programs and greatly increased stress in the management of these programs on more active local community participation and an enlarged role for the private sector. In this connection, we call in particular for improved management and closer integration of the U.S. Employment Service and CETA.

Third, there is need for much wider use of various kinds of intermediary organizations to assist business in becoming more fully involved in special training and employment efforts. Experience shows that many firms which have been reluctant to hire the disadvantaged directly will do so if the intermediate organizations help them in dealing with such groups.

These organizations can be particularly useful in handling job placement, cutting the red tape connected with federally supported on-the-job training contracts, and providing special counseling and other services for the hard-to-employ. Let me cite three types of intermediate organizations that we found to be particularly promising:

The Chicago Alliance of Business Manpower Services (CABMS) is a private nonprofit organization created by a coalition of 20 major business firms and 20 minority firms and groups in Chicago. It has a permanent staff and can act as a direct contractor for federally financed on-the-job training programs. This type of arrangement has been unusually effective in developing on-the-job training contracts, particularly with small firms. It has, for example, cut the red tape involved in CETA contracting from several months to about 10 days.

The experimental Manpower Demonstration Research Corporation is a form of "jobs corporation" which takes on some of the most severely disadvantaged persons as its employees, trains them and moves them into supported work, and then gradually shifts them into permanent nonsubsidized private employment.

Various specialized private job-finding organizations can be particularly effective in facilitating job development, training and placement of especially hard-to-employ groups. An example is the Vocational Foundation in New York, which deals primarily with exoffenders and chronic welfare cases.

Our fourth set of recommendations calls for approaches specifically "tailored" to the needs of individual groups, involving: an improved transition from education to work, including increased use of apprenticeship and work-study program; greater stress on job-readiness preparation, skill training and upgrading for the disadvantaged; more productive use of older workers and retirees, including steps to smooth the transition from regular work to retirement; more flexible work schedules and job arrangements to make added employment available to persons who cannot conform to a regular full-time schedule.

Fifth, we call for fuller exploration of various alternatives to outright layoffs in recessions, including changes in unemployment compensation arrangements to facilitate greater reliance on work sharing and skill upgrading during such periods.

Finally, we recommend increased incentives for private employment and training of the hard-to-employ, particularly through greater experimentation with categorical tax credits.

I am glad to report, Mr. Chairman, that our proposals have already received considerable attention within the executive branch. During recent months, we have had an opportunity to discuss them directly with the Secretaries of Labor and Commerce and the senior White House staff.

Secretary Marshall has appointed a committee within his department which will examine each of our recommendations and report to him what further action should be taken. More broadly, we are, of course, very pleased that the President's economic messages place major stress on a new initiative for private sector training and hiring of the hard-core unemployed.

While the details of his proposal have not yet been announced, the recommended creation of local industry training councils appears to be similar to our proposal for much wider use of the Chicago CABMS-type arrangement. We are hopeful that implementation of many of our other recommendations will also be facilitated by the administration's forthcoming policy initiatives.

The most important part of the solution, however, will have to come at the local community level, with business leadership. In this connection, I am glad to report that CED will in the coming year and a half conduct a series of six regional policy forums in major cities with particularly severe unemployment. At these forums, the community leaders will explore the implications of our statement for their own communities. We are hopeful that these forums will serve as a focal point for mobilizing local support for the kind of program to deal with structural unemployment that we have recommended.

[The document attached to Mr. Burns' statement follows:]

Jobs for the Hard-to-Employ

New Directions
For a Public-Private Partnership

A Statement on National Policy
by the Research and Policy Committee
of the Committee for Economic Development

CED

January 1978

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Responsibility for CED Statements on National Policy

The Committee for Economic Development is an independent research and educational organization of two hundred business executives and educators. CED is nonprofit, nonpartisan, and nonpolitical. Its purpose is to propose policies that will help to bring about steady economic growth at high employment and reasonably stable prices, increase productivity and living standards, provide greater and more equal opportunity for every citizen, and improve the quality of life for all. A more complete description of the objectives and organization of CED is to be found on page 98.

All CED policy recommendations must have the approval of the Research and Policy Committee, a group of trustees whose names are listed on these pages. This Committee is directed under the bylaws to "initiate studies into the principles of business policy and of public policy which will foster the full contribution by industry and commerce to the attainment and maintenance" of the objectives stated above. The bylaws emphasize that "all research is to be thoroughly objective in character, and the approach in each instance is to be from the standpoint of the general welfare and not from that of any special political or economic group." The Committee is aided by a Research Advisory Board of leading social scientists and by a small permanent professional staff.

Research and Policy Committee

The Research and Policy Committee is not attempting to pass judgment on any pending specific legislative proposals; its purpose is to urge careful consideration of the objectives set forth in this statement and of the best means of accomplishing those objectives.

Each statement on national policy is preceded by discussions, meetings, and exchanges of memoranda, often stretching over many months. The research is undertaken by a subcommittee, assisted by advisors chosen for their competence in the field under study. The members and advisors of the subcommittee that prepared this statement are listed on page 6.

The full Research and Policy Committee participates in the drafting of findings and recommendations. Likewise, the trustees on the drafting subcommittee vote to approve or disapprove a policy statement, and they share with the Research and Policy Committee the privilege of submitting individual comments for publication, as noted on this and the following page and on the appropriate page of the text of the statement. *

Except for the members of the Research and Policy Committee and the responsible subcommittee, the recommendations presented herein are not necessarily endorsed by other trustees or by the advisors, contributors, staff members, or others associated with CED.

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* Memoranda of comment, reservation, or dissent appear on pages 88 to 91.

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Purpose of this Statement

TEN YEARS AGO, AT A TIME OF GREAT TROUBLE in many urban areas, there was a strong outpouring of business commitment to bring jobs and businesses back to the central city. However in many cases, these commitments were made without an understanding of the problems involved and without the experience necessary to develop effective programs. As a result, many of these efforts failed. Many business leaders concluded that there was really very little they could do that would be effective and lasting. It became, in their minds, primarily a problem for government.

However some business groups continued to work at the problems of the hard-to-employ and began to gain in experience and deeper understanding. In the past two years there has been a renewal of business's commitment to developing jobs for the hard-to-employ and for helping prepare the disadvantaged, particularly minority youths, for steady, responsible jobs. What makes current efforts different from those of the 1960's is that now there is a realization of the difficulties involved and an understanding of the effort that must be put into each job and into preparing each individual for that job.

The CED subcommittee that prepared this report spent two years examining what kinds of programs have worked, what kinds have not, and why. In cooperation with the Work in America Institute, CED has conducted a survey of its own trustee companies and other firms that are carrying out many of the types of efforts called for in this statement. The results of this survey are contained in *Training and Jobs Programs in Action: Case Studies in Private Sector Initiatives for the Hard-to-Employ*, which is being issued with this statement.

Achieving high employment has long been a national goal. Yet after more than two years of recovery from the nation's worst post-war recession, unemployment rates remain distressingly high.

Over the years, the basic response to high unemployment has been to develop a set of fiscal and monetary policies that can promote a vigorous and sustained demand expansion without causing undue inflation. Yet both business and government are coming to realize that while fiscal and monetary policies and other sound economic policies are essential, special measures are needed to deal with the growing problem of structural unemployment—the kind of unemployment that even in the best of times affects the undereducated, the unskilled, and those who are considered too young or too old, or who are subject to discrimination.

This statement by the CED Research and Policy Committee focuses on ways of overcoming unemployment and underemployment for those groups that typically experience high or prolonged joblessness. From the beginning of this project, we have felt that finding ways to deal with structural unemployment is vital to achieving the longer-term goal of high employment without inflation.

A Practical Approach. One of our major conclusions was that unemployment and underemployment are both costly to society and to the economy. Therefore we believe that the kind of steps we recommend are not only good social policy, but also good business. In addition, we agreed that the principal stress of public policy should be on developing productive jobs rather than on paying people for not working.

Although there is an important role for government in the employment picture, it is the private sector that provides most of the jobs in the American economy. Therefore, the statement calls for increased training and job opportunities in the private sector and stepped-up transition of the hard-to-employ from government income support and subsidized jobs into permanent private employment.

Expanded private sector efforts should not be limited to large corporate employers, but should take advantage of the many opportunities to be found among small businesses.

New Directions for the Private Sector. Both business and government have gained valuable lessons from the training and jobs efforts of the last decade. During the 1960's many programs were hastily conceived —often in response to various forms of social unrest.

The country has now moved beyond this crisis atmosphere, and there are already many private sector programs throughout the country that are meeting both the needs of business and the hard-to-employ.

The Importance of Work. The subcommittee that prepared this policy statement was also concerned with a concept of work that goes beyond simply being a source of income. Work and the work ethic have intrinsic benefits—to the individual and to society. Work provides a point of identification, a source of self esteem, and a vital part of most people's system of values.

Because of the importance of work, we were also concerned with the social and economic consequences of separating millions of people from productive jobs. In addition to the personal desperation and frustration that stems from unemployment, there are major economic costs in terms of lost output, waste of human and capital resources, and support of an ever increasing number of nonworkers.

While no firm should be asked to make special efforts if it would jeopardize their efficiency, we see several strong indications that both business and society will benefit from an increased private sector commitment to training and hiring the hard-to-employ.

As the economy grows, there will be an increasing need for skilled workers. This need will be even greater if, as population trends suggest, the work force grows more slowly than in the past.

There is also a growing awareness on the part of government that the private sector should play a larger training and employment role and a growing concern over the inflationary impact of broadening the scope of public sector programs.

No one policy or set of programs will work for all businesses. What is needed instead are increased options and incentives for businesses, unions, and profit and nonprofit organizations to enlarge employment and training programs for groups that face special difficulties.

Acknowledgements. The CED subcommittee that prepared this statement brought together an extraordinary range of talents, interests, and experience. The list of subcommittee members appears on page
The subcommittee benefited greatly from the skilled and persuasive leadership of its chairman John L. Burns, former president of RCA and former board chairman and chief executive officer of Cities Service Company.

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We also wish to extend special thanks to project director Frank W. Schiff, vice president and chief economist of CED, for providing a clear and incisive approach to this complex issue.

We are indebted to the Edna McConnell Clark Foundation for the generous support which has allowed us to produce this statement. We are especially grateful for the Foundation's support of a program of information and education activities which will enable CED to conduct a series of policy forums on this subject in areas of the country where structural unemployment is especially severe.

Franklin A. Lindsay, *Chairman*
Research and Policy Committee

Chapter 1
Introduction and Summary of Major Recommendations

AMERICANS HAVE LONG CONSIDERED it a basic goal to have the opportunity to work, to earn a decent living, and to provide for their families. For the vast majority of adults, what they do to earn that living constitutes a vital part of their identity and sense of values.

Yet, the United States has within its population a growing number of people with special burdens that keep them out of the mainstream of the labor force. Most jobs in this country are designed for prime-age, full-time, socially disciplined workers. However, there are large groups of people in this country who want to work but cannot obtain useful jobs, even in relatively good times, because they

- are undereducated, unskilled, or inexperienced
- are considered too young or too old
- are unable to work full time
- are subject to discrimination or restrictive labor market practices
- lack the basic work disciplines and abilities necessary to get and hold a steady job

For the past thirty years, high employment has been a major goal of the nation's economic policy. But except during wartime, this goal has rarely been achieved. During recent years, in fact, the official unemployment rate reached its highest level since the Great Depression. In the first eleven months of 1977, the average number of unemployed still amounted to 6.9 million persons, or 7.1 percent of the civilian labor force.

We believe that this country must make a strong national commitment to high employment and to a situation in which the number of job openings essentially matches the number of those seeking jobs at reasonable wages and in which people able and willing to work have adequate opportunities to be trained and guided toward suitable job vacancies within a reasonable period of time. This commitment must, of course, be pursued in a manner consistent with the nation's other major economic and social objectives, especially the need to curtail inflation.

The primary means of developing adequate training and job opportunities is through strengthening the demand for goods and services in the economy as a whole and in particular sectors and regions.*

A vigorous and sustained demand expansion is necessary to overcome *cyclical* joblessness (which stems primarily from an overall deficiency in demand). It is also the single most effective means of reducing *structural unemployment* which affects particular groups of job seekers because their educations, skills, or locations do not readily match available jobs or because they are handicapped by discrimination and other labor market barriers. However, experience has shown that by itself, a demand expansion strong enough to result in a dramatic rise in jobs for the hard-to-employ is also likely to create serious inflationary pressures.

But the tasks of achieving sustained high employment and conquering inflation are not mutually exclusive. They can and must be attacked simultaneously. Therefore, any steps toward healthy demand expansion need to be accompanied by a range of measures to make the economy less inflation-prone. These should include steps to increase its competitiveness and efficiency, to eliminate restrictive practices in product and labor markets and to enlarge capacity and supply availability.

In earlier policy statements, CED has dealt extensively with ways to improve overall demand management, strengthen economic efficiency and investment incentives, and fight inflation. We are continuing active studies in all these areas. In addition, our new study *Revitalizing America's Cities* is examining the massive problems of the nation's urban centers, including the plight of the deteriorated inner cities, where unemployment is highest. We will explore ways to create the conditions that might bring needed

*See memorandum by R. STEWART RAUCH, JR., page 88 jobs back to these areas and, where necessary, to help bring inner-city residents to suitable jobs in other locations. In other studies, we shall examine means of averting or overcoming the special unemployment problems caused by such factors as unfair foreign trade competition and excessive government regulation.

In this policy statement, we are primarily concerned with the urgent need for a wide variety of measures to cope *directly* with the structural unemployment problems of those groups that have consistently had special difficulties in the labor market—particularly the young, the old, and the disadvantaged—and to increase incentives for productive work.

Unfortunately, there is no single solution or major policy program that can eliminate unemployment for all these chronically affected groups. What is needed instead is an integrated set of public and private actions that will benefit groups and areas of the economy with particularly severe unemployment problems without aggravating the existing inflation.

Government programs to train and provide jobs for the hard-to-employ, including public-service employment, must continue to play a major role in national manpower policy.* We welcome the recent increased emphasis by both Congress and the Administration on direct measures to deal with the unemployment problems of hard-hit groups, particularly disadvantaged youths and veterans.

However, four out of five jobs in the United States are in the private sector. A stronger private-public partnership must be developed to increase training and job opportunities in that sector and to speed the transition of the hard-to-employ from government income support and subsidized public or private jobs to permanent private employment. Key ways in which this can best be accomplished are the focus of this study. In particular, we recommend the following measures:

- **New and expanded use on a nationwide basis of private-sector programs that already work effectively and creation of a clearinghouse for disseminating information about successful and innovative programs** (see Chapter 4)

- **Stronger organizational mechanisms to mobilize private-sector involvement** (see Chapter 4), including much wider use of

  —direct government manpower contracts with private nonprofit organizations created by consortia of business firms

*See memorandum by HENRY B. SCHACHT, page 88

—other types of intermediary organizations that can help business handle job development, training, and placement activities
—jobs corporations to provide training and jobs for the hardest-to-employ
—cooperative community efforts, involving businesses, nonprofit organizations, unions, schools, and governments, to increase training and job opportunities

● **Increased incentives and reduced disincentives for private employment of the hard-to-employ,** including additional experimentation with categorical tax credits, stipends for trainees and apprentices, selective exemptions from the minimum wage, and increased social security earnings ceilings (see Chapter 4)

● **Improved approaches to the problems of particular groups among the hard-to-employ** (see Chapter 5), including

—increased stress on business involvement in skill training and upgrading of the disadvantaged
—an improved transition from school to work for youths as well as other age-groups, including increased use of apprenticeship and cooperative education programs
—more productive use of midcareer and older workers, including steps to smooth the transition from regular work to retirement
—increased and wider use of alternative work patterns to make more employment available to the young, old, and other workers who cannot conform to a full-time work schedule

● **Greater business use of alternatives to outright layoffs in recessions,** including skill upgrading and work sharing (see Chapter 5)

● **Improved management and closer integration of government programs that facilitate the employment of the hard-to-employ,** particularly the U.S. Employment Service and the Comprehensive Employment and Training Act (CETA) programs (see Chapter 6)

This agenda for action is neither impractical nor visionary. In fact, many businesses, nonprofit organizations, and governments throughout the country are currently carrying out many such programs that are increasing training and job opportunities for the hard-to-employ. In connection with this policy statement, CED has surveyed its own trustees' companies and other firms and has found numerous instances of successful private-sector programs and constructive business-government cooperation. Examples of these programs are cited in Chapters 4 and 5. We will publish fuller descriptions of close to 60 private-sector programs in a companion volume of case studies.

These and other successful programs can and should serve as models for more action and innovation by both large and small businesses and for more active business-government-community cooperation. Focusing attention on these programs should also help government agencies and civil servants to be more receptive to such initiatives.

To be fully effective, the approaches that we recommend in this statement must be paralleled by continuing strong efforts to overcome the barriers to employment and career advancement that are the result of discrimination. For example, even the best skill-training program for the hard-to-employ is of little use if those who complete it are refused jobs because of their race, sex, or age. There is also a major need for identifying and changing various existing legislative requirements, government regulations, and union or business practices that tend to discourage employment of the disadvantaged and other hard-to-employ groups.*

There have been suggestions that the nation can learn to live with unemployment and can simply give income support to those who are poorly equipped to compete for available jobs. However, we believe that this country cannot justifiably deny its citizens the opportunity to work for an adequate income and to be free from the desperation and frustration that frequent or long-term unemployment can bring. Nor can the country ignore the huge economic and social costs of goods not produced and services not rendered and the truly enormous costs of supporting an increasing number of nonworkers. In the long term, such wasteful use of resources is likely to add to rather than curtail inflation.

Both government and business must acknowledge these costs and begin to break down the barriers that separate millions of people from productive work. In doing so, they will find, we believe, that most people want to work, that most of the unemployed are employable, and that most of the untrained are trainable.

*See memorandum by JAMES Q. RIORDAN, page 88

Chapter 2
The Dimensions and Costs of Unemployment

To many people, it seems paradoxical that this country is experiencing high and continuous unemployment at a time when the total number of jobs is increasing at near-record rates and when in various areas and occupations the number of job vacancies apparently exceeds the number of job seekers. The fact is that today's unemployment is not the result of an absolute reduction in the total number of jobs, as had been true during the recent business downturn. Indeed, the proportion of Americans working today is actually somewhat higher than it was a decade ago. But the number of persons seeking work has risen even faster than the number of available jobs over the decade, and the rate of unemployment is now almost double what it was ten years ago (see Figure 1 and "Changing Character of the Labor Force").

Why is it so difficult to attain high employment? One reason is that the traditional remedy of creating jobs by expanding total demand through fiscal and monetary policies cannot be pushed beyond a certain point without creating serious inflationary pressures. Such inflation would not only be harmful by itself but could also serve to worsen the unemployment problem. Equally important, however, is the fact that traditional remedies alone cannot adequately resolve the unemployment problems of many groups that typically experience unusually high or prolonged levels of joblessness: the young, the old, and the disadvantaged, especially blacks and members of other minority groups living in inner cities.

WHO ARE THE UNEMPLOYED?

In 1976, an average of 7.3 million persons, or 7.7 percent of the civilian labor force, was out of work each month. Over 20 million persons experienced unemployment sometime during the year. Many were jobless for a relatively short time; close to 40 percent were unemployed for less than five weeks. However, 32 percent of the total suffered extended periods of joblessness (fifteen weeks or more), compared with 24 percent in 1972.

The official unemployment totals provide only a partial indication of the real extent of unemployment. Not counted in the overall number for 1976 were 910,000 discouraged workers who wanted a job but were not looking for one because they believed that none was available. It is also noteworthy that in 1975 over 4 million persons were employed full time but their income remained below the poverty level.

Heads of households, the group that the public usually associates with high unemployment, constituted less than 40 percent of the total unemployed in 1976. The 5.1 percent unemployment rate for this group was far lower than the national average.

For some groups and regions, however, unemployment has typically been much higher than for others (see Figures 2 and 3 and Table 1 of the Appendix).

- Young people (16 to 24 years of age) accounted for close to half of the total unemployed in 1976, even though they constituted less than a quarter of the labor force. The unemployment rate for 16- to 19-year-olds was 19 percent; for 20- to 24-year-olds, it was 12 percent.

- The 1976 unemployment rate for nonwhites (13.1 percent) was almost twice as high as that for whites (7 percent), roughly the same differential that has prevailed for over two decades.

- Less educated workers and those with limited skills suffered particularly high rates of unemployment. High school dropouts had an unemployment rate of 32.9 percent in 1975. In some inner cities, the

Figure 1. **Although the employed proportion of the U.S. population is higher today than it was ten years ago, the unemployment rate has almost doubled, and the number of persons looking for work has risen much faster than the number of available jobs.**

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unemployment rate for dropouts was reported to be as high as 60 percent.

- The unemployment rate in 1976 for adult women (7.4 percent) was significantly higher than that for adult men (5.9 percent).

- Unemployment was far higher in some cities and areas than in others. In 1976, the central cities of Detroit and Saint Louis had unemployment rates of 13.1 percent and 12.8 percent, respectively, compared with the national average of 7.7 percent.

Although the unemployment rates for older workers were lower than the average, these workers tended to be out of work for a much longer time (see Figure 4). Also—and this is not adequately reflected in the statistics—a significant number of older workers would like to work but have been pressed into early retirement. Moreover, the number of discouraged workers among both older workers and nonwhites tends to be particularly high.

Unemployment problems are multiplied when a person belongs to more than one high-unemployment-risk category. Unemployment among black teen-agers was close to 40 percent in 1976, and the percentage was even higher for black teen-agers living in inner cities.

A major factor complicating the U.S. unemployment problem is the presence and continuing inflow of a large number of illegal immigrants. Estimates of the number of illegal aliens in this country vary greatly, but the total clearly comes to several million. Some recent estimates have placed it at over 8 million.[1] Illegal aliens are often in direct competition

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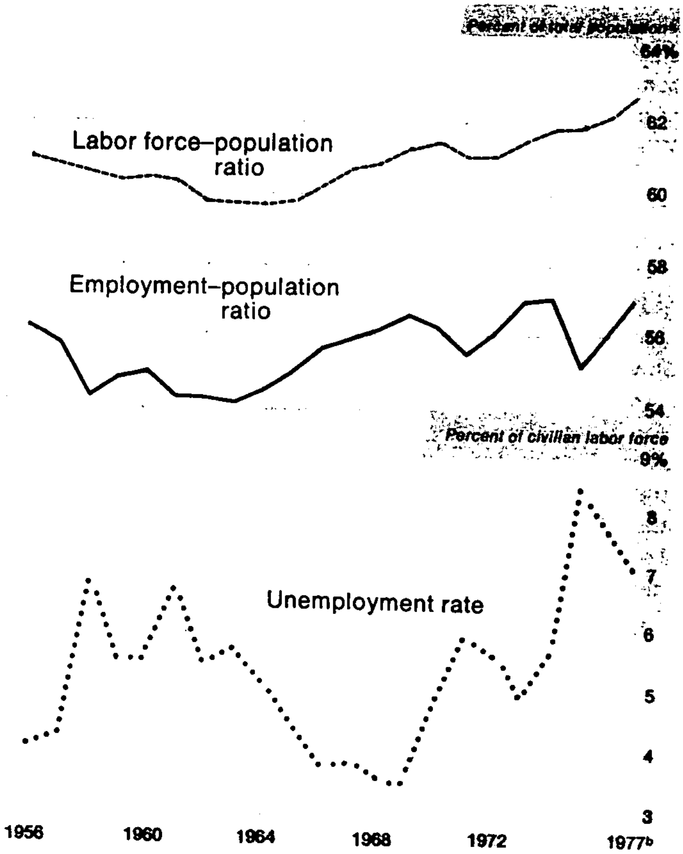
1./ For more detailed discussions, see National Council on Employment Policy, *Illegal Aliens: An Assessment of the Issues* (October 1976), and Economic Development Council of New York, *The Illegal Alien and the Economy* (April 1977).

Employment-Population Ratio and Unemployment Rate, 1956 to 1977



[a] Excludes persons under 16 years of age and inmates of institutions (prisons, hospitals, and mental institutions).
[b] Average for the first eleven months of 1977.
Sources: Department of Labor, *Employment and Training Report of the President* (1977) and *Employment and Earnings* (various issues).

Figure 2. For some groups, unemployment in the last twenty years has consistently been much higher than it has for others—in good times as well as bad. The unemployment rate for white teen-agers has remained three to four times as high as the rate for male adults, and the unemployment rate for black teen-agers has been approximately double the rate for white teen-agers. The jobless rate for adult women has also been persistently higher than that for adult males.

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with the most disadvantaged groups in the regular U.S. labor force for unskilled and low-skill jobs. Partly because of their illegal status, many are willing to accept working conditions and pay not acceptable to legal residents, and employers hiring illegals can often avoid payment of payroll taxes for such workers.

In our view, the illegal alien problem and its relation to unemployment have by now reached such serious proportions that they call for priority attention and action by both government and the private sector. **We urge that a major effort be undertaken promptly to obtain more accurate information regarding the size of the illegal alien problem and to develop remedial steps, such as use of universal social security cards and stronger penalties for employers who knowingly hire illegal aliens.***

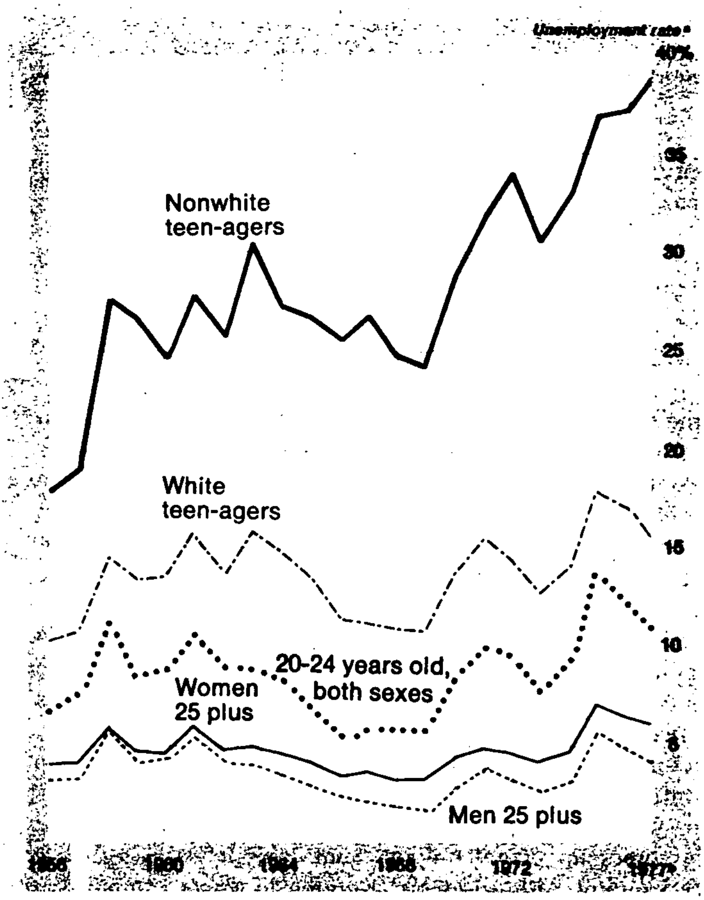
THE CHANGING CHARACTER OF THE LABOR FORCE

Future employment strategies must take careful account of the changing character of the labor force during the next ten to fifteen years. (See Appendix, Tables 2, 3, and 4 for the latest Census–Bureau of Labor Statistics projections of population trends and labor force participation rates and the resultant percent distribution of the labor force according to age and sex.)

Nearly two-thirds of the growth of the labor force over the last decade reflected the large number of women and youths entering the job market. For example, 16- to 24-year olds, represented approximately 24 percent of the labor force in 1976, compared with 17 percent in 1960.

*See memorandum by W. D. EBERLE, page 89

Unemployment Rate, by Age and Sex, 1956 to 1977



a Unemployed in group as percent of civilian labor force.

b Average for the first eleven months of 1977.

Sources: Department of Labor, *Employment and Training Report of the President* (1977) and *Employment and Earnings* (various issues).

Moreover, women constituted 40 percent of the labor force in 1976, compared with 33 percent in 1960.

But this does not mean (as is often mistakenly assumed) that women and teen-agers account for most of the recent *rise* in joblessness. On the contrary, the increase in unemployment associated with the recent recession was most pronounced among adult men and heads of families. Although unemployment rates for these groups are still far higher than at the prerecession peak, these are also the groups that will be more readily absorbed into the work force as the recovery progresses.

In the next ten to fifteen years, labor force growth will be concentrated in the prime-age groups, as persons born during the postwar baby boom move from their teens into their twenties. Thus, although the importance of teen-agers in the labor force will decline only gradually through 1980, it will fall in both percentage and absolute terms by 1990, when they will represent only 6.7 percent of the labor force, compared with 9.5 percent in 1976.

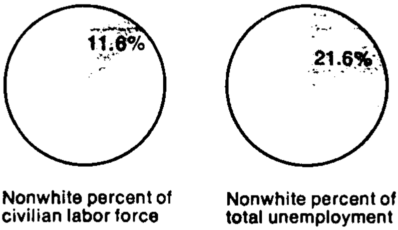
A second major trend will be a continued upturn in the labor force participation of women. According to the projections issued by the Bureau of Labor Statistics in December 1976, the rate of female labor force participation can be expected to increase from 47 percent in 1976 to 52 percent by 1990. In recent months, the rise in this rate has substantially exceeded the projected trend, and it seems quite possible that female participation rates will prove to be considerably higher by 1980 and 1990 than current official projections indicate.

A third factor will be the changing role of older workers. The share of persons aged 65 and over in the total population will continue to rise through 1990. Partly because of the trend toward early retirement, the recent Bureau of Labor Statistics projections indicated that labor force participation rates of workers 55 and older will decline significantly, particularly among men. However, the pending 1977 legislation that would prohibit mandatory retirement before age 70 for most workers could modify this projected decline.

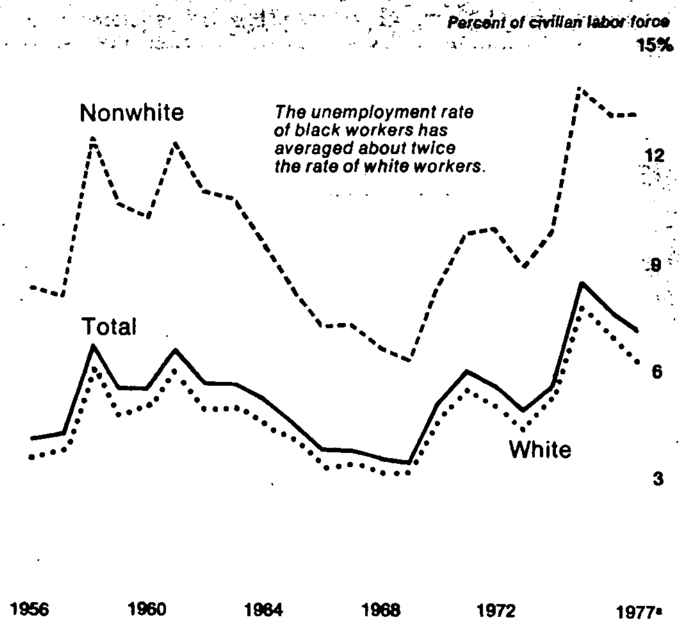
In general, current trends suggest that the coming decade's labor force is likely to be more stable and probably more productive because a larger percentage of the total labor force will become concentrated in the prime age-groups, which have relatively regular attachment to the labor market. These developments may make it easier to achieve somewhat lower overall unemployment rates with given levels of capacity utilization and rates of economic expansion than has been the case in recent years.

Nevertheless, serious problems remain. The percentage of teen-agers

Figure 3: Unemployment Rate, by Race, 1956 to 1977



Although black workers currently make up 11.6 percent of the labor force, they account for 21.6 percent of the unemployed.



[a] Average for the first eleven months of 1977.

Sources: Department of Labor. *Employment and Training Report of the President* (1977) and *Employment and Earnings* (various issues).

Figure 4. Older workers have lower overall rates of recorded unemployment than other age-groups. However, they include a higher percentage of persons who want a job but are too discouraged to look for work and are not counted as unemployed. Furthermore, when older workers become unemployed, they tend to remain jobless longer than other age-groups.

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in the economy is not expected to drop significantly during the remainder of the decade, and projections indicate that the percentage of nonwhite teen-agers will not drop at all during the next ten years. At the same time, the fact that after 1980 there will be fewer young entrants into the labor force increases the possibility of future shortages of skilled workers. These statistics also raise troubling questions about whether this society may seriously underutilize the productive resources represented by older workers.

THE COSTS OF UNEMPLOYMENT: HOW SERIOUS?

Although there is a widespread consensus that current unemployment levels are too high, there are different views of how severe unemployment is and by how much it can and should be reduced. However, the full costs of unemployment, not only to the individuals affected but also to all sectors of the economy and society, are often not taken into account.

Economic Hardship. For many, joblessness means serious hardships and deprivation, not only in terms of foregone income but also in terms of lost skills, self-respect, and general physical and emotional well-being.

However, the degree of hardship caused by unemployment can vary widely. For example, there is a difference between the hardships experienced by an unemployed worker who is permanently laid off and by one who expects to be recalled within a relatively short period, particularly if his income is almost fully protected by regular and supplemental unemployment benefits. Similarly, very different problems are faced by the unemployed head of a low-income family and by teen-agers or other secondary wage earners, particularly those from families with above-average incomes.

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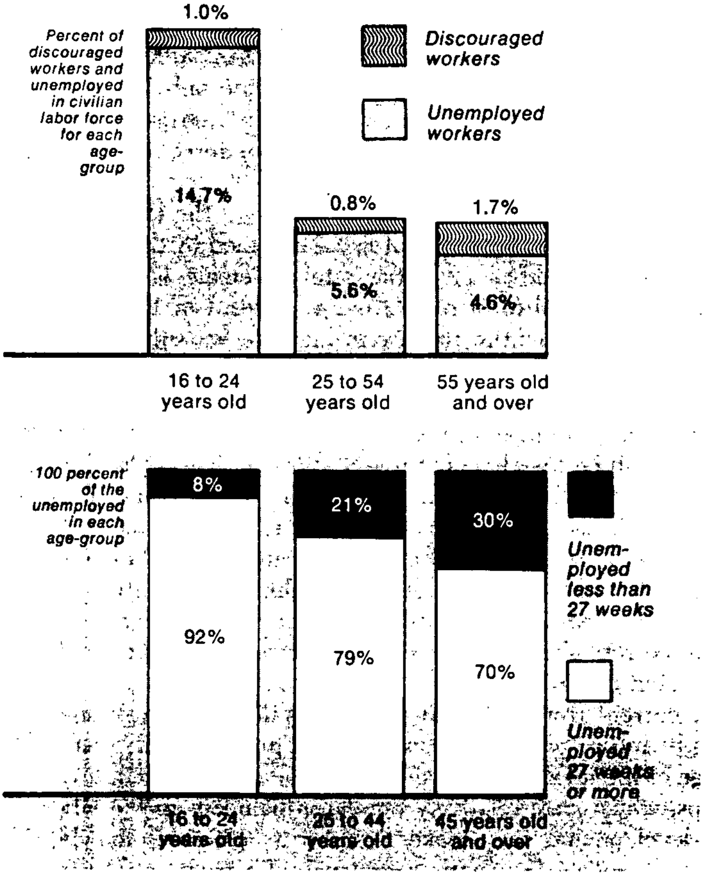
Characteristics of Older Unemployed Workers, in 1976



Source: Department of Labor, *Employment and Training Report of the President* (1977).

THE UNEVEN RECOVERY AND THE PROBLEM OF BLACK UNEMPLOYMENT

A striking feature of the economic recovery since the recession trough of [redacted] MARCH 1975 is that the net reduction in unemployment has been largely due to reemployment of experienced workers in the prime age-groups. For these workers, unemployment had been cut by about one-half by mid-1977. In contrast, there has been little net change in unemployment levels for new entrants or reentrants into the labor force (primarily teen-agers and women). Moreover, reemployment has been lagging for laid-off minority members and workers over 40. In previous periods of upswing, new entrants and other marginal labor force groups were also usually by-passed in the first several years of the recovery (or at least until the expansion became vigorous enough to move the economy closer to capacity levels). But this pattern seems to be more pronounced in the current expansion.

The situation is most serious for black Americans, especially black teen-agers. In November 1977, the black unemployment rate of 13.8 percent was only about ½ percentage point below its 1975 recession peak; whereas the white unemployment rate (6 percent) was more than 2 per-

For many, the extent of hardship associated with a given overall unemployment rate today is less severe than it was ten or twenty years ago. A significantly higher percentage of the labor force consists of teen-agers and adults from two-income families, many of whom are less dependent on full-time employment than heads of households. In fact, more than one-half of today's unemployed come from families that have one or more members with a full-time job. Another major change is the marked improvement in the amount and coverage of unemployment insurance benefits and the dramatic rise in federal income-security transfer payments.

Although these changes have been significant, unemployment still causes considerable hardship. For example, by no means all unemployment of teen-agers and women can be regarded as of secondary importance. About one-fourth of the women in the labor force are heads of centage points below its record 1975 high. Black teen-age unemployment stood at 39.0 percent, compared with white teen-age joblessness (14.5 percent). This also constituted a widening of the black-white unemployment gap since 1975. A number of factors contributed to these developments: The working-age black population is expanding at a much more rapid pace than the comparable white population. As economic conditions have improved, many blacks who had previously been too discouraged to look for work have started to enter the labor market. Black employment has grown much more slowly than white employment.

In part, this slower employment growth reflects the fact that the largest employment gains in the current recovery have been in industries with a low concentration of black workers. More fundamentally, the disproportionate share of blacks among the unemployed can in large part be traced to the effects of current and past discrimination. As a recent Labor Department study showed, it also reflects the related high concentration of black workers in central cities, where suitable jobs are often unavailable; their disproportionate representation in the nation's poverty areas; their generally lower levels of educational attainment; and their overrepresentation in low-paying, less-skilled jobs.

households, and for many families, regular paychecks for both husband and wife have become a matter of necessity if the family is to maintain its standard of living, particularly at the current high rates of inflation. In coming years, furthermore, more and more women are likely to view regular employment as a basic part of their way of life. In the case of teenagers, it is noteworthy that a sizable proportion of 18- and 19-year-olds is no longer in school. Failure to absorb these youths into productive employment within a reasonable time can do permanent harm to their long-term job prospects. Moreover, for many young people who are still in school, part-time work is often essential to their remaining in school.

A closer look at the unemployment statistics suggests that many of the real hardship cases are concentrated among poor blacks and other low-income families living in inner cities and among those elements in the youth and older populations who have the greatest difficulty coping with work. It is striking that the share of discouraged workers is particularly high among these groups. For example, inclusion of discouraged workers would almost double the unofficial unemployment rate for all nonwhite men and would triple the rate for nonwhite men between the ages of 45 and 54. Among teen-agers, the most serious problems of unemployment are concentrated among lower-income, out-of-school youths who have been jobless for fifteen weeks or more.

Social and Human Costs. Statistics on income losses by no means tell the full story of the human and social damage that frequent or prolonged unemployment can impose. Many of these costs are indirect and may be felt only after considerable delay. Nevertheless, they are very real.

A recent study conducted at the Johns Hopkins School of Hygiene and Public Health shows a strong correlation between higher unemployment rates and increases in mental disorders, heart diseases, alcoholism, homicide rates, and suicide among adults and in infant and maternal mortality. There is also a positive correlation between the rate of unemployment and applications for disability benefits under social security. Although many of the medical problems resulting from increased unemployment can be traced to the stress, uncertainty, and despair of prolonged joblessness, there are also direct effects. For example, because of the loss of medical insurance benefits, unemployed persons tend to postpone the use of health services, which can lead to increased disabilities.

For some groups, prolonged or frequent unemployment can also lead to alienation from many of the values that are basic to the mainstream of American society, including belief in the work ethic and the importance of a regular day's work. This problem is especially serious for many unemployed youths, particularly disadvantaged teen-agers in deteriorated inner cities who have dropped out of school. Such youths may spend their formative years in a setting in which regular jobs are not readily available and in which many of those with whom they come in contact live in a nonwork environment.

Older workers are also seriously affected by high unemployment. This may seem surprising because average unemployment rates are lower for older age-groups than for younger ones. But as we have noted, the duration of unemployment tends to be greater for older workers, and they make up a disproportionate share of the discouraged-worker category.

Of course, the unemployment problems of teen-agers and older workers are not necessarily separate. When older workers become unemployed, their teen-age children may be forced to leave school to seek a job.

MEASURING HARDSHIP

There is no regular official index that can be used to measure the degree of hardship associated with unemployment. However, one attempt to construct this kind of measurement has been made by Sar Levitan and Robert Taggart, who have proposed the use of the Employment and Earnings Inadequacy Index (EEI). This index initially includes all persons now covered in the unemployment total and those wanting a job but not actively seeking work because they believe they cannot find it, persons working part time but looking for full-time work, and those employed family heads and single persons not living with families whose earnings for the previous year have been below the poverty level. The index then excludes from the total those groups among the unemployed that can be assumed to include many people who are not suffering hardship, including all unemployed persons 65 or older, all those under 22 who are going to school, and all individuals who are members of families earning more than the median income. These exclusions are, of course, somewhat arbitrary and are likely to be on the high side. For example, by no means all unemployed persons 65 or older are without hardship. Using this approach, the index shows that in 1975, 13 percent of the labor force was suffering hardship from unemployment or low incomes, compared with the official unemployment rate of 9.1 percent.

Comparable figures are not available for significantly earlier periods. Therefore, the index does not necessarily alter the conclusion that the degree of hardship associated with a given total unemployment figure may have lessened over the past ten to twenty years. However, the index does suggest that the extent of hardship stemming from the combined effects of unemployment and low incomes is still very substantial; it may, in fact, be greater than the official unemployment statistics alone suggest. Moreover, the index highlights the special severity of unemployment and low earnings for nonwhite families. Thus, for black female heads of households, the Employment and Earnings Inadequacy Index amounted to a staggering 56 percent.

Waste of Resources. Even when the potential hardships of unemployment are alleviated by various forms of income maintenance, society suffers a loss in terms of the goods and services that persons who are out of work or underemployed could have produced if they had been adequately employed. Other costs to society arise from a decline of skills and self-confidence through long-term unemployment, reduced training, the loss of tax revenues that would otherwise have resulted from higher output, and the expense of supporting the unemployed. In addition, society suffers major losses in terms of budgetary outlays and deterioration in the quality of life as it tries to cope with the costs imposed by higher levels of crime, illness, alcoholism, family breakup, child abuse, and other social burdens and disorders.

One type of cost involves the loss of output of goods and services when the economy operates below high-employment levels. In the recession year 1975, this loss is estimated to have amounted to about $140 billion (in 1972 dollars) if high employment is associated with an unemployment rate of 5 percent. Also added to this cost in terms of foregone output should be the costs of reduced training and deteriorated skills that are consequences of extended joblessness.

A second measurement of cost focuses on the impact of unemployment on the federal budget in terms of both lost revenues and added expenditures. The Senate Budget Committee has estimated that for each 1 percent increase in the unemployment rate (involving an increase of about 1 million unemployed), the U.S. government lost approximately $12 billion in potential income tax revenue in 1975 and was forced to pay an additional $5 billion for such items as unemployment insurance, Medicaid, food stamps, and welfare. In addition, each 1 percent rise in joblessness was estimated to have added $6 to $7 billion to state and local budget costs through revenue losses and added expenditures. This added up to a total budgetary loss of $22 to $23 billion for each 1 percent rise in the unemployment rate.

The Congressional Budget Office has estimated that in fiscal 1977, federal program outlays for creating employment, increasing worker employability, and providing assistance to the unemployed will total $46.6 billion. This total does not include other federal, state, and local government costs that are indirectly created by unemployment, such as foregone tax revenues and increased expenditures for welfare, food stamps, and Medicaid. Nor does it take into account the added expenses of dealing with increased crime, illness, and other social problems directly correlated with higher unemployment.

Clearly, these numbers provide only a partial indication of the waste of resources caused by unemployment. Eliminating that waste goes beyond measures to secure jobs for the unemployed. The real need is to develop ways to make the most productive use of this country's total work force—of younger as well as older people, of those who could profitably work on a part-time basis, of the unskilled as well as the skilled. Among other things, this calls for eliminating job discrimination based on race, sex, or age; making productive use of persons who are now subject to mandatory retirement but who are able and eager to continue working either full or part time; giving a larger proportion of young people some work experience while they are still in school; and creating part-time or part-year jobs for parents with young children, students, older people, and others who are not able to work full time.

If the nation does not begin to utilize its available labor force more fully and productively, the burden of work will increasingly be imposed on a declining portion of the total population, thus making it more and more difficult for society to bear the growing burden of retirement costs and other social payments.

Unemployment and Inflation. High and persistent unemployment erodes the efficiency and flexibility of the economy. This further cost of unemployment stems from wasteful and inefficient use of human and physical resources as large numbers of persons who are unable to find work or to contribute to society's output have to be supported by society and as many firms are forced to operate below optimum capacity. Moreover, with general slack in the economy, the incentives for investment in both physical and human capital are reduced, and existing skills atrophy. Thus, the economy's ability to produce more during any future period of stronger demand will be handicapped, the risks of capacity and skill bottlenecks in particular areas and industries will be heightened, and inflationary price rises may be triggered more quickly.

The fear of unemployment also promotes uneconomic practices that add to costs and this may generate further unemployment. Attempts by different groups to protect themselves against possible job losses often result in protectionist trade policies, restrictive labor-union practices, and resistance to the introduction of improved production processes. Moreover, the secondary effects of unemployment in the form of increased illness, crime, and social conflict can add significantly to living costs by raising insurance rates and causing retailers to mark up their prices.

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Over shorter periods, increased cyclical unemployment can limit wage demands to some extent and enable some firms to operate more efficiently by eliminating less needed positions. Even when these factors do exert a short-term anti-inflationary influence, however, the immediate benefits must be weighed against the longer-run adverse effects of unemployment on investment, skills, and overall economic productivity.

Appropriately expansive demand-management policies (i.e., fiscal and monetary policies that affect total demand) are, of course, central to any strategy for vigorous and enduring economic growth. However, past experience has made it painfully clear that *exclusive* reliance on strongly expansive demand-management policies to stimulate growth and overcome unemployment is apt to produce high or even accelerating rates of inflation. Properly designed demand policies must be combined with a wide range of other programs in order to improve the likelihood that increased demand will lead to higher employment and output rather than to more rapidly rising prices. The main elements of such a multipronged strategy to achieve high employment without inflation will be examined in Chapter 3.

Chapter 3
An Integrated Employment Strategy

WE BELIEVE THAT CED's long-held goal of achieving noninflationary high employment must be neither modified nor abandoned. Pursuit of that goal is not only sound economics and humane social policy but also good business. *Today more than ever, there is a need for a strong national commitment to high employment that will make it possible for all those who are willing and able to work to find suitable jobs at reasonable wages within a reasonable period of time.*

Adequate job-vacancy statistics that would make it possible to measure progress toward high employment as defined in this statement are not now available. We urge that more intensive efforts be devoted to exploring the feasibility and specific means of developing adequate data in this area and that the newly appointed National Commission on Employment and Unemployment Statistics include this matter as a priority item on its agenda.

SETTING TARGETS

High employment cannot be achieved overnight. Interim targets need to be set to assure adequate progress toward the high-employment goal. **Interim high-employment targets and the choice of policies for achieving them should be developed in conjunction with appropriate targets for reducing inflation.** The tasks of achieving high employment and conquering inflation are not mutually exclusive. They can and must be attacked simultaneously.

Because of the changing character and composition of the labor force and the unemployed, interim high-employment goals should not be expressed in terms of a single national unemployment rate. **We endorse the recent recommendation of the National Commission for Manpower Policy that at least three measures be used to assess the nation's progress toward high employment: the overall unemployment rate, the net change in the number of employed persons, and changes in the unemployment rates of the disadvantaged and other groups that typically experience unusually high unemployment.**

As more specific targets, we endorse the commission's suggested rate of job formation in the range of 2.5 million persons a year between now and 1980, a lowering of the overall national unemployment rate to 5 percent by the end of 1980, and a substantially more rapid reduction of unemployment rates than in past recovery periods for those segments of the labor force that tend to experience particularly difficult problems in the labor markets. We believe that these goals are both desirable and attainable *provided* they are pursued as part of a forceful and integrated overall strategy to combat both unemployment and inflation.

ELEMENTS OF POLICY STRATEGY

Expanding Demand. The single most effective means of reducing unemployment is a strong economy. This Committee has long been committed to appropriate demand-management policies that aim at steady but vigorous economic growth to achieve high employment. We reject prescriptions for using massive unemployment or chronic stagnation as a means of combating inflation. Such a course inhibits adequate capital formation, weakens productivity growth, and results in large-scale waste of human skills and resources. It is counterproductive over the long run.

Measures to expand effective demand must go well beyond the use of general fiscal and monetary policies to expand total spending. Within the constraints of a sound overall budget, they must also include specific sectoral policies for such purposes as revitalizing the nation's cities, rehabilitating deteriorated housing and transportation, and accelerating energy development and conservation. Many of these policies call for more effective basic approaches, rather than simply increasing government outlays. Moreover, in recessions, there is usually need for special government expenditure programs such as countercyclical public-service employment.

A vigorous and sustained demand expansion is not only needed to overcome cyclical joblessness; by and large, it is also the most effective single means of reducing structural unemployment. As labor markets tighten, the incentives for business firms to train and employ the unskilled and disadvantaged increase, the search for available workers becomes more intense, and discrimination becomes more costly. By no means all the structural problems of the more marginal labor force groups disappear as overall demand pressures increase. Nevertheless, past experience has shown that in a briskly growing economy, the scope for finding useful training and jobs for the unskilled, the poorly educated, and other structurally unemployed groups is often much greater than had previously been thought possible.

Anti-Inflation Policies. Unfortunately, the pace of demand expansion that would by itself result in a dramatic reduction in structural unemployment is also likely to create serious inflationary pressures as capacity and supply bottlenecks develop. Such a rapid expansion can also tend to produce skilled labor scarcities and serious cost-push pressures. Accordingly, demand growth should not be pushed to so rapid a pace.

To maximize the scope for demand expansion without intensified inflation, a wide range of policy measures should be used to improve the functioning of the market system, enlarge capacity and supply availability, and generally make the economy less inflation-prone. Such policies include tax and related measures to stimulate more capital investment, steps to anticipate and avert materials and skill bottlenecks, and measures to increase productivity and competitiveness.

Even if relatively vigorous demand expansion is accompanied by specific anti-inflation measures, it does not seem likely that these policies could *by themselves* reduce the overall unemployment rate to less than 5 to 5½ percent by the end of this decade without producing intensified inflation.[2] That prospect creates a major need for combining such policies

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2./ The situation described here is sometimes interpreted to mean that there is no way in which unemployment can be reduced below 5 to 6 percent without a sharp with more direct approaches for dealing with structural unemployment.

Direct Measures for Attacking Structural Unemployment. A third component of the needed policy strategy, therefore, is the use of a wide range of public and private measures specifically designed to deal with the unemployment problems of particular groups and to strengthen incentives for productive work. Such a targeted approach is needed to achieve major reductions in the chronic unemployment of groups that cannot be adequately reached by other means. Furthermore, by concentrating on high-unemployment sectors or areas in which the risks of inflation are lowest and by raising the productivity of the groups involved, it can also enable the economy to move more vigorously toward noninflationary high employment than would otherwise be possible.

Recent actions by the Administration and Congress have placed greatly increased emphasis on such measures. The new youth employment legislation, in particular, provides a major increase in targeted assistance to youth for training and work experience, and the size of the Job Corps has been doubled. Moreover, the Administration's new welfare reform proposals call for a dramatic increase in welfare clients' incentives to work and for special incentives to do so in the private sector.

The Labor Department has indicated that both the current expansion in subsidized public-service jobs and the projected additional large-scale increase in such jobs under the proposed welfare reform program are to place major focus on new types of jobs to provide needed services to local communities. These are to include improving public safety by patrolling dangerous areas and escorting people through such areas, providing home services and other aid to the elderly and the sick, building and repairing recreational facilities, expanding child-care services, assisting in weatherization of existing low-income housing and in environmental monitoring, and numerous other activities.

We welcome this increased stress on dealing more directly with structural unemployment and the announced emphasis on providing useful work. However, the precise directions that these policies are to take

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acceleration of inflation. This is not necessarily true. As we have noted, the unemployment-inflation relationship can be changed by specific anti-inflation policies aimed at expanding capacity and supply and by measures to reduce structural unemployment. Moreover, changes in the composition of the labor force in coming years, particularly the declining proportion of teen-agers, should tend to lower the unemployment rate at which demand expansion would trigger accelerated inflation.

still need to be clarified. We believe that an effective attack on structural unemployment problems that makes optimum use of both government and private resources should be based on the following general principles:

1. Policy solutions should be carefully tailored to the character of the groups, regions, and problems involved. In particular, a clearer distinction should be made between programs designed to overcome temporary cyclical unemployment and those directed at longer-term structural problems.

2. Government policies should provide for an equitable sharing of employment and training opportunities among different target groups. Greater efforts need to be devoted to developing employment-creating strategies for individual groups, particularly teen-agers and older workers, that are complementary and mutually reinforcing rather than competitive. In cases where competition does occur, priorities should be determined in a fair and carefully considered manner.

3. The principal emphasis of public policies to deal with the unemployment problems of those who are able to work should be on providing useful job and training opportunities rather than on paying people for not working.

4. There should be a substantially greater effort to find or create these added training and job opportunities in the private sector, both profit and nonprofit. Although special public-sector training and employment programs must continue to be a substantial component of the efforts to overcome unemployment, the eventual aim of such programs is to move a high proportion of the persons covered into regular private employment. Direct placement of the unemployed in the private sector avoids the need for such a shift.

5. A range of additional incentives should be developed to help the private sector provide such opportunities, and disincentives should be eliminated.

6. Particular stress should be placed on intensified training of the disadvantaged for job vacancies that already exist.

7. There is a special need for enlarging training and employment in the small business sector. Public policies to deal with unemployment have underemphasized this sector. Yet, small businesses account for about one-half of private-sector employment covered by social security[3] and play a particularly important role in many service industries, in which the potential for added employment of the young, old, and disadvantaged is especially high.

8. Public and business policies should be designed to respond to the needs and capacities of unemployed *individuals* as well as to the various groupings in which they are classified.

3./ This estimate applies if the small business sector is defined as including those firms with 100 employees or less. Firms with 500 employees or less constitute about three-fourths of private employment covered by social security.

Chapter 4
Toward a Stronger Private-Public Partnership: Enlarging the Private Sector's Role

WITHIN THE STRATEGY PACKAGE outlined in Chapter 3, a key feature should be the enhancement of the role of the private sector. This will require some changes in approach. The federal budget for 1977–78 provides for a substantial expansion in training and job assistance targeted to the hard-to-employ, particularly youth and the disadvantaged. However, of the total $11 billion budget program devoted to employment and training in fiscal 1978, less than 10 percent is scheduled to be devoted directly to private-sector programs. We believe that this proportion should be significantly enlarged.

THE IMPROVING CLIMATE FOR PRIVATE-SECTOR INVOLVEMENT

Greater reliance on the private sector will not be easy to achieve. Partly because of the recent deep recession, total private-sector involvement in special training and employment programs for severely disadvantaged groups is much less today than it had been in the late 1960s and early 1970s. When private firms are forced to lay off part of their regular work force, they usually have little opportunity or inclination to provide extra training and jobs for groups that they are reluctant to employ in more normal times. But other factors also contributed to lagging private support for special training and job programs, including concern that these activities were imposing an undue burden on the firms' regular profit-making operations, disappointments with particular program results, and impatience with the red tape and lack of stability in funding and management frequently connected with federally assisted private programs.

We strongly agree that individual firms should not be asked to create training and job opportunities for special groups if this jeopardizes their efficient functioning. But for a number of reasons, *we also believe that the time is ripe for significantly increased private involvement in such activities in ways that will be sound business practice as well as good public policy.* These reasons include the following:

- If the economy is able to maintain a healthy rate of expansion, business will be in a much better position than it was in the recent period of severe recession to provide special assistance to youths, older workers, and the disadvantaged.

- Both business and government have gained valuable lessons from the experience with special training and placement efforts in the last decade and have developed a variety of new approaches that can be used to overcome past difficulties.

- There is increased recognition that the character of structural unemployment problems will be changing over the next five to ten years and that it is in the interest of business itself to search for new types of solutions to deal with these problems. Business is already finding that many skilled jobs remain unfilled. More business firms see the need for a more productive labor force, for helping to avoid further skill bottlenecks, and for providing greater flexibility in work schedules, job design, and retirement arrangements to assist youths, working parents, and older workers.

- There is increased concern that without greater private involvement, the current rapid expansion in public training and employment programs could lead to excessive increases in public-sector employment and spending and add to inflationary risks. At the same time, the feeling is growing that greater reliance on training and

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employment-creating activities in the private sector may in many cases prove to be more efficient and less costly.

- Both the executive branch and Congress are showing increased interest in greater private involvement in special training and employment activities. Numerous special provisions and incentives to facilitate this involvement have been included in recent legislation. In addition, the Administration's proposed welfare reform program provides strong incentives for the placement of welfare recipients in regular private-sector jobs, in part by making it financially more attractive for welfare recipients to accept such jobs rather than specially funded public-service positions.

We do not believe that any one policy prescription or type of incentive to aid the young, old, and disadvantaged will work for all firms or industries or even for different branches of a single firm operating in different parts of the country. Rather, the need is to provide business firms, labor unions, and voluntary agencies with increased *options* to make use of approaches and incentives that will help to enlarge employment and training opportunities for the groups that face special difficulties in the labor market.

PRIVATE-SECTOR APPROACHES AND INCENTIVES: INCREASING THE OPTIONS

New and Expanded Use of Private-Sector Programs that Work. Although *total* private-sector involvement dealing with employment problems has lagged in recent years, there are numerous specific instances of special training and job-creation programs conducted by private firms and nonprofit organizations that are working effectively. Many of these are new and imaginative, and quite a number represent the result of joint efforts by private firms and government manpower programs operating within the CETA framework.

These programs are often small in relation to the size of any one company's total employment, but most are of the type that could be carried out by many other companies in many more communities. *We believe that there would be a substantial increase in the private sector's contribution toward reducing structural unemployment if private programs that already work in some firms and areas were to be adopted on a wider scale nationally and by a much larger number of firms.**

*See memorandum by FRAZAR B. WILDE, page 90

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In Chapter 5, we present a number of more specific recommendations regarding key areas in which substantially wider use of existing private-sector activities could make a very substantial contribution toward solving the special employment problems of youths, older workers, and the disadvantaged. These areas include, in particular:

- Improved transition from education to work

- More productive use of older workers and retirees

- Improved job-readiness preparation, skill training, and upgrading for the disadvantaged

- Better matching of job seekers and job opportunities through greater business support for more effective public and private placement services and through development of more flexible work schedules and job arrangements

- Work sharing and other means of minimizing the volume of unemployment associated with given reductions in business activity during recessions

A major obstacle to wider use of existing private-sector programs is the fact that far too little information about the nature and results of such programs is available to the business community as a whole or to national and local government officials. The volume of case studies that we will publish on the basis of the Subcommittee's survey of CED trustee companies will cover only a part of existing private-sector activities that deserve to be more widely recognized. We believe it would be highly useful if such information could be made available on a broader and more continuous basis. **We recommend establishment of a clearinghouse for information about the character, problems, and success of private-sector programs concerned with assisting those groups in the labor force that have the highest or most persistent rates of unemployment. Such a clearinghouse might best be operated by a private organization but should receive active federal support and funding.**

Stronger Mechanisms for Active Business Participation. A key ingredient in many successful business efforts to increase training and employment opportunities has been active and coordinated support by national and local business leadership groups working closely with local community organizations, labor unions, and government units. Such nationwide organizations as the National Alliance of Businessmen can be a major element in energizing such support. However, some of the most effective cases of private participation have also involved the creation of new types of organizational mechanisms at the local level. Here are four noteworthy examples:

- In Chicago, twenty of the largest companies have combined with twenty leading minority firms and organizations to form Chicago United, which seeks to attack the city's most intractable social problems. The Chicago Alliance of Business Manpower Services (CABMS), a branch of Chicago United, is a private nonprofit organization with a permanent staff that is able to act as a direct contractor for federally financed manpower programs. This organization has been unusually innovative and effective in carrying out a wide variety of activities designed to serve the training and employment needs of marginal groups in the labor force.

- In Oak Ridge, Tennessee, Union Carbide and a group of forty-three Southern colleges and universities have been remarkably successful in jointly operating a technical-skill-training program for unskilled and disadvantaged enrollees and in assuring placement in useful jobs for over 90 percent of the program's graduates.

- With the active support of major business firms and the National Manpower Institute, a network of local education-work councils is being developed in twenty selected communities to facilitate the transition from school to work.

- The Greater Philadelphia Partnership, active since 1974, is a consortium of business leaders that fosters community development and employment in Philadelphia and particularly aids inner-city housing services and supported-work programs for the hardest-to-employ.

We urge leading business firms in communities that have not already formed such special organizations to take the initiative in developing similar cooperative ventures in a form best suited to the circumstances in their individual communites. We also urge national firms that have been leaders in successful programs in their headquarter cities to strongly encourage their local managers to help organize and support similar programs in other areas where the firms have significant operations.

This Committee has been particularly impressed by the potential of direct contracting for training and employment programs with a private nonprofit organization, such as CABMS, that is formed by a coalition of business firms. CABMS currently handles the direct marketing and management of all of the city of Chicago's federally supported on-the-job training (OJT) contracts with private and nonprofit employers. By making direct use of business experience, expertise, and innovation, this arrangement has led to a sharp reduction in the delays and red tape previously involved in awarding OJT contracts (approval time has been cut from several months to ten days), costs of training programs have been cut significantly, a large number of subcontractors (particularly smaller firms) have been brought into the OJT effort, and various innovative approaches to job placement have been developed. (See Chapter 5 for a fuller discussion.)

We recommend that government-assisted training and job programs make substantially greater use of direct contracts with private nonprofit organizations that are organized by consortia of business firms and community groups.

Strengthening Intermediate Organizations. One of the most important ways of increasing private firms' efforts to overcome structural unemployment is greater use of intermediate profit or nonprofit organizations to handle job development, training, and placement activities for groups with special problems in the labor market. For example, Opportunities Industrialization Centers of America, Inc. (OIC), a nonprofit organization founded and run by blacks that operates in forty-seven states, concentrates on skill training and job placement for members of minority groups. A recent study showed that from 1964 to 1975, 350,000 persons received OIC training, 250,000 were placed in jobs, and retention rates in these jobs were relatively high. Other examples include such community-based nonprofit groups as the Urban League; Services, Employment and Redevelopment (SER); the Boys' Club of America; the Vocational Foundation in New York; various organizations that aid the handicapped; and specialized agencies for the placement of older workers. Some profit-making organizations can also perform valuable intermediary functions.

It is clear that many business firms are reluctant to train or hire the disadvantaged *directly*. However, they will often do so if specialized intermediate organizations help them deal with these groups. For many firms, the use of an intermediary organization means that they can be relieved of many troublesome tasks that skill-training and other programs might ordinarily entail; this is particularly important in gaining support for such programs among line managers. Intermediate organizations can be very helpful in dealing with the red tape and complications often involved in government contracting, can concern themselves with the inevitable paper work associated with new hirings of disadvantaged workers, and can furnish needed counseling and support services to the individual trainee. Moreover, they help provide continuity for special training and related programs because they have a self-interest in seeing to it that the programs are effective and gain new funding.

Intermediary organizations can also help private firms increase the ways in which they can help the structurally unemployed. For example, firms that are not willing to directly hire workers with special labor market disabilities can still provide physical facilities for training courses, special transportation, and technical advice. Some firms can specialize in providing technical training under contract while relying on intermediary groups to arrange for the placement of trainees. Other companies are willing to hire a specified number of persons who have graduated from special skill-training programs but prefer not to conduct these programs themselves. Specialized intermediate organizations can also be helpful in mobilizing retirees to assist in private-sector job placement of both youths and older workers. (See Chapter 5 for a fuller discussion of this issue.)

We urge that private business firms as well as government training and employment agencies give strong encouragement to greater reliance on intermediate organizations in efforts to deal with the special problems of youths, older workers, and the disadvantaged, particularly in areas of chronically high unemployment.

Greater Reliance on Jobs Corporations for Dealing with the Hard-to-Employ. In our 1970 policy statement *Training and Jobs for the Urban Poor*, we recommended the experimental introduction of a new form of intermediate nonprofit organization known as a *jobs corporation*. This corporation was designed to provide training and jobs for marginal workers and hard-core unemployed who would become the corporation's "employees" and then be placed in training and public or private employment. A special feature of the proposal was that the corporation would be partly financed by welfare and other public assistance funds that would have had to be spent on the "employees" in the absence of the program. Local management of each corporation was to be entrusted to a board of directors that included business representatives, public personnel officers, labor-union officials, and the representatives of client groups.

Since the publication of that statement, an experimental jobs corporation, the Manpower Demonstration Research Corporation (MDRC), has been established that closely follows the format suggested in the statement. MDRC is a nonprofit organization that oversees supported-work programs in thirteen different locations around the country; it currently employs about 1,900 persons. Its clients are some of the most severely disadvantaged groups in the labor force: ex-addicts, ex-offenders, long-term welfare mothers, and minority youths from low-income families. They are provided with partially subsidized (supported) work, both in the public and in the private sector, into which they are moved under conditions of "graduated stress." In time, they are expected to take on regular full-time jobs. Funding is provided primarily by government agencies and private foundations.

The results of the program (which are further discussed in Chapter 5) have been quite encouraging. An initial analysis of a sample of persons involved in the supported-work program showed that after the first nine months of the program, participants worked more hours, earned more money, and received fewer or smaller welfare payments than a control group of nonparticipants equally eligible for the program. There were additional positive results. Those in the program used drugs and alcohol less frequently and were less often involved in criminal activity.

Questions remain about whether a substantial enlargement of the present relatively small-scale experiment would encounter an equal degree of success. Nevertheless, the known experience with MDRC confirms our belief that the jobs corporation model holds special promise as an organizational mechanism for dealing with the problems of the hard-to-employ and for providing the private sector with greater opportunities to participate constructively in that effort.

One major advantage of this form of organization is that it allows strong focus on the problems of the individual. Employees can be placed in different types of training and employment on the basis of their needs and capabilities. There is a central place to which they can turn for special counseling and other assistance. At the same time, the jobs corporation can take advantage of the shifting economic situation to seek out alternative job opportunities for its clients. For example, as the economy strengthens, workers who had been placed in public employment can be shifted to suitable private job opportunities as more of these open up.

Because of the need for more aggressive efforts to deal with structural unemployment problems in the next few years, we urge a major enlargement of the existing jobs corporation effort. The possibility of

utilizing the jobs corporation format for groups other than the most severely disadvantaged should also be explored.

Legal and administrative changes to provide incentives for private-sector training and employment. As we noted earlier, recent legislation governing federal employment and training assistance contains numerous provisions that encourage wider private-sector participation. For example, part of the funds for public-service employment is to be devoted to socially useful projects that can be carried out by private nonprofit groups. The new youth employment legislation provides for a sizable amount of discretionary funds to be used for innovative programs, including those administered by the private sector. Under the newly launched program, Help through Industry Retraining and Employment (HIRE), federal subsidies are to be provided to create approximately 100,000 private-sector job-training positions over the next eighteen months, mostly for unemployed veterans. The HIRE program is being accompanied by a new national drive to induce large corporations to take on graduates of the program as permanent employees.

Government agencies and private firms should make full use of these increased options for private-sector involvement. **We believe that the volume and scope of federally assisted on-the-job training programs should be expanded through simplification of contract procedures and extension of the HIRE program to a larger number of nonveterans.**

Another possible method of inducing employers to train or hire more of the structurally unemployed is the use of wage subsidies in the form of employment tax credits. Congress recently enacted an incremental employment tax credit that benefits firms which raise their total employment to more than 102 percent of the prior year's level. However, because the total credit is limited to $100,000 per firm, this provision is of assistance mainly to small businesses.

We have strong reservations about the economic merits of the incremental employment tax credit, mainly because of the fact that in an expanding economy, many firms will receive the credit for employees they would have hired in any case. Nevertheless, now that this tax credit has been enacted, we believe that information about its availability should be widely disseminated and that business should support efforts to conduct careful evaluations of the effects of the new approach. Moreover, the federal government should give high priority to economic and operational research regarding the use of other forms of wage subsidies as a means of creating jobs for the hard-to-employ.

Despite our reservations about the *incremental* employment tax credit, we believe that additional experimentation with *categorical* tax credits to subsidize private-sector training and employment is justified. Such credits, which apply only to specified categories of the unemployed, are more likely to add to net employment than incremental credits because they would cover groups not likely to be hired without a subsidy even after the recovery is well on its way. To be sure, there are important disadvantages in using tax credits rather than direct contracts to subsidize jobs, and we continue to favor direct contracts as the primary form of subsidy. Actual experience with one existing categorical tax credit to aid employment, the 20 percent Work Incentive Program (WIN) credit applicable to employment of welfare recipients, has been quite discouraging.

However, given the fact that direct contracts have also had only limited success in the past, we feel that further experimentation with categorical tax credits as an added tool is justified. Such tax credits might be particularly useful for small business firms, and as we have noted, expanding training and job opportunities in the small business sector deserves high priority. Moreover, we believe that improved design of a categorical tax credit may produce better results than those achieved by the WIN program. **Persons eligible for categorical credits should include not only the welfare clients now covered by the Work Incentive Program but also the long-term unemployed and lower-income groups eligible for public-service employment programs. In addition, the credits might be specifically geared to youths and older workers. Experiments might also be conducted to determine whether a higher percentage subsidy of first-year wages and decreasing subsidies in subsequent periods would prove more successful in attracting business participants.**

Reducing disincentives to private-sector training and jobs for the hard-to-employ. Existing laws and regulations contain numerous provisions that inhibit increased private employment for the young, old, and disadvantaged. Some, such as minimum wage laws and social security payroll taxes, reduce employers' demands for labor by increasing labor's price. Others, such as earning restrictions for social security and welfare recipients, hold back the supply of labor.

Before such laws and regulations are modified, however, a number of things should be determined. For example, would a change intended to aid one group cause increased unemployment for another? If so, would the change on balance still benefit the economy as a whole? Would the budget costs involved (if any) be worth the expected benefits? Could the same amount of dollars be more effectively used in a different fashion? The answers to these and related questions will vary depending not only on the type of disincentive involved but also on the basic demographic and economic changes.

With regard to the possible use of a differential minimum wage, for example, this Committee recommended in *Training and Jobs for the Urban Poor* that "some differentiation in [minimum wage] rates be made for the below-20 age group, the aged, and the partially disabled to avoid the real danger that employers will refuse to hire inexperienced or otherwise less productive workers at wages as high as those required for the more experienced and able." Various attempts made since that time to legislate broad-scale differentials of this type have failed. Labor unions, in particular, have been opposed to such provisions because they fear that jobs would be taken away from prime-age workers.

A number of recent studies suggest that a uniform minimum wage does have some adverse effects on the employment of teen-agers, although estimates about the extent of these effects vary considerably. There is also evidence, however, that a lower minimum wage for all teen-agers would lead to some job losses for adults. Because the main increase in new young job seekers in the next few years will come from the 20- to 24-year-old age-group rather than from the teen-age population, the question is raised whether a lower minimum wage for all teen-agers might not draw an undue number of jobs away from 20- to 24-year-olds at the very time when some of the most serious youth unemployment problems are becoming concentrated in that age-group.

For some youths, lower minimum wages already exist. The Labor Department grants about 155,000 to 175,000 exemptions from the minimum wage requirement each year to full-time students who work part time in retail and service establishments and to some other youths who participate in special training programs. The allowable quota for such exemptions is usually not filled. Procedures also exist for exempting apprentices and handicapped workers in regular private industry, but these have been used only on a very small scale. However, a sizable number of handicapped workers can be employed below the minimum wage in federally subsidized sheltered workshops, such as Goodwill Industries. Federal outlays for vocational rehabilitation of handicapped workers came to about $800 million in fiscal 1977.

We believe that before a lower minimum wage is introduced for all teen-agers, older workers, and the partially disabled, there should be additional experimentation with wider use of administrative exemptions

from minimum wage requirements for selected groups and with simplified procedures for granting such exemptions.* We also believe that much more use should be made of stipends for trainees and apprentices that come to less than prevailing wages and may start below the minimum wage but are then progressively raised as the trainees gain the experience and skill needed to move into regular jobs.

Another proposed incentive to employers to hire young people would be to exempt youths under 21 from the required employer and employee contributions to social security. This would result in a payroll tax savings of about 6 percent for the employer and an equivalent increase in take-home pay for the employee. However, it would also produce a sizable loss for the social security system, which is already faced with major financing problems. Moreover, the proposed exemption would benefit many youths from relatively well-to-do backgrounds unless it was restricted to members of low-income families.[4]

More specifically targeted direct wage subsidies or categorical tax credits, such as those discussed in the preceding section, might be a more effective way to increase employer incentives for hiring teen-agers and others in greatest need of special assistance in obtaining regular employment.

In any event, we believe that careful experiments should be undertaken in selected areas to test proposals for increasing incentives for teen-age employment. Because experience has shown that the long-term prospects of disadvantaged teen-agers greatly increase after they have stayed in one job for six months to a year, these experiments should also cover proposals for special incentives during the first critical year on the job. Such proposals could include exempting teen-agers from social security payments during the first year of employment or offering special bonuses and subsidies for remaining in one job for a full year.

Other possible steps involve the relaxation or elimination of the earnings limits applying to social security recipients under age 72. Under the statutory provisions in effect during 1977, a person's social security benefit was reduced by $1 for every $2 earned in excess of $250 a month

4./ Restricting the exemption to low-wage *teen-agers* would not necessarily be appropriate. Recent studies show that the family income of low-wage teen-agers tends to be higher than that of high-wage teen-agers.

5./ In addition to this "implicit tax," the earnings of social security recipients are also subject to regular taxes. As a result, the net take-home pay resulting from extra work

*See memorandum by ROBERT R. NATHAN, page 90

($3,000).[5] For many retirees in need of extra income, however, it would be far more desirable and equitable to earn the added income through productive work. To help deal with this problem, the newly enacted social security legislation provides for a rise in the social security earnings limit for persons between age 65 and age 72 to $4,000 in 1978 and for subsequent annual increases of $500 in the limit until it rises to $6,000 in 1982.

Moreover, starting in 1982, the age at which the earnings limitation no longer applies will be lowered from 72 to 70. However, the new law does not provide for total elimination of the earnings limit. Nevertheless, the issue of total elimination is likely to remain a subject of continuing Congressional and public debate. Such a step, which would benefit the well-to-do as well as the needy, would entail a net cost to the social security system of perhaps $2 to $3 billion a year,[6] requiring a further increase in the combined employer-employee payroll tax if it were to be financed out of current revenues. This may not be the best way to spend several billion dollars in funds collected through the tax system, particularly in view of the fact that some of the added work performed by social security recipients could result in increased unemployment for groups in the labor force that have more urgent needs for jobs.* These issues will be taken up more fully in a projected CED study of retirement reform.

These reservations do not apply to cases where added work by social security recipients could help to overcome skill bottlenecks and other labor shortages. **We reiterate the recommendation made in our 1970 statement *Further Weapons Against Inflation* that consideration be given to raising the ceiling on earnings by social security recipients in cases where such earnings are derived from work in which certified labor shortages exist.** The total current budgetary cost of such a provision would be modest. Moreover, as the economy moves closer to capacity and skill bottlenecks increase, part of or all the extra budget cost is likely to be recouped as the added availability of older workers with needed skills helps to avoid potential inflationary pressures.

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by persons on social security could in some cases turn out to be less than the costs of working, such as transportation and lunch money.

6./ This cost would arise because social security benefits would have to be paid to several million persons over age 65 who work but currently cannot draw benefits because of the earnings limit. However, the net cost to the federal tax system as a whole might be less than the figure cited because social security recipients who otherwise would not have worked beyond age 65 would now become subject to income taxes.

*See memorandum by JAMES T. HILL, JR., page 91

Chapter 5
Expanding Training and Job Opportunities for the Hardest-To-Employ: Some Key Areas for Action

IMPROVING THE TRANSITION FROM SCHOOL TO WORK

ONE OF THE MAJOR SOURCES of high youth unemployment has been the inadequate transition between education and work. For a variety of reasons, including the greater complexity of the subjects to be learned, young people today often stay in school longer than their parents and grandparents did and have little exposure to the experiences they will face when they enter regular employment. The difficulty of transition is further aggravated by the time gap that exists between the age at which young people complete their high school education (17 or 18) and the age at which employers generally begin to hire them for regular entry-level jobs. According to recent studies, about 80 percent of employers start to hire personnel for such jobs at age 21 or 22.

For many youths, neither the experience gained in school nor intermittent exposure to searching for a job and working at the kinds of jobs usually open to teen-agers is an adequate preparation for an adult career. Indeed, many are caught in a classic double bind in which they are unable to get a job because they lack the right kind of work experience but cannot get the experience without a suitable job. Nor is the problem necessarily resolved once they reach the age at which firms are willing to offer them regular adult jobs. Many of these youths prove to be far less productive and adaptable than they could have been if the link between learning and earning had been stronger.[7]

An improved transition that makes school and work mutually reinforcing calls for efforts involving all segments of the community and extending through all stages of life. This is an area in which business can play an especially constructive role.

Improving Basic Education. Inadequate school preparation is proving increasingly costly for the private sector, which must often make up for these educational inadequacies through supplemental training or suffer the effects of a less productive work force. **Central to preparing workers for meaningful jobs is a significant improvement in the country's basic educational services for both youths and adults.** At a minimum, primary and secondary schools should be given clear directions and should be held accountable for seeing to it that no student is graduated who is not at least functionally literate. More generally, we consider it particularly important that expectations regarding student performance be set at a sufficiently high level and that laws for compulsory school attendance be more effectively enforced. We also believe that in designing their curricula, secondary schools as well as colleges and graduate schools need to pay closer attention to emerging changes in the types of jobs that are likely to be available.

Improving Job Information, Counseling, and Placement. One way to improve the link between school and work is to help overcome the glaring inadequacies in occupational guidance, counseling, and placement services now available to young people. In particular, there should be:

- *Better occupational information.* Young people need much more information about jobs in their communities, what these jobs are like, and what kind of preparation employers want. **We recommend**

7./ Those who enter the job market as school dropouts are often still worse off. A recently released report by the Ohio State Longitudinal Survey found that over three-fourths of high school dropouts who had aspired to additional schooling in 1966 continued to feel the need for such schooling in 1971.

that government agencies, schools, employers, and unions undertake an intensified cooperative effort to develop and distribute comprehensive occupational information. Moreover, as indicated by the current oversupply of university graduates in various professional fields, there is a major need for improved information on job prospects for college and graduate students.

• *More effective career counseling.* On average, the equivalent of the services of only about one full-time counselor for the school year is currently available for each 1,000 high school students. Moreover, much of that time is spent helping college-bound students select schools rather than helping youths who need jobs. The counselors themselves are frequently unfamiliar with the jobs and careers available. **To help overcome these gaps, we urge more active corporate and union programs that make experienced executives and other staff members available to students as career counselors on a released-time basis.** Special emphasis should be placed on retirees who can provide counseling assistance for extended periods.

• *Improved job placement assistance.* Schools and public employment services have been slow to meet the needs of students desiring work experience and high school graduates needing jobs. Improved placement services should be developed in close cooperation with employers and unions, drawing more extensively on specialized private placement agencies and involving more effective cooperation between local CETA prime sponsors and the state Employment Service offices. Business firms can also do a great deal to give students wider opportunities to visit plants and participate in special programs to acquaint them with the types of tasks these firms perform.

• *Special counseling for the most disadvantaged groups, especially minorities.* These groups have far less access to the informal job search network of employed friends and relatives that is available to other groups; their friends also tend to be severely disadvantaged in the job market. Moreover, many of these youths face special problems in relating to the most basic elements and disciplines of the adult workplace. They can benefit greatly from continuous counseling, starting early in their school career, that focuses on giving them self-confidence, teaches them how to pursue attainable goals step by step, and helps them deal with practical problems and disappointments after they obtain their initial jobs. For example, organizations such as the Boys' Club of America conduct regular counseling sessions for boys who start working while still in school, enabling them to share with counselors and their peers the special problems encountered in connection with their jobs.

In all these activities, there should be more stress on mobilizing the assistance of retired executives and workers on either a volunteer or a paid basis. Retirees can be of special help to youths because of their wide experience and contacts and their ability to provide special assistance for extended periods.

Integrating Classroom and Workplace. The most promising and potentially far-reaching means of bringing schools, youths, and the world of work closer together is through increasing the ways in which the teen-age years can become a time for gaining experience through *both* schooling and working. Schools need to take as part of their responsibility the arranging of work-experience opportunities and the creation of flexible classroom schedules that will allow youths to take advantage of those opportunities. Employers need to create part-time work-experience opportunities for youths still in school and to enter into joint training-education enterprises with their local school systems. Such arrangements have major direct advantages for schools, youths, and employers alike.

- Schools will be seen by youths as more relevant to the employment world, of being able to demonstrate a clearer connection between basic education and employment, and—by bringing paid work within the reach of students—reducing the lure that employment has in attracting youths out of the schools altogether.

- Youths will have the opportunities to test the employment world *before* leaving school, to gain exposure to one or more jobs before making a choice, to work into a regular adult job on a junior apprentice basis, and to identify their educational weaknesses while there is still time to correct them.

- Employers will have the advantages of stabilizing their supply of entry-level workers through close working arrangements with the schools; of getting workers they have trained on the job and on their equipment, rather than youths with schooling but without the maturity that comes with job responsibility; and of being able to point out to schools those educational defects in students that can be remedied by the schools before employers hire young people as regular workers.

At the high school level, at least 400,000 youths are now enrolled in some form of work or cooperative education program, and its use is expanding in postsecondary education as well.

- The Skyline Center in Dallas, Texas, is a joint effort of the schools and the business community that involves business firms intensively in career training and counseling.

- The Continental Illinois National Bank and Trust Company in Chicago has evaluated its last three years' experience with half-time employment and half-time schooling for about 500 youths and has found that work-study employees had better attendance records, retention rates, and overall performance than regular employees.

- The General Electric Company has had a long involvement with a wide variety of cooperative education programs across the country.

- A new engineering development program by Texas Instruments provides for four hours of employment each day and for four hours to attend classes at one of the participating schools in Dallas. In addition to assisting youths who would otherwise not be able to pursue an engineering degree, the program provides Texas Instruments with a source of engineering talent for the future.

Thus, integrated education and work efforts have already proved practical. They can be carried out locally. They can be started wherever a school system and employers are willing to work together. There is no need to wait for federal programs or government money (although added assistance is now available under the new youth employment legislation).

But despite the proven advantages of integrated education-work efforts, the total scope of existing programs is far less than seems feasible. For example, Chicago has a variety of well-run cooperative education programs, but they cover only 2 percent of the city's public school students. Elsewhere, some of the more promising efforts in this field have been discontinued because of recession-induced cuts in city budgets. This happened to the pioneering continuing education program in Atlanta, which operated on a four-semester basis and required high school students to have at least one-quarter of responsible work experience to be eligible for a high school diploma.

We recommend that businesses, schools, unions, nonprofit organizations, and other community groups work together to expand the volume and scope of cooperative education programs linking school and work and that the federal government make greater use of incentive funding to encourage effective work-study programs. We urge business to take the initiative in developing such cooperative arrangements.

Of course, the programs that may be developed should in no way encourage youths to leave school prematurely in order to work, nor should they downplay the inherent value of a general education.

Strengthening Vocational Education. Much more needs to be done to improve in-school vocational education. **Vocational education should be expanded and upgraded and should be brought into closer contact with the world of work and the specific needs of employers.** Moreover, some of the most successful vocational training is conducted outside the regular school systems, notably through career academies and through programs run by such groups as the Boys' Club of America and by 7001 (an organization that concentrates on supplementary vocational education for high school dropouts). In some cases, businesses, unions, and schools cooperate to have vocational education programs help in rehabilitating deteriorated housing in inner cities. All such efforts deserve strong encouragement and support. Serious consideration should also be given to the creation of a national extension service that would make available to workers in urban and inner-city areas the types of basic training and educational services that have long been provided for farmers through the agricultural extension service.

Other Avenues for Improving the Transition. Not all youths are best served by being in either formal education or regular jobs. For many, the important thing is merely to have work experiences that will in some way be useful to them in later life; frequently, these are the youths who have not yet made a definite career choice. Often, their main need is for exposure to the kind of work, some of it quite simple in nature, that introduces them to the elementary disciplines of a job. Others will benefit from wider opportunities for community service, particularly if such service can be usefully combined with various kinds of stipends or delayed payments in the form of tuition credits.

We welcome the fact that the recently enacted youth employment legislation substantially increases the range of such opportunities. Important additional work experience will be provided through the expansion of the Job Corps, a program that permits disadvantaged young people living in inner cities to engage in useful community work. The legislation allows other avenues for youths (primarily unemployed teen-agers from low-income families) to participate in, and obtain academic credit for, a wide range of community projects, such as neighborhood improvements, weatherization and basic repairs of low-income housing, energy conservation, and restoration of natural resources.

We also believe that job opportunities in the armed services should be taken into account in the formulation of a comprehensive policy to combat youth unemployment. Although the military experiences difficulties in attracting sufficient numbers of qualified applicants to fill the 400,000 annual vacancies, it nevertheless rejects more than 150,000 applicants a year who cannot meet physical or mental standards. We recommend closer cooperation between the new civilian programs for disadvantaged youths and the employment and training activities of the armed forces.

Job Corps centers could be used to work with rejected applicants to help them meet military entrance requirements. In addition, the Department of Labor might initiate pilot efforts to provide major assistance in securing employment or training opportunities for military personnel who leave the service before completing their first term. Such a program could help ensure that failure in the military does not result in a lifetime of failure for these youths.

Need for Community Support. An effective attack on the problem of the school-to-work transition requires strong backing and close collaboration of all the major community elements, including businesses, educators, union officials, voluntary agencies, and local CETA organizations as well as government youth service agencies. National public and private organizations can help, but the principal drive for making the programs work must come at the local level.

A number of promising initiatives have recently been instituted by private national organizations to spur the development of collaborative local efforts. The National Manpower Institute, as noted in Chapter 4, has organized a work-education consortium of twenty communities that is forming community-wide education-work councils. Similar efforts are being supported in a number of other communities by the National Alliance of Businessmen and other business and educational organizations. These programs can serve as models for greater involvement by national business firms in such community efforts.

MAKING FULLER USE OF THE OLDER WORK FORCE

Older workers (officially defined as workers over 40) often face particularly serious problems of unemployment and underemployment. If laid off in recessions, they tend to experience particularly long periods of joblessness. Many become discouraged about finding a job and drop out of the job-seeking process altogether. Even in nonrecession periods, older workers constitute a significant segment of the long-term unemployed, partly because of the lingering effects of the prior recession, partly because of skill obsolescence, partly because of age discrimination in hiring, and partly because of difficulties in finding jobs suited to their needs.

In addition, employment of older persons who want to continue working is frequently curtailed by mandatory retirement at age 65 or even earlier and by the severe limits on the total earnings permitted to social security recipients after retirement.

The personal and social losses from unemployment or wasteful use of the older work force are very serious. Many older individuals are faced with sharply rising prices, skyrocketing medical costs, and an inability to earn an adequate income through part-time or full-time work. Stress and anxieties increase as the people involved become more dependent on the financial resources of relatives and friends or on public assistance. For these people, retirement can represent an abrupt and painful shift from being able to keep up with changing economic conditions to becoming subject to events beyond their control. For society, inadequate use of older persons in the work force can represent the loss of highly valuable skills and human resources.

A major obstacle to a more productive use of older workers and retirees has been the persistence of numerous misleading stereotypes.

One such stereotype is that workers are bound to become obsolete as they move into the middle and older age-groups. Actually, a great many ways exist by which employers and government can enhance worker productivity at all stages of life. There is a major need to strengthen programs to prevent worker obsolescence while the workers are still employed, not after they have become unemployed. These programs involve effective training and retraining for adult and older workers throughout their working lives, special opportunities for developing second careers, and a variety of efforts to make more productive use of the work capabilities of retirees. Much can also be done through more flexible approaches to retirement and by creating a wider range of job opportunities specifically tailored to the needs of middle-aged and older workers.

A second widely accepted stereotype is that providing jobs for middle-aged and older workers and retirees will necessarily take jobs and income away from younger workers.* It is true, of course, that some competition for jobs among different age-groups is bound to occur. But it is by no means always true that extra work for older workers is against the interests of other age-groups.

- Many jobs especially suitable for older workers, particularly retirees, do not compete with those suitable for other members of the labor force. Frequently, they involve part-time or odd-hours jobs that employers find difficult to fill. Many others call for skills or experience that younger persons do not have. Moreover, as the economy moves closer to capacity and the labor market tightens, there will be a growing need to use older workers and retirees who can provide various types of services that will be in scarce supply.

- Older workers and retirees can increasingly be drawn on to perform socially needed tasks that are now being sadly neglected, including homemaker assistance to young families in which both husband and wife are working, home care to the rising number of elderly persons living alone, hospital work, and specialized counseling and job placement assistance for persons of all ages.

- In many cases, extra work and income for middle-aged and older workers or retirees is of direct aid to their children and families. It often means that sons and daughters who would otherwise have to drop out of school can continue their studies and that housewives who had only started to look for work because their husbands were unemployed have the option of returning to homemaking. The ability of older persons to earn an adequate income in addition to their social security benefits can relieve their children and others in the family of major financial burdens.

*See memorandum by FRANCIS E. FERGUSON, page 91

- There are 30 retired social security beneficiaries for every 100 taxpayers today. If present trends remain unchanged, this ratio is expected to be 45 to 100 by 2030. Unless a larger number of older workers and retirees contribute in some way to productive work and total tax payments, the overall economic and tax burden on the rest of the population will become increasingly heavy.

A third stereotype is that the early retirement of workers during recessions is invariably less burdensome, more humane, and more effective in coping with business slowdowns than full or partial layoffs of younger workers. Again, this is not necessarily valid. (For a fuller discussion of this issue, see the final section of this chapter, "Minimizing Unemployment in Recessions.")

We urge business and government to increase training and job opportunities for midcareer and older workers as well as for retirees in ways that will make maximum use of these groups as a productive resource. This can be accomplished through a number of approaches:

Continuing Education, Skill Renewal, and Retraining. Close integration of education and the workplace should apply to workers at all stages of life, not merely to the young. Employees at all age levels should have access to continuing education and periodic opportunities for skill renewal and retraining. This applies particularly to the broad spectrum of industries and occupations where the processes of innovation and automation are producing major changes in job tasks.

Responsibility for providing such opportunities falls jointly on public and private educational institutions, employers, labor unions, and community organizations. Most communities need a substantial expansion of publicly supported adult education and training facilities.[8] As one way to assist this process, we believe that serious consideration should be given to recent proposals for using publicly supported universities to provide the same wide range of adult education and technical training facilities to urban wage earners that has long been made available to farmers through the agricultural extension service. A constructive step in this direction is the current effort by the American Association of Community

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8./ Over the next decade, such an expansion should also help to offset the slack in demand for the services of already trained teachers and for the use of existing educational facilities that might otherwise emerge as a result of the slower growth of the school-age population.

and Junior Colleges to stimulate the provision of services by community colleges to older adults who seek work or other meaningful service. The use of government support of deferred educational grants for middle-aged and older workers should also be explored, particularly for those who have never been able to finish high school.

Even if public education facilities are expanded, much of the task of preserving and increasing the skills and interests of middle-aged and older employees must be carried out by employers, in many cases in close collaboration with unions. Many companies not only offer periodic opportunities for skill renewal and upgrading but also provide training and other assistance to employees who wish to develop a second career. Special attention should also be paid to helping women in their middle years who reenter the labor force after years as homemakers.

Reassignment and Second Careers. The extent of job changing and movement into second careers in the American economy is growing, particularly for workers over 45. An increasing number of companies are finding it cost-effective to support midcareer changes by their employees through reassignment or retraining. Many firms also find it beneficial to help employees change to new careers that they can pursue elsewhere or after retirement. The mere knowledge that such options are available often makes an important contribution to employee morale and productivity, particularly in jobs involving high stress and rapid obsolescence.[9]

In view of the growing number of second careerists in their forties and fifties, business firms should reexamine their negative preconceptions about older job applicants. Apart from the fact that firms have a legal obligation not to discriminate against workers between the ages of 40 and 64, many need to take fuller account of the skills, experience, and maturity they can gain through hiring older workers.

The development of systematic career appraisal and planning systems can help detect changes in career interests, even among more experienced and skilled workers. Employees can then be assisted in reassessing career choices and making better decisions about possible changes in job assignments, work schedules, or levels of stress and responsibility.

9./ One of the most comprehensive second-career programs in the nation is conducted by the Federal Aviation Administration for its air-traffic controllers. The agency actually pays the full cost of retraining and full salary for up to two years to middle-aged air-traffic controllers who become disqualified. Although this program covers highly specialized employees in the public sector, some of its elements may be applicable to selected employment situations in the private sector.

Job Retention. Business firms should avoid unnecessary dismissals or early retirements of older and middle-aged workers because of technological changes or recessions (see "Minimizing Unemployment in Recessions"). Firms with many branches and locations can make sure that persons no longer needed in one place will have the first opportunity for openings elsewhere within the company, if necessary after some retraining financed by the firm. Johnson and Johnson, for example, has established a headquarters job bank that matches displaced or laid-off employees with specific openings in any unit of the company. Other firms that apply such practices extensively, such as IBM and General Electric, report that older workers respond with a high degree of company loyalty and a greater willingness to adapt to technological changes and reassignments.[10] Although the success recorded by these companies with such policies cannot necessarily be duplicated by firms with different products and vulnerability to cyclical patterns, elements of such policies can probably be effectively used by many more companies than is now the case.

Better Transition from Work to Retirement. Another major ingredient of policies for more productive and humane use of the older work force is to provide for a less abrupt transition from regular work to retirement and to postretirement activities. This Committee plans to deal in greater depth with issues of retirement policy in a future study. However, there are already trends that point to numerous options for improving the transition from work to retirement.

Many firms and institutions have never adopted mandatory retirement. Some have dispensed with such policies and substituted more flexible arrangements. Proposed legislation would prohibit mandatory retirement before age 70 for most workers. Exemptions are being discussed for special cases, such as college faculty members and senior corporate managers. Where mandatory age limits do apply, a great deal can be done to provide for a more gradual shift to less demanding and stressful work well before the formal retirement age is reached, including lateral transfers, shifts to permanent part-time work, and greater flexibility in work scheduling and assignments. For example, one firm permits its em-

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10. IBM, which since 1970 has retrained over 7,000 of its employees and relocated about 11,000, also makes it a practice to move work to facilities that have surplus people. The company reports that, as a result of its traditional policy of assuring company-wide full employment, no employee has lost any time through involuntary layoffs during the past thirty-five years, despite recessions and major product shifts.

ployees to shift to a four- or three-day workweek one year before retirement with comparable reductions in pay. In an increasing number of cases, firms are also arranging for retirees to return to work on a part-time or nonregular basis.

Tapered retirement can help older workers and retirees to supplement their income and retain a sense of continuing usefulness through productive work. At the same time, employers are able to call on experienced and reliable personnel for a variety of special tasks. Many companies also report that a mingling of experienced older workers with younger employees leads to significant net gains in efficiency and morale.

There should also be new types of job opportunities especially tailored to the needs of older people and their employers. One such technique is the use of a *ready work force* of experienced retired personnel that is subject to recall on a part-time or full-time basis during periods of peak work loads. Another is *job sharing*, in which two persons working part time at different hours during a given day or on alternate days, weeks, or months are responsible for carrying out one full-time job.

Among noteworthy efforts by business firms and financial institutions to stimulate postretirement careers for their former employees are the following:

- Several companies in the Los Angeles area have contracted with a nonprofit agency called Second Careers to help place retirees in paying jobs, in meaningful volunteer roles, or in training to form small businesses.

- The Equitable Life Assurance Society of the United States operates its own retiree volunteer program, through which retired managers or agents are referred as consultants to community agencies that need their expertise.

- IBM provides education grants of $500 a year for five years to any pre-retiree or retiree who wishes to develop a second career or retirement interest.

One major reason for greater use of tapered retirement and the use of retirees on a part-time or nonregular basis is the growing evidence of the adverse effects of abrupt retirement. For example, the highest suicide rates in this country are found among men aged 64 and over. Many retirees suffer from loneliness, alcoholism, or withdrawal from community and social activities. Hence, in addition to providing more part-time or nonregular work opportunities for older workers, an increasing number of employers are developing extensive preretirement and postretirement counseling assistance, often in cooperation with local unions.

We urge employers to foster a smoother transition from regular work to retirement and to valuable postretirement activities.

JOB PREPARATION, TRAINING, AND UPGRADING TO AID THE DISADVANTAGED

We believe that greatly increased private and public training opportunities should be central to any attack on persistently high unemployment, particularly for the disadvantaged.* Instead of concentrating on low-skill, dead-end jobs, the approach we favor would reduce the chronic structural unemployment problem on a permanent basis, increase productivity, and help avert potential inflationary pressures from future skill bottlenecks. Even now, many actual potential job openings exist that could be filled if properly trained personnel were available. As the economy expands more strongly, many more vacancies requiring special skills and capacities will emerge. These could be filled either by drawing directly on newly trained workers who are now unemployed or by upgrading currently employed workers and thus opening new entry-level job opportunities for the hard-to-employ.

More and better training is essential because the extraordinary longer-term changes in the economy and in the composition of available jobs are not being adequately matched by needed adaptations in the work force. The economy is becoming less dependent on muscle power and more dependent on professional, technical, and clerical skills. At the beginning of the century, over one-half of the total work force was unskilled; today, that figure is less than 10 percent. Moreover, there is a continuing shift from blue-collar to white-collar job openings, particularly in the service field. Yet, there are large numbers of people in the work force who currently lack the most elementary qualifications for filling such jobs, and existing training and education efforts for these new types of jobs are sadly inadequate.

If the disadvantaged are to help fill these needs, a wide range of

*See memorandum by FRANCIS E. FERGUSON, page 91

special development efforts is required, aimed at job readiness, skill training, general education, counseling, job placement, and skill upgrading. As many manpower projects of the last five years have demonstrated, disadvantaged and inadequately skilled persons *can* be brought up to the performance level of other employees given time, thorough training, and special services. Many firms have found that the graduates of special programs for the disadvantaged perform as well as, or even better than, people hired through normal channels.*

Clearly, the type of preparation and training suitable for the disadvantaged and other hard-to-employ groups must vary according to the particular group involved. For young teen-agers and others with little work experience, even menial work that introduces them to the elementary disciplines of the workplace may be adequate.[11] Others need more technical or professional training. In other cases, the emphasis should be on upgrading. The following paragraphs outline key areas (in addition to improved vocational guidance and training) in which we believe that significantly stepped-up training and education efforts based on a constructive government-private partnership are particularly desirable.

There should be a major increase in the volume and coverage of apprenticeship and similar programs to enlarge the supply of highly skilled workers. Apprenticeship programs do not exist in many growth occupations in which there is a strong need for more skilled employees, especially auto repair, health care, some energy-related activities, and numerous other service jobs. Moreover, systematic training in service-sector management techniques is widely needed.

Some labor unions and some employers have been reluctant to support wider use of apprenticeship programs. **We urge government, business, and unions to cooperate in strengthening apprenticeship or com-**

11./ A corollary is that job-entry requirements for such workers should be based on their capacity for doing the jobs in question rather than on high school diplomas or purely academic tests. Although there is indeed a major need for better basic education, disadvantaged youngsters in their late teens or early twenties who have dropped out of school and are in need of jobs to support themselves should not be barred from useful work by excessive emphasis on academic credentials. A recent study by the Vocational Foundation shows that this emphasis is often a principal barrier to needed employment of the most disadvantaged inner-city youths. For many of these young people, entry into a regular job can be the alternative to "hustling" or welfare and can provide the best chance for giving them needed training and opportunities for further education.

*See memorandum by FRANCIS E. FERGUSON, page 91

parable high-skill-training programs and in using them in a much larger number of occupations. Entry into such programs should be based solely on merit, and the programs should be open to midcareer and older workers as well as to youths. We also recommend increased financial incentives for apprenticeship programs, primarily in the form of training stipends that would in some cases start below the minimum wage level and move step by step toward the going wage rate for the jobs in question. In addition, we support greater experimentation with training vouchers in connection with apprenticeship and other skill-training programs. Such vouchers could improve the quality of the training by enabling apprentices and trainees to shop around for the best available training opportunities.

Greater emphasis should be placed on expansion of on-the-job training programs. We believe that such a step-up is possible if nonprofit organizations formed by major business firms and minority enterprises can work under direct contract with CETA as turn-key operators for administering and monitoring the programs. Such an arrangement could help secure the cooperation of a significant number of smaller firms, particularly in inner-city areas. In addition, there should be wider use of training subsidies, in the form of either simplified direct contracts (mainly for larger business firms) or special incentives (mainly applicable to smaller firms). In most cases, subsidies paid should be substantially larger during the critical first six months to a year.

More stress should be placed on private-sector training programs in poverty areas, both urban and rural. A number of such programs have been conducted successfully in the past.[12] Programs of this kind can be particularly effective in reaching unskilled youth in inner-city or rural poverty areas, where the highest unemployment rates are registered.

Federally assisted training programs should put more emphasis on upgrading employees from entry-level jobs. Appropriate career ladders are needed, supported by both on-the-job and off-the-job training and counseling. Equal employment and affirmative action programs can give a major impetus to such employee upgrading, but additional financing for CETA and related government assistance programs is also desirable.

Strong encouragement should be given to qualified private intermediate organizations that carry out job-readiness and skill-training pro-

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12./ Examples are the IBM Bedford-Stuyvesant facility in Brooklyn, Control Data Corporation plants in Minneapolis and in Washington, D.C., and a computer plant in Kentucky using a rural poverty work force.

grams in simulated work settings. These include special skill-training centers, such as those conducted by OIC, and special institutes and training centers sponsored by individual corporations. Much wider use should be made of highly focused technical training programs, such as the Training and Technology program in Oak Ridge, Tennessee (cited in Chapter 4). In that joint effort by government, universities, and private corporations, training is closely linked to the employers' needs and to the job market in technical occupations. In this instance, the trainees, most of whom are young and disadvantaged, are trained in a factory setting, according to actual plant rules and discipline, by instructors furnished by Union Carbide.

There should be increased efforts to draw gifted minority individuals and women into professional fields where they have been largely absent, such as engineering, the higher levels of business administration, accounting, law, and medicine. These people need various kinds of special training and support, often at younger ages. One excellent example is provided by Inroads, Inc., an organization incorporated in five cities (Chicago, Saint Louis, Milwaukee, Cleveland, and Pittsburgh) that is supported by government funds and by major corporations. Inroads provides precollege and college training for the gifted poor from black and Hispanic backgrounds to help prepare them for business and engineering careers. With the help of corporations and educational institutions, a considerable number of other organizations have also been established to increase the proportion of minorities entering engineering. With added organizational efforts and incentives, the number and scope of such programs could be substantially increased.

Very special kinds of training must be offered to the most severely disadvantaged who have basic difficulties in relating to the world of work. This type of training, often in the form of supported work, involves learning job discipline, punctuality, relationships to supervisors and peers, and a sense of quality control. As indicated in Chapter 4, we believe that for this group, a major expansion in the use of jobs corporations is appropriate.

BETTER MATCHING OF JOB SEEKERS AND JOBS

Increased employment for youths, older workers, and the disadvantaged depends on better education and training as well as on breaking down legal barriers to their employment, inflexible industry and union practices, and discrimination. But even when persons in the target groups have become job-ready and when possible vacancies exist, there are often major problems in matching these job seekers with suitable job opportunities. This section focuses on a number of approaches for helping to deal with this problem that we regard as particularly promising and that call for greater private initiatives or public-private cooperation.

Strengthening the Employment Service. The United States Employment Service (ES) has special responsibilities and opportunities to find jobs for groups with particular difficulties in labor markets. Yet, its overall contribution toward this goal has fallen far short of what seems either possible or desirable. We believe there is need for a far more aggressive effort than has yet been mounted to make the Service more effective. In Chapter 6, we discuss ways in which the Employment Service can be improved through organizational changes, notably much closer coordination with federally assisted CETA programs. Various other improvements, such as expansion of computerized job banks to include listing of both job applicants and job openings, are also urgently needed.

A central requirement for increased effectiveness of the Employment Service is establishment of a more productive relationship with employers. The Service has little chance of success if employers will not list their job openings with it. This aspect of the Service's operations has often been badly neglected, but in the last few years, ES has made a special effort to improve its services to employers. Although some of these efforts have been encouraging, they have been carried out in only about 10 percent of the local ES offices. **We urge that a much more forceful effort be made to develop improved services to employers by Employment Service offices throughout the country.**

One of the best ways to cement a mutually beneficial relationship between the Employment Service and employers is the use of Account Representatives. Under this arrangement (which has been used with particular success in Chicago and Pittsburgh), potential employers deal with a single designated ES officer, a process that provides accountability and continuity of service. Each ES Account Representative is assigned a block of companies, preferably those with similar occupational lines, and assumes full responsibility for all job orders, including screening, referral, verification, and other follow-up functions.

This procedure permits the Account Representative to work closely with selected companies and to develop expertise in filling their needs. **We urge further development and wider use of the Account Representa-**

tive system. We also recommend further development of the practice, already followed in some centers, that involves personnel exchanges between the ES offices and given employers in the interest of a better reciprocal understanding of needs and services.

The Account Representative system should be combined with increased use of applicant officers in CETA prime sponsor offices. These officers would be responsible for a block of applicants and would follow each applicant from admission to the program through training and referral for placement. Particular applicant officers should specialize in handling older people, younger persons, or the disadvantaged. In effect, these applicant officers would become ombudsmen for persons with special difficulties in entering the labor market; they would advise Account Representatives about the best strategy for placing such persons. The applicant-officer function can also be subcontracted to private employment agencies that have special interest and expertise in the problems of particular groups, such as older workers. (See "A Larger Role for Specialized Job-Finding Agencies.")

We believe that this arrangement will be more effective in placing special client groups than the existing formal requirements for assigning priorities to certain groups. By working closely with both employers and CETA, Account Representatives may also be able to negotiate agreements to hire more of the disadvantaged, old, or young. In this way, they not only fill an employer's job needs but also help employers to fulfill their affirmative action obligations.

A Larger Role for Specialized Private Job-finding Agencies. For many of the hardest-to-employ, in good times as well as in recessions, the usual kind of job placement efforts carried out by the Employment Service and regular employment agencies are simply not enough. These people include our most severely disadvantaged youths, many of whom are school dropouts or have criminal records or drug problems or are handicapped, and many older persons who may be entirely job-ready but who have become discouraged from searching for a job because of the difficulties of locating suitable opportunities on their own.

For these groups, it is not enough to point out job openings listed by employers. Instead, an intensive effort is required to seek out or develop job opportunities that fit their individual capabilities and requirements. In many cases, it calls for special full-time or part-time jobs for which somebody is willing to pay but which are currently nonexistent. Often, it also calls for seeking out disadvantaged persons for whom job openings are available but who are unaware that such opportunities exist. In fact, it is quite common for agencies specializing in this work to succeed in developing more job opportunities for disadvantaged workers than they are able to fill from their current pool of job seekers.

Such tasks can in part be carried out through the vocational training and guidance work of secondary schools, by CETA and other public agencies, and by community-based organizations that also carry out other functions. But we believe that there is particular promise in wider use of specialized nonprofit job placement agencies for the difficult-to-employ that receive partial support from public funds. A number of such organizations already exist and have had notable success in particular communities.

- The Vocational Foundation in New York City, which has operated since 1936, finds jobs for disadvantaged youngsters 16 to 19 years of age who have had some past trouble with delinquency and have few marketable skills. In 1976, the foundation dealt with 2,400 youths, developed 3,700 job openings, and placed about 1,100 youths in jobs. (Before the recent recession and New York's financial crisis, the total number of placements was about 3,000 a year.) Although this organization has had a remarkable record as an employment agency of last resort, its specialized services reach only a small proportion of the total number of youths in New York City who need this kind of assistance. Furthermore, in most cities, this type of service is simply not available.

- Various intermediary nonprofit organizations in many communities bring together employers and older workers. Two of the largest of these are Retirement Jobs, Inc., in the San Francisco area and the Senior Personnel Employment Committee in White Plains, New York. Both operate a number of offices in their target areas and use both volunteer and paid older workers for job development and referral functions. The Senior Personnel Employment Committee, which has existed for about twenty-five years, currently finds jobs for about 700 older workers annually.

These specialized agencies provide highly individualized counseling and support services both before and after placement or training. The Vocational Foundation has found that such services make a critical difference in job-retention rates for the youths they place. Without such support, half of these youths usually drop out of the work force in the crucial first six weeks.

Another important advantage of specialized private agencies is their ability to develop suitable job opportunities with medium-sized and smaller firms. Many of the jobs suitable for the hardest-to-employ are with small firms, particularly in the service industries. Yet, these very firms often do not use regular private employment agencies or the Employment Service. However, once contacted by a representative of a specialized job-finding agency, smaller firms are often more receptive than larger ones to hiring youths as well as older workers because their recruitment specifications tend to be less formal. Moreover, both young and older persons who have had difficulty in securing jobs often respond more favorably to the more informal atmosphere of smaller firms.

Although such agencies perform useful services, they reach only a small proportion of the people who need assistance. **We urge that government and the private sector support wider use of specialized private job placement agencies for hard-to-employ groups.** Such an effort should include these major ingredients:

- Business leaders, working with government and community groups and federal manpower programs, should take the initiative in encouraging the creation of such agencies in areas where they do not now exist. Very often, all that is involved is the addition of this function to programs of existing agencies.

- Government agencies, including the Employment Service and CETA, should subcontract with specialized private job-finding agencies to help cope with the special placement needs of disadvantaged persons.

- Financial incentives should be used much more aggressively to encourage creative entrepreneurship in the placement of hard-to-employ youths. We urge federal support, through CETA or other suitable agencies, for responsible private job-finding agencies that pay commissions to job developers working full or part time. The amount of commissions payable under such government contracts should be liberal enough to provide strong incentives for a major increase in the volume and intensity of job-finding activities. Commissions would have to be contingent on verification of placement and a minimum period of job retention. Moreover, the private job-

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finding agencies aided by public funds should be held accountable for high-quality service provided by its commission workers.

● In staffing these agencies, major emphasis should be placed on the use of qualified older persons, both as commission workers and as volunteers. This practice is already successfully used by many existing agencies. **As a special incentive for increased reliance on older persons, we urge that commissions or other remuneration paid to job developers in qualified job-finding agencies be exempt from the limitation on earnings applicable to social security recipients.**

This approach would help solve two persistent unemployment problems simultaneously. It would provide many older persons with part- or full-time work and at the same time bring to the young the experience, know-how, and network of contacts of people who have the time and patience to find ways of remedying the deficiencies and removing the obstacles that have made employment for young people so difficult.

Many older persons are already known to be efficient job developers, in part because of their wide familiarity with employers.[13] With a special stress on older staffers and greater financial incentives, it should be possible to enlist a much larger number of qualified job developers than is now possible.

Adapting Jobs to People: Alternative Work Patterns and Designs. Often, a better match between people and jobs will call for basic changes in the nature of the jobs themselves. Most jobs are still designed for prime-age, full-time workers operating in a factory, office, or store on a relatively rigid time schedule. However, because of changes in the composition of the labor force and in life-styles, there are many people today who are willing and eager to work but who find that they do not or cannot fit into such a restricted job design. For these people, getting jobs and becoming productive members of the labor force often depend upon the availability of work opportunities more closely tailored to their needs, such as flexible hours and part-time work.

Such people include youths who are still in school or are participating in special training programs, working parents with children and other home responsibilities, older workers who need relief from high-stress work

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13./ According to a 1974 Louis Harris survey, 135,000 Americans who are 65 or older are already engaged as volunteers in providing employment services.

schedules, and retirees who are only able to work part time and are subject to social security limitations on outside earnings. Such alternative work arrangements are especially important for the disadvantaged, such as women heads of households on welfare who want to work but must devote part of their time to taking care of school-age children. But alternative kinds of work opportunities are often also needed to attract a larger proportion of high-skilled workers into the labor force and thereby reduce the risks of future skill bottlenecks.

Flexible working hours are now being used in over 6,000 European companies and have been adopted by several hundred larger American concerns. "Flexitime" is now being given a three-year test in certain federal agencies. Some of the larger private firms that have used this technique, such as the Metropolitan Life Insurance Company in New York, have found that it increases employee morale and sense of responsibility, reduces absenteeism, and improves productivity.

Part-time employees are one of the fastest-growing components of the U.S. work force. As recently as 1970, 1 out of every 8 workers was a part-timer. Today, 1 out of every 5½ employees works part time. About two-thirds of all part-time employees are adult women. Reliance on part-time work is widespread among teen-agers and persons over 60.

Although many part-time jobs are temporary and involve only short hours, a growing number of part-timers work on a permanent schedule. Permanent part-timers, many of whom are older housewives with fixed family responsibilities, are used on a large scale by department stores and other retail outlets, insurance companies, and financial institutions. Many manufacturers are also making substantial use of part-time workers. For example, one large pharmaceutical company has a part-time work force that is three times as large as its full-time work contingent. These employers find that part-timers do not fit the stereotype of marginal, temporary, or uncommitted workers. They are a stable work force of individuals who want regular but not full-time work.

Business firms are increasing their use of special work schedules that fit the requirements of particular groups of workers as well as the requirements of the firm. For example, in some companies, older workers are employed on a schedule of two or three days a week as well as on special shifts. Other special time arrangements that can be particularly helpful to older workers include job sharing and job alternating and the use of a ready work force of retirees subject to call during peak load periods. Another promising arrangement enables parents to work only during those months when their children are in school.

Significant increases in work opportunities can also result from changes in the design and location of jobs. As we have noted, some firms make active efforts to taper down the work responsibilities of employees as they approach retirement age. Conversely, various techniques can be used to gradually increase the demands on workers in supported-work programs. In the future, technological changes may make it practicable for an increasing number of tasks now performed in factories and offices to be carried out at home. This could apply, for example, to many types of complex technical calculations that can be performed with the aid of a computer terminal.

In our view, a broadening of options for the use of alternative work patterns could make a significant contribution toward reducing the more intractable forms of unemployment and underemployment. At the same time, such options can do much to contribute to greater business efficiency and flexibility in operations. **We recommend that employers review the organization and scheduling of their work flow to determine whether more job opportunities could be created for youths, the disadvantaged, older workers, and retirees through development of a wider range of alternative work patterns, including more part-time work and nonregular employment.**

MINIMIZING UNEMPLOYMENT IN RECESSIONS

Although recessions usually stem from widespread reductions in overall demand and output, their adverse effects on jobs and earnings tend to fall disproportionately on those members of the work force who lose their jobs or who are unable to secure new jobs. For many of these people, unemployment is compounded by the loss of medical and other social benefits, reduced self-confidence, increased personal stress, and erosion of skills.

The groups that suffer most in recessions are frequently the same ones that are particularly vulnerable at other times. Youths and the disadvantaged are often among the first to be laid off. Older workers are more protected through seniority rules, but once laid off, they face greater difficulties in finding new jobs. They are also often pressured to opt for early retirement, even when that is not in their own best interest.

Clearly, the principal response to recessions should be a set of fiscal and monetary policies that will restore adequate levels of total demand and output. Because it takes time before such policies can become fully effective, antirecession measures should also include adequate provisions to cushion the impact on individuals through unemployment compensation and other income-maintenance payments, plus steps to provide new temporary job opportunities through public employment. Recent antirecession strategies have made active use of all these approaches.

We believe, however, that there is need for a harder look at an additional approach: namely, more systematic efforts to minimize outright layoffs and forced idleness during recessions.

First, business firms should, wherever feasible, fully explore alternatives to outright layoffs when their sales volume is reduced as a result of recessions. The scope of such alternatives will, of course, vary greatly for different companies and in different situations. Firms should not be asked to retain employees where this runs counter to the companies' longer-term productivity. However, we believe that a careful assessment of longer-term costs and benefits would uncover a larger number of instances in which the companies would benefit from a reduced number of dismissals.

Without a careful cost-benefit analysis, companies may underestimate the extent to which outright layoffs in recessions are now often more costly or represent less of a saving than in the past, especially where increased training costs have substantially added to the capital value of current employees and where the cost of searching for qualified new employees is high. Conflicts between seniority and equal employment rights have also increased the costs of layoffs, resulting in extra legal expenses as well as morale problems. At the same time, the savings from layoffs have often been reduced because of increased company contributions to unemployment compensation and supplementary benefit payments.

Second, the federal government should actively encourage corporate policies to provide skill-upgrading programs and other training opportunities as alternatives to layoffs in recessions. There should be standby authorization for enlarged government subsidies for such programs that could be automatically made available when national and area unemployment rises above specified levels. These subsidies should be available not only to companies that provide on-the-job training for their own employees but also to firms that initiate special training programs for unemployed persons who will subsequently be placed with other employers. The net cost to the government of supporting such training and education programs during recessions will be relatively low because the beneficiaries of these programs would have received unemployment insurance or some other form of government support in any case.[14]

Third, we recommend active exploration of possible legal and administrative changes to facilitate work sharing as an alternative to cyclical layoffs in cases where such a solution is desired by both management and labor. Work sharing can be important in reducing the uneven burdens that now fall on a limited number of employees with the least seniority during recessions. Furthermore, because work sharing avoids layoffs altogether, it can be particularly useful in preventing conflicts between seniority and equal employment considerations during recessions.

The needed administrative or statutory changes might include allowing payment of unemployment insurance for single days in cases in which work schedules have been cut to four days (although this arrangement might have to be limited to companies that have bona fide work-sharing programs and are located in areas of high unemployment), permitting workers in plants operating at reduced capacity to work on alternate weeks and draw unemployment insurance when not working (along lines that have already been successfully tried in the state of Connecticut), and compensatory payments to employers for increased per unit cost of medical and other fringe benefits that result from work-sharing arrangements. It should be emphasized that our recommendations relate to work sharing only as an alternative to cyclical layoffs; consideration of the issues involved in wider use of work sharing and shorter hours over the longer term is beyond the scope of this statement. Moreover, our comments concern the kind of work sharing that produces four days' work for four days' pay, not four days' work for five days' pay.

Fourth, substantially greater efforts should be made to assure that persons now receiving unemployment insurance payments during recessions be given more active opportunities and encouragement to benefit from useful training or work opportunities. More specifically, we recommend that recipients of unemployment insurance be able to participate in retraining and education programs within a reasonable period after they

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14./ In the case of programs of this type run during the last recession by General Electric and by Zenith Radio, net costs to the government came to only about one-third of the cost of normal government-funded training activities.

receive their initial unemployment insurance checks. Participation in such programs (where available) is now required for persons who have drawn unemployment insurance benefits for more than thirty-nine weeks. We believe that, where feasible, such a requirement should be made effective considerably sooner (after twenty-six weeks or even earlier). Moreover, in future recessions, greater efforts should be made wherever possible to find better alternatives to such extended eligibility periods for unemployment benefits as the sixty-five-week maximum period used in the last recession. In particular, more advance arrangements should be made to provide training and subsidized public or private work opportunities to the unemployed after their unemployment insurance has expired.

In applying any of these prescriptions, great care will have to be taken to assure that there is no undue interference with layoffs and job search efforts needed to allow permanent resettlement of workers whose jobs have become outmoded or who are operating in distressed firms, industries, or localities. For such workers, more relocation and retraining assistance will often be desirable.

Chapter 6
More Effective Management of Federally Assisted Employment and Training Programs

An intensified national attack on structural unemployment through a strengthened public-private partnership not only requires changes in the basic orientation of many public and private programs but also calls for more effective organization and management of federally assisted employment and training programs. Despite recent improvements, the efficiency of many of these programs is still seriously impaired by unclear policy direction, overlapping or uncoordinated administrative structures, and bureaucratic inflexibility.

THE CURRENT ADMINISTRATIVE STRUCTURE

Since CED called for a range of reforms in the administration of federally assisted employment and training programs in *Training and Jobs for the Urban Poor*, a number of far-reaching changes in the administration of federal manpower programs have been instituted. Most important among these were the enactment of the Comprehensive Employment and Training Act (CETA) in 1973, the creation of a temporary countercyclical public-service employment (PSE) program in 1971 and the revival of such a program in 1974, recent improvements in the legislation governing that program, and the enactment of the 1977 Youth Employment Act.

As its title implies, CETA was designed to substitute a comprehensive and integrated approach to federally assisted employment and training programs for the more than twenty existing categorical manpower programs that had been administered by a wide range of separate and often competing bureaucracies. CETA's main features are decentralization and decategorization. Primary responsibility for planning and delivery of manpower services was shifted from the federal government to state and local government units, although these remain subject to federal oversight. It was hoped that this change would make it possible to gear these services more closely to the unique characteristics of local labor markets. The basic focus of the overall program continued to be on preparing the hard-to-employ for self-sustaining jobs. However, in place of the many federal directives regarding categories of unemployed to be served, decisions about priorities were to be made primarily at the local level.

Some 445 prime sponsors (mostly state and local governments) have been organized under the act. These prime sponsors engage in training and placement programs, principally through subcontracts with various public agencies and public or nonprofit community-based organizations, including those that serve racial and ethnic minorities or other specialized clienteles.

In an important number of instances, this arrangement has resulted in more comprehensive and innovative approaches to the delivery of manpower services at local and regional levels. But there have also been many areas where performance under the program has been far from satisfactory. The following are some of the principal difficulties that have been encountered:

- Although CETA was created primarily to help the structurally unemployed, the severe recession of 1974–75 resulted in a widespread reallocation of CETA funds toward support of countercyclical public-service employment. Thus, CETA funds originally intended for disadvantaged groups were often used to avert layoffs of regular city workers, particularly policemen, firemen, and other essential employees. As a result, a high proportion of CETA clients has turned out to consist of middle-income whites rather than members of minority groups or others who encounter chronic difficulty in obtaining employment.

- The rearrangement of functions among federal, state, and local officials has in many cases proved to be less than ideal. Under the previous system, federal control over local activities may often have been too tight and too narrowly pinpointed to particular categories of the unemployed. The pendulum now frequently appears to have swung too far in the other direction.

- The fact that the U.S. Employment Service continues to be run as a separate manpower system under state control continues to fragment federally assisted manpower services. At the local level, rivalry between the Employment Service and CETA often remains intense, resulting in considerable inefficiency and duplication of effort. For example, in many jurisdictions, the local ES offices do not share job-bank information with CETA prime sponsors.

KEY REQUIREMENTS FOR IMPROVING THE SYSTEM

It is still too early for a full evaluation of the experience under CETA, particularly because the special difficulties that have arisen as a result of the recession are diminishing in importance and because recent basic changes in the CETA legislation should help channel a higher proportion of CETA funds to the disadvantaged and the long-term unemployed. Nevertheless, we believe that there is need for a major effort to strengthen and revitalize the structure and administration of federally assisted employment and training services. An effective system for planning and delivery of these services should

- be subject to clear and integrated direction at all levels of government

- place principal responsibility for delivery of services at the regional and local community levels but provide for sufficient federal direction to assure that appropriate local coordination is in fact caried out

- provide strong incentives for increased involvement of the private sector (profit as well as nonprofit) in the development and implementation of training and employment programs

- clearly distinguish between broad categories of employment programs that are designed to serve different types of needs: the elimination of cyclical unemployment, the enlargement of training and employment opportunities for groups that experience special difficulties in the labor market but are basically able to cope with work, and assistance to the most severely disadvantaged groups that are not able to cope with the world of work without major additional aid

The following administrative improvements would be especially helpful in fostering a stronger public-private partnership.

REALIGNING FEDERAL, STATE, REGIONAL, AND LOCAL FUNCTIONS

To eliminate the existing duplication of U.S. Employment Service and CETA functions, we recommend that appropriate administrative and, if necessary, legislative actions be taken to bring the two organizations into a closely integrated structure from the Department of Labor down through regional, state, local, and neighborhood offices.* This will require strong directives to produce both the needed integration at each level of government and adequate flexibility to allow for diverse needs and circumstances in different states and local areas.

Our stress on stronger federal oversight does not mean that the trend toward shifting responsibility for integrated delivery of manpower services to regional and local levels should be reversed. On the contrary, we believe that regions and local communities should be given increasing responsibility for carrying out these functions; they should, however, be subject to federal standards and performance audits. But this increased delegation of operational functions to regional and local jurisdictions that receive federal assistance should not give such jurisdictions discretion to adopt a do-nothing approach or to tolerate continued wasteful duplication of services. Nor should it allow such jurisdictions to ignore the need for greater and more imaginative efforts to involve the business sector, labor unions, private nonprofit organizations, schools, and other elements of the local community more fully in CETA activities along the lines recommended in Chapter 4.

*See memorandum by CHARLES KELLER, JR., page 91

The federal government needs to give more forceful and explicit encouragement to both CETA programs that foster active community participation and an enlarged role for the private sector. It can do this in part by technical assistance and incentive funding for community programs that move in this direction and by more systematic efforts to provide information about successful instances of public-private cooperation to government units and private firms throughout the country. In this connection, we recommend that the Secretary of Labor be authorized to allocate up to 20 percent of CETA funds at his discretion to prime sponsors whose performance merits special recognition and support. (This would be in addition to discretionary funds already available for other purposes.)

The regional offices of the Employment and Training Administration (ETA) should be a focal point for encouraging greater local community participation in the design and administration of manpower programs. Regional ETA offices should, at a minimum, develop explicit cooperative arrangements between the Employment Service and CETA. Where possible, however, they should aim at developing arrangements that will allow unified local agencies to become the operating arms of both the federal and the state governments in providing a full spectrum of employment and training programs.

This process should be started now. In some states and for selected prime sponsors who have demonstrated strong administrative competence, state governors could negotiate the assumption of Employment Service functions by local authorities under subcontracting arrangements. Moreover, in local areas or neighborhoods where structural unemployment is particularly acute—and eventually, in other areas as well—regional ETA administrators should take the initiative in establishing comprehensive manpower service centers; this initiative could eventually be taken in other areas as well. Such centers would bring under integrated administration the full range of federally assisted manpower services, including those provided by ES and CETA. Where possible, private-sector agencies providing manpower services to structurally disadvantaged groups should also be included in these centers.

CLARIFYING EMPLOYMENT SERVICE AND CETA FUNCTIONS

The Employment Service should be clearly recognized as having the main responsibility among public agencies for *labor-exchange* functions, including job referral and placement of the best-qualified candidates for available employment opportunities. The role of CETA should be devoted primarily to *employability development* of the disadvantaged and other groups that encounter special difficulties in participating in the labor market. Under this arrangement, the Service should normally screen applicants, refer those who are not job-ready to CETA prime sponsors for training and supplementary services, and be staffed and organized to offer placement services to CETA participants who are job-ready.

The Labor Department should make the separate functions of the Employment Service and CETA clear. We recommend, moreover, that ETA regional administrators be authorized to require each prime sponsor and related State Employment Service office to agree on their respective functions and on means of cooperation, subject to the approval and subsequent monitoring by the regional administrator.

Putting most referral control in ES offices does not mean that CETA organizations and their contractors would or should be prohibited from all job development and placement activities. Many of these organizations have unique capacities for opening job opportunities to their clients who have completed periods of special training. Provided they are adequately coordinated with ES, CETA placement efforts on behalf of the disadvantaged as well as young and older workers will remain highly useful.

FURTHER WAYS TO MAKE THE EMPLOYMENT SERVICE MORE EFFECTIVE

In addition to this clarification of ES functions and the use of Account Representatives and other reforms discussed in Chapter 5, the effectiveness of the Employment Service can be increased by relieving the Service of unnecessary requirements and functions.

The Employment Service has long been faced with a basic dilemma: On the one hand, its effectiveness depends on inducing employers to list suitable job vacancies with it. This, in turn, is likely to occur only if employers know that the Service will present the best available candidates for placement in response to job orders. On the other hand, ES is under legal and other mandates to give preference in job referrals to a wide array of priority categories of people, thus reducing its ability to offer the best candidates. The number of these mandated priority categories has become so large that the whole preferential system has become counterproductive.

We are convinced that more job opportunities will open up for the disadvantaged as well as the other hard-to-employ groups under a system that attracts a broader mix of employer job orders than those that can be filled by applicants of marginal employability. **We recommend that except for veterans who must be accorded preference by statute and migrant and seasonal workers under judicial mandate, the present list of placement priorities stipulated by administrative regulation should be abandoned.** Instead, provisions should be made to assure that sufficient consideration is given to the long-term unemployed, those claiming unemployment insurance benefits after fifteen weeks of unemployment, and registrants under aid for dependent children.

Of course, the Employment Service must adhere strictly to the requirements of equal employment opportunity laws. Furthermore, the changed policy should not relieve the Service of its obligation to cooperate with CETA in the placement of the hard-core unemployed. However, such referrals should meet basic qualification standards.

The ability of the Employment Service to carry out its basic labor-exchange functions is currently also seriously impeded by its legal obligation to carry out a wide variety of enforcement and compliance responsibilities not directly related to its basic mission. It is required to inspect business premises for compliance with safety and health regulations, the Civil Rights Act, and numerous other statutes. This not only preempts an undue share of ES resources but also increases employer reluctance to rely on the Service for job referrals. With the emergence of new regulatory agencies in specific fields related to the workplace (e.g., the Occupational Safety and Health Administration, the Office of Federal Contract Compliance, and the Equal Employment Opportunity Commission), numerous ES enforcement and compliance activities have become redundant.

In the interest of upgrading Employment Service labor-exchange functions, we urge that a systematic review be undertaken to determine what enforcement responsibilities are not essential to those functions and can be transferred to other federal or state agencies without in any way weakening antidiscrimination and other protective social legislation.

COUNTERCYCLICAL AND STRUCTURAL MANPOWER PROGRAMS

As we indicated earlier, many of the recent difficulties in implementing employment and training programs aimed at the hard-to-employ and at securing greater private-sector involvement in this connection stemmed from the fact that during the recession, countercyclical public-service employment often tended to crowd out such programs.

There is a clear need for both types of measures. Although they overlap to some extent, they tend to be directed at different segments of the population, to involve different time horizons, and to call for distinctive policy approaches and administrative structures.

To be most effective, programs to train and place the structurally unemployed should be clearly separated from countercyclical unemployment measures in terms of both allocation and administration at the state and local levels, although all such manpower services should be concentrated under the direction of the Department of Labor. Specifically, funds provided under Title VI of CETA (which covers countercyclical public-service employment assistance) should not be unduly mixed with or substituted for funds intended for the long-term structurally unemployed and for reducing unemployment in distressed areas (Title I and Title II).

To meet these requirements, the legislation governing countercyclical public-service employment was recently changed to assure that more PSE jobs go to those most in need and that they are not simply used to support ongoing government services. Thus, the law now requires that a substantial and rising proportion of CETA enrollees meet an income test and that they must have been unemployed for fifteen weeks or more, exhausted their unemployment benefits, or be on welfare. Also, to minimize substitution, most CETA public-service employment jobs must now be for specific projects of no more than one year's duration. In addition, the project emphasis should permit significantly greater involvement of nonprofit and community-based organizations. These changes in the law are laudable and should result in making PSE programs both more effective and more directly responsive to needs.

However, we believe that additional changes are needed to make PSE more countercyclical and to avoid carrying enrollees in PSE jobs for periods of several years. **We recommend that no individual be retained in a public-service employment job for more than a year (or perhaps a longer specified period at times when the national unemployment rate exceeds a specified figure).** This limitation would give many more difficult-to-place participants an opportunity to gain valuable work experience and yet give them an incentive to continue their search for regular employment.

Many of the recent problems with employment and training programs emerged because adequate countercyclical programs were not in effect when the recession hit. To reduce such problems in the future and to increase the likelihood that needed steps will be taken on a systematic rather than on an ad hoc basis, we urge that more advance thought and preparation be devoted to the types and contents of measures that might be called for and to procedures that would allow appropriate antirecessionary actions to be taken in a timely fashion and without adverse effects on existing programs to cope with long-term structural unemployment.

Taken together with the other measures recommended in this statement, we believe that the changes in the organization and administration of federally aided employment and training programs proposed here would do much to improve the job prospects of hard-to-employ Americans.

Memoranda of Comment, Reservation, or Dissent

Page 12, by R. STEWART RAUCH, JR.

This statement is not valid under all circumstances, and it is not a helpful guide to policy at the present time. Adequate demand is a *sine qua non* for high employment; but the chief concern now is that many structural barriers interfere with the job placement for the hard-to-employ. Such barriers have not been destroyed by past periods of high demand for goods and services. In fact, the speed and nature of technological change and geographical shifts have made many structural barriers more resistant to generalized demand pressures.

Page 13, by HENRY B. SCHACHT

This statement effectively deals with structural unemployment on the assumption that there is an additional need for labor in the private sector, if it can be better trained and identified. Given this assumption, the private sector experimentation on job-related issues is gratifying; governmental programs should be better organized to create additional incentives for these programs. It is beyond the scope of this statement to analyze whether, given inflationary pressures and prospective slower economic growth, private sector demand can sustain full employment. If job demand should prove inadequate, then greater consideration should be given to public jobs programs and/or other forms of public assistance.

Page 15, by JAMES Q. RIORDAN

I disapprove of the Statement.

I do not think that the problems of employment can be achieved with additional detailed initiatives developed in the public sector. In a public/private partnership, the public (i.e., the government) is inevitably the senior partner.

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In our democratic society the senior partner's decisions must reflect political compromises. Political compromises result in inconsistent push/pull directives. The resulting administration is often costly and confused.

We should not be surprised in these circumstances to find that an elderly citizen is "encouraged" to work but is penalized by having his social security pension reduced when he does so. When he complains of the inconsistency, he is told that the penalty must accompany the encouragement in order to keep the social security fund fiscally sound.

We now call for increased hiring of disadvantaged youth and at the same time mandate increases in the minimum cost of doing so in order that the youth shall not take jobs from older unionized workers.

The seemingly intractable problems in our economy relating to employment (and other issues) are not likely to be solved by increased push/pull government participation. I am afraid that such increased participation would be a major consequence of the proposed "new directions for a public/private partnership" and it is for that reason I disapprove the statement.

Page 20, *by* W. D. EBERLE

This recommendation misses the key point —more study is not needed as the estimates of the magnitude of illegal aliens is so large, taken together with the new illegal alien flow, that a policy of action is needed promptly if more jobs are to be available. The present and past two Presidential Administrations have collected substantial background information and material both as to the nature and the magnitude of the problem and possible solutions. The longer laws go unenforced, you either get a breakdown in violating more laws or an over reaction by new laws to correct the problem. The illegal alien problem involves not only jobs, but the rights of people, foreign policy as to our neighbors, and realism as to enforcement. It seems to me that CED should have urged prompt policy action by the President and Congress to (1) adopt a policy as to future illegal aliens entering into the United States with consideration of enlarging the quotas from certain nations but providing for return of new illegal aliens who enter after a certain date; (2) provide for a secure social security card with strict enforcement by employers for employment; (3) a program to make the adjustment to the new policy as is reasonable and appropriate.

This is not an easy action program as it involves foreign policy, jobs and civil rights but postponing prompt action for such a sizable problem will only create justified increased discontent in our democratic society.

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Page 41, by FRAZAR B. WILDE

From the employer's standpoint, it would be helpful if there were a single point of contact with the many programs in existence now and those proposed. It is counterproductive to business and industry, and therefore to the employment of disadvantaged groups, when employers must coordinate many programs with several groups who are concerned only with their own clientele. A "United Way" or "Combined Health Appeal" of these groups would be helpful.

Page 50, by ROBERT R. NATHAN

If there were to be any exemptions from minimum wages there should be experiments with alternatives rather than adopting exemptions without reasonably clear understanding of the consequences. Theoretically, minimum wage levels might price some inexperienced youngsters out of the market. But there are definite costs and dangers involved. Subminimum pay for young people may well serve to transfer jobs from workers at other age levels to those whom employers can hire for less than the minimum standard. Analyses of this issue are not very encouraging with respect to sizable additions to total employment that might result from minimum wage exemptions.

The erosion in the setting of minimum wage standards could, over time, be very costly. Perhaps many who favor exemptions would, in essence, like to discard the whole concept of minimum wages. Until there is convincing evidence that the net additions to employment is significant and outweighs the undermining of reasonable labor standards, we should not tinker with this measure. The burden of anti-inflation efforts and of stimulating jobs should not be put primarily on the backs of those least able to bear that burden. The less skilled young people and minorities want and need to work. But our society ought to be able to provide them with jobs without resorting to substandard pay. We ought to be able to fight inflation successfully without focusing primarily on those at the bottom of the pay scale.

Another consideration is the likely distortion among industries and employers within industries deriving from paying different wages for similar work. If the marketplace were to function effectively, employers would tend to displace present employees at minimum wage levels with those in the exempted category. The resulting shifts and bitterness can be far more costly than the claimed benefits of those favoring exemptions.

Page 51, by JAMES T. HILL, JR.

I would favor the total elimination of penalties on social security benefits by reason of earned (i.e. employment) income during the period between age 65 and age 72. It seems to me difficult, if not impossible, to justify the current distinction between investment income (in whatever form) which involves no penalties, and the penalty currently imposed on earned income during the period between age 65 and age 72. The appropriateness of the elimination of the penalty seems to me to be strongly reinforced by the present movement to lift the mandatory retirement age to 70 in the interest of at least partially mitigating current age discrimination policies. In short, I do not believe our recommendations go far enough in this area or adequately address the grave inequity to which I have adverted.

Page 60, by FRANCIS E. FERGUSON

I do believe that this is more than a stereotype and is dismissed too lightly in the policy statement.

Page 65, by FRANCIS E. FERGUSON

I buy this as part of it, but far more central in my opinion is a return to plain basic education in our public and private schools to readin', writin' and 'rithmetic.

Page 66, by FRANCIS E. FERGUSON

Our experience is not as favorable as indicated on page 66.

Page 82, by CHARLES KELLER, JR.

I hope the importance of Chapter VI will not be overlooked because it comes last in the statement. The United States has no effective national labor exchange, and it is essential that ES be reorganized to provide this essential service. I would go further than the policy statement suggests and urge the removal of ES from state control and its merger into CETA. The steps suggested in Chapter VI are the minimum required.

Appendix Table 1. Comparison of Major Unemployment Indicators, 1965, 1973, and 1976

Selected Categories	*Number of Unemployed (thousands)*			*Unemployment Rate (percent)*			*Percent of Total Labor Force*			*Percent of Total Unemployed*		
	1965	1973	1976	1965	1973	1976	1965	1973	1976	1965	1973	1976
Total, 16 and over	3,366	4,304	7,302	4.5	4.9	7.7	100.0	100.0	100.0	100.0	100.0	100.0
Both sexes, 16 to 19	874	1,225	1,701	14.8	14.5	19.0	7.9	9.5	9.4	26.2	28.5	23.3
Both sexes, 20 to 24	557	985	1,670	6.7	7.8	12.0	11.1	14.3	14.7	16.6	22.9	22.9
Men, 25 and over	1,109	1,076	2,131	2.8	2.5	4.9	53.7	47.9	46.3	33.1	25.0	29.2
Women, 25 and over	809	1,016	1,799	4.0	4.1	6.4	27.3	28.3	29.5	24.1	23.6	24.6
White	2,691	3,411	5,871	4.1	4.3	7.0	88.8	88.7	88.5	79.9	79.2	80.4
Black and others	676	894	1,432	8.1	8.9	13.1	11.2	11.3	11.5	20.1	20.8	19.6
Nonwhite, 16 to 19	169	275	345	26.2	30.2	37.1	0.9	1.0	1.0	5.1	6.4	4.7
Household heads	1,257	1,471	2,763	2.7	2.9	5.1	62.5	57.2	57.2	37.3	34.2	37.9
Married men with spouse	883	905	1,687	2.4	2.3	4.2	49.4	44.4	42.4	26.2	21.0	23.1
Full-time workers	2,791	3,291	5,874	4.2	4.3	7.3	88.5	85.5	85.3	82.9	76.5	80.6
Part-time workers	575	1,013	1,414	6.7	7.9	10.1	11.5	14.5	14.7	17.1	23.5	19.4

Sources: Department of Labor, *Employment and Training Report of the President*, 1977; and *Employment and Earnings* (various issues).

Table 2. Total Population, by Age and Sex *(millions)*

Age	Actual			Projected		
	1960	1970	1975	1980	1985	1990
Both sexes						
16 years and over	121.8	141.1	153.6	165.3	174.0	181.1
16 to 19 years	10.7	15.2	16.6	16.6	14.2	13.4
20 to 24 years	11.1	17.1	19.1	20.8	20.4	17.8
25 to 44 years	47.1	48.1	53.4	61.4	70.6	77.0
45 to 54 years	20.6	23.1	23.6	22.5	22.2	25.0
55 to 64 years	15.6	18.5	19.5	20.8	21.2	20.3
65 years and over	16.7	19.1	21.3	23.3	25.3	27.5
Males						
16 years and over	59.4	67.7	73.6	79.1	83.1	86.4
16 to 19 years	5.4	7.7	8.4	8.4	7.2	6.8
20 to 24 years	5.6	8.6	9.6	10.4	10.2	8.9
25 to 44 years	23.2	23.6	26.2	30.2	34.7	37.9
45 to 54 years	10.1	11.1	11.4	10.9	10.8	12.2
55 to 64 years	7.6	8.7	9.2	9.8	10.0	9.6
65 years and over	7.5	8.0	8.8	9.5	10.2	11.0
Females						
16 years and over	62.4	73.3	80.0	86.2	90.9	94.7
16 to 19 years	5.3	7.5	8.2	8.2	7.0	6.6
20 to 24 years	5.5	8.5	9.5	10.4	10.2	8.9
25 to 44 years	23.9	24.5	27.2	31.2	35.9	39.1
45 to 54 years	10.4	12.0	12.2	11.6	11.4	12.9
55 to 64 years	8.1	9.8	10.3	11.0	11.2	10.7
65 years and over	9.1	11.1	12.5	13.8	15.1	16.5

Source: Bureau of Labor Statistics, *Special Labor Force Projections to 1990*, Special Labor Force Report 197.

Table 3. Percent Distribution of Total Labor Force, by Age and Sex

Age	Actual			Projected		
	1960	1970	1975	1980	1985	1990
Both sexes						
16 years and over	100.0	100.0	100.0	100.0	100.0	100.0
16 to 19 years	7.2	8.9	9.7	9.1	7.5	6.9
20 to 24 years	10.6	14.3	15.1	15.4	14.4	12.2
25 to 44 years	44.0	40.1	42.2	45.2	49.7	52.4
45 to 54 years	20.7	19.8	18.1	15.9	14.9	16.2
55 to 64 years	13.0	13.1	11.8	11.5	10.8	9.7
65 years and over	4.4	3.7	3.1	2.9	2.7	2.7
Males						
16 years and over	67.7	63.3	60.8	59.7	58.6	58.0
16 to 19 years	4.4	5.1	5.4	5.0	4.1	3.7
20 to 24 years	7.1	8.6	8.6	8.5	7.7	6.4
25 to 44 years	30.9	26.5	26.4	27.8	29.9	31.0
45 to 54 years	13.4	12.2	11.0	9.6	8.8	9.4
55 to 64 years	8.9	8.3	7.4	7.0	6.4	5.8
65 years and over	3.2	2.5	2.0	1.8	1.7	1.6
Females						
16 years and over	32.3	36.7	39.1	40.3	41.4	42.0
16 to 19 years	2.9	3.8	4.3	4.1	3.4	3.2
20 to 24 years	3.6	5.7	6.4	6.9	6.7	5.8
25 to 44 years	13.1	13.6	15.8	17.4	19.8	21.4
45 to 54 years	7.3	7.6	7.0	6.4	6.1	6.7
55 to 64 years	4.1	4.8	4.5	4.4	4.3	3.9
65 years and over	1.3	1.2	1.1	1.1	1.1	1.1

Source: Bureau of Labor Statistics.

Table 4. Total Labor Force, by Age and Sex *(millions)*

Age	Actual				Projected		
	1950	1960	1970	1975	1980	1985	1990
Both sexes							
16 years and over	63.9	72.1	85.9	94.8	103.8	110.7	115.9
16 to 19 years	4.5	5.2	7.6	9.2	9.4	8.3	8.0
20 to 24 years	7.9	7.7	12.3	14.3	16.0	16.0	14.2
25 to 44 years	29.3	31.7	34.5	40.0	46.9	55.0	60.7
45 to 54 years	11.5	14.9	17.0	17.1	16.5	16.5	18.7
55 to 64 years	7.6	9.4	11.3	11.2	11.9	11.9	11.2
65 years and over	3.0	3.2	3.2	2.9	3.0	3.0	3.1
Males							
16 years and over	45.4	48.9	54.3	57.7	62.0	64.9	67.2
16 to 19 years	2.8	3.2	4.4	5.1	5.2	4.5	4.3
20 to 24 years	5.2	5.1	7.4	8.2	8.9	8.6	7.5
25 to 44 years	21.0	22.3	22.8	25.0	28.8	33.0	35.9
45 to 54 years	8.2	9.6	10.5	10.5	9.9	9.7	10.9
55 to 64 years	5.8	6.4	7.1	7.0	7.3	7.2	6.7
65 years and over	2.5	2.3	2.2	1.9	1.9	1.8	1.9
Females							
16 years and over	18.4	23.3	31.6	37.1	41.8	45.8	48.7
16 to 19 years	1.7	2.1	3.3	4.1	4.2	3.8	3.7
20 to 24 years	2.7	2.6	4.9	6.1	7.1	7.4	6.7
25 to 44 years	8.3	9.4	11.7	15.0	18.1	22.0	24.8
45 to 54 years	3.3	5.3	6.5	6.7	6.6	6.8	7.8
55 to 64 years	1.8	3.0	4.2	4.2	4.6	4.7	4.5
65 years and over	0.6	0.9	1.1	1.0	1.1	1.2	1.3

Source: Bureau of Labor Statistics, *New Labor Force Projections to 1990*, Special Labor Force Report 197.

Table 5. Total Labor Force Participation Rates, by Age and Sex *(percent)*

Age	Actual			Projected		
	1960	1970	1975	1980	1985	1990
Both sexes						
16 years and over	59.2	60.9	61.7	62.8	63.6	64.0
16 to 19 years	48.9	50.4	55.1	57.3	58.3	59.3
20 to 24 years	67.5	71.8	74.9	77.0	78.5	79.5
25 to 44 years	67.6	71.7	75.0	76.3	77.9	78.8
45 to 54 years	71.5	73.6	72.7	73.6	74.4	74.9
55 to 64 years	60.2	61.1	57.4	57.1	56.0	55.4
65 years and over	20.3	16.9	13.8	12.9	11.9	11.3
Males						
16 years and over	82.4	80.3	78.5	78.4	78.1	77.8
16 to 19 years	58.6	57.3	60.9	62.6	62.7	63.2
20 to 24 years	88.9	86.1	85.7	85.4	84.4	83.6
25 to 44 years	96.4	96.8	95.5	95.4	95.1	94.9
45 to 54 years	94.3	94.2	92.0	91.3	90.6	90.2
55 to 64 years	85.2	81.8	75.7	74.3	71.6	69.9
65 years and over	32.2	26.9	21.7	19.9	18.0	16.8
Females						
16 years and over	37.1	43.0	46.4	48.5	50.4	51.5
16 to 19 years	39.1	43.4	49.2	51.9	53.7	55.3
20 to 24 years	46.1	57.5	64.2	68.6	72.6	75.3
25 to 44 years	39.6	47.6	55.1	57.8	61.2	63.3
45 to 54 years	49.3	54.5	54.6	57.1	59.1	60.6
55 to 64 years	36.7	42.6	41.0	41.9	42.2	42.3
65 years and over	10.5	9.6	8.2	8.1	7.8	7.6

Source: Bureau of Labor Statistics, *Special Labor Force Projections to 1990*, Special Labor Force Report 197.

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Financing a Better Election System *(December 1968)*

Innovation in Education: New Directions for the American School *(July 1968)*

Modernizing State Government *(July 1967)*

*Trade Policy Toward Low-Income Countries *(June 1967)*

How Low Income Countries Can Advance Their Own Growth *(September 1966)*

Modernizing Local Government *(July 1966)*

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Representative BOLLING. Thank you, Mr. Burns, for a very interesting and helpful statement.

Ms. Reubens, will you proceed. We will hear all the witnesses before we start questions.

STATEMENT OF BEATRICE G. REUBENS, SENIOR RESEARCH ASSOCIATE, CONSERVATION OF HUMAN RESOURCES, COLUMBIA UNIVERSITY

Ms. REUBENS. Mr. Chairman and members of the committee, I appreciate the opportunity to discuss a subject which the President's state of the Union address identified as a major priority. He called for the elimination of the barriers that restrict the job opportunities available to women. I see three main issues relevant to structural unemployment.

The first is the persistent and widening gap between the unemployment rates of men and women which is exacerbated by the heavier incidence of hidden or discouraged unemployment among women. The second issue is the underemployment suffered by employed women who would like to work more hours and weeks than they do at present.

The third issue concerns the qualitative underemployment of women, which takes the form of occupational concentration in relatively few fields, obstacles to entering male-dominated occupations, unequal pay for equal qualifications and job functions, and restricted access to career ladders and upward mobility.

My prepared statement gives details about these three conditions. I will review this part quickly in order to get to the policy issues.

Table 1 in my prepared statement shows what has happened in the past 30 years, dividing the period into two 15-year segments. I found that the excess of female unemployment over male was minimal in the fist part of the period, but in the last 15 years it has been over 1 percent in every single year.

The latest report of the Council of Economic Advisers attributes the differences between the male and female unemployment rates to the loose labor market attachment of women. But if you look at my table 5 in my prepared statement, you will see that there has been a marked increase in the labor force attachment of women, particularly of married women, and specifically among black women in the younger age group where there is a spouse present and presumably there are children that require home care. Women's rates are beginning to approach male rates. Our thinking about the labor force attachment of women has to be reviewed.

I found that the differences between male and female unemployment rates by age groups are most pronounced and consistent in the prime age groups, especially in the 25- to 44-year range. Among teenagers and young adults, female unemployment rates actually have been slightly lower than male rates in many years.

The concentration of excess female unemployment in the prime age groups probably is due to the fact that reentrants to the labor force form a larger share of female unemployment than of male and that female reentrants are most likely to be prime age women. This again is not loose attachment to the labor market. It represents women coming in who have been out of the labor market for a long time and who may have quite specific needs in order to find jobs.

At this point, it may be well to say that women are not a hard-to-employ group. Nor are they a minority. A question might be raised of why they figure in today's discussion of structural unemployment. The answer is that certain features of their employment situation make women a bit different than males. The solutions to their problem are often somewhat different. But it is important to remember that in recent years some 60 percent of net additional jobs have been taken by women. This, again, is a somewhat different situation than applies to other groups, referred to as hard to employ. The economy simply has not provided enough jobs for all the women who seek them.

Part-time work by women has grown rapidly. The part-time women account for one-third of all women who have done some work during the year. Even male part-time working has been growing faster than full time. We must think of part-time work as a serious and permanent part of people's working patterns.

I think insufficient attention has been given to the impact of inflation on women's labor market decisions, and that, if in the future some control is obtained over inflation, we may see some slowing down of the rate of female labor force entry, which should occur in any case because there is an upper limit to the increase and women's participation rates are not likely to exceed men's.

Inflation is only one of the many factors that enter into forecasts of female participation rates. We need closer approximations to accuracy in such forecasts than the Bureau of Labor Statistics has achieved. Such accuracy is essential if a full employment policy is to be devised.

The underemployment that arises when people work part time who would like to work full time has several components. It consists first of those working part time for economic reasons. In 1976 an average of 1.7 million women were recorded in this category, a larger number than for men. Then there is another group of women whose numbers cannot even be estimated. They normally work part-time, but they would like to move to full-time jobs if those were available. Finally, there is another group of women who now work part time because it is the only schedule that fits their household and child care responsibilities. A number of them would prefer full time if those responsibilities could be shared more fully with husbands or if services were available at reasonable cost. But I think it should be said that the majority of women now working part time prefer such a schedule.

There may be policy conflicts over the priorities that should be set in regard to attempts to satisfy women who want to exchange part-time jobs for full-time work versus unemployed women who seek full-time jobs. Moreover, it can be argued that public policy should stress the further development of part-time jobs over full-time jobs. Part-time jobs are a means of work sharing when the total number of jobs is deficient. They are an approach to protecting those with low job seniority. They are a way of permitting fathers and mothers to share household and child care functions. And they are a method of reducing the income disparity between two-earner and one-earner families.

Support for increased numbers of part-time jobs might be given more readily if such jobs included the public and private fringe benefits associated with full-time jobs. Legal provisions to this effect have been introduced in several countries and women workers are the particular beneficiaries.

I come now to the third type of employment problem, the qualitative underemployment of women. Some might question whether employed women who are underutilized because of occupational segregation should be included in a discussion of structural unemployment. An argument for their inclusion is the adverse effect on female unemployment rates of women's limited access to male-intensive occupations, leading to crowding into the limited range of occupations where females are easily accepted. In 1970, 85 percent of women were employed in the female-intensive or gender-free occupations which accounted for only 44 percent of the Nation's employment.

In principle, this crowding of females increases female unemployment rates. But it has been mitigated by two factors. Employment in the female-intensive occupations, such as clerical jobs, has expanded more rapidly in the postwar period than has employment in the male-intensive occupations. And the female-intensive occupations happen to be less subject to job losses in recession. In fact, female entrance to male-intensive jobs in large numbers may increase women's unemployment rates. In the longer run, however, the anticipated continued rise in female labor force participation rates and the closer approximation of female educational attainment to male levels must cause concern about the receptivity of the male-intensive occupations to female penetration, especially because the male-intensive occupations yield higher earnings and contain a highly disproportionate share of the best-paying and most prestigious jobs.

These occupations have registered some programs in occupational desegregation in recent years. From 1972 to 1977 the proportion of women among professional and technical workers increased from 0.39 to 0.43 and rose from 0.18 to 0.22 among managers and administrators. However, in the craftsman and foreman category, the change in the female share has been slight and women were only 5 percent of the total in 1977.

Vigorous monetary and fiscal policy cannot eliminate all of the employment problems of special groups in the labor force or reconcile the geographical and occupational imbalances between the demand and supply of labor. But a buoyant economy makes an important contribution to the reduction of unemployment and is a highly desirable accompaniment to efforts to cope with structural unemployment. Therefore the highest priority should be given to devising and implementing policies that restrain inflationary pressures in order that monetary and fiscal measures may be applied more freely to expand economic activity. The political and economic constraints on adopting stimulatory measures in the absence of antiinflationary price and wage policies indicate that the two issues are inextricably joined.

If the slack in the economy is taken up, women stand to benefit from an expansion of activity. It will bring reductions in their unemployment rate, the number of discouraged unemployed, and the number of involuntary part-time workers. It also provides a better climate for the desegregation of male-dominated occupations.

A sustained period of full employment, such as many foreign countries enjoyed in the 1960's, tends to cause the convergence of the unemployment rates of various demographic groups in the labor market. Although some groups have more frequent entrance and reentrance to the labor market and higher job turnover rates, the high level of demand results in relatively little unemployment on labor market entrance or in job changing.

We have become so accustomed to a large labor reserve that we take it as an immediate law that women and youth will have much higher unemployment rates than prime age males, although the relationships are in fact determined by specific social and economic conditions and policies.

An attempt to reduce our labor reserve of unemployed and underemployed women at this time poses special problems for expansionary policy, beyond the fears of inflation, rising energy costs and resource constraints. The rate of growth of our female labor force, more rapid than in many countries, has outstripped the economy's creation of new jobs, although an extraordinary record on new jobs was set in 1977.

Moreover, in the laudable effort to satisfy individual desires, guarantee rights, and diminish dependency, we have initiated policies and programs which encourage further expansion of the labor force. Through various measures, potential retirees, welfare mothers, legal and illegal immigrants, and school age youth are encouraged to enter the labor force. These programs have been adopted independently of and in advance of any assurance that the total number of jobs in the economy can grow sufficiently to absorb both the ordinary growth of the labor force and the new additions.

The sequence of policy—the reverse of what the situation requires—that is, it would be desirable to know first that there will be growth in private sector jobs and then encourage groups to enter the labor force. Moreover, the individual actions which result in an increase in the labor force have been taken separately without cross-consultation, setting of priorities for groups or assessment of the impact of social measures on the labor force. Unfortunately, the same criticism can be made of employment and training programs. The total numbers chosen for programs, the criteria for their selection, and the priorities assigned to various groups are at best poorly coordinated with the absorptive capacity of the economy or the occupational and geographic demand for labor.

Success is sometimes equated with making people more competitive in a game where there are many losers. The programs are continued in the hope of future job expansion, in the desire to help individuals and disadvantaged groups, in the understandable belief that doing nothing for the unemployed is worse, in the desire to provide some income maintenance, and in the conviction that some programs can make a direct contribution to society and the economy. Many of the problems of adjusting labor market policy could be diminished if macroeconomic policy had a freer scope for action.

The issue has been raised that if the economy continues its recovery, we will face a shortage of skilled workers, and one of the groups to draw upon would be underutilized women. I agree with the conclusion, but I would point out that the real issue is whether we have sufficient training capacity in industry and whether it is maintained over the business cycle, such that all of the workers, and that includes males, who would be available for skill upgrading, are getting the chance to acquire those skills.

The United States, contrary to the experience of almost all other advanced countries, has no national training policy and it particularly has no policy that fills the void between what private enterprise does on its own and what the Government does for the hard-to-employ or disadvantaged groups. This gap, I think, refers not only to women but to all workers. It is where the real trouble lies, and it may result in tension in the labor market because too few workers have been trained in skills over the recession period. It is not sufficient to rely on public training programs for the disadvantaged.

I submit that one of the key issues that should be addressed in connection with possible shortages of skilled workers in the future is the need for a national training policy, in which employers, the Government, and trade unions sit down and look at the skill needs of the economy, not simply the needs of individuals for jobs. There are many examples from other countries that could be cited where this is done on a national basis.

Now, to return to the needs of women. The programs classified as dealing with employment and training may conveniently be divided into four types, without regard to the Government agencies that provide them. The four are: preparation for employment, support services, basic education and skill training, and job creation, whether public or private.

Women require programs that emphasize preparation for employment, since many are new entrants or reentrants after a prolonged absence from the labor market. As succeeding generations of young women establish attachment patterns almost like those of men, this aspect will diminish in importance. But at present there are many women who enter the job market lacking confidence in themselves, not knowing what they can do and what is available, and needing information about how to present and conduct themselves.

A short introductory course which can be offered in institutions where occupational training occurs can provide occupational information, a review of available training opportunities and brief exposure to several training courses in different occupations as a precursor to a choice of a training or educational course. Such courses are offered in other countries and have been successful. Such courses should have a study unit on job search methods.

Although public programs should set an income limit for applicants, it is possible to charge fees to higher income women, such as displaced homemakers, for whom such programs may be well suited and not otherwise available. It is useful to have outreach programs to find women who can benefit from such programs and might otherwise rely on public income programs.

Women in such programs particularly need to take training courses that enable them to earn sufficient income so they do not return to the dependency situation. An investment in training should consider the access to the higher paid occupations, which frequently are the male-intensive occupations.

Two basic questions can be raised about all of these programs as they affect women. Should there be separate programs for women, as there are for young people? And should all of the programs addressed to women make a special point of directing women toward the male-intensive occupations? It may seem paradoxical to sponsor sex segregated employment and training programs in order to foster sex desegregation of jobs. But the grounds for establishing separate programs for special groups are persuasive. Separate programs may be indicated if existing programs do not give adequate representation to a group, such as women, or if women or subgroups of women, such as welfare mothers, need services that are not routinely part of general programs, or if groups are organized and exert political pressure.

Almost all countries, no matter how comprehensive their labor market programs, establish programs for special groups, among them women. Administrative tidiness may be less important in this instance than convenience and the ability to target programs.

The second question—whether programs addressed to women should stress the advantages of male-dominated occupations—would receive a rousing positive answer from many who are concerned about the status of women. Antidiscrimination laws, affirmative action, counseling programs, and programs to change the educational system all are engaged in this effort, outside of the realm of employment and training programs. Several successful training programs, such as the minority women's employment program (MWEP) to place minority women in professional jobs, the apprenticeship outreach program (AOP) to find, coach, and place women in apprenticeships, and similar programs, also have this goal.

While there is still a long way to go before women take over highly valued male preserves, some questions arise about the single-minded pursuit of male-dominated occupations. The alternative of upgrading the female occupations, through trade union organization and other methods, is rarely mentioned. Yet such a move would not only serve women well, but would make the female occupations attractive to males who might then willingly make more room for women in their traditional occupations.

As a part of social policy we ought to consider that, as more and more women work and more and more children are left in day-care centers, there is a greater need for men to work in day-care centers and in elementary schools. There are other social objectives, in addition to increasing the GNP, that might dictate an effort to direct men into traditionally female jobs. In the longer run, if women's entrance into male-dominated occupations is not matched by an equal effort to move men into the traditionally female occupations, a major success story for women will necessarily be accompanied by large-scale male unemployment or withdrawal from the labor market. The much needed effort to redress the occupational concentration of women and their inferior status in the labor market should not become the vehicle for creating new imbalances.

Thank you, Mr. Chairman.

[The prepared statement of Ms. Reubens follows:]

Prepared Statement of Beatrice G. Reubens

Employment Problems of Women

Mr. Chairman and members of the committee: I appreciate the opportunity to discuss a subject which the President's State of the Union address identified as a major priority. He called for the elimination of the barriers that restrict the job opportunities available to women. I see three main issues. The first is the persistent and widening gap between the unemployment rates of men and women which is exacerbated by the heavier incidence of hidden or discouraged unemployment among women. The second issue is the temporal underemployment suffered by employed women who would like to work more hours and weeks than they do at present. The third issue concerns the qualitative underemployment of women which takes the form of occupational concentration in relatively few fields, obstacles to entering male-dominated occupations, unequal pay for equal qualifications and job functions, and restricted access to career ladders and upward mobility.

EXTENT OF THE PROBLEM

Unemployment

Since 1970 the female unemployment rate has been higher than it was in earlier periods. In addition the disparity between male and female unemployment rates has worsened. While the differences have not been so staggering as those between white and black unemployment rates or between prime-age and teenage rates, there has been no year in the postwar period when the average annual female unemployment rate was lower than the male rate. However, in the 15 years from 1947 through 1961, the women's rate was not much above the male and it exceeded the male rate by 1 percent or more in only two years. But in the succeeding 15 years, from 1962 through 1976, the gap between the two unemployment rates was 1 percent or more in every single year, and in 10 of the 15 years the excess was closer to 2 percent. It appears that a new, higher level of female unemployment rates in relation to male may have been established.

TABLE 1.—UNEMPLOYMENT RATES, 16 YEARS AND OVER, BY SEX, ANNUAL AVERAGES 1947 TO 1976

Year	Male	Female	Excess of female over male	Year	Male	Female	Excess of female over male
1947	4.0	3.7	0.3	1962	5.2	6.2	1.0
1948	3.6	4.1	.5	1963	5.2	6.5	1.3
1949	5.9	6.0	.1	1964	4.6	6.2	1.6
1950	5.1	5.7	.6	1965	4.0	5.5	1.5
1951	2.8	4.4	1.6	1966	3.2	4.8	1.6
1952	2.8	3.6	.8	1967	3.1	5.2	2.1
1953	2.8	3.3	.5	1968	2.9	4.8	1.9
1954	5.3	6.0	.7	1969	2.8	4.7	1.9
1955	4.2	4.9	.7	1970	4.4	5.9	1.5
1956	3.8	4.8	1.0	1971	5.3	6.9	1.6
1957	4.1	4.7	.6	1972	4.9	6.6	1.7
1958	6.8	6.8	.0	1973	4.1	6.0	1.9
1959	5.3	5.9	.6	1974	4.8	6.7	1.9
1960	5.4	5.9	.5	1975	7.9	9.3	1.4
1961	6.4	7.2	.8	1976	7.0	8.6	1.6

Source: U.S. Department of Labor, "Employment and Training Report of the President," 1977, table A-1.

An examination of the differences between male and female unemployment rates by age groups reveals that the excess of female over male rates is most pronounced and consistent in the prime age groups, especially in the 25 to 44 year range. Among teenagers and young adults, female unemployment rates actually have been slightly lower than male rates in many years. The concentration of excess female unemployment in the prime age groups probably is due to the fact that reentrants to the labor force form a larger share of female unemployment than of male and that female reentrants are most likely to be prime age women.

The unemployment rates must be supplemented by taking account of the discouraged or hidden unemployed. According to the Bureau of Labor Statistics count, roughly twice as many women as men were hidden unemployed in the period 1967–1976. For the most recent recession, a study by Ralph Smith, commissioned by this Committee, has estimated the "jobless rate." This measure calculates the total number of jobs lost by various demographic groups because

TABLE 2.—PERSONS NOT IN THE LABOR FORCE WHO WANT A JOB NOW, BY SEX, ANNUAL AVERAGES, 1967 TO 1976

Year	Persons 16 yr and over (thousand)		Year	Persons 16 yr and over (thousand)	
	Males	Females		Males	Females
1967	222	511	1972	239	525
1968	213	454	1973	225	454
1969	183	391	1974	227	459
1970 [1]	221	417	1975	359	722
1971	238	536	1976	321	590

[1] Because of a change in 1970 in the sampling pattern for persons not in the labor force, the date for 1967–69 may not be strictly comparable with data for subsequent years.

Source: U.S. Department of Labor, "Employment and Training Report of the President," 1977, table A–12.

unemployment was not held to the 4 percent level, based on the normal rather than actual growth of the labor force. Application of this method for the period 1970–1975 results in an excess of the female (20 years and over) "jobless rate" over the male considerably greater than the gap between the respective official unemployment rates.[1]

Information about the employment records of males and females also is relevant. Divergent trends for men and women are revealed by the employment/population ratio which is calculated as the average annual employed proportion of the population 16 years and over.

TABLE 3.—RATIOS OF CIVILIAN EMPLOYMENT TO NONINSTITUTIONAL POPULATION, BY SEX AND RACE, UNITED STATES, ANNUAL AVERAGES, 1947–76

Year	Employment/population ratios, 16 yr and over		Employment/civilian population							
			18–19 yr				20–24 yr			
			Male		Female		Male		Female	
	Male	Female	White	Black	White	Black	White	Black	White	Black
1947	80.4	30.6								
1948	81.1	31.3	69.0	69.6	49.9	35.2	79.0	75.6	43.2	42.3
1949	78.8	31.1								
1950	78.8	31.9								
1951	79.1	33.1								
1952	78.3	33.4								
1953	78.2	33.3								
1954	76.1	32.5								
1955	77.3	33.9								
1956	78.1	35.1	64.9	65.0	48.6	34.2	82.3	78.2	44.1	38.3
1957	77.3	35.1								
1958	74.9	34.5								
1959	75.8	34.9								
1960	75.5	35.5								
1961	74.2	35.3								
1962	74.1	35.5								
1963	73.7	36.4								
1964	73.9	36.3								
1965	74.2	37.1	58.3	53.2	43.8	28.9	80.3	81.4	46.1	47.6
1966	74.1	38.3								
1967	73.8	39.0								
1968	73.6	39.6	60.3	51.3	47.4	34.6	78.6	77.9	50.8	51.2
1969	73.6	40.7								
1970	72.6	40.8	59.3	47.5	48.5	30.0	75.5	73.0	53.7	49.0
1971	71.9	40.3								
1972	72.5	40.9								
1973	73.2	42.0	65.1	47.8	52.5	30.1	80.2	71.5	57.3	47.4
1974	72.7	42.5	65.0	45.8	52.5	29.6	79.8	69.5	58.6	47.7
1975	68.5	42.0	60.3	38.6	50.7	27.8	74.2	60.4	58.1	43.6
1976	70.1	43.2	62.1	36.7	52.5	28.1	76.8	62.2	59.3	44.8

Source: U.S. Department of Labor, "Employment and Training Report of the President" 1977, table A1; Department of Labor unpublished data.

[1] Achieving the Goals of the Employment Act of 1946—Thirtieth Anniversary Review. Vol. 1 Employment, Paper No. 6. The Impact of Macroeconomic Conditions on Employment Opportunities for Women. Joint Committee Print. 94th Congress, 2d session, January 3. 1977; Ralph E. Smith and Jean E. Vanski, *The Jobless Rate: Another Dimension of the Employment Picture,* Washington: The Urban Institute, 1975.

Those who have been citing the trend in the employment/population ratio without making a sex breakdown must reconsider their view that the economy has performed well in regard to providing jobs in spite of higher unemployment rates, unless they wish to rest their case entirely on the female side. There has been a definite decline in the male ratio from 1947 through 1976—from 80 percent at the beginning of the period to around 70 percent at the end. Women, on the contrary, showed a marked increase in the ratio, from over 30 percent in 1947 to 43 percent in 1976. In 1947 the male ratio exceeded the female by about 50 percentage points. If an age cut-off of 65 had been used, the female ratio would have advanced even more compared to the male, because the greater longevity of females and their lower rate of employment after 65 affects the ratio.

These trends in employment ratios suggest that the growth in female employment and in women's share of total employment owes almost as much to the decline on the male side as to the increase on the female side. It also suggests that some inquiries should be made into the male situation to make certain that sub-groups of men, in addition to black men, are not disadvantaged in the labor market. Their employment problems tend to be neglected because they are unorganized.

For policy purposes it is significant that the excess of female unemployment rates over male since 1947, and the widened gap between the two since 1962, occurred in the face of a pronounced increase in female employment by any measure. The economy has not provided jobs as fast as women seek them, but by no stretch of the imagination can it be said that the economy has stood still with respect to the quantity of employment of the two sexes, even allowing for the greater propensity of females to work at part-time jobs. This Committee's compendium of papers on *American Women Workers in a Full Employment Economy*, among other studies, presents in detail the causes of this surge of women, especially married women, into the labor market. It has been a movement which seems to exemplify the advertising slogan "the more you have, the more you want."

Insufficient attention may have been given to the impact of inflation on women's labor market decisions. It is one of the many factors that should enter into forecasts of female labor force participation rates. Closer approximations to accuracy in such forecasts than the Bureau of Labor Statistics has shown are essential if a full employment policy is to be devised.

Temporal Underemployment

Many women whose work schedules provide less than a full-time week would like to work full-time. Some of them work part-time for economic reasons. Available statistics for 1967 through 1970 show that the number of males in normally full-time non-agricultural employment who were on part-time for economic reasons usually exceeded the number of females. But since 1970 the position has been reversed. In 1976, 1.7 million women, on average, worked part-time for economic reasons and presumably wanted to work full-time. Another group of women whose number cannot even be estimated are in part-time jobs, but are eager and able to move to full-time jobs if suitable employment is offered. Over the years there has been an increase in the proportion of women in part-time jobs. In 1976, over one-third of all women with work experience during the year worked part-time, and a considerable number undoubtedly prefer it.

Still another group of women now work part-time because it is the only schedule that fits with their household and child-care responsibilities. But a number undoubtedly would prefer full-time jobs if their household and child-care responsibilities were shared more fully or if services were available at reasonable cost.

Conflicts over priorities may arise between attempts to satisfy women who want to exchange part-time jobs for full-time work and unemployed women who seek full-time jobs. Moreover, it can be argued that the further development of part-time jobs should be stressed by public policy. Part-time jobs are a means of work-sharing when the total number of jobs is deficient, an approach to protecting those with low seniority, a way of permitting fathers and mothers to share household and child-care functions, and a method of reducing the income disparity between two-earner and one-earner families. Support for increased numbers of part-time jobs would be given more readily if such jobs included the public and private fringe benefits associated with full-time jobs. Legal provisions to this effect have been introduced in several countries and women workers are the particular beneficiaries.

TABLE 4.—PERSONS WITH WORK EXPERIENCE DURING THE YEAR WHO NORMALLY WORK PART-TIME, SELECTED YEARS, 1950–76

Year	Percent of all women in part-time jobs [1]	Percent of all men in part-time jobs [1]
1950	26.6	9.8
1952	25.5	8.5
1954	26.8	10.6
1956	29.4	10.9
1958	31.7	13.1
1960	32.4	13.1
1962	32.1	13.1
1964	32.1	13.1
1966 [2]	29.9	11.2
1968	29.7	11.3
1970	32.1	12.4
1972	30.8	12.3
1975	33.0	12.4
1976	33.6	12.5

[1] Usually work less than 35 hr a week

[2] Data revised to refer to persons 16 yr and over in accordance with the changes in age limit and concepts introduced in 1967.

Source: U.S. Department of Labor, "Employment and Training Report of the President," 1977, table B-14; "Special Labor Force Report 201, Work Experience of the Population in 1976."

It is significant that an increasing proportion of women part-time workers has been accompanied by an increasing proportion of full-year women participants in the labor force. The rising share having a full-year attachment to the labor force is particularly conspicuous among black women and married women with spouse present. Contributing to the soaring female participation rates, the higher proportion of women with full-year participation weakens the argument that women are intermittent workers who cannot be given the on-the-job experience and training necessary for promotion.

TABLE 5.—PERCENT OF WOMEN WITH WORK EXPERIENCE DURING THE YEAR WHO WERE IN THE LABOR FORCE 50–52 WK, SELECTED YEARS, 1965–76

[In percent]

Year	All Women	White women				Black and other women			
		All	Single and other marital status	Married, spouse present	Married, spouse present 25–44 yr old	All	Single and other marital status	Married, spouse present	Married, spouse present 25–44 yr old
1965	55.5	55.6	60.1	52.5	50.5	55.1	59.1	50.9	51.5
1967	56.4	56.3	56.7	56.0	52.8	57.2	57.0	57.3	60.0
1968	55.0	54.8	55.7	54.2	50.8	56.1	54.9	57.3	57.5
1970	56.5	56.1	56.2	56.0	52.0	59.3	56.7	62.2	65.5
1972	59.2	58.9	58.6	59.1	56.3	61.6	61.1	62.0	63.0
1974	60.8	60.5	60.6	60.4	57.8	63.0	61.9	64.3	66.2
1975	62.5	61.9	61.7	62.0	58.5	66.5	65.0	68.2	69.0
1976	60.8	60.2	59.9	60.3	57.4	66.1	64.1	68.6	72.3

Source: U.S. Bureau of Labor Statistics, Special Labor Force Reports, Work Experience of the Population, nos. 76, 91 107, 115, 141, 162, 171, 181, 192, 201.

QUALITATIVE UNDEREMPLOYMENT

Some might question whether employed women who are underutilized because of occupational segregation should be included in a discussion of structural unemployment. An argument for their inclusion is the adverse effect on female unemployment rates of women's limited access to male-intensive occupations, leading to crowding into the limited range of occupations where females are easily accepted. In 1970, 85 percent of women were employed in the female-intensive or gender-free occupations which accounted for only 44 percent of the nation's employment. To put it another way, the male-intensive occupations that provided 80 percent of male employment included only 15 percent of all employed women in 1970.[2]

In principle, this crowding of females increases female unemployment rates. But it has been mitigated by two factors. Employment in the female-intensive occupations has expanded more rapidly in the postwar period than has employment in the male-intensive occupations. And the female-intensive occupations happen to be less subject to job losses in recession. In fact, female entrance to these jobs in large numbers may increase women's unemployment rates. In the longer run, however, the anticipated continued rise in female labor force participation rates and the closer approximation of female educational attainment to male levels must cause concern about the receptivity of the male-intensive occupations to female penetration, espcially because the male-intensive occupations yield higher earnings and contain a highly disproportionate share of the best-paying and most prestigious jobs.

These occupations have registered some progress in occupational desegregation in recent years. From 1972 to 1977 the proportion of women among professional and technical workers increased from .39 to .43 and rose from .18 to .22 among managers and administrators. However, in the craftsman and foreman category, the change in the female share has been slight and women were only 5 percent of the total in 1977.[3]

There is some disagreement about the definition, measurement and causes of this type of female underemployment. Its magnitude has not been established beyond the calculation of what would be required to obtain the same proportion of women in the male intensive occupations as prevails in the entire labor force. According to calculations I and my co-author made for this Committee's Compendium on "American Women Workers in a Full Employment Economy" in 1976, between 12 and 13 million women, then employed in female intensive occupations, would have had to displace the same number of men in male intensive occupations in order to establish the overall female share of employment in the male intensive occupations. All of the displaced men would have to move into female intensive occupations, such as office work, or face unemployment. If only new hires were to be affected by the policy of equalizing male and female employment in all occupations, it would take many years to achieve the goal. Access to career ladders and the higher positions in firms and institutions are issues beyond the basic matter of occupational segregation. Again no reliable estimates of the number of underemployed women are available.

The concern about qualitative female underemployment is not confined to covert or overt employer and institutional discrimination against qualified women. It reaches back into the formation from earliest childhood of female and male attitudes toward work roles, educational and career choices, and labor force attachment. Parents, the broader society, and educational institutions instill sex-differential roles, models, and ambitions. As a consequence, the type and amount of education and training obtained by women does not match that of men. Moreover, the unequal sharing of household and child care obligations and the growing proportion of female-headed households present particular problems in augmenting the women's share of the more demanding male-intensive occupations. In short, many of the issues that arise in regard to the quantity of jobs available to women are intensified when the focus shifts to the quality of job openings. Policy conflicts may arise between the goal of expanding the quantity of female employment, in which the nature of the jobs is not at issue, and the goal of desegregating occupations, which pays attention only to the nature of the job.

POLICIES FOR FEMALE STRUCTURAL UNEMPLOYMENT

Macroeconomic Policy

Vigorous monetary and fiscal policy cannot eliminate all of the employment problems of special groups in the labor force or reconcile the geographical and

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[2] Beatrice G. Reubens and Edwin P. Reubens, "Women Workers, Nontraditional Occupations and Full Employment," "American Women Workers in a Full Employment Economy." A compendium of papers submitted to the Subcommittee on Economic Growth and Stabilization of the Joint Economic Committee, Washington: Government Printing Office, 1977.

[3] Clair Vickery, Barbara R. Bergmann and Katherine Swartz, "Unemployment Rate Targets and Anti-inflation Policy as More Women Enter the Workforce," a paper presented at the annual meeting of the American Economic Association in New York, December 1977.

occupational imbalances between the demand and supply of labor. But a buoyant economy makes an important contribution to the reduction of unemployment and is a highly desirable accompaniment to efforts to cope with structural unemployment. Therefore, the highest priority should be given to devising and implementing policies that restrain inflationary pressures in order that monetary and fiscal measures may be applied more freely to expand economic activity. The political and economic constraints on adopting stimulatory measures in the absence of anti-inflationary price and wage policies indicate that the two issues are inextricably joined.

If the slack in the economy is taken up, women stand to benefit from an expansion of activity which brings a reduction in their unemployment rate, in the number of discouraged unemployed, and in the number of involuntary part-time workers. It also provides a better climate for the desegregation of male-dominated occupations. A sustained period of full employment, such as many foreign countries enjoyed in the 1960s, tends to cause the convergence of the unemployment rates of various demographic groups in the labor market. Although some groups have more frequent entrance and reentrance to the labor market and higher job turnover rates, the high level of demand results in relatively little unemployment on labor market entrance or in job-changing. We have become so accustomed to a large labor reserve that we take it as an immutable law that women and youth will have much higher unemployment rates than prime age males, although the relationships are in fact determined by specific social and economic conditions and policies.

An attempt to reduce our labor reserve of unemployed and underemployed women at this time poses special problems for expansionary policy, beyond the fears of inflation, rising energy costs and resource constraints. The rate of growth of our female labor force, more rapid than in many countries, has outstripped the economy's creation of new jobs, although an extraordinary record was set in 1977. Moreover, in the laudable effort to satisfy individual desires, guarantee rights, and diminish dependency, we have initiated policies and programs which encourage further expansion of the labor force. Through various measures, potential retirees, welfare mothers, legal and illegal immigrants, and school age youth are encouraged to enter the labor force. These programs have been adopted independently of and in advance of any assurance that the total number of jobs in the economy can grow sufficiently to absorb both the regular growth of the labor force and the new additions.

Not only is the sequence of policy the reverse of what the situation requires, but the individual actions which result in an increase in the labor force have been taken separately without cross-consultation, setting of priorities for groups or assessment of the impact of social measures on the labor force. Unfortunately, the same criticism can be made of employment and training programs. The total numbers chosen for programs, the criteria for their selection, and the priorities assigned to various groups are at best poorly coordinated with the absorptive capacity of the economy or the occupational and geographic demand for labor. Success is sometimes equated with making people more competitive in a game where there are many losers. The programs are continued in the hope of future job expansion, in the desire to help individuals and disadvantaged groups, in the understandable belief that doing nothing for the unemployed is worse, in the desire to provide income maintenance, and in the conviction that some programs can make a direct contribution to society and the economy. Many of the problems of adjusting labor market policy could be diminished if macroeconomic policy had a freer scope for action.

Employment and Training Programs for Women

The programs classified as dealing with employment and training may conveniently be divided into four types, without regard to the government agencies that provide them. The four are: Preparation for Employment; Support Services; Skill Training and Education; and Job Creation, Public and Private.

Women require programs that emphasize preparation for employment, since many are new entrants or reentrants after a prolonged absence from the labor market. As succeeding generations of young women establish attachment patterns almost like those of men, this aspect will diminish in importance. But at present there are many women who enter the job market lacking confidence in themselves, not knowing what they can do and what is available, and needing information about how to present and conduct themselves. A short introductory course which can be offered in institutions where occupational training occurs, can provide occupational information, a review of available training opportunities and brief exposure to several training courses in different occupations as a precursor to a choice of a training or educational course. Such courses should have a study unit on job search as the period of study comes to an end.

Although public programs should set an income limit for applicants, it is possible to charge fees to higher income women, such as displaced homemakers, for whom such programs may be well suited and not otherwise available. It is useful to have outreach programs to find women who can benefit from such programs and might otherwise rely on public income programs.

Two basic questions can be raised about all of these programs as they affect women. Should there be separate programs for women, as there are for young people? And should all of the programs addressed to women make a special point of directing women towards the male intensive occupations? It may seem paradoxical to sponsor sex segregated employment and training programs in order to foster sex desegregation of jobs. But the grounds for establishing separate programs for special groups are persuasive. If existing programs do not give adequate representation to a group such as women or if women or a sub-group of women, such as welfare mothers, need services that are not routinely part of general programs or if groups are organized and exert political pressure, separate programs may be indicated. Almost all countries, no matter how comprehensive their labor market programs, establish programs for special groups, among them women. Administrative tidiness may be less important in this instance than convenience and the ability to target programs.

The second question—whether programs addressed to women should stress the advantages of male-dominated occupations—would receive a rousing positive answer from many who are concerned about the status of women. Anti-discrimination laws, affirmative action, counseling programs and programs to change the educational system all are engaged in this effort, outside of the realm of employment and training programs. Several successful training programs, such as the Minority Women's Employment Program (MWEP) to place minority women in professional jobs, the Apprenticeship Outreach Program (AOP) to find, coach and place women in apprenticeships, and similar programs, also have this goal and more are likely to arise.

While there is still a long way to go before women take over highly valued male reserves, some questions arise about the single-minded pursuit of male dominated occupations. The alternative of ungrading the female occupations, through trade union organization and other methods, is rarely mentioned. Yet such a move would not only serve women well, but would make the female occupations attractive to males who might then willingly make more room for women in their traditional occupations. In the longer run, if women's entrance into male dominated occupations is not matched by an equal effort to move men into the traditionally female occupations, a major success story for women will necessarily be accompanied by large-scale male unemployment or withdrawal from the labor market. The much needed effort to redress the occupational concentration of women and their inferior status in the labor market should not become the vehicle for creating new imbalances.

Representative BOLLING. Thank you, Ms. Reubens.

Next we have Mr. Michael Wiseman, assistant professor of economics, University of California at Berkeley. Sir, if you could summarize your prepared statement, it will be helpful.

STATEMENT OF MICHAEL WISEMAN, ASSISTANT PROFESSOR OF ECONOMICS, UNIVERSITY OF CALIFORNIA, BERKELEY

Mr. WISEMAN. Mr. Chairman and members of the committee, thank you for the opportunity to join in this discussion of policies related to structural unemployment. Structural unemployment, as I use the term, refers to joblessness left when the economy has been pushed to full capacity, that is, the maximum rate of output consistent with nonaccelerating inflation. We do not know what full capacity output is, nor are we sure about the level of aggregate unemployment that is associated with full capacity utilization given the existing structure of the economy and current policies. But, we do know quite a bit about what the makeup of full employment-unemployment is likely to be, and we can evaluate the impact of various policies in terms of impact on this residual joblessness.

I will organize my remarks around the approach to structural unemployment in the latest annual report of the Council of Economic Advisers. In their report, members of the Council emphasize the problems posed for the administration's longrun unemployment goals by structural unemployment. They evaluate the $10 billion-plus of Federal manpower programs now in operation largely in terms of possible effects on structural unemployment and the ability of the economy ever to achieve an unemployment rate on the underside of 6 percent in an environment of moderate, nonaccelerating inflation.

Three recommendations constitute the bottom line of the report: (1) We should work for better targeting of PSE; (2) the country should consider some sort of wage-subsidy for employment of the unskilled; and (3) as always, we need better data.

As I see it, there are at least two important aspects of the Council's discussion that deserve extended thought by this committee. One is the problem of structural unemployment defined along nondemographic lines. The second is the issue of direction of development in CETA PSE. Below I take up each in turn.

Before starting I should mention my background. I have been, for the past 5 years, engaged in research in poverty and public service employment supported in one way or another by the Office of Research and Development of the Employment and Training Administration of the U.S. Department of Labor. Along with professor Harry Katz of the department of economics at MIT, I am currently completing a paper on regulation development in CETA PSE policy for the National Commission on Manpower Policy. This paper will be published as part of the Commission's report to Congress on the net effects of PSE. In addition to this paper, I serve as a field monitor for the Brookings Institutions study of PSE operations; this also is NCMP-sponsored research.

Reading the Council's report, one gets the impression that structural unemployment is exclusively a demographic issue, that is, it can be defined in terms of the special unemployment problems of youth, minority workers, the aged, and women. This characterization leads to the natural conclusion that what we need are policies oriented toward these demographic groups. Teenage unemployment, for example, requires a PSE work experience program oriented toward youth.

But this ignores the geographic aspect of structural unemployment. The decline in employment and population in older cities in the United States is clearly a major trend in American economic development during the past 10 years. While our young cities, principally in the sun belt, but elsewhere as well, have been flourishing, those cities that matured before the Great Depression-World War II hiatus in home construction and privately financed business investment have been stagnating.

There are many reasons for the stagnation of economic development in some of our cities. An important one is that our older cities grew up at a time when manufacturing provided a much more significant share of national product and employment than it does now, and the employment structure of those cities reflects the way it was back then. Since the 1920's, the share of manufacturing employment in national employment has been declining, both because of the nature of demand and because of the substitution of imported manufactured goods for those domestically produced. And, in older cities, the employment generating effect of new investment, when it occurs, is offset by loss of jobs due to retirement of obsolete plant and equipment. This retirement, job loss process is accelerated during recessions. Unlike cyclically induced layoffs, however, the jobs lost in older cities during a downturn are not recovered when things pick up. Once the plant is closed and burned for insurance, or whatever, the jobs can't reappear.

The great thing about the jobs in manufacturing such as jobs making toasters is that people do not care too much about how the person who made their toaster looks or the quality of his English. It only really matters that the toaster works. When the manufacturing worker went home with a paycheck, it provided a big boost for everyone else as well. It is not clear that the new jobs that are appearing in older cities can play this role. It is even less clear that PSE or any other employment and training policy alone will suffice for attacking the structural problems generated by these shifts in the composition of national output and the location of new investment.

By and large, PSE trains people for white-collar, service-type jobs, and the focus of transition efforts is on getting such people into the public sector. But, surely, our objective for the future is not the creation of major cities that serve as reservations for federally subsidized public servants and nothing else. What is required is demand side policies oriented toward facilitating and speeding the process of modernization of the employment base of older cities and assuring access to new jobs by disadvantaged workers housed there.

What can be done? I think policy should move in two directions here. One of my proposals is similar to that implied by the Council's report; the other is dramatically different from a current administration proposal.

My first proposal is oriented toward creating special incentives for hiring the hard-to-employ: CETA prime sponsors should be given the resources for provision of bonuses to private employers for employment of selected hard-to-employ workers in the private sector.

If the administration is serious about providing "incentives for private employers to hire from among these groups with the most severe incidence of structural unemployment," then perhaps now is the time to begin experimentation in this direction. Suppose that prime sponsors, as part of title I funds, were given moneys to be distributed to employers who fill jobs with the priority targets of CETA that are so certified by local prime sponsors. Such bonuses could be divided into two parts, one to be paid on accession, the other to be paid after the employee has remained on the job for, say, 6 months. Most schemes of this type have the disadvantage that they might encourage turnover. One employee might be fired so that another, a person for whom a subsidy was available, could be hired. I believe this sort of thing can be monitored by prime sponsors, and over time it should be relatively easy to discriminate between firms with poor track records and firms with good ones. The advantage of such a program would be that it would assist in reorienting CETA toward private sector employment, and it fits into the existing CETA framework.

My second proposal is oriented toward helping to assure that jobs are there for CETA trainees: the across-the-board investment tax credit should be reduced, but the amount allowed should be increased by 1 percent for every percentage point to 2-year average unemployment rates in the area in which investment occurs have exceeded some level, say 6 percent.

What I am arguing for is an attempt to create incentives for private investment in manufacturing plant and equipment in areas with longrun employment problems. As I understand the outlook over the next 2 years, it is essential that investment pick up now so that we will have the productive capacity in 1979 to sustain the expansion without inflation. Making the ITC permanent does not accelerate investment. One accelerates investment by creating a creditable presumption that the credit will diminish in the not-too-distant future. In addition to this, I see no reason for not adding to the credit special incentives for its application in high unemployment areas. It might be that such targeting could be limited only to the credit granted for investment in construction or rehabilitation of structures. We need to think about these things, because, in the absence of such adjustments, the extension of the ITC to structures in general may only exacerbate the jobs problems of our older areas.

While these proposals may not be viable without substantial modification, the emphasis is critical: we should refocus the direct employment-related aspects of CETA away from the public sector, and something should be done about the structural unemployment associated with the changing patterns of urbanization.

The administration appears to be committed to a welfare reform proposal which folds much of current CETA PSE funds into creation of minimum wage "jobs of last resort" for work-obligated principal earners in low-income families. This is not the place to evaluate that proposal. But regardless of the merits of the welfare reform proposal per se, the PSE program it calls for is a very special policy, quite different from anything we have seen in PSE in either the EEA or CETA programs. I think it is inappropriate to put all PSE eggs in this one basket. Given the administration's timetable, welfare reform won't be implemented for some time. And there is the possibility that no such program will see the light of day. So, it seems appropriate to ask how CETA, and in particular CETA PSE, can be altered to improve its impact on the structurally unemployed.

The great problem with incremental reforms of this type is that they are often overlooked or ignored because of the expectations that the program will soon be phased out or significantly changed. The revealed lesson of recent history is that PSE is never phased out and is rarely, if ever, significantly changed.

In thinking about PSE it is important to draw a distinction that is missed in the Council's report. The Council's third recommendation is for "the collection of better data that will permit an assessment of the extent to which its component programs are actually having a beneficial impact."

CETA PSE programs are really two policies, not one. One policy is the provision of jobs for selected workers. The other is the development and targeting of such jobs through grants in aid to local government. Suppose that better data show CETA PSE is not having a beneficial impact. How will we know whether it is the grants policy or the theory that has failed? In general we won't be sure.

My experience with CETA indicates that there are many possibilities for improving the impact of the programs as a device for attacking structural unemployment problems. While I agree with the Council that better data on impact are needed, such data always take time to collect, and in the interim many dollars get spent. Also, even should the benefits prove illusory under existing programs. It is possible that changes in the quality of jobs the Government gets for its grants will change the outcome.

I am just about out of time. But, let me point out two recommendations for improving CETA PSE and make an advertisement for the forthcoming report of the National Commission for Manpower Policy, without implicating them in my recommendations.

The first is a matter of incentives. Overhead payments permitted prime sponsors in CETA should not be made on the basis of wages paid. The existing CETA program permits payments of wages up to $10,000 and overhead payments for nonwage costs equal to 15 percent of the wage bill up to this amount. Think about what this does. It provides the greatest overhead payment for jobs with the greatest skill requirements, precisely those not matched to the structurally unemployed. Costs of job creation and targeting go exactly the other way: It takes much more management and setup time for a typical $3.50-an-hour job than for a $5 one. A better policy might be to let the overhead payment vary with worker characteristics or at least to make it change inversely with the wage level.

The second proposal is a matter of making sure that the CETA PSE experience is allocated to as many workers as possible. Tenure in CETA PSE should be limited to 1 year. We have no evidence that the on-the-job training benefits the public sector jobs filled through CETA provide are not accomplished in a year. It is becoming increasingly clear, however, that little transition occurs and that the present program harbors a substantial class of permanent PSE participants. In many cases these are the best of PSE workers, and they are kept in CETA jobs by supplementation of CETA wages and inertia. Requiring turnover would not only spread the benefits of CETA PSE around, it would also refocus the attention of both participant and prime sponsor on the central aim of a structural unemployment program, preparation of the hard-to-employ for productive unsubsidized employment.

Thank you.

Representative BOLLING. Senator McGovern.

Senator McGOVERN. Members of the panel, there is a general view that most economists hold that the only way to have anything approach full employment with an acceptable level of inflation is through some measure of public service employment, manpower training programs.

I wonder if each of you have any comment on how effective you think the public service programs and manpower training programs are in trying to materially reduce unemployment levels without triggering more inflation?

Mr. BURNS. I think that public service employment, especially for a temporary period, is a useful instrument. But I have to underline that four out of five jobs in the economy are in the private sector. I think it is more important to stress all of the programs which involve Government participation that try to encourage the private sector to provide the jobs.

I would like to make one point in connection with this. The chairman made the point very strongly, with which we concur; namely, that macroeconomic alone will not solve the structural unemployment problem. I would further like to stress that a micro approach alone will not solve these problems of unemployment. Unfortunately, in order to do the job, as we tried to point out in the report, a wide variety of detailed as well as broad-based measures are required.

I do not want to make this answer too long. But I would like to stress that solutions which work in one situation or location may not work in another. For example, we have spoken to one business firm which had a successful experience with work-sharing. But this arrangement only worked in one establishment where women with relatively long-term service were in the predominance. We have spoken to other large companies that make good use of the U.S. Employment Service but can use it only in two locations. There is an awful lot of nitty-gritty that has to be dealt with here.

Senator McGOVERN. I have not had a chance to look at your report, Mr. Burns. But just glancing through it, it looks to be a substantial contribution. Before I turn to Ms. Reubens, I notice in the report, and in your testimony, you talk about giving the private sector a great role in dealing with the problems of structural unemployment. What is the work incentive that the Federal Government would be involved in.

Would it be direct subsidy, through a kind of bonus payment that Mr. Wiseman was talking about? What would be the most workable way to encourage a response to the private sector?

Mr. BURNS. I am not sure we can focus on one or two. I think you need an integrated set of policies which are covered in the paper. Frank, can you think of any we might stress?

Mr. SCHIFF. Yes. We found by experience that no one method is likely to work equally well in all situations and in every location. This is why we favor experimentation with tax incentives, as well as with direct subsidies. We found, for example, that direct subsidies under existing programs of public-private partnership seem to work better in the case of large firms. Some of the small firms, on the other hand, favor some type of tax incentive. We also found that one of the major problems in dealing with these very difficult to employ groups is that regardless of the specific incentive used, many companies are not very eager to take on such people directly.

The companies need help in dealing with the hard to employ, and these people in turn need help in dealing with job problems. That is why we stressed creating an intermediate organization that can help with the redtape that might be involved in government training and job programs and that can help with counseling. Very often the client groups involved need special assistance in terms of placement and so on, as well as counseling both before and after they get on the job.

We think what is likely to work best is a combination of various kinds of financial incentives with better use of intermediate organizations.

Senator McGovern. The sponsors of the Humphrey-Hawkins bill agree, that the major emphasis has to come from the private sector. Have you looked at that piece of legislation as a possible device for accomplishing what you want to do?

Mr. Burns. We have not tried to do that because it has been a kind of moving target, and furthermore, we do not want to address ourselves to specific legislation. We wanted to make our study a little more basic, and perhaps a little more long range.

Ms. Reubens. I come to this question from having done a study of European programs for the hard to employ which was published in 1970. I had examined the period of the 1960's, when there was high full employment and public service employment was used satisfactorily as a measure for the structurally unemployed. The assumption was that people in the programs could be moved into the regular economic sector because demand was so great. In fact, most countries had a good deal of success in moving people from public service employment into either private enterprise or regular public jobs. At present, however, the European countries have many of the economic problems we do. Public service employment no longer has a high transfer rate. The program is questionable if it merely is an aging vat for youth. These are problems in using such programs to give transferable experience if a recession persists.

But we should recall that we turned from manpower training in the 1960's to public service employment because we were disappointed that training did not lead to jobs. This thought was to combine the training and jobs in public service employment.

However, we have used public service employment in quite a different way from other countries. Elsewhere public service employment jobs are confined to tasks that would not otherwise be at all or would be done much later. Public service jobs do not substitute for regular local government functions. The allocation of funds from the national or Federal Government to local subdivision during a recession ensures that regular local functions can be continued. Public service employment therefore is peripheral. In Britain, which has cut back on local government funds, the same problem with public service has cropped up; namely, the substitution of PSE funds for local government funds. But it works quite differently in other countries and they manage to get a social output that would not otherwise be produced.

Mr. WISEMAN. I have three points in response. The first one is that I am not sure that the consensus is as strong as you say. I think economists, or at least a significant share of professional economists, are concerned about the impact on long-range job creation of the size of the Federal deficit.

In a sense, when one borrows money to fund PSE, you might be doing something in the short run that is different from the long run. I do believe there is a consensus that there are identifiable groups in the economy whose employment can be expanded through PSE with minimum wage pressure. The group for which this is clearest is the teenage joblessness. It seems to me the overwhelming bulk of evidence suggests that a portion is generated by the Federal minimum wage policy and that means a genuine excess supply. It is possible that a part of that excess supply can be taken in by Federal job creation efforts.

The problem with the existing PSE, and that is up to the 1976 Emergency Job Program Extension Act, has been that the targeting has been very loose, so the program tended to hire labor market participants that looked like everyone else that State and local governments use, and the suspicion is that they were not drawn from the genuine excess supply.

As a consequence, any favorable wage impact that might be gained with an ideal PSE program was not explored or exploited. But the evidence is clear on the teenage group, and they are a significant share of the employment rate.

Senator JAVITS. First, I would like to thank both witnesses for their testimony. May I say to Mr. Wiseman, that about a year ago I had your piece called "Public Employment as a Fiscal Policy" printed in the Congressional Record because I thought it was such an important statement. We have taken the liberty of appropriating some of your suggestions in connection with amendments to CETA, which we are considering on the Human Resources Committee of the Senate.

Also, may I say much the same thing to Ms. Reubens. I found your facts and figures extremely helpful. I hope that we will be able to thread them into our legislation.

I think we have taken for granted the whole issue of sex, equal pay, and equal promotions. I do not think we have taken into account the other problems which you have raised and which I consider fascinating.

For the remainder of my time, I would like to determine if we can get some actual cooperation and advice from business because I think therein lies the big opportunity. I was deeply disappointed that we did not do more for the jobless through NAP and other programs. I would like to lean heavily on CED as a point of entry into the business system.

For example, I would like to submit to you a bill that I introduced. It does two things you recommended. One, it gives a tax incentive to business to hire the hard-to-employ. This provision is especially targeted to the employment of youths by giving a 50 percent credit for insured unemployment compensation over and above the insured compensation paid in the previous year.

Second, this bill provides subsidization for the hard-to-employ workers who are employed directly in a business activity of a Community Development Corporation. There are about 40 organizations, the largest being Bedford-Stuyvesant in New York, which engaged in a variety of business.

Knowing the trouble these workers have with entering the job market, we thought a good way to encourage their employees was to subsidize their employment and thereby feeding the workers into the business stream.

I would like your comments. Although I do not expect them now. I would like to have those in writing, if possible.

Last, I hope you will study the biggest of these organizations to which you refer, that is, an intermediary organization between private sector jobs and labor—the raw materials.

There is an outfit called the OIC, run by Leon Sullivan from Philadelphia. It trains about 60,000 people. It is a model. It has confounded all Government programs because it pays no stipend, and yet it has the biggest and best record of connecting the jobs with the trainees. I see you did not mention OIC. However, you did mention the Vocational Foundation for which I have served on the board of directors.

There is another organization I would like to call your attention to, Agudatch, Israel, which is very successful. It has been commended time and again. It is an Orthodox Jewish operation in Brooklyn with a large number of trainees, and parallels the experience of the OIC.

Finally, these community development corporations would function as an intermediary organization to serve the poor.

There are about 40 of these organizations. We have given much support to their activities. In this year Ted Kennedy and I hope to improve our participation. Would you be good enough to comment? I would like to make you a partner.

Mr. BURNS. I would like to call your attention to the fact that we did cover the OIC. You'll find a discussion of OIC on page 44 of the policy statement.

Senator JAVIS. Page 44, you say?

Mr. BURNS. Yes.

Senator JAVITS. In the study?

Mr. BURNS. You will also find a chapter on OIC in the supplemental study, where there is a rather liberal coverage of that. And furthermore—I do not believe you were here when I said this. But we are going forward with arranging policy forums in six communities. One of them will be Philadelphia, and we have had considerable communication with Mr. Sullivan over there. Thank you very much.

Senator JAVITS. My last two points. One, we also would like to beef up what is in the Youth Employment Act that was signed last year. Senator Humphrey and I sponsored it. The Act relates to a work-study program in the secondary school level, that is, to keep kids in school and give them a job at the same time. There is a significant experimental program authorized and ongoing with quite a bit of money attached to it.

If you would like to discuss it further for us, I think your comments would be very helpful. Would you do that?

Mr. BURNS. I shall.

Senator JAVITS. Furthermore, I noticed in your statement, in reference to local retraining councils, that there is a growing movement in our country to see what can be done in the labor management fields. I suppose I have been its principal advocate. We now have quite a few good experiments. We are trying very hard to put the Federal Mediation Service in the business.

Again, could we subsume local retraining councils in a labor management committee effort, especially when it is done on a regional basis? I think that working from a regional basis is more effective than working from a tradewise basis.

Last, with regard to continuing education, why could you not only make this program part of the universities but also tie it in to a community college curriculum? To do so would allow a person to continue his education while making the transition from school or training to a job. I know there is a movement in our country to lend out skills to businessmen and supervisors; this is good. Then, Mr. Chairman, if I may have your attention, I would suggest that you ought to consider—and we ought to consider—whether the Joint Economic Committee should have an advisory council of business and labor.

I see no reason why we should have to wait every year for you to come here to tell us these important points about what is happening. Why can we not have an ongoing relationship in which you through our staff—because we are so busy—apprise us of what is going on, and we ask you for things that we would like advice and ideas on from the business community? I would commend to our chairman, to our ranking member, and to you, the creation of such an approach, not to involve you in politics but to render a service.

Representative BOLLING. I have thought a good deal about this over time. I have discovered, and I suspect my good friend the ranking minority member is a classic example of this, that most of us do have a core of people from all groups that we use. But I think the possibility of having it more formalized is a consideration.

Congressman Rousselot.

Representative ROUSSELOT. Thank you, Mr. Chairman. We do appreciate all of you appearing today and helping us with your input on this issue, and your experience in this area. We have been told by Mr. Shiskin from time to time that the hardcore long-term unemployed in this country are basically concentrated in 30 metropolitan areas.

Each of you has tried to address the issue of how we permit a transition from long-term unemployment. Mr. Burns, I was interested in your statement describing your study, that it was initiated, or requested—you say in the introduction, in mid-1976. What time frame does it cover? Or is it just immediate experiences.

Mr. BURNS. The study is the product of a series of specialized studies that were commissioned to various groups and organizations as we went along. We had input from a very wide range of people, not just businessmen but people from academia, the Government, and so on. So this is a synthesis of this whole operation and draws on the experience of these people over whatever their lifetime is.

Representative ROUSSELOT. Is it a snapshot for 1976. Or is it their experience going back over a period of time——

Mr. BURNS. For as long as they have had experience, because as you know, our experience affects us all along, and a lot are not brand-new programs.

Representative ROUSSELOT. They sure are not. So, would you say the average person participating in providing information in this survey had been in business for some time trying to deal with this problem. It is not just short-range, quick, immediate solutions that are talked about here?

Mr. BURNS. That is correct.

Representative ROUSSELOT. They are the more experienced solutions.

In your statement, you say you feel strongly that public policy should place more stress on ways to put people to work than on paying them for not working. Would you comment a little more? I, too, have not had a chance to go through your very substantial report here in great detail. So could you expand on that a little more?

Mr. BURNS. I think the implication is that paying people for not working is the last thing that the person wants and the last thing that we would seek. We would like to feel that every person could be gainfully employed and that is not only from the standpoint of economics but from the standpoint of their mental and physical well-being.

Representative ROUSSELOT. You may say that in studying that issue these are some of the key points. Is the Federal Government—without putting you on the spot, is the Federal Government paying a lot of people not to work, or do you want to answer that?

Mr. BURNS. I do not think the Federal Government is doing that in quite that way. But——

Representative ROUSSELOT. I am sure that it was not our intent.

Mr. BURNS. Any kind of income maintenance payment, from a welfare standpoint, for people who can work, is money that could be used better if it helped such people to become gainfully employed.

Mr. SCHIFF. To add some specific examples, we looked at a variety of ways of putting more stress on work because the committee took the view that all people who want to work should have an opportunity to do so. Sometimes there are restrictions on their ability. But to give you one example that is covered in our statement: if you have a recession, a lot of people are obviously thrown out of work, and many of them will receive unemployment insurance. Our committee said: Let's explore the possibilities where instead of simply laying off the people at the end of the line, a company could put all its workers on a 4-day workweek and these workers could get unemployment insurance for the fifth day.

That sort of work sharing may be the kind of thing that should be encouraged. Or there may be possibilities where firms whose business has become sluggish in a recession could keep people on their payrolls if they received financial support to provide more training during such periods. Not all such support would necessarily have to be by the government.

We said that these and other opportunities to keep people working ought to be explored more fully than is often the case.

Representative ROUSSELOT. Did you address that issue?

Mr. BURNS. Yes.

Mr. SCHIFF. Very definitely.

Mr. BURNS. As a matter of fact, I think you are looking—is that the supplemental document?

Representative ROUSSELOT. Yes. It is called, "Advanced Copy of Your Training and Jobs Program in Action, Case Studies for the Hard-To-Employ." Do your case studies show where individual groups have done that?

Mr. BURNS. Yes, they do, and the point of that study was to find some—instead of being negative about the issue, to find constructive and positive action programs that were going on, not only in the profit sector but in the not-for-profit sector—programs that were successful. In addition, we looked at various Government programs.

Representative ROUSSELOT. We look forward to studying that. Many of us agree with you that the overwhelming portion of people in the unemployment category really want to be gainfully employed and are not looking for ways to prolong their unemployment status.

Mr. Wiseman, you mentioned in response to Senator McGovern's question, something about the impact of the minimum wage. Do you want to follow up on that?

Mr. WISEMAN. I was trying to find an example of a clearer case in which the great majority of economists would agree—it is hard to find any case where the majority of economists will agree—that there is a structural excess supply of labor that is generating unemployment and that sopping up some of this excess supply would not create any upward wage pressure.

I think there is a consensus that could be reached that this is true for teenage unemployment. The Economic Report confirms the effect of the minimum wage on teenage unemployment, but says that the actual magnitude of the minimum wage on the volume of teenage unemployment is difficult to assess.

Representative ROUSSELOT. Have you tried to assess it?

Mr. WISEMAN. Not personally. I was on the Brookings panel last year and am familiar with the work of Ned Gramlich of the University of Michigan, and others who have done work in this area. I think the evidence is overwhelming—in fact, is as conclusive as anything in economics is—that the minimum wage only exacerbates teenage unemployment.

Representative ROUSSELOT. How?

Mr. WISEMAN. By raising it. There are other reasons why we want to have a minimum wage, and a minimum wage tied to the wages of other workers. But nonetheless, we cannot ignore the consequences of that policy for that particular group.

Representative ROUSSELOT. It does have an impact?

Mr. WISEMAN. Certainly. I find it difficult to believe that anyone would argue that the minimum wage does not raise teenage unemployment.

Representative ROUSSELOT. You do not think anybody can?

Mr. WISEMAN. Not conclusively. I would be willing to debate anybody on that.

Representative ROUSSELOT. We needed to hear from you before.

Mr. WISEMAN. There are many reasons for having a minimum wage. I am not sure that my opinion is to oppose the changes in the law made. It does other things. It probably raises the wages of women in the labor force because, in fact, there seems to be a substitution of older female workers for teenagers in response to the minimum wage changes.

Every other economic policy we can identify had side effects, and that certainly is one of them.

Representative REUSS. I have a number of questions. Based on your consensus that doing something more than we are now doing about structural unemployment is a vital domestic goal—I take it that is your testimony, certainly the CED, and I congratulate you for what you have done.

One of the things I have been talking about is more in the domain of political science than economics. But I suppose it is all the same thing. I think there is not enough visibility to the point you are making, that structural unemployment in this country, and for that matter, all around the industrialized free world, is a major problem and structural unemployment is something that can be attacked without running into huge inflationary dangers if you do it right.

Should we not heighten the visibility of a joint Federal-State local and private sector attack on the structural unemployment problem by setting up in each labor market area—maybe there are 30 of them, maybe more; I think there are more—a distinguished private citizen, probably a thoroughly senior private citizen, who would be an appointed member, by the President, the Governor, the mayor, the county board, whatever governmental institutions are involved, whose job it would be to ride herd on the attack on structural unemployment in that area, both public and private.

If the CETA gets foolish and concentrates on hiring junior planners fired last week, the expediter ought to get on the tube and say so. He ought to get together a consortia of local manufacturers and industrialists and employers, and see if more cannot be done, and particularly, what kind of an environment and what kind of aids are necessary.

As it is now—handling the whole problem, you have yearly hearings like this; putting out reports, but which are not very visible. Therefore, I would like anyone to comment on the specific suggestion that there be an unpaid, maybe a dollar-a-year person, with a small staff—a czar or expediter—to raise public awareness of what needs to be done.

Mr. BURNS. I would say that anything that would raise the visibility would be very worthwhile thing to do. On your specific suggestion, I am not sure exactly how that person would operate or how his office would be organized to make him effective. I think that on your basic aim, to raise the visibility, that I would be all for that. But as to precisely how that person would operate, I would want to study that carefully, so we would not get into something worse administratively.

Representative REUSS. He would not have any power, I envision. It is a directive given him by the President, the Governor, the chairman of the county board, and the mayor. It would be to proceed to analyze and publicize, tell the world in print and on television how many structurally unemployed there are in the metropolitan labor market, who they are, what the problem is, who is doing it, how existing programs are working, and why in the world it is that we cannot get jobs for all of those willing to work.

Then you would know the dimensions. He would have nothing to lose by doing it, and, having a reputation, he would be in a good position to speak out publicly. If the private sector has not been doing anything, he should write and criticize them. If the public service jobs have been mismanaged, he should criticize Congress or the administration. There is plenty of criticism as well as affirmative things to be said.

Mr. BURNS. I would think that with that clarification this would be a good thing to do as long as we are not talking about his getting into the mechanisms of how the thing works.

Ms. REUBENS. I would agree with that. I think, in fact, in the city of New York, the mayor has just removed all the program responsibility to his own office for such programs. That is a good beginning for the kind of thing you are talking about.

It is important that such a person does not get the illusion that he will control programs. A person who gets appointed to such a post soon feels either shunned or like a PR man. It would have to be a very senior, very solid kind of citizen. But it sounds like a good idea.

Representative REUSS. I am thinking of people like—just plucking names out of the air, a Felix Rohatyn in New York or a Ben Heinemann in Chicago. I could name others.

Ms. REUBENS. But they are not people that like to stand off in the corner and not have a voice in the actual programs.

Representative REUSS. That is why I envision a joint appointment.

Mr. WISEMAN. I think it is an interesting proposal. My first reaction to all programs is programmatic, how it matches under the existing program. In CETA we have manpower—employment training counselors, they are now called, whose responsibility it is to monitor the whole PSC framework at the local level. Those things are not very powerful, and they probably do not have the amount of visibility that we would like in this case. Their function is to give community-based organizations power over the allocation of resources. It is a political device. We might want to think of such a proposal as being related to structures we already have in place, the effectiveness of which we would not wish to imperil.

Representative REUSS. How can we better integrate the U.S. Employment Service with CETA to place people in jobs, and how can we improve the existing computerized job bank system? There are starts of it in some areas. I have a feeling we could do much more. Do any of you address yourselves to that in your papers?

Mr. BURNS. We did address ourselves to the subject and did have a separate study made to advise the committee. I would like to ask Mr. Schiff to comment on this, because he did get into it more fully.

Mr. SCHIFF. The last chapter of our report deals with the subject. We call for much closer integration of the Employment Service and of CETA. We do not call for a complete merger. But we felt in some instances it may be possible to have CETA and the Employment Service operate jointly at the local level. We thought that the regional CETA administrator would have major responsibilities for insuring closer integration of the two organizations.

We also felt that the Employment Service should be relieved of many of the responsibilities it now has that involve functions that are also being carried out by other agencies and that should devote itself much more fully to the task of job placement. We have a number of other recommendations. For example, we found that in a great many cases the basic problem with the Employment Service is that employers do not go to it because they do not feel they get the kind of applicant they could use. As a result, there is not a very close relationship between employers and the Employment Service.

But there are some areas where new systems have been developed, and where much more attention is paid to the needs of the employers. For example, Chicago and a number of other places have an account representative system whereby certain individuals in the Employment Service are assigned to work with particular firms and get to know their needs precisely. This system seems to work far better than the usual arrangements.

So we think there are a variety of methods to strengthen the Employment Service and to achieve a better integration of the Employment Service and CETA. In particular we feel there ought to be a lot of stress on integrating the two at the local level in ways that help to bring in the private sector a lot more than has been the case in the past.

Representative REUSS. Thank you. My time is almost up, unless Ms. Reubens or Mr. Wiseman have anything to say.

Representative BROWN of Ohio. First, I want to observe that the committee is doing its part. We have two stenographers taking testimony today. That is not to imply there is doubletalk going on, but rather that we are doing on-the-job training. As you see, Ms. Reubens, we are even in accord with equal employment opportunity.

I would like to pick up on a point that I think both Mr. Burns and Mr. Wiseman made in their testimony, and also ask Ms. Reubens to comment. I did not catch it in your testimony.

That is, the suggestion that there ought to be tax incentives or some kind of employment incentives for hiring people in certain categories. I have explored this at some length since last year, and I finally put a bill in. But I am not totally satisfied with the bill because what we tried to do was set up a formula or a statistical method by which everyone got a number, a sort of negative number I guess. If a business hired such people they would get something off on their taxes for hiring them.

A black person from the ghetto, who happened to be female, or a youth, unemployed for a long period of time, would give a business a large tax reduction if they hired this person. But if you hired a white, middle-aged male that had previously been employed in some trained skill, you would not get any credit. If you were a small corporation you would get more credit than if you were a big corporation. Is the tax subsidy or credit approach a sound approach and do you have some recommendation as to what the structural system may be by which you would encourage business to employ people in this hard-to-employ area?

Mr. SCHIFF. We felt that there should be a series of approaches. Frankly, in a statement that we issued about 8 years ago we came out against a tax incentive approach and favored only direct subsidies under contract for a variety of reasons that seemed persuasive at the time. But our committee, after a good deal of further study felt that the direct approach also has a lot of disadvantages and that the need to get at the problem is so great that other approaches should also be tried. Therefore, we now feel that an important part of the effort should be in the direction of a tax incentive.

We took quite a negative view of the so-called incremental tax incentives that are now in existence. These simply give tax credits for added workers above a certain number, regardless of whether they belong to especially hard-to-employ groups. The trouble with this approach is that it is hard to tell whether or not the jobs would have been provided in any case. We favor an approach that focuses on the groups that are hard to employ. This is partly because these are the people who are hard to place, under all circumstances, so that you have a much better assurance that those who are employed with the help of the tax credit are getting extra jobs.

We also felt that in choosing the kinds of people involved, one should rely on the kinds of criteria that are now being used for public service employment, such as long-term unemployment, certain income tests, and so forth. It may be that this kind of approach is especially useful for small firms in the service sector. Some of our case studies suggest that where such experiments have been tried, the fears that many people have regarding such credits—for example, that the persons hired with the aid of the credit would be fired once the credit was over—have not proved justified. This is because, especially in small firms, the man who runs the service or the business puts an awful lot of his own time and effort into dealing with these people, and it does not pay him to fire them.

Representative BROWN of Ohio. I could not agree with you more. I think that is extremely important. If GM or Ford takes advantage of this program, their firing and hiring is literally done by a machine, because they do not have personnel relationships. But if it is a small-business employer, and he has suffered through getting the person trained, he is not about to let him go.

You could also do this by insisting that the credit not come off until 2 years after the training program and that the person would still have to be employed.

Ms. REUBENS. I would like to comment on this from the perspective of the experience of other countries, which is an area that I have specialized in. It is not necessarily completely relevant to the United States. But it is always wise to look at what has happened elsewhere.

In this recession they have used these devices much sooner and much more than we have. First off, the direct subsidy is much more favored than a tax credit or incentive. This does not mean that it is better but only that it has been the first choice.

Representative BROWN of Ohio. Would you just comment further on that? Are you saying that direct subsidy has been used and is effective?

Ms. REUBENS. I am saying that, as a matter of choice, there has been much use of subsidies and some use of tax incentives. In France they are using both. Most countries have decided in favor of direct subsidies. More money——

Representative BROWN of Ohio. Politics, too.

Ms. REUBENS. But one must consider the size of the subsidy. This is critical. Unless the subsidy is large enough, many employers do not respond, or do only what they would have done anyway. In Sweden, the subsidy for youth is up to 50 percent of the hourly wage, which is over $5 an hour for some youth under 20.

Representative BROWN of Ohio. Does that speak to the minimum wage issue?

Ms. REUBENS. I have some thought on the minimum wage issue but I will come to that if someone has time to ask about it.

Subsidies have been used in many ways, with Sweden leading the way. Sweden has given employers a wage subsidy directed to hiring women for nontraditional occupations. It can be used only in those occupations, and now there are about 8,000 such women at work under subsidy.

Then, I would like to refer to the British youth subsidy. They began with a subsidy for new school leavers because that was the group about whom they were most concerned. To qualify, a school leaver had to have been unemployed for 6 weeks since leaving school. This subsidy was terminated because a study discovered that 76 percent of the school leavers would have been hired in any case. They turned instead to a youth employment subsidy which required 6 months of unemployment before someone was taken on with the subsidy. That subsidy is also being terminated as of March of this year because they discovered that 60 percent would have been hired anyhow. They have turned now to a work experience and work preparation program for youth.

On the other hand, Britain has continued wage subsidies, as other countries have, to employers who retain workers that they would otherwise discharge because of insufficient orders. The added employment period may be used for training. We may be too far along in our progress to recovery to think about this type of subsidy.

I would make the general observation that all tax incentive and subsidy programs for employment should have a training element built in, or else they tend to prove illusory in terms of long-run gains. This principle results in a greater success in subsidizing apprenticeship programs in the European countries than in subsidizing ordinary jobs. I refer particularly to disadvantaged youth. Of course, if they have already had adequate training in a governmental program they may require simply to have the right employment come along.

Those are the main points I would like to make. If you want me to say something about the minimum wage, my feeling is that we have not sufficiently disaggregated our youth population. I find that 85 percent of 16- and 17-year-olds are in school and almost that high proportion of those in that age group who are in the labor force are in school. This is the group that earns close to the minimum wage.

There are various approaches to what that age group needs. My own view is they need incentives to stay in school to master the basic cognitive skills. If they seek jobs it is because they want income. It is not in order to get good work experience. We have evidence that those who work and go to school drop out of school more easily if they have a heavy work load. I am in favor of taking the 16- and 17-year-olds who are in school out of the labor force through work-study programs. It is not a hard or costly thing to do. It would change the youth unemployment picture.

The majority of 18–19-year-olds are out of school, and most earn far above the minimum wage. Adjustments of that wage are not going to contribute much to their employment. We have to decide which group it is that we are concerned about. If we want 16 to 17-year-olds who are in school to get more jobs, reduction of the minimum wage will contribute to taking part-time jobs away from the 18–19-year group, especially those in school. The minimum wage adjustment is a more complex program than has been revealed. Economists who deal with this subject usually are not experts on the particular youth groups involved, in my opinion.

Representative Brown of Ohio. Let me just expand on one thought, and this is said not as an economist but as a parent.

I think the problem of employment of young people is a threefold problem. First, skills; second, work attitude and the learning experience of work, as well as the value of money; and third, all those other subtleties that I think are perhaps a social problem as much as they are in an employment statistic.

Mr. Wiseman.

Mr. Wiseman. I just want to make two quick comments on the notion of tax credits or other incentives for employment of the hard to employ. We began with that subject.

I think serious consideration should be given to trying to operate such incentives through local employment training efforts. This brings me back to the CETA framework, and reasons why local discretion should be permitted in these matters.

It is very difficult to derive inflexible criteria that do a very good job of focusing. It seems like it should be possible, using census data and so forth. You could have an unemployment rule and race rule and location rule that would get that tax credit right where you want it. But the reality in the field seems to be something much different. The whole business of identifying such people seems to be difficult to do with simple rules when jobs ride on such decisions.

I have never understood why it is not possible to experiment with giving either the State employment services—and this is back to Congressman Reuss' question—or local CETA prime sponsors the ability to certify people as eligible for such bonuses or such payments, credits, based on their experience.

The State employment services have the enormous advantage of having files with a person's employment experience for years. They are now in many States involved in the certification process for CETA.

That kind of perspective is what is really ideally used in attaching tax incentives to persons for employment by business, and I would urge consideration of such decentralization rather than using mechanical formulas.

Representative BROWN of Ohio. We have a lot of good answers to one question, and my time is pretty well up. I would like, however, to just get in one more quick one, if I could, and see what you do with it.

Because of the shift from production labor, that is, production of goods labor, to services labor, do you feel that we are going to have to restructure our welfare system, or change the legal limitation on hours, straight working hours, overtime, that is, reduce it. Or is the service industry expansion able to absorb the work force that we now have?

Just a quick answer on that, if you would—as our goods production industries begin to automate and the number of jobs either stabilizes or shrinks.

Mr. BURNS. I do not think there is any great difference between the production and the service industries, and we could cite one example that we did run across in Chicago, where one of the major banks there has made it possible for a lot of people to be employed by adjusting its work schedules to meet the schedules of these people. The bank found that a lot of people, and particularly women, could work four or five hours provided these came at certain times of the day. Since these hours did not match up with the usual three-shift schedules, the bank altered its work schedules to make such a matching possible. So, I think that with such adjustments, the service industries can absorb much more of the work force.

I would like to say one thing about getting the people to work—about the importance of dealing with the individual in order to prepare him for work. There are really three categories of training that you are talking about.

The first is the elementary preparation for some who have never been out of their area and never really had work experience.

The second are more specific preparations for people who are past that stage.

The third is the actual job training in specific companies.

There was one company in Detroit that went into the ghetto area with the intention of hiring a lot of people. They did that, but very few of the people who were hired, showed up for work in the factory.

The first reaction was, "Well, maybe these people don't really want to work." But somebody was wise enough to go back in to find out what the answers were, and they found some rather elementary things.

One was that many of the ghetto people did not have the money to pay the bus fare for a week in order to get to the job.

The second was that a lot of these people did not know how to get to the bus or how to go about doing it.

The third was that there were quite a number of people who were concerned about the social aspect of working in a common workroom.

Now, I would like to stress that, in addition to the money payments and so on, an effective way of using money here is to help create intermediary organizations that take the individual and prepare him for the job. Companies, by and large, are not set up to do this kind of thing, but if these elementary things are done first, then the hard-to-employ can become employable.

Representative BROWN of Ohio. Are you talking about OIC?

Mr. BURNS. Yes, and the CABMS in Chicago.

Representative BROWN of Ohio. Yes.

Ms. REUBENS. I think that part-time schedules are instituted at the employer's desire, and are more common in service-type occupations that particularly affect women's employment. Employers have found that part-time older and middle-aged women have given them a more stable labor force than the full-time people they previously recruited.

This again is a worldwide development in the advanced industrialized countries. Encouragement probably would not accomplish much unless industry itself feels that this is a good move.

Mr. WISEMAN. I do not know the answer to your question. It is outside my range of research.

I certainly endorse Mr. Burns' comment about the importance of intermediary organizations. In the San Francisco area we have had extraordinary luck.

We have a significant immigrant problem. People come into the labor force speaking very little English, and we have trouble matching any job to them, and there is difficulty in their finding their way out of Chinatown.

Our getting community-based organizations just to monitor such people and help them through the first 6 months—ride on the bus with them, do preliminary training—has worked for several large business organizations, such as Wells Fargo Bank, Levi Strauss, et cetera. It seems very, very promising.

I, too, do not understand why more of it is not done.

Representative BOLLING. I am interested in how far we seem to have come and how much farther we still have to go. I remember that when we worked on the first manpower training bill, it turned out shortly after it became law that we knew so little about what we were dealing with, that we had neglected to make it clear to the people who would be trained to read and write. So, the Secretary of Labor had to make a special ruling, which was rather on the edge of the law, to get us back to reality.

I take it we have come some distance from there, but we have not really solved the fundamental problem, which seems to be how to get the American society involved pretty generally in this project.

Mr. BURNS. Right.

Representative BOLLING. Most of the problems that I see today on the question of full employment and law enforcement have a major component, which is that for some reason or another the society is not succeeding in doing as well today in working together as it did, let's say, from right after World War II to the middle of the sixties.

My own guess is that this kind of session is very important because it points out not only the specific difficulties which are more than technical, it also points out the very broad-gage social problems that are not social problems in the sense that they are a maladjustment of some kind, but they are just not an adjustment by very large and diverse communities to a new set of situations that have to be faced if the whole entity is going to survive in relatively good health.

I intend, of course, to call on the other members if they have further questions, but I do not think I will have any questions. I will just tell you that I think it was a very interesting session, and I will proceed to find out if Mr. Reuss has further questions.

Representative REUSS. I have some further questions. I agree with you in your appreciation for the appearance of the witnesses. I have one question of Mr. Wiseman.

In your prepared statement you say:

But the share of manufacturing employment in national employment has been declining, both because of the nature of demand and because of the substitution of imported manufactured goods for those domestically produced. And in older cities the employment-generating effect of new investment, when it occurs, is offset by loss of jobs due to retirement of obsolete plant and equipment.

I suppose what you are saying is that a general macroeconomic stimulus, that is, a tax cut, may not make much contact with the regional- or urban-oriented part of structural unemployment, that putting more money in the pockets of middle-income consumers may simply generate a lot of demand for imported manufactured goods and not result in domestic job creation.

What do you mean when you say the share of manufacturing employment in national employment has been declining because of the nature of the demand? Do you mean these people want more services and fewer——

Mr. WISEMAN. That is correct. I have been engaged for the past year in research on city employment patterns with Prof. Provin Varaiya at the University of California at Berkeley. We have been looking at data on changes in employment overtime in major urban areas since 1948.

The impressive thing that has emerged from this research is how utterly devastating recessions are to older areas. What seems to happen is that plants in older areas on the average tend to have older equipment and a lot of equipment that is marginal, economically speaking. Recessions cause permanent retirement of that capacity and the employment associated with it. In addition, capacity in older cities tend to be more labor-intensive in technique and that also means that just in the process of depreciation one loses a lot of employment.

Our impression has been that many older cities are going through a process of transition in which this plant is gradually being taken out of production and to some extent replaced. But it is clear that that process of retirement is hastened by downturns.

Our research suggests that our first order of business is to continue stable economic expansion, because any business cycle hits older cities particularly hard and produces permanent closing of jobs.

So, I think having a 3 or 4 percent steady growth is far better than a 5 percent one year, or 2 percent and 1 percent next year, because of the allocation of employment effects of those cyclical changes.

When we go back and look at the "happy days" of 1963 to 1967, we find that employment and manufacturing, in older cities actually grew at almost the rate of employment in young ones. This experience seemed to be associated with the fact that during the period of buoyant demand equipment was kept in operation, older capacity continued to be used, and employment associated with that capacity continued to take place.

But the period from 1967 to 1972 with its ups and downs had a devastating effect on employment in older cities. Although the data are still not in, I am sure that the 1974–75 recession will prove to have had equally grave consequences.

So, in that statement I was striving to give some background as to the root of urban economic problems, especially the older Northeastern cities, and to begin to understand the indirect effects of macroeconomic policy on those employment problems, as well as the direct ones, when we talk about that.

Representative REUSS. Well, I take it—straighten me out if I am wrong—what you would like to see is more manufacturing jobs in older cities because, as you well put it, somebody needs a toaster, comes home Saturday night with a nice take-home paycheck, and that is good all around. So, you want more manufacturing jobs. I do, too.

Mr. WISEMAN. I think that would be desirable. The next question—how do we get them—I do not know the answer to. That bothers me.

Representative REUSS. That is what troubles me. If you go from macroeconomic methods, are you not spilling or wasting a lot of that stimulus, because a lot of it will go into demands of upper income people for more services which get to people who are not able to supply—financial counseling, playing a violin, whatever—and, second, the stimulus will spill over into demand for more Japanese color television sets, Volkswagens, and French wines? So, where are we when all this macroecomic stuff comes into play?

Mr. WISEMAN. I don't know what the alternative to that is. It is true that a tax cut that is heavily weighted toward lower income classes, lower income families, will probably produce a greater demand for produced manufactured goods, but even there we still seem to be turning at an alarming rate into an agricultural producer instead of a manufacturing nation, and I am deeply concerned about the longrun consequences of it.

Representative REUSS. You are on an interesting kick there, and I would like to see you or somebody quantify that. That is to say, a tax cut only affects people who pay taxes. That rules out a third of the underclass in this country.

So, you want to ask what are the things which people would buy with the money being put into their pockets by a tax cut which would help on structural unployment. Obviously, if they are going to buy toasters, that would help if you renovate a toaster plant in the center of the city. I would like to know the answer to that.

Also, in that context, I would like your comment on a couple of items in the administration's program. You have already faulted the economic report somewhat for talking about structural unemployment solely in terms of the demography—women, teenagers, blacks, et cetera—whereas you say that really it is very largely urban and regional. Is that a fair assessment of your statement?

Mr. WISEMAN. Yes.

Representative REUSS. What do you say about another substantive aspect of the administration's program as relating to the Sun Belt/Cold Belt argument; namely, the administration now wants to extend the investment tax credit not only to the machinery which it has always applied to, but to a new plant.

Isn't that likely simply to mean that a manufacturer putting a plant in a Northeast/Midwest/central city were to move it down to the Sun Belt is not going to think twice about moving it down to the Sun Belt if he gets the credit on the entire new plant.

He is going to operate heavily in favor of building a new plant and, having done that, why not put it in a place where labor is cheap and the sun is warm?

Mr. WISEMAN. I agree.

Representative REUSS. Isn't there a very, very gross hurdle of "overalls into the chowder" in that part of the administration program?

Mr. WISEMAN. No; I agree.

In your comments you point out an important thing: We can overstate the decline of manufacturing employment. It is growing very rapidly in some areas of the country. Socially it seems to be important to try to stimulate a more equitable distribution of that employment change.

I did in one section in my statement argue for reducing the ITC instead of making it permanent or promising to reduce it next year to stimulate investment. I also suggested that some consideration be given to the structural component of the ITC by allowing it to vary on the basis of long-term average unemployment differentials across labor or market areas.

That sounds pretty good but it turns out that the technical difficulties in formulating such a thing are enormous. I am not sure that it is possible but I did propose that consideration be given to that.

One of the difficulties is that even in the Northeast the geographical areas for which we have sufficiently reliable unemployment rates to create such triggers are very large. If you had some sort of differential or special investment tax credit across such areas that served to concentrate the credit on high unemployment areas you could still create intra-area movements that will be structurally bad. Such a credit might, for example, move firms out from the center of town to the periphery and the like. I would say that such changes in comparison probably have less bad consequences than having firms move from State to State or all new investment concentrated in the Sunbelt.

So, I agree with the implications of your question that more attention should be given to the issue of extension of the ITC to rehabilitation and new construction. And I made a movement towards a proposal to create incentives to target such investment or the credit.

But I think we should acknowledge that there are severe technical problems.

I think that Frank Schiff probably knows more about that actually than I do. It would be worth hearing what he has to say.

Representative Bolling. Do you want to throw him into the chowder, too? [Laughter.]

Representatives Reuss. My time is up, but I am sure we can negotiate extra time if you want to add something, Mr. Schiff.

Mr. Schiff. I don't really want to speak at any length about this, and I should also note that CED has not taken a position on this specific proposal. I would, however, like to comment on one point—well, on two points, very briefly.

One relates to Mr. Wiseman's statement that it really does not help to make the ITC permanent. Having talked extensively to businessmen, I know that many businessmen feel it is very important that the credit be permanent because they feel that in order to make long-term decisions they really need to know what kind of tax treatment faces them.

That is an attitude that seems to affect businessmen. I think we ought to take that into account.

The other point is that the logic for putting structures into this credit stems from the fact that we do not have an adequate total volume of capital investment at the present time. The shortfall has been primarily in investment in new plants, in getting firms to make decisions to start needed basic new plants. Questions have thus arisen on how to encourage this kind of investment.

Now, there is clearly need for paying attention to the additional question of how the proposed broadening of the investment credit will affect the location of new plant, and whether this broadening can be designed in a way that will aid rather than harm urban centers with high unemployment. On balance, however, there would seem to be good arguments for the view that it is important not to limit the credit to equipment only.

Representative Reuss. Thank you, Mr. Chairman.

Representative Bolling. Congressman Brown.

Representative Brown of Ohio. Mr. Wiseman, I do not want to be in any way unkind, but I want to respond to your reference to the agricultural situation. If you look historically at the number of people who produced the agricultural goods of this country, you will find that it has declined sharply. The development of our now being an agricultural export Nation has been one of development of technology and automation. It makes the argument that people prefer services because it is automation, or technological advancement—not that tractors are automated but they do replace strong sons—that made us a productive Nation.

I would argue that maybe it is not so much a shift in desire for services as it is the fact that the modern foundry has one man doing a job which is relatively clean by punching buttons on a machine rather than a guy with big muscles and the gauze mask and so forth doing work that used to be much more physical than it is now.

The automatic process, whether that machine is made in Germany or Cincinnati, Ohio, by Germans, still does require manufacturing machines in the first instance. But it is that automation process that I have some concern about, because we are having more goods produced literally with the same or less numbers of people. And that leads me to the question I want to ask, and I ask for a comment from all of you.

Even in societies that have relatively full employment, such as the German society, they are importing labor from other cultures generally not accepted as graciously as the Germans accept low-income people or others into their own culture. I am trying to say that delicately.

And I have to say at this time, that I buy the NAACP approach that blacks are the ones who are going to benefit if we have full employment and blacks are the ones that will suffer if we do not more than the average. Also, you can extrapolate that to women or Appalachians and other groups and, I suppose, similarly, geographic locations, sites, etc.

But my questions is this:

In a society where we have a lot of unemployment, we are having some difficulty finding people to do unpleasant kinds of service work, either unpleasant because they are psychologically demeaning—the cleaning woman, the cook, the chauffeur—because they seem to be part of a class caste system, or physically undesirable—caring for the bedridden elderly, doing the ditch digging or reparing the sewer system, and so forth.

Now, to what extent do any of the programs that you are aware of address that part of the problem, the lack of enthusiasm for certain kinds of work?

Shall I change the subject? I think everybody seems to want to rush into that. [Laughter.]

Mr. WISEMAN. Maybe the answer is "none."

Mr. BURNS. I would say we have not covered that directly in the CED studies.

Representative BOLLING. I am sure the gentleman is aware that at least in many areas many of those jobs are now being done by immigrants, legal or illegal.

Representative ROUSSELOT. That is right.

Representative BROWN of Ohio. I guess really that is my point. We have an immigrant problem, for lack of a better term for it; yet, we have an unemployment problem with native-born Americans, and how do we bridge that gap. How do we address that problem? These are the nonautomated jobs.

Now, to go back to your comment, Mr. Burns, that we would rather have a system that pays people to work than not to work, I could not agree with you more. But there are jobs that are not apparently in our society as pleasant, and the social benefits that we have set up tend to free people from those jobs, if that is not an unkind way of saying it. Would you agree?

Ms. REUBENS. I would comment that it is not an American problem as you suggested, and in fact none——

Representative BROWN of Ohio. No, no, I don't mean to suggest it is an American problem. My German example is that they hire the Turks or the southern Europeans to do those jobs because the Germans don't want to do those jobs but then in a full employment system that isn't noticed.

Ms. REUBENS. I want to qualify it to say that since the 1975 recession the Germans have had quite a lot of unemployment. They have stopped the importation of foreign workers and they have encouraged some to return home, but they have a problem in that Germans are not filling some vacancies in the jobs that had been the province of the guest workers, as they were called. This is true in virtually every European country. These were brought in legally. There now seem to be permanent social barriers so that certain kinds of jobs simply are not accepted by unemployed citizens of the country when there is a recession.

Our recession experience is the same as that of other countries. We don't know for sure what part of the illegal aliens employment in this country concerns jobs that Americans really don't want to do. We know it is a substantial part of it, but there also is an area where illegals are in direct competition because of union-set wages. In the case of painters in New York City, for example, many illegals work on nonunion paint jobs.

There also are some well paid jobs held by illegals.

No one has an answer to what you do in an affluent society when people's standards are elevated and all the social programs have upgrading intentions. What should be done about jobs for welfare mothers? Many of the jobs that would be suitable in terms of their background and education do not pay enough to get them out of dependency. We have not addressed two questions concerning welfare mothers that bother them a great deal. One is obtaining supplementation of low wages. Many could be willing to work at low-paid full-time jobs if they had a certain system of supplementation that provided at least their real income on welfare.

The other is the problem of getting back on welfare quickly if your job folds which it frequently does in these low level, insecure jobs. This is handled poorly at the administrative level and encourages remaining on welfare.

What is more, we overlook what has been called the subterranean economy. There may be much less unemployment, even in a structural sense, than any of us have realized because so many people are working off the books, are doing various kinds of jobs that never get reported anywhere. Welfare mothers in New York City, as I know from close personal contacts with people who see them on a professional basis, do work off the books in order to make ends meet. One of the problems with the welfare reform program is that it may remove from the labor market and put into PSE a lot of people who are in fact working off the books.

Representative Brown of Ohio. That would seem to be a downside result; would it not?

Ms. Reubens. Well, we do have to come to grips with this whole area that is unreported and that we know very little about.

Representative Rousselot. It is nontaxable income, also.

Ms. Reubens. Yes.

Representative Rousselot. It is tax avoidance.

Ms. Reubens. Yes. A story in the New York Times reflects something about our society. A young man of 30 told a reporter:

> When I graduated from high school a man offered me a job to steal cars for him; I made $200 a week at it, and in a couple of years I went into business for myself and I was making $60,000 to $70,000 a year at it.

He is now employed legitimately at the coliseum showing of new cars, demonstrating auto theft devices at which he was a master.

Now, this is someone who could come out in the open and describe his career as if this were a perfectly normal kind of procedure in society, I would suggest that this area—which we find it difficult to talk about because we haven't any hard facts—is really quite an important one in the inner city.

Representative BOLLING. That relates to the fact I believe that the cities in the East lost about 5 million people in the last census. That is a substantial and significant statistical area with a large number of human beings.

Representative BROWN of Ohio. I don't want to belabor this, but it does seem to me that you cannot address the problem of unemployment, of training, of structurally unemployed without addressing partly at least the reason that they are structurally unemployed. But we must find ways that can coax these people out of unemployment instead of accepting the "benefits" of being unemployed—as opposed to low paying jobs.

I would say to Mr. Burns that from practical experience from my standpoint as a working politican, back in the 1967 time frame which in the unemployment sense was a good time, in some other senses a pretty difficult time.

In some of the factories where I know of, they would have a 2.7 unemployment rate, and the manager of the factory said, "We are now giving everybody who applies for a job with us a complete physical examination because we don't want them on workmen's compensation 3 weeks after they have been on the job.

"We are getting the physical and mental and social misfits applying which," he went on to say, ". . . means that we are attracting them off the welfare rolls because the job here is so much more desirable than even sitting at home waiting for the welfare check to come in."

But they are people who have some kind of problem, sometimes not physical, and, therefore, would benefit from the kind of work you conduct in Chicago or the OIC program and get the psychological work habit instilled in them and move into the work force.

But some were physical problems that when they reached down to pick up the 5-pound motor, their back was going to go out or something else, and he felt that he had to protect himself as an employer from this kind of circumstance.

But it is a clear message that the NAACP is right, that when we have full employment minorities benefit relatively more than other segments of society.

I might say to Ms. Reubens and Mr. Wiseman, also, that automation or technological improvement, if that's what it is, has been the thing that has freed women for this employment opportunity.

When women didn't work, they had the pleasure of doing the laundry by hand and preparing the vegetables and killing the chicken themselves and they were not an unemployment problem.

Now that they don't have to do those things, it is all done automatically for them and it is there in the supermarket, they are an employment problem for the society.

I am not sure how that all works out, but it seems to me that we have to address not just that element that frees up more people for employment rolls but also the question of why even some of the jobs that are available cannot find anyone who wants to do them.

Mr. BURNS. I am sure in any society that you will always have some of that no matter what you do.

Also, I would like to point out that I don't know very many people who have not done an awful lot of work that they didn't want to do and who have not at some time had the kind of jobs that they didn't like.

I think the incentive to those people is to take those jobs and get on to the next stage. So, I think that there is another side to this.

Representative BROWN of Ohio. If you let me interrupt one more time and I say this to the chairman, in my area which is a small city area with a lot of industrial assembly-line kinds of jobs, many of the assembly line jobs fall into that category.

The work force is there from the age of 20 to maybe 30; their average employment, I believe, a few years ago was running something like 7.5 years, which is hardly 20 and out, because it was big money, they worked in that job for a while, and then they moved on to something that they thought was a culturally more desirable job, it may not have paid as well, but the kind of thing they would prefer to do.

Representative BOLLING. We thank you very much. This has been a very stimulating session and very useful.

The committee stands recessed until Friday, February 3, at 10 a.m. in this room.

[Whereupon, at 12:15 p.m., the committee recessed, to reconvene at 10 a.m., Friday, February 3, 1978.]

THE 1978 ECONOMIC REPORT OF THE PRESIDENT

FRIDAY, FEBRUARY 3, 1978

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

The committee met, pursuant to recess, at 10 a.m., in room 345, Cannon House Office Building, Hon. Richard Bolling (chairman of the committee) presiding.

Present: Representatives Bolling, Reuss, and Rousselot; and Senator Proxmire.

Also present: John R. Stark, executive director; Louis C. Krauthoff II, assistant director; G. Thomas Cator, L. Douglas Lee, Katie MacArthur, Deborah Norelli Matz, and Philip McMartin, professional staff members; Mark Borchelt, administrative assistant; and Charles H. Bradford, Stephen J. Entin, George D. Krumbhaar, Jr., and Mark R. Policinski, minority professional staff members.

OPENING STATEMENT OF REPRESENTATIVE BOLLING, CHAIRMAN

Representative BOLLING. The committee will be in order.

In recent weeks, there has been a great deal of discussion about the adequacy and appropriateness of our labor market statistics as measures of "full employment" and economic hardship.

To a large extent, these discussions are a result of the vast improvement in the employment and unemployment situation during 1977 when employment increased by 4.1 million jobs and unemployment declined by 1.4 percent.

Although it is unlikely we will repeat our 1977 performance this year, we will still make continued progress toward our goal of "full employment." This progress will, no doubt, further heighten the level of discussion relating to our labor market statistics.

This morning, in addition to our normal review of the employment and unemployment situation, we will be looking into the issues surrounding the reliability of current unemployment, employment, and labor force measures.

We are pleased to have the Government's two top experts on this subject testify before us, Julius Shiskin, Commissioner of the Bureau of Labor Statistics, and Sar Levitan, Chairman of the National Commission on Employment and Unemployment Statistics.

Commissioner Shiskin, we again welcome you. Mr. Lavitan, this is your first appearance before this committee as Chairman of the National Commission on Employment and Unemployment Statistics, and we look forward to your testimony.

Commissioner Shiskin, we are always glad to have you, and you may proceed.

STATEMENT OF HON. JULIUS SHISKIN, COMMISSIONER, BUREAU OF LABOR STATISTICS, DEPARTMENT OF LABOR, ACCOMPANIED BY W. JOHN LAYNG, ASSISTANT COMMISSIONER, OFFICE OF PRICES AND LIVING CONDITIONS; AND ROBERT L. STEIN, ASSISTANT COMMISSIONER, OFFICE OF CURRENT EMPLOYMENT ANALYSIS

Mr. SHISKIN. Thank you, sir.

As usual, I have a brief statement. I don't think I need to introduce my colleagues. They have been here with me for several years.

Representative BOLLING. I would like to have their names for the record.

Mr. SHISKIN. To my right is Robert Stein, in charge of our current employment statistics work. He will help me on questions of unemployment, and on my left, is John Layng, who is in charge of our Office of Prices and Living Costs, who will help me with questions on prices.

I might say in passing that we have a very big event coming off in a few weeks: On February 27, when we will be releasing for the first time the new revised Consumer Price Index. That will be a very momentous event in the life of the BLS, because we have been working on these indexes for 7 years, and they will be of major importance to the American public, to the administration, and to the Congress, because of the tremendous impact they have on the bread and butter issues of the American people.

We will be answering your questions shortly, but I would like an opportunity to read a very brief statement.

Representative BOLLING. Proceed as you wish.

Mr. SHISKIN. Mr. Chairman and members of the committee, I am glad to have this opportunity to offer the Joint Economic Committee a few brief comments to supplement our press release, "The Employment Situation," issued this morning at 9 a.m.

The overall labor market situation showed some improvement in January 1978 as the economy completed the 34th month of the economic expansion that has been underway since the spring of 1975.

The unemployment rate was 6.3 percent in January, slightly lower than in December. The drop in the unemployment rate for adult women was offset by a slight rise for other groups. Unemployment rates for both white and black workers were unchanged over the month.

Over the year, rates were down for nearly every worker group, with the notable exception of black workers, whose rates remained the same.

It should be noted that the January figures from the household survey are not strictly comparable with prior months because of an increase in the sample—from 47,000 households to 56,000 households—and some improvements in the estimation procedures. After allowance for these changes, the civilian labor force, total employment and the ratio of employment to the working age population would all appear to be little changed from December.

Nonfarm employment, as measured by the household survey, showed a small rise—about 150,000—after taking into account the effect of shifting to the larger sample in January. The business survey based upon payroll reports of employers showed another substantial rise—about 250,000.

Employment gains were widespread, as 65 percent of the 172 industries that comprise the BLS diffusion index of private nonagricultural employment showed increased employment over the month.

At the same time, the average workweek declined, as a result of unusually bad weather during the January survey period. As a result, the index of aggregate hours of production or nonsupervisory workers decreased sharply. Despite this drop, the index was well above the level of a year ago.

A few comments on seasonal adjustment, a subject which has occupied a lot of time in the hearings of this committee.

In the past 2 years, there has been a relatively sharp drop in unemployment and the labor force, after seasonal adjustment, between December and January. Many analysts believe that this was due to a bias in the seasonal-adjustment method and, thus, did not reflect the true change.

We have carried on extensive studies of this particular question over the past year and have not found an acceptable alternative method which gives much different results. We have, however, introduced a procedural improvement in the current method.

This improvement, made because of the sharp upward trend in unemployment between 1973–75, appears to have reduced the magnitude of the declines in the unemployment rate between December and January 1976 and 1977—by 0.1 percentage point each year.

This modified procedure has been used to seasonally adjust the unemployment rate in the current month, and we believe this improves the identification of the true December–January change. As usual, however, we will be better able to confirm the adequacy of this adjustment only as future results become available.

I would also like to call your attention to certain changes that are introduced this month in the presentation of the unemployment rate computed by alternate seasonal adjustment methods.

In order to make this table more useful for analysis of the effect of the seasonal adjustment process, we have provided a greater variety of alternatives on this table which accompanies my testimony each month.

The modifications we are introducing include a presentation of the unemployment rate as computed with the procedures used in the past 2 years—column 3; an additional stable adjustment which averages the seasonality of the series for the entire period of seasonal computation, 1967–77—column 10; and an added concurrent adjustment rate—column 8—in which the historical rates are revised each month as the current rate column provides an early view of the revisions that will be made in the 1977 rates at the beginning of next year.

Let me add two comments to that. One is to emphasize the last point, which is new. By using column 8 of this table, you will be able to see before the end of the year what kind of revisions we will be getting at the very end of the year. So they will not come to us as a big surprise in the future, as they did this year.

Second, I would like to call to the attention of the committee the fact that, in the recent months, all the seasonal adjustment methods have given about the same results. The variance among them is really very, very small, and that lends further credit to the figures we publish.

For example, in January 1978, we have different methods shown in our alternative seasonal adjustment table. The unemployment rate ranged from 6.2 to 6.4 Some adjusted rates were 6.2, some 6.3 and some 6.4. The official one happens to fall in the middle, but I don't take that too seriously. It is clear that January's unemployment rate is lower than those of prior months, and it seems to me that January confirms what was said in December—the unemployment rate has taken a very substantial drop over the past year.

Thank you, sir.

[The table and press release referred to in Mr. Shiskin's statement, together with an attached memorandum, follow:]

UNEMPLOYMENT RATES BY ALTERNATE SEASONAL ADJUSTMENT METHODS

Month and year	Unadjusted rate	Official adjusted rate	Alternative procedures: Official procedure used in 1976–77	Alternative procedures: Unemployed all multiplicative	Alternative procedures: Unemployed all additive	Alternative procedures: Year ahead	Alternative procedures: Concurrent: First computed	Alternative procedures: Concurrent: Revised	Alternative procedures: Stable: 1967–73	Alternative procedures: Stable: 1967–77	Other aggregations (multiplicative): Total	Other aggregations (multiplicative): Residual	Direct adjustment rate	Range (cols. 2–13)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)
1976:														
January	8.8	7.9	7.8	7.8	8.0	7.8	7.8	7.9	8.1	7.8	7.9	8.1	7.9	0.3
February	8.7	7.7	7.6	7.6	7.8	7.6	7.6	7.7	7.7	7.6	7.6	7.7	7.7	.2
March	8.1	7.6	7.5	7.5	7.6	7.5	7.5	7.6	7.7	7.5	7.5	7.6	7.6	.2
April	7.4	9.6	7.6	7.6	7.6	7.4	7.4	7.6	7.6	7.6	7.6	7.6	7.6	.2
May	6.7	7.4	7.4	7.5	7.2	7.2	7.2	7.4	7.5	7.4	7.5	7.3	7.5	.3
June	8.0	7.5	7.5	7.5	7.5	7.5	7.6	7.5	7.5	7.5	7.4	7.5	7.4	.1
July	7.8	7.7	7.8	7.8	7.8	7.8	7.8	7.8	7.7	7.8	7.7	7.7	7.7	.1
August	7.6	7.8	7.8	7.8	7.8	7.9	7.9	7.8	7.7	7.8	7.8	7.8	7.9	.2
September	7.4	7.7	7.8	7.8	7.7	7.8	7.8	7.7	7.6	7.8	7.8	7.7	7.8	.2
October	7.2	7.7	7.8	7.9	7.8	7.9	7.9	7.7	7.7	7.8	7.8	7.7	7.8	2
November	7.4	7.8	7.8	7.8	7.8	8.1	8.0	7.8	7.8	7.8	7.8	7.7	7.8	.4
December	7.4	7.8	7.8	7.8	7.8	7.9	7.8	7.8	7.9	7.8	7.8	7.8	7.8	.1
1977:														
January	8.3	7.4	7.3	7.3	7.4	7.3	7.4	7.4	7.5	7.3	7.4	7.6	7.5	.3
February	8.5	7.6	7.5	7.5	7.6	7.5	7.5	7.5	7.6	7.5	7.5	7.5	7.5	.1
March	7.9	7.4	7.4	7.4	7.4	7.3	7.3	7.4	7.5	7.4	7.4	7.3	7.4	.2
April	6.9	7.1	7.1	7.1	7.1	7.0	7.0	7.1	7.1	7.1	7.1	7.1	7.1	.1
May	6.4	7.1	7.1	7.1	6.9	6.9	7.0	7.1	7.1	7.1	7.1	7.0	7.2	.3
June	7.5	7.1	7.1	7.1	7.1	7.1	7.1	7.1	7.0	7.1	7.0	7.1	7.0	.1
July	7.0	6.9	7.0	7.0	7.0	6.9	6.9	6.9	6.8	6.9	7.0	6.9	7.0	.2
August	6.8	7.0	7.0	7.0	7.1	7.1	7.0	7.0	6.9	7.0	7.1	7.1	7.0	.2
September	6.6	6.8	6.9	6.9	6.9	6.9	6.9	6.8	6.7	6.9	6.9	6.9	6.9	.2
October	6.3	6.8	6.9	6.9	6.9	7.0	6.9	6.8	6.8	6.9	6.9	6.9	6.8	.2
November	6.4	6.7	6.7	6.7	6.8	6.9	6.8	6.7	6.8	6.7	6.8	6.7	6.7	.2
December	6.0	6.4	6.4	6.3	6.4	6.4	6.4	6.4	6.5	6.4	6.3	6.4	6.3	.2
1978:														
January	7.0	6.3	6.2	6.2	6.2	6.3	6.4	6.4	6.4	6.3	6.3	6.3	6.3	.2
February														
March														
April														
May														
June														
July														
August														
September														
October														
November														
December														

See footnotes continued on next page.

Source: U.S. Department of Labor, Bureau of Labor Statistics, Feb. 1978.

(1) Unadjusted rate. Unemployment rate not seasonally adjusted.

(2) Official rate. This is the published seasonally adjusted rate. Each of 4 unemployed age-sex components—males and females, 16–19 and 20 yrs of age and over—is independently adjusted. The teenage unemployment and nonagricultural employment components are adjusted using the additive procedure of the X–11 method, while adults are adjusted using the X–11 multiplicative option. Adult male unemployment is adjusted multiplicatively using a prior trend adjustment procedure. The rate is calculated by aggregating the 4 and dividing them by 12 summed labor force components—these 4 plus 8 employment components which are the 4 age-sex groups in agriculture and nonagricultural industries. This employment total is also used in the calculation of the labor force base in columns (3)–(9).

The current "implicit" factors for the total unemployment rate derived by dividing the original unemployment rate by the seasonally adjusted rate for the months of 1977, are:

Jan	112.2	July	101.2
Feb	112.6	Aug	97.6
Mar	106.7	Sept	96.6
Apr	95.6	Oct	92.6
May	90.1	Nov	95.3
June	106.2	Dec	93.6

(3) Official procedure used in 1976–77. Only teenage unemployment components are adjusted using the additive procedure of X–11; all other series are adjusted with the multiplicative option. The prior adjustment is not used for adult male unemployment.

(4) Unemployed all multiplicative. The 4 basic unemployed age-sex groups—males and females, 16–19 and 20 yr and over—are adjusted by the X–11 multiplicative procedure. This procedure was uesd to adjust unemployment data in 1975 and previous years.

(5) Additive rate. The 4 basic unemployed age-sex groups—males and females, 16–19 and 20 yr and over—are adjusted by the X–11 additive procedure.

(6) Year-ahead factors. The official seasonal adjustment procedure for each of the components is followed through computation of the factor for the last years of data. A projected factor—the factor for the last year plus one-half of the difference from the previous year—is then computed for each of the components, and the rate is calculated. The rates shown are as first calculated and are not subject to revision.

(7) Concurrent adjustment through current month (first computed). The official procedure is followed with data re-seasonally adjusted incorporating the experience through the current month, i.e., the rate for March 1976 is based on adjustment of data for the period, January 1967–March 1976. The rates are as first calculated and are not subject to revision.

(8) Concurrent adjustment through current month (revised). Follows the same procedures as used in computation of col. 7. Each month, however, revisions in the entire time series are made. This column provides an indication, as the year progresses, of the scope of the revisions and provides the best portrayal of movements in the series.

(9) Stable seasonals (January 1967–December 1973). The stable seasonal option in the X–11 program uses an unweighted average of all available seasonal-irregular ratios to compute final seasonal factors. In essence, it assumes that seasonal patterns are relatively constant from year-to-year. A cut-off of input data as of December 1973 was selected to avoid the impact of cyclical changes in the 1974–75 period.

(10) Stable seasonals (January 1967–December 1977). Follows the same procedures asjusted in col. 9, except that the unweighted average is based on seasonal-irregular ratios for the 1967–77 period.

(11) Total. Unemployment and labor force levels adjusted directly.

(12) Residual. Labor force and employment levels adjusted directly, unemployment as a residual and rate then calculated.

(13) Direct adjustment. Unemployment rate adjusted directly.

(14) Average of cols. 2–12.

Note.—The X–11 method, developed by Julius Shiskin at the Bureau of the Census over the period 1955–65, was used in computing all the seasonally adjusted series described above.

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USDL 78-94
TRANSMISSION OF MATERIAL IN THIS RELEASE IS EMBARGOED UNTIL 9:00 A. M. (EST), FRIDAY, FEBRUARY 3, 1978

THE EMPLOYMENT SITUATION: JANUARY 1978

Both total employment and unemployment in January were about unchanged from December levels following strong improvements in recent months, it was reported today by the Bureau of Labor Statistics of the U. S. Department of Labor. The Nation's overall unemployment rate was 6.3 percent, not much different from December's 6.4-percent rate but down substantially from the rates prevailing during 1977.

Total employment--as measured by the monthly survey of households--was 92.9 million in January. An apparent increase of 270,000 from December was strongly affected by technical modifications that were introduced in January 1978. An explanation of various procedural changes appears on page 6.

Nonfarm payroll employment--as measured by the monthly survey of establishments--did show further growth in January, rising by 255,000 over the month to 83.7 million. Over the year, nonfarm payroll jobs have increased by 3.0 million.

Unemployment

There were 6.2 million persons unemployed in January (seasonally adjusted), virtually the same level as in December after declining markedly from November. The overall rate of unemployment, 6.3 percent, remained at about the level reported for December but was 1.1 percentage points lower than in January 1977 and the lowest reported since October 1974. (See table A-1.)

Although jobless rates for adult men (4.7 percent) and teenagers (16.0 percent) were essentially unchanged over the month, there was an improvement in unemployment among adult women; their rate dropped 0.5 percentage point to 6.1 percent. Unemployment rates for both black and white workers, at 12.7 and 5.5 percent, respectively, were unchanged over the month. (See table A-2.)

Over the year, joblessness has been reduced for all major demographic groups except blacks, whose unemployment rate was virtually the same as it had been in January 1977. During the same period, the rate for whites dropped 1.2 percentage points to 5.5 percent. Since January 1977, the jobless rate for adult men has declined by 1.1 percentage points, and there was an even greater reduction--2.4 points--for teenagers. The rate for adult women decreased by 0.8 percentage point over the year.

The median duration of unemployment fell from 7.1 to 6.6 weeks in January and was down a full week from a year earlier. This measure, which is being introduced for the first time to supplement the data on the mean duration of unemployment, depicts the

Table A. Major indicators of labor market activity, seasonally adjusted

Selected categories	Quarterly averages					Monthly data		
	1976	1977				1977		1978
	IV	I	II	III	IV	Nov.	Dec.	Jan.
HOUSEHOLD DATA	Thousands of persons							
Civilian labor force	95,625	96,221	97,153	97,559	98,622	98,877	98,919	99,107
Total employment	88,182	89,059	90,264	90,823	92,069	92,214	92,609	92,881
Unemployment	7,443	7,161	6,889	6,736	6,554	6,663	6,310	6,226
Not in labor force	59,218	59,225	58,941	59,205	58,777	58,512	58,689	58,709
Discouraged workers	944	942	1,062	1,067	969	N.A.	N.A.	N.A.
	Percent of labor force							
Unemployment rates:								
All workers	7.8	7.4	7.1	6.9	6.6	6.7	6.4	6.3
Adult men	6.0	5.7	5.2	5.0	4.8	4.7	4.6	4.7
Adult women	7.5	7.1	7.0	7.0	6.8	6.9	6.6	6.1
Teenagers	19.1	18.6	18.1	17.6	16.7	17.2	15.6	16.0
White	7.1	6.7	6.3	6.1	5.8	5.9	5.5	5.5
Black and other	13.4	12.9	12.8	13.6	13.3	13.7	12.7	12.7
Full-time workers	7.4	6.9	6.6	6.5	6.2	6.2	5.9	5.8
ESTABLISHMENT DATA	Thousands of jobs							
Nonfarm payroll employment	80,111	80,925	81,871	82,548	83,193p	83,245	83,432p	83,685p
Goods-producing industries	23,456	23,788	24,265	24,359	24,504p	24,528	24,548p	24,652p
Service-producing industries	56,655	57,137	57,606	58,189	58,689p	58,717	58,884p	59,033p
	Hours of work							
Average weekly hours:								
Total private nonfarm	36.2	36.1	36.2	36.0	36.2p	36.2	36.2p	35.7p
Manufacturing	40.0	40.1	40.4	40.3	40.5p	40.5	40.5p	39.7p
Manufacturing overtime	3.1	3.3	3.4	3.3	3.5p	3.5	3.5p	3.5p

p=preliminary.

N.A.=not available.

midpoint in terms of weeks of joblessness currently experienced by the unemployed. In other words, half of the unemployed workers in January 1978 had been jobless for less than 6.6 weeks and half for a longer duration. (See table A-4.)

Total Employment and the Labor Force

Total employment was little changed in January at 92.9 million, seasonally adjusted, after allowance for revisions in the household survey estimation procedures and sample expansion. Over the year, however, total employment increased by about 4 million. The employment-to-population ratio--the proportion of the total noninstitutional population that is employed--was 58.1 percent in January. (See table A-1.)

The civilian labor force also was essentially unchanged over the month at 99.1 million. There has been an increase of about 3 million over the past year, with adult women accounting for more than half of the growth. The overall civilian labor force participation rate--the proportion of the civilian noninstitutional population either working or seeking work--was 62.8 percent. Participation rates among adults were 80.0 percent for men and 48.9 percent for women, while the rate for teenagers was 56.9 percent.

Industry Payroll Employment

Nonfarm payroll employment increased by 255,000 in January to 83.7 million, seasonally adjusted. Most of the major industry groups registered gains, as employment increased in 65 percent of the 172 industries that comprise the BLS diffusion index of private nonagricultural payroll employment. As in December, employment totals were affected by the strike activity in the coal mining industry, which has removed approximately 160,000 workers from the payrolls. It is not possible to determine at this time what effect, if any, this strike might have had on other industries.

The largest over-the-month employment gains were in manufacturing (105,000), particularly in the durable goods industries, wholesale and retail trade (95,000), and services (55,000). While these three industries comprise less than two-thirds of total payroll employment, they accounted for nearly all of the over-the-month employment gains.

Contract construction employment remained about unchanged from December but was undoubtedly affected by the unusually high levels of precipitation over much of the Nation during the survey period. The weather may also have contributed to a decline in transportation and public utilities.

Total nonfarm payroll employment in January was 3.0 million above the year-ago level, with the greatest percentage increases in contract construction, durable goods manufacturing, and services.

Hours.

The average workweek for production or nonsupervisory workers on private nonagricultural payrolls was down sharply in January, declining one-half hour to 35.7 hours, seasonally adjusted. As was also the case in January a year earlier, the reduction in hours was largely the result of poor weather conditions throughout much of the country. The average workweek in contract construction was particularly hard hit, declining almost 2 hours. The manufacturing workweek declined by 0.8 hour; manufacturing overtime, however, remained unchanged from December, at 3.5 hours. (See table B-2.)

The index of aggregate weekly hours of production or nonsupervisory workers on nonagricultural payrolls decreased by 1.1 percent in January to 116.3 (1967=100). Despite this drop, the overall index was 3.6 percent above the year-ago level. (See table B-5.)

Hourly and Weekly Earnings

Average hourly earnings of production or nonsupervisory workers on nonagricultural payrolls increased 0.9 percent in January, seasonally adjusted. Average weekly earnings declined by 0.5 percent, however, as a result of the sharp decline in the workweek. Compared to their year-ago levels, average hourly and weekly earnings were up 7.9 and 7.6 percent, respectively.

Before adjusting for seasonality, average hourly earnings were 6 cents above their December 1977 level and 40 cents above their year-ago level. Average weekly earnings fell by $3.29 over the month to $193.09. Over the year, average weekly earnings rose by $13.61. (See table B-3.)

The Hourly Earnings Index

The Hourly Earnings Index--earnings adjusted for overtime in manufacturing, seasonality, and the effects of changes in the proportion of workers in high-wage and low-wage industries--was 207.3 (1967=100) in January, 1.2 percent higher than in December. The index was 7.7 percent above January a year ago. During the 12-month period ended in December, the Hourly Earnings Index in dollars of constant purchasing power rose 0.8 percent. (See table B-4.)

Note on Household Survey Revisions and New Data Series

This release introduces revisions in the national household survey resulting from a sample expansion and changes in the estimation procedures. Also introduced is a new monthly data series (table A-8) on the employment status of residents of the 10 large States that have a sufficiently large sample to meet the reliability standard established by the Bureau for monthly estimates.

In addition, seasonally-adjusted data for 1977 appearing in tables A-1 through A-7 have been revised. As announced in the December Employment Situation press release (USDL 78-16) issued on January 11, it is the annual practice of the Bureau to recalculate the seasonal factors for unemployment and other labor force series at the beginning of each calendar year to take into account data from the previous year. Revised seasonally-adjusted data covering the December 1976 to 1977 period for many labor force groups were published in the January 24 release, Annual Revisions in Seasonally-Adjusted Labor Force Data (USDL 78-53). A description of the current seasonal-adjustment procedures, the factors to be used to calculate the overall unemployment rate during 1978, and revised data for the entire 1973-77 revision period, including a larger number of labor force series, will be published in the February 1978 issue of Employment and Earnings. Historical data may be obtained from BLS upon request.

Beginning in January 1978, the national sample has been expanded from approximately 47,000 to 56,000 households. This additional 9,000 household sample had previously been utilized only to provide annual average estimates of labor force status for individual States in 1976 and 1977. The procedures used in weighting the national sample to represent the population 16 years and over have been revised so as to reflect the population of States as well as the Nation as a whole. The use of the expanded sample for national estimates is expected to improve the reliability of some survey characteristics--particularly those associated with nonmetropolitan areas--by reducing the degree of sampling error associated with the estimates. Because of these changes in sample size and estimation procedures, the estimates published in this release for January 1978 are not strictly comparable with pre-1978 data. An approximation of the impact on major labor force groups can be gauged from the table below. As can be seen, the overall differences are comparatively small and generally within the range of sampling error. The civilian labor force was 236,000 greater in December 1977 as measured by the expanded sample. There was virtually no difference in the overall level of unemployment. Estimates of employment in agriculture were affected more than those for nonagricultural industries. Differences for adult women were, in general, larger than for other groups. Comparisons of current data with pre-1978 estimates should make allowance for these sample and procedural changes. All of these revisions will be described in greater detail in an article to appear in the February issue of Employment and Earnings.

Differences between expanded and unexpanded household sample estimates of employment status for major sex-age groups, December 1977

Employment status	Total, 16 years and over	Men, 20 years and over	Women, 20 years and over	Both sexes, 16-19 years
Civilian labor force	236,000	63,000	142,000	31,000
Employed	248,000	36,000	174,000	38,000
Agriculture	130,000	74,000	43,000	13,000
Nonagricultural industries	117,000	-37,000	130,000	25,000
Unemployed	-11,000	27,000	-31,000	-6,000
Not in the labor force	-235,000	-62,000	-141,000	-30,000

Explanatory Note

This release presents and analyzes statistics from two major surveys. Data on labor force, total employment, and unemployment (A tables) are derived from the Current Population Survey—a sample survey of households which is conducted by the Bureau of the Census for the Bureau of Labor Statistics. Beginning in September 1975, the sample was enlarged by 9,000 households in order to provide greater reliability for smaller States and thus permit the publication of annual statistics for all 50 States and the District of Columbia. These supplementary households were added to the 47,000 national household sample in January 1978; thus the sample now consists of about 56,000 households selected to represent the U.S. civilian noninstitutional population 16 years and over.

Statistics on nonagricultural payroll employment, hours, and earnings (B tables) are collected by the Bureau of Labor Statistics, in cooperation with State agencies, from payroll records of a sample of approximately 165,000 establishments. Unless otherwise indicated, data for both statistical series relate to the week containing the 12th day of the specified month.

Comparability of household and payroll employment statistics

Employment data from the household and payroll surveys differ in several basic respects. The household survey provides information on the labor force activity of the entire civilian noninstitutional population, 16 years of age and over, without duplication. Each person is classified as either employed, unemployed, or not in the labor force. The household survey counts employed persons in both agriculture and nonagricultural industries and, in addition to wage and salary workers (including private household workers), counts the self-employed, unpaid family workers, and persons "with a job but not at work" and not paid for the period absent.

The payroll survey relates only to paid wage and salary employees (regardless of age) on the payrolls of nonagricultural establishments. Persons who worked at more than one job during the survey week or otherwise appear on more than one payroll are counted more than once in the establishment survey. Such persons are counted only once in the household survey and are classified in the job at which they worked the greatest number of hours.

Unemployment

To be classified in the household survey as unemployed an individual must: (1) Have been without a job during the survey week; (2) have made specific efforts to find employment sometime during the prior 4 weeks; and (3) be presently available for work. In addition, persons on layoff and those waiting to begin a new job (within 30 days), neither of whom must meet the jobseeking requirements, are also classified as unemployed. The unemployed total includes all persons who satisfactorily meet the above criteria, regardless of their eligibility for unemployment insurance benefits or any kind of public assistance. The unemployment rate represents the unemployed as a proportion of the civilian labor force (the employed and unemployed combined).

The Bureau regularly publishes a wide variety of labor market measures. See, for example, the demographic, occupational, and industry detail in tables A-2 and A-3 of this release and the comprehensive data package in Employment and Earnings each month. A special grouping of seven unemployment measures is set forth in table A-7. Identified by the symbols U-1 through U-7, these measures represent a range of possible definitions of unemployment and of the labor force—from the most restrictive (U-1) to the most comprehensive (U-7). The official rate of unemployment appears as U-5.

Seasonal adjustment

Nearly all economic phenomena are affected to some degree by seasonal variations. These are recurring, predictable events which are repeated more or less regularly each year—changes in weather, opening and closing of schools, major holidays, industry production schedules, etc. The cumulative effects of these events are often large. For example, on average over the year, they explain about 95 percent of the month-to-month variance in the unemployment figures. Since seasonal variations tend to be large relative to the underlying cyclical trends, it is necessary to use seasonally-adjusted data to interpret short-term economic developments. At the beginning of each year, seasonal adjustment factors for unemployment and other labor force series are calculated for use during the entire year, taking into account the prior year's experience, and revised seasonally-adjusted data are introduced in the release containing January data.

All seasonally-adjusted civilian labor force and unemployment rate statistics, as well as the major employment and unemployment estimates, are computed by aggregating independently adjusted series. The official unemployment rate for all civilian workers is derived by dividing the estimate for total unemployment (the sum of four seasonally-adjusted age-sex components) by the civilian labor force (the sum of 12 seasonally-adjusted age-sex components).

For establishment data, the seasonally-adjusted series for all employees, production workers, average weekly hours, and average hourly earnings are adjusted by aggregating the seasonally-adjusted data from the respective component series. These data are also revised annually, often in conjunction with benchmark (comprehensive counts of employment) adjustments. (The most recent revision of seasonally-adjusted data was based on data throuigh August 1977.)

Sampling variability

Both the household and establishment survey statistics are subject to sampling error, which should be taken into account in evaluating the levels of a series as well as changes over time. Because the household survey is based upon a probability sample, the results may differ from the figures that would be obtained if it were possible to take a complete census using the same questionnaires and procedures. The standard error is the measure of sampling variability, that is, of the variation that occurs by chance because a sample rather than the entire population is surveyed. The chances are about 68 out of 100 that an estimate from the survey differs from a figure that would be obtained through a complete census by less than the standard error. Tables A through H in the "Explanatory Notes" of Employment and Earnings provide approximations of the standard errors for unemployment and other labor force categories. To obtain a 90-percent level of confidence, the confidence interval generally used by BLS, the errors should be multiplied by 1.6. The following examples provide an indication of the magnitude of sampling error: For a monthly change in total employment, the standard error is on the order of plus or minus 182,000. Similarly, the standard error on a change in total unemployment is approximately 115,000. The standard error on a change in the national unemployment rate is 0.12 percentage point.

Although the relatively large size of the monthly establishment survey assures a high degree of accuracy, the estimates derived from it also may differ from the figures obtained if a complete census using the same schedules and procedures were possible. However, since the estimating procedures utilize the previous month's level as the base in computing the current month's level of employment (link-relative technique), sampling and response errors may accumulate over several months. To remove this accumulated error, the employment estimates are adjusted to new benchmarks (comprehensive counts of employment), usually on an annual basis. In addition to taking account of sampling and response errors, the benchmark revision adjusts the estimates for changes in the industrial classification of individual establishments. Employment estimates are currently projected from March 1974 levels, plus an interim benchmark adjustment based on December 1975 levels.

One measure of the reliability of the employment estimates for individual industries is the root-mean-square error (RMSE). The RMSE is the standard deviation adjusted for the bias in estimates. If the bias is small, the chances are about 68 out of 100 that an estimate from the sample would differ from its benchmark by less than the RMSE. For total nonagricultural employment, the RMSE is on the order of plus or minus 81,000. Measures of reliability (approximations of the RMSE) for establishment-survey data and actual amounts of revision due to benchmark adjustments are provided in tables J through O in the "Explanatory Notes" of Employment and Earnings.

NOTE: Household survey data for periods prior to January 1978 shown in tables A-1 through A-7 are not strictly comparable with current data because of the introduction of an expansion in the sample and revisions in the estimation procedures. As a result, the overall civilian labor force and employment totals in January were raised by roughly a quarter of a million; unemployment levels and rates were essentially unchanged. An explanation of the supplementation procedures and an indication of the differences will appear in "Revisions in the Current Population Survey in January 1978," Employment and Earnings, February 1978 Vol. 25 No. 2.

HOUSEHOLD DATA

Table A-1. Employment status of the noninstitutional population

[Numbers in thousands]

Employment status	Not seasonally adjusted			Seasonally adjusted					
	Jan. 1977	Dec. 1977	Jan. 1978	Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
TOTAL									
Total noninstitutional population[1]	157,381	159,736	159,937	157,381	159,114	159,334	159,522	159,736	159,937
Armed Forces[1]	2,133	2,129	2,121	2,133	2,131	2,134	2,132	2,129	2,121
Civilian noninstitutional population[1]	155,248	157,608	157,816	155,248	156,982	157,201	157,389	157,608	157,816
Civilian labor force	94,704	98,503	97,950	95,719	97,756	98,071	98,877	98,919	99,107
Participation rate	61.0	62.5	62.1	61.7	62.3	62.4	62.8	62.8	62.8
Employed	86,856	92,623	91,053	88,653	91,088	91,383	92,214	92,609	92,881
Employment-population ratio[2]	55.2	58.0	56.9	56.3	57.2	57.4	57.8	58.0	58.1
Agriculture	2,672	2,914	2,868	3,121	3,199	3,243	3,357	3,323	3,354
Nonagricultural industries	84,184	89,710	88,185	85,532	87,889	88,140	88,857	89,286	89,527
Unemployed	7,848	5,880	6,897	7,066	6,668	6,688	6,663	6,310	6,226
Unemployment rate	8.3	6.0	7.0	7.4	6.8	6.8	6.7	6.4	6.3
Not in labor force	60,544	59,105	59,866	59,529	59,226	59,130	58,512	58,689	58,709
Men, 20 years and over									
Total noninstitutional population[1]	66,930	68,052	68,148	66,930	67,745	67,852	67,948	68,052	68,148
Civilian noninstitutional population[1]	65,250	66,364	66,467	65,250	66,056	66,161	66,257	66,364	66,467
Civilian labor force	51,718	52,921	52,741	52,017	52,366	52,739	52,971	53,122	53,153
Participation rate	79.3	79.7	79.3	79.7	79.3	79.7	79.9	80.0	80.0
Employed	48,174	50,514	49,822	49,007	49,888	50,118	50,459	50,688	50,673
Employment-population ratio[2]	72.0	74.2	73.1	73.2	73.6	73.9	74.3	74.5	74.4
Agriculture	2,030	2,192	2,171	2,238	2,320	2,326	2,330	2,346	2,394
Nonagricultural industries	46,144	48,322	47,651	46,769	47,568	47,792	48,129	48,342	48,279
Unemployed	3,544	2,407	2,919	3,010	2,470	2,621	2,512	2,434	2,480
Unemployment rate	6.9	4.5	5.5	5.8	4.7	5.0	4.7	4.6	4.7
Not in labor force	13,532	13,443	13,726	13,233	13,690	13,422	13,286	13,242	13,314
Women, 20 years and over									
Total noninstitutional population[1]	73,642	74,883	74,991	73,642	74,543	74,660	74,768	74,883	74,991
Civilian noninstitutional population[1]	73,550	74,783	74,892	73,550	74,444	74,561	74,669	74,783	74,892
Civilian labor force	34,829	36,708	36,624	34,788	36,203	35,984	36,451	36,418	36,595
Participation rate	47.4	49.1	48.9	47.3	48.6	48.3	48.8	48.7	48.9
Employed	32,205	34,530	34,184	32,372	33,690	33,537	33,923	34,009	34,348
Employment-population ratio[2]	43.7	46.1	45.6	44.0	45.2	44.9	45.4	45.4	45.8
Agriculture	394	436	421	484	496	525	589	543	517
Nonagricultural industries	31,811	34,094	33,763	31,888	33,194	33,012	33,334	33,466	33,831
Unemployed	2,623	2,179	2,440	2,416	2,513	2,447	2,528	2,409	2,247
Unemployment rate	7.5	5.9	6.7	6.9	6.9	6.8	6.9	6.6	6.1
Not in labor force	38,721	38,075	38,268	38,762	38,241	38,577	38,218	38,365	38,297
Both sexes, 16-19 years									
Total noninstitutional population[1]	16,810	16,802	16,798	16,810	16,825	16,822	16,806	16,802	16,798
Civilian noninstitutional population[1]	16,448	16,460	16,457	16,448	16,483	16,480	16,463	16,460	16,457
Civilian labor force	8,157	8,873	8,585	8,914	9,187	9,348	9,455	9,379	9,359
Participation rate	49.6	53.9	52.2	54.2	55.7	56.7	57.4	57.0	56.9
Employed	6,477	7,580	7,046	7,274	7,510	7,728	7,832	7,912	7,860
Employment-population ratio[2]	38.5	45.1	41.9	43.3	44.6	45.9	46.6	47.1	46.8
Agriculture	248	286	275	399	383	392	438	434	443
Nonagricultural industries	6,229	7,293	6,771	6,875	7,127	7,336	7,394	7,478	7,417
Unemployed	1,680	1,294	1,539	1,640	1,677	1,620	1,623	1,467	1,499
Unemployment rate	20.6	14.6	17.9	18.4	18.3	17.3	17.2	15.6	16.0
Not in labor force	8,291	7,587	7,872	7,534	7,296	7,132	7,008	7,081	7,098
WHITE									
Total noninstitutional population[1]	138,415	140,264	140,421	138,415	139,789	139,962	140,095	140,264	140,421
Civilian noninstitutional population[1]	136,654	138,523	138,687	136,654	138,046	138,218	138,351	138,523	138,687
Civilian labor force	83,839	86,879	86,405	84,691	86,407	86,812	87,292	87,193	87,425
Participation rate	61.4	62.7	62.3	62.0	62.6	62.8	63.1	62.9	63.0
Employed	77,450	82,375	81,061	78,995	81,203	81,614	82,181	82,391	82,650
Employment-population ratio[2]	56.0	58.7	57.7	57.1	58.1	58.3	58.7	58.7	58.9
Unemployed	6,389	4,505	5,344	5,696	5,204	5,198	5,111	4,802	4,775
Unemployment rate	7.6	5.2	6.2	6.7	6.0	6.0	5.9	5.5	5.5
Not in labor force	52,814	51,644	52,283	51,963	51,639	51,406	51,059	51,330	51,262
BLACK AND OTHER									
Total noninstitutional population[1]	18,966	19,473	19,516	18,966	19,325	19,372	19,427	19,473	19,516
Civilian noninstitutional population[1]	18,594	19,084	19,129	18,594	18,936	18,983	19,038	19,084	19,129
Civilian labor force	10,864	11,624	11,546	11,038	11,344	11,398	11,551	11,761	11,725
Participation rate	58.4	60.9	60.4	59.4	59.9	60.0	60.7	61.6	61.3
Employed	9,406	10,249	9,992	9,645	9,854	9,842	9,966	10,271	10,238
Employment-population ratio[2]	49.6	52.6	51.2	50.9	51.0	50.8	51.3	52.7	52.5
Unemployed	1,458	1,375	1,554	1,393	1,490	1,556	1,585	1,490	1,487
Unemployment rate	13.4	11.8	13.5	12.6	13.1	13.7	13.7	12.7	12.7
Not in labor force	7,730	7,460	7,583	7,556	7,592	7,585	7,487	7,323	7,404

[1] The population and Armed Forces figures are not adjusted for seasonal variations; therefore, identical numbers appear in the unadjusted and seasonally adjusted columns.

[2] Civilian employment as a percent of the total noninstitutional population (including Armed Forces).

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Table A-2. Major unemployment indicators, seasonally adjusted

Selected categories	Number of unemployed persons (in thousands)		Unemployment rates					
	Jan. 1977	Jan. 1978	Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
CHARACTERISTICS								
Total, 16 years and over	7,066	6,226	7.4	6.8	6.8	6.7	6.4	6.3
Men, 20 years and over	3,010	2,480	5.8	4.7	5.0	4.7	4.6	4.7
Women, 20 years and over	2,416	2,247	6.9	6.9	6.8	6.9	6.6	6.1
Both sexes, 16-19 years	1,640	1,499	18.4	18.3	17.3	17.2	15.6	16.0
White, total	5,696	4,775	6.7	6.0	6.0	5.9	5.5	5.5
Men, 20 years and over	2,412	1,894	5.2	4.2	4.4	4.1	4.0	4.0
Women, 20 years and over	1,937	1,737	6.4	6.2	6.1	6.1	5.9	5.5
Both sexes, 16-19 years	1,347	1,144	16.7	15.8	14.9	14.7	12.7	13.7
Black and other, total	1,393	1,487	12.6	13.1	13.7	13.7	12.7	12.7
Men, 20 years and over	554	554	10.1	10.5	11.3	10.0	9.1	9.8
Women, 20 years and over	516	548	11.0	11.2	11.4	12.6	11.5	10.8
Both sexes, 16-19 years	323	385	36.2	37.4	38.0	39.0	38.0	38.7
Married men, spouse present	1,527	1,156	3.8	3.3	3.6	3.3	3.2	2.9
Married women, spouse present	1,422	1,284	6.5	6.4	6.3	6.5	6.2	5.6
Women who head families	395	369	9.1	10.0	9.3	9.3	8.1	7.9
Full-time workers	5,623	4,891	6.9	6.4	6.4	6.2	5.9	5.8
Part-time workers	1,417	1,319	10.1	9.7	9.6	9.6	8.9	8.9
Unemployed 15 weeks and over[1]	2,244	1,688	2.3	1.9	1.9	1.8	1.8	1.7
Labor force time lost[2]	—	--	8.1	7.4	7.4	7.3	7.0	6.8
OCCUPATION[3]								
White-collar workers	2,089	1,755	4.5	4.2	4.1	4.2	4.0	3.6
Professional and technical	453	390	3.3	3.0	3.0	2.9	2.8	2.7
Managers and administrators, except farm	294	261	3.0	2.5	2.6	3.0	2.5	2.5
Sales workers	335	242	5.6	5.1	5.0	4.9	4.7	3.9
Clerical workers	1,007	862	6.0	6.0	5.7	5.7	5.5	5.0
Blue-collar workers	2,752	2,374	8.5	7.8	8.0	7.6	7.2	7.1
Craft and kindred workers	785	685	6.3	5.1	5.4	5.2	5.2	5.4
Operatives, except transport	1,059	921	9.3	9.9	9.8	9.3	8.5	7.9
Transport equipment operatives	261	196	7.2	5.7	6.1	5.3	5.6	5.4
Nonfarm laborers	647	572	13.0	11.3	11.8	11.9	10.6	11.0
Service workers	1,124	1,044	8.6	7.9	8.1	7.8	7.8	7.6
Farm workers	130	116	4.6	4.7	4.4	4.1	3.9	3.9
INDUSTRY[3]								
Nonagricultural private wage and salary workers[4]	5,189	4,464	7.5	6.8	6.9	6.7	6.3	6.2
Construction	677	552	15.1	10.4	12.1	11.2	10.8	11.7
Manufacturing	1,510	1,231	7.1	7.0	6.8	6.5	5.7	5.6
Durable goods	846	676	6.7	6.4	6.1	6.0	5.6	5.2
Nondurable goods	664	555	7.6	7.9	7.8	7.2	5.9	6.1
Transportation and public utilities	236	216	4.8	4.8	4.8	4.7	4.9	4.3
Wholesale and retail trade	1,500	1,299	8.4	7.6	7.9	7.4	7.3	7.1
Finance and service industries	1,235	1,133	6.2	5.7	5.7	6.0	5.5	5.3
Government workers	670	676	4.3	4.1	4.1	4.3	4.3	4.2
Agricultural wage and salary workers	182	138	12.7	10.4	10.3	9.3	9.6	9.0
VETERAN STATUS								
Male Vietnam-era veterans:[5]								
20 to 34 years	491	355	7.6	7.4	7.1	6.8	5.6	5.7
20 to 24 years	160	97	16.5	18.9	15.3	14.1	11.8	12.9
25 to 29 years	234	149	7.9	6.1	6.6	6.4	6.1	6.1
30 to 34 years	97	109	3.8	4.8	5.0	4.8	3.7	3.5
Male nonveterans:								
20 to 34 years	1,269	1,169	8.2	7.1	7.3	6.9	6.9	7.1
20 to 24 years	736	719	10.7	9.4	9.3	9.3	9.4	10.1
25 to 29 years	371	296	7.6	5.9	6.4	5.5	5.2	5.4
30 to 34 years	162	154	4.4	4.7	4.9	4.5	4.5	4.0

[1] Unemployment rate calculated as a percent of civilian labor force.

[2] Aggregate hours lost by the unemployed and persons on part time for economic reasons as a percent of potentially available labor force hours.

[3] Unemployment by occupation includes all experienced unemployed persons, whereas that by industry covers only unemployed wage and salary workers.

[4] Includes mining, not shown separately.

[5] Vietnam-era veterans are those who served between August 5, 1964, and May 7, 1975.

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Table A-3. Selected employment indicators

(In thousands)

Selected categories	Not seasonally adjusted Jan. 1977	Not seasonally adjusted Jan. 1978	Seasonally adjusted Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
CHARACTERISTICS								
Total employed, 16 years and over	86,856	91,053	88,653	91,088	91,383	92,214	92,609	92,881
Men	51,618	53,608	52,962	53,964	54,341	54,745	55,012	54,975
Women	35,238	37,445	35,691	37,124	37,042	37,469	37,597	37,906
Married men, spouse present	37,737	38,181	38,199	38,338	38,425	38,531	38,682	38,645
Married women, spouse present	20,490	21,530	20,586	21,185	21,119	21,278	21,416	21,638
OCCUPATION								
White-collar workers	44,527	46,535	44,539	45,493	46,083	46,251	46,316	46,547
Professional and technical	13,578	14,169	13,467	13,778	14,042	13,918	13,981	14,057
Managers and administrators, except farm	9,546	10,037	9,575	9,747	9,911	9,894	9,939	10,067
Sales workers	5,509	5,736	5,681	5,741	5,718	5,804	5,796	5,913
Clerical workers	15,894	16,593	15,816	16,227	16,412	16,635	16,600	16,510
Blue-collar workers	28,376	29,601	29,651	30,324	30,247	30,603	30,807	30,942
Craft and kindred workers	11,254	11,760	11,596	11,992	11,860	12,116	12,153	12,111
Operatives, except transport	10,010	10,411	10,338	10,239	10,320	10,423	10,424	10,755
Transport equipment operatives	3,321	3,381	3,371	3,533	3,457	3,525	3,555	3,432
Nonfarm laborers	3,792	4,050	4,346	4,560	4,610	4,539	4,675	4,644
Service workers	11,685	12,484	11,893	12,556	12,473	12,590	12,617	12,704
Farm workers	2,267	2,432	2,675	2,695	2,755	2,809	2,805	2,872
MAJOR INDUSTRY AND CLASS OF WORKER								
Agriculture:								
Wage and salary workers	1,033	1,146	1,251	1,339	1,387	1,405	1,405	1,387
Self-employed workers	1,405	1,498	1,505	1,572	1,577	1,590	1,605	1,604
Unpaid family workers	233	224	356	272	305	368	346	342
Nonagricultural industries:								
Wage and salary workers	78,093	81,671	79,256	81,363	81,727	82,281	82,692	82,915
Government	15,223	15,496	14,997	15,304	15,463	15,415	15,422	15,267
Private industries	62,870	66,175	64,259	66,059	66,264	66,866	67,270	67,648
Private households	1,299	1,329	1,389	1,403	1,358	1,403	1,436	1,421
Other industries	61,571	64,846	62,870	64,656	64,906	65,463	65,834	66,227
Self-employed workers	5,695	6,090	5,851	6,084	6,080	6,082	6,182	6,259
Unpaid family workers	397	424	411	505	460	467	442	439
PERSONS AT WORK [1]								
Nonagricultural industries	79,819	83,407	79,766	82,783	82,788	83,347	83,662	83,304
Full-time schedules	65,437	68,537	65,717	67,817	67,827	68,240	68,574	68,812
Part time for economic reasons	3,159	2,915	3,243	3,306	3,263	3,285	3,220	2,986
Usually work full time	1,260	1,188	1,106	1,244	1,237	1,255	1,247	1,043
Usually work part time	1,899	1,727	2,137	2,062	2,026	2,030	1,973	1,943
Part time for noneconomic reasons	11,223	11,955	10,806	11,660	11,698	11,822	11,868	11,506

[1] Excludes persons "with a job but not at work" during the survey period for such reasons as vacation, illness, or industrial disputes.

Table A-4. Duration of unemployment

(Numbers in thousands)

Weeks of unemployment	Not seasonally adjusted Jan. 1977	Not seasonally adjusted Jan. 1978	Seasonally adjusted Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
DURATION								
Less than 5 weeks	3,163	3,067	2,784	2,784	2,804	2,851	2,628	2,700
5 to 14 weeks	2,425	2,131	2,118	2,152	2,117	2,037	1,937	1,861
15 weeks and over	2,260	1,700	2,244	1,834	1,848	1,829	1,797	1,688
15 to 26 weeks	1,081	906	1,020	908	920	936	941	864
27 weeks and over	1,180	794	1,224	926	928	893	856	824
Average (mean) duration, in weeks	14.5	12.4	15.3	14.0	13.8	13.7	13.8	13.1
Median duration, in weeks	7.2	6.2	7.7	6.9	7.1	7.0	7.1	6.6
PERCENT DISTRIBUTION								
Total unemployed	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Less than 5 weeks	40.3	44.5	39.0	41.1	41.4	42.4	41.3	43.2
5 to 14 weeks	30.9	30.9	29.6	31.8	31.3	30.3	30.4	29.8
15 weeks and over	28.8	24.6	31.4	27.1	27.3	27.2	28.2	27.0
15 to 26 weeks	13.8	13.1	14.3	13.4	13.6	13.9	15.0	13.8
27 weeks and over	15.0	11.5	17.1	13.7	13.7	13.3	13.5	13.2

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Table A-5. Reasons for unemployment

[Numbers in thousands]

Reasons	Not seasonally adjusted		Seasonally adjusted					
	Jan. 1977	Jan. 1978	Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
NUMBER OF UNEMPLOYED								
Lost last job	4,073	3,367	3,264	3,055	3,035	2,969	2,748	2,698
On layoff	1,247	1,129	848	847	840	780	687	768
Other job losers	2,825	2,238	2,416	2,208	2,195	2,189	2,061	1,930
Left last job	953	876	932	869	876	881	877	856
Reentered labor force	2,043	1,877	1,981	1,879	1,906	1,891	1,886	1,821
Seeking first job	779	778	915	935	857	901	820	914
PERCENT DISTRIBUTION								
Total unemployed	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Job losers	51.9	48.8	46.0	45.3	45.5	44.7	43.4	42.9
On layoff	15.9	16.4	12.0	12.6	12.6	11.7	10.9	12.2
Other job losers	36.0	32.4	34.1	32.8	32.9	33.0	32.6	30.7
Job leavers	12.1	12.7	13.1	12.9	13.1	13.3	13.9	13.6
Reentrants	26.0	27.2	27.9	27.9	28.6	28.5	29.8	29.0
New entrants	9.9	11.3	12.9	13.9	12.8	13.6	13.0	14.5
UNEMPLOYED AS A PERCENT OF THE CIVILIAN LABOR FORCE								
Job losers	4.3	3.5	3.4	3.1	3.1	3.0	2.8	2.7
Job leavers	1.0	.9	1.0	.9	.9	.9	.9	.9
Reentrants	2.2	1.9	2.1	1.9	1.9	1.9	1.9	1.8
New entrants	.8	.8	1.0	1.0	.9	.9	.8	.9

Table A-6. Unemployment by sex and age, seasonally adjusted

Sex and age	Number of unemployed persons (in thousands)		Unemployment rates					
	Jan. 1977	Jan. 1978	Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
Total, 16 years and over	7,066	6,226	7.4	6.8	6.8	6.7	6.4	6.3
16 to 19 years	1,640	1,499	18.4	18.3	17.3	17.2	15.6	16.0
16 to 17 years	760	717	20.7	19.8	18.8	19.0	17.8	18.2
18 to 19 years	890	791	16.9	16.7	16.2	15.9	13.7	14.5
20 to 24 years	1,625	1,547	11.4	10.7	10.4	10.4	10.2	10.5
25 years and over	3,763	3,155	5.2	4.7	4.9	4.7	4.4	4.2
25 to 54 years	3,135	2,632	5.4	4.8	5.1	4.8	4.6	4.3
55 years and over	599	503	4.2	4.1	4.2	4.1	4.0	3.5
Men, 16 years and over	3,839	3,232	6.8	5.9	6.0	5.8	5.5	5.6
16 to 19 years	829	752	17.3	17.7	16.7	16.4	15.3	14.9
16 to 17 years	381	371	19.2	19.2	18.6	18.2	16.7	17.2
18 to 19 years	456	389	16.2	15.8	15.1	15.0	13.9	13.4
20 to 24 years	895	840	11.4	10.4	9.9	9.8	9.8	10.5
25 years and over	2,063	1,601	4.7	3.9	4.3	3.8	3.6	3.5
25 to 54 years	1,680	1,297	4.8	3.8	4.3	3.9	3.6	3.6
55 years and over	364	289	4.1	3.9	4.1	3.7	3.7	3.2
Women, 16 years and over	3,227	2,994	8.3	8.2	8.0	8.1	7.6	7.3
16 to 19 years	811	747	19.6	18.9	18.0	18.1	16.1	17.4
16 to 17 years	379	346	22.4	20.6	19.1	20.1	19.2	19.5
18 to 19 years	434	402	17.6	17.7	17.4	16.8	13.5	15.8
20 to 24 years	730	707	11.5	11.0	11.0	11.1	10.8	10.5
25 years and over	1,700	1,554	6.0	6.0	5.8	6.0	5.7	5.2
25 to 54 years	1,455	1,335	6.3	6.4	6.2	6.3	6.0	5.5
55 years and over	235	214	4.4	4.5	4.5	4.8	4.4	3.8

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Table A-7. Range of unemployment measures based on varying definitions of unemployment and the labor force, seasonally adjusted

[Percent]

Measures	Quarterly averages					Monthly data		
	1976	1977				1977		1978
	IV	I	II	III	IV	Nov.	Dec.	Jan.
U-1—Persons unemployed 15 weeks or longer as a percent of the civilian labor force	2.5	2.2	1.9	1.9	1.9	1.8	1.8	1.7
U-2—Job losers as a percent of the civilian labor force	3.8	3.4	3.1	3.2	3.0	3.0	2.8	2.7
U-3—Unemployed persons 25 years and over as a percent of the civilian labor force 25 years and over*	5.5	5.2	5.0	4.9	4.7	4.7	4.4	4.2
U-4—Unemployed full-time jobseekers as a percent of the full-time labor force	7.4	6.9	6.6	6.5	6.2	6.2	5.9	5.8
U-5—Total unemployed as a percent of the civilian labor force (official measure)	7.8	7.4	7.1	6.9	6.6	6.7	6.4	6.3
U-6—Total full-time jobseekers plus ½ part-time jobseekers plus ½ total on part time for economic reasons as a percent of the civilian labor force less ½ of the part-time labor force	9.6	9.0	8.7	8.6	8.2	8.3	7.9	7.7
U-7—Total full-time jobseekers plus ½ part-time jobseekers plus ½ total on part time for economic reasons plus discouraged workers as a percent of the civilian labor force plus discouraged workers less ½ of the part-time labor force	10.6	10.0	9.7	9.7	9.2	N.A.	N.A.	N.A.

N.A.—Not available.

*Prior to this month, the U-3 measure was comprised of household heads.

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Table A-8. Employment status of the noninstitutional population for ten large States

[Numbers in thousands]

State and employment status	Not seasonally adjusted[3]			Seasonally adjusted					
	Jan. 1977	Dec. 1977	Jan. 1978	Jan. 1977	Sept. 1977	Oct. 1977	Nov. 1977	Dec. 1977	Jan. 1978
California									
Civilian noninstitutional population[1]	15,737	16,090	16,099	15,737	16,005	16,034	16,062	16,090	16,099
Civilian labor force	9,913	10,320	10,280	9,921	10,207	10,227	10,355	10,317	10,288
Employed	8,939	9,606	9,467	9,056	9,389	9,420	9,529	9,602	9,584
Unemployed	974	714	813	865	818	807	826	715	704
Unemployment rate	9.8	6.9	7.9	8.7	8.0	7.9	8.0	6.9	6.8
Florida									
Civilian noninstitutional population[1]	6,294	6,453	6,465	6,294	6,398	6,416	6,435	6,453	6,465
Civilian labor force	3,439	3,639	3,630	(2)	(2)	(2)	(2)	(2)	(2)
Employed	3,117	3,388	3,358	(2)	(2)	(2)	(2)	(2)	(2)
Unemployed	322	251	272	(2)	(2)	(2)	(2)	(2)	(2)
Unemployment rate	9.4	6.9	7.5	(2)	(2)	(2)	(2)	(2)	(2)
Illinois									
Civilian noninstitutional population[1]	8,106	8,194	8,189	8,106	8,173	8,180	8,187	8,194	8,189
Civilian labor force	5,066	5,256	5,254	5,115	5,261	5,269	5,305	5,276	5,299
Employed	4,710	4,964	4,858	4,795	4,933	4,942	4,936	4,945	4,943
Unemployed	356	292	396	320	328	327	369	331	356
Unemployment rate	7.0	5.6	7.5	6.3	6.2	6.2	7.0	6.3	6.7
Massachusetts									
Civilian noninstitutional population[1]	4,274	4,317	4,315	4,274	4,304	4,308	4,313	4,317	4,315
Civilian labor force	2,733	2,789	2,819	(2)	(2)	(2)	(2)	(2)	(2)
Employed	2,455	2,626	2,607	2,497	2,574	2,587	2,591	2,613	2,649
Unemployed	279	164	212	(2)	(2)	(2)	(2)	(2)	(2)
Unemployment rate	10.2	5.9	7.5	(2)	(2)	(2)	(2)	(2)	(2)
Michigan									
Civilian noninstitutional population[1]	6,511	6,590	6,590	6,511	6,567	6,575	6,582	6,590	6,590
Civilian labor force	4,023	4,139	4,164	(2)	(2)	(2)	(2)	(2)	(2)
Employed	3,666	3,848	3,825	(2)	(2)	(2)	(2)	(2)	(2)
Unemployed	357	291	339	348	346	341	356	319	330
Unemployment rate	8.9	7.0	8.2	(2)	(2)	(2)	(2)	(2)	(2)
New Jersey									
Civilian noninstitutional population[1]	5,388	5,440	5,439	5,388	5,424	5,429	5,435	5,440	5,439
Civilian labor force	3,285	3,450	3,360	3,331	3,412	3,411	3,441	3,487	3,406
Employed	2,909	3,212	3,097	2,987	3,091	3,083	3,141	3,226	3,175
Unemployed	376	239	263	344	321	328	300	261	231
Unemployment rate	11.4	6.9	7.8	10.3	9.4	9.6	8.7	7.5	6.8
New York									
Civilian noninstitutional population[1]	13,290	13,326	13,317	13,290	13,309	13,315	13,321	13,326	13,317
Civilian labor force	7,609	7,785	7,789	7,714	7,691	7,794	7,863	7,906	7,906
Employed	6,773	7,153	7,107	6,945	6,996	7,108	7,160	7,246	7,278
Unemployed	836	631	682	769	695	686	703	660	628
Unemployment rate	11.0	8.1	8.8	10.0	9.0	8.8	8.9	8.3	7.9
Ohio									
Civilian noninstitutional population[1]	7,740	7,814	7,812	7,740	7,794	7,801	7,807	7,814	7,812
Civilian labor force	4,647	4,798	4,746	4,688	4,881	4,880	4,921	4,842	4,787
Employed	4,297	4,556	4,455	4,368	4,569	4,582	4,598	4,580	4,526
Unemployed	351	242	291	320	312	298	323	262	261
Unemployment rate	7.5	5.1	6.1	6.8	6.4	6.1	6.6	5.4	5.5
Pennsylvania									
Civilian noninstitutional population[1]	8,782	8,847	8,842	8,782	8,828	8,834	8,840	8,847	8,842
Civilian labor force	5,053	5,209	5,120	5,097	5,215	5,180	5,182	5,207	5,166
Employed	4,608	4,829	4,714	4,694	4,791	4,785	4,790	4,800	4,802
Unemployed	445	380	406	403	424	395	392	407	364
Unemployment rate	8.8	7.3	7.9	7.9	8.1	7.6	7.6	7.8	7.0
Texas									
Civilian noninstitutional population[1]	8,888	9,101	9,108	8,888	9,045	9,064	9,083	9,101	9,108
Civilian labor force	5,666	5,893	5,905	5,739	5,775	5,846	5,872	5,932	5,984
Employed	5,289	5,617	5,580	5,402	5,465	5,525	5,570	5,625	5,692
Unemployed	376	276	325	337	310	321	302	307	292
Unemployment rate	6.6	4.7	5.5	5.9	5.4	5.5	5.1	5.2	4.9

[1] The population figures are not adjusted for seasonal variations; therefore, identical numbers appear in the unadjusted and the seasonally adjusted columns.

[3] These are the official Bureau of Labor Statistics' estimates used in the administration of Federal fund allocation programs.

[2] Seasonally-adjusted data are not presented for this series, because the seasonal component is not sufficiently strong relative to the other components (irregular and trend cycle).

ESTABLISHMENT DATA

Table B-1. Employees on nonagricultural payrolls, by industry

[In thousands]

Industry	Not seasonally adjusted				Seasonally adjusted					
	JAN. 1977	NOV. 1977	DEC. 1977 p	JAN. 1978 p	JAN. 1977	SEPT. 1977	OCT. 1977	NOV. 1977	DEC. 1977 p	JAN. 1978 p
TOTAL	79,473	84,092	84,185	82,514	80,574	82,763	82,902	83,245	83,432	83,685
GOODS-PRODUCING	23,005	24,840	24,496	24,026	23,585	24,360	24,436	24,528	24,548	24,652
MINING	806	865	709	710	817	856	859	863	713	720
CONTRACT CONSTRUCTION	3,198	4,096	3,893	3,558	3,549	3,892	3,911	3,950	3,956	3,949
MANUFACTURING	19,001	19,879	19,894	19,758	19,219	19,612	19,666	19,715	19,879	19,983
Production workers	13,606	14,339	14,339	14,197	13,807	14,091	14,132	14,184	14,325	14,403
DURABLE GOODS	11,141	11,720	11,778	11,736	11,236	11,545	11,604	11,625	11,752	11,836
Production workers	7,936	8,429	8,474	8,419	8,024	8,266	8,313	8,337	8,449	8,510
Ordnance and accessories	156.9	151.8	156.1	155.8	156	155	150	152	155	155
Lumber and wood products	602.1	658.1	653.9	644.3	625	648	653	662	665	669
Furniture and fixtures	493.4	527.7	529.6	527.7	495	510	517	521	528	530
Stone, clay, and glass products	609.1	672.1	665.7	651.8	633	658	657	667	672	677
Primary metal industries	1,180.2	1,199.9	1,202.6	1,208.8	1,185	1,211	1,208	1,206	1,205	1,214
Fabricated metal products	1,403.3	1,493.6	1,496.4	1,485.7	1,415	1,456	1,473	1,479	1,492	1,498
Machinery, except electrical	2,130.9	2,246.4	2,274.8	2,276.5	2,122	2,217	2,243	2,237	2,259	2,267
Electrical equipment	1,871.9	1,995.5	2,002.9	2,005.4	1,874	1,944	1,961	1,974	1,989	2,007
Transportation equipment	1,769.0	1,813.6	1,843.6	1,832.6	1,787	1,809	1,801	1,782	1,829	1,851
Instruments and related products	519.2	534.9	537.9	538.0	521	528	530	532	536	540
Miscellaneous manufacturing	404.5	426.2	414.5	409.4	423	409	411	413	422	428
NONDURABLE GOODS	7,860	8,159	8,116	8,022	7,983	8,067	8,062	8,090	8,127	8,147
Production workers	5,670	5,910	5,865	5,778	5,783	5,825	5,819	5,847	5,876	5,853
Food and kindred products	1,659.5	1,723.7	1,695.6	1,653.0	1,723	1,711	1,696	1,703	1,713	1,717
Tobacco manufacturers	74.1	72.8	71.9	68.1	73	67	67	65	63	67
Textile mill products	956.2	995.5	992.5	986.2	960	985	987	993	991	990
Apparel and other textile products	1,252.0	1,306.0	1,288.1	1,271.8	1,279	1,285	1,285	1,291	1,295	1,299
Paper and allied products	680.3	706.1	708.0	703.9	685	702	702	700	706	709
Printing and publishing	1,089.3	1,124.2	1,132.9	1,126.3	1,092	1,116	1,117	1,120	1,124	1,129
Chemicals and allied products	1,036.2	1,061.0	1,061.7	1,060.5	1,045	1,058	1,058	1,059	1,065	1,069
Petroleum and coal products	200.3	212.5	211.1	208.2	205	210	211	212	213	214
Rubber and plastics products, nec	651.7	691.5	691.3	688.6	656	671	673	681	685	693
Leather and leather products	260.6	266.1	262.8	255.3	265	262	266	265	263	260
SERVICE-PRODUCING	56,468	59,252	59,689	58,488	56,989	58,403	58,466	58,717	58,884	59,033
TRANSPORTATION AND PUBLIC UTILITIES	4,499	4,657	4,655	4,582	4,544	4,616	4,610	4,634	4,650	4,628
WHOLESALE AND RETAIL TRADE	17,791	18,796	19,250	18,474	17,994	18,431	18,414	18,512	18,592	18,686
WHOLESALE TRADE	4,297	4,469	4,480	4,456	4,323	4,410	4,415	4,438	4,458	4,483
RETAIL TRADE	13,494	14,327	14,770	14,018	13,671	14,021	13,999	14,074	14,134	14,203
FINANCE, INSURANCE, AND REAL ESTATE	4,379	4,583	4,595	4,577	4,419	4,545	4,572	4,597	4,609	4,619
SERVICES	14,740	15,608	15,581	15,430	15,010	15,482	15,533	15,608	15,659	15,713
GOVERNMENT	15,059	15,608	15,608	15,425	15,022	15,329	15,337	15,366	15,374	15,387
FEDERAL	2,697	2,716	2,724	2,701	2,721	2,728	2,730	2,727	2,718	2,726
STATE AND LOCAL	12,362	12,892	12,884	12,724	12,301	12,601	12,607	12,639	12,656	12,661

p=preliminary.

 ESTABLISHMENT DATA

Table B-2. Average weekly hours of production or nonsupervisory workers,[1] on private nonagricultural payrolls, by industry

Industry	Not seasonally adjusted				Seasonally adjusted					
	JAN. 1977	NOV. 1977	DEC. 1977 p	JAN. 1978 p	JAN. 1977	SEPT. 1977	OCT. 1977	NOV. 1977	DEC. 1977 p	JAN. 1978 p
TOTAL PRIVATE	35.4	36.1	36.3	35.3	35.8	36.0	36.2	36.2	36.2	35.7
MINING	42.4	44.9	43.7	42.9	43.1	44.3	44.6	44.6	43.6	43.6
CONTRACT CONSTRUCTION	33.9	36.4	36.4	33.5	35.4	36.4	36.8	36.9	36.8	35.0
MANUFACTURING	39.0	40.6	41.1	39.2	39.5	40.3	40.4	40.5	40.5	39.7
Overtime hours	3.0	3.6	3.7	3.2	3.2	3.3	3.5	3.5	3.5	3.5
DURABLE GOODS	39.5	41.3	41.9	39.9	40.0	41.0	41.2	41.1	41.2	40.3
Overtime hours	3.1	3.8	4.0	3.4	3.4	3.5	3.8	3.7	3.7	3.7
Ordnance and accessories	40.4	40.4	41.5	40.4	40.6	40.6	40.8	40.2	40.8	40.6
Lumber and wood products	38.7	39.9	40.2	38.5	40.0	40.0	40.1	40.3	40.1	39.8
Furniture and fixtures	36.4	39.6	40.2	37.4	36.9	39.2	39.5	39.4	39.4	37.9
Stone, clay, and glass products	39.0	41.9	41.9	39.8	40.0	41.0	41.1	41.8	41.8	40.8
Primary metal industries	40.0	41.2	41.7	40.8	40.1	40.9	41.3	41.3	41.4	40.9
Fabricated metal products	39.4	41.3	42.1	39.9	39.8	40.9	41.1	41.1	41.4	40.3
Machinery, except electrical	40.5	42.2	43.0	41.4	40.5	41.8	42.0	41.9	41.9	41.4
Electrical equipment	39.1	40.6	41.0	39.4	39.4	40.3	40.3	40.2	40.3	39.7
Transportation equipment	40.6	42.5	43.7	40.2	41.6	42.6	42.7	42.5	42.3	41.1
Instruments and related products	39.5	40.8	41.1	39.2	39.7	40.3	40.6	40.4	40.3	39.4
Miscellaneous manufacturing	37.6	39.4	39.3	37.7	38.1	39.0	39.1	39.0	38.9	38.2
NONDURABLE GOODS	38.3	39.7	39.8	38.3	38.8	39.3	39.4	39.5	39.5	38.7
Overtime hours	2.8	3.2	3.2	2.9	3.0	3.0	3.1	3.2	3.1	3.1
Food and kindred products	39.2	39.9	40.1	39.0	39.4	39.5	39.5	39.8	39.7	39.2
Tobacco manufacturers	35.7	40.1	38.8	36.8	36.1	38.6	38.2	38.8	38.0	37.2
Textile mill products	39.3	40.5	41.0	39.4	40.1	40.3	40.5	40.7	40.7	40.2
Apparel and other textile products	33.5	35.9	35.9	33.2	34.2	35.3	35.6	35.7	35.8	33.9
Paper and allied products	41.8	42.9	43.5	41.9	41.9	42.7	42.8	42.7	42.9	42.0
Printing and publishing	37.0	38.1	38.4	37.1	37.5	38.0	37.9	37.9	37.8	37.6
Chemicals and allied products	41.4	41.8	42.0	41.1	41.6	41.7	41.6	41.7	41.6	41.3
Petroleum and coal products	41.6	43.6	43.7	43.2	42.3	42.8	43.2	43.3	43.7	43.9
Rubber and plastics products, nec	40.7	41.1	41.3	39.6	40.9	40.7	40.9	40.9	40.8	39.8
Leather and leather products	34.7	37.9	37.6	35.8	35.3	37.6	37.7	37.8	37.2	36.4
TRANSPORTATION AND PUBLIC UTILITIES	39.5	40.3	40.4	39.5	39.8	39.9	39.7	40.3	40.3	39.8
WHOLESALE AND RETAIL TRADE	32.8	33.0	33.5	32.3	33.3	33.2	33.5	33.2	33.3	32.8
WHOLESALE TRADE	38.5	38.9	39.2	38.3	38.7	38.8	39.1	38.9	38.8	38.5
RETAIL TRADE	31.1	31.3	32.0	30.6	31.7	31.6	31.9	31.6	31.7	31.2
FINANCE, INSURANCE, AND REAL ESTATE	36.8	36.6	36.5	36.6	36.7	36.6	36.7	36.7	36.5	36.5
SERVICES	33.3	33.2	33.3	33.2	33.5	33.2	33.5	33.3	33.4	33.4

[1] Data relate to production workers in mining and manufacturing; to construction workers in contract construction; and to nonsupervisory workers in transportation and public utilities; wholesale and retail trade; finance, insurance, and real estate; and services. These groups account for approximately four-fifths of the total employment on private nonagricultural payrolls.
p=preliminary.

ESTABLISHMENT DATA

Table B-3. Average hourly and weekly earnings of production or nonsupervisory workers[1] on private nonagricultural payrolls, by industry

Industry	Average hourly earnings				Average weekly earnings			
	JAN. 1977	NOV. 1977	DEC. 1977 p	JAN. 1978 p	JAN. 1977	NOV. 1977	DEC. 1977 p	JAN. 1978 p
TOTAL PRIVATE	$5.07	$5.41	$5.41	$5.47	$179.48	$195.30	$196.38	$193.09
Seasonally adjusted	5.07	5.41	5.42	5.47	181.51	195.84	196.20	195.28
MINING	6.76	7.13	6.66	6.86	286.62	320.14	291.04	294.29
CONTRACT CONSTRUCTION	7.96	8.24	8.25	8.35	269.84	299.94	300.30	279.73
MANUFACTURING	5.46	5.61	5.88	5.92	212.94	235.89	241.67	232.06
DURABLE GOODS	5.81	6.21	6.29	6.31	229.50	256.47	263.55	251.77
Ordnance and accessories	6.06	6.45	6.54	6.55	244.82	260.58	271.41	264.62
Lumber and wood products	4.95	5.22	5.23	5.34	191.57	208.28	210.25	205.59
Furniture and fixtures	4.15	4.42	4.48	4.49	151.06	175.03	180.10	167.93
Stone, clay, and glass products	5.50	5.94	5.97	5.97	214.50	248.89	250.14	237.61
Primary metal industries	7.03	7.77	7.80	7.87	281.20	320.12	325.26	321.10
Fabricated metal products	5.63	6.03	6.06	6.06	221.82	249.04	255.13	241.79
Machinery, except electrical	6.01	6.40	6.48	6.51	243.41	270.08	278.64	269.51
Electrical equipment	5.16	5.51	5.60	5.63	201.76	223.71	229.60	221.82
Transportation equipment	6.95	7.46	7.56	7.50	282.17	317.05	330.37	301.50
Instruments and related products	5.10	5.33	5.42	5.48	201.45	217.46	222.76	214.82
Miscellaneous manufacturing	4.24	4.44	4.51	4.52	159.42	174.94	177.24	170.40
NONDURABLE GOODS	4.95	5.21	5.26	5.34	189.59	206.84	209.35	204.52
Food and kindred products	5.22	5.50	5.57	5.59	204.62	219.45	223.36	218.01
Tobacco manufacturers	5.16	5.57	5.75	6.00	184.21	223.36	223.10	220.80
Textile mill products	3.83	4.10	4.12	4.17	150.52	167.69	168.92	164.30
Apparel and other textile products	3.57	3.70	3.74	3.85	119.60	132.83	134.27	127.82
Paper and allied products	5.69	6.13	6.18	6.19	237.84	262.98	268.83	259.36
Printing and publishing	5.92	6.25	6.27	6.35	219.04	238.13	240.77	235.59
Chemicals and allied products	6.18	6.60	6.65	6.72	255.85	275.88	279.30	276.19
Petroleum and coal products	7.40	7.81	7.86	8.17	307.84	340.52	343.48	352.94
Rubber and plastics products, nec	5.07	5.22	5.24	5.27	206.35	214.54	216.41	208.69
Leather and leather products	3.57	3.71	3.71	3.79	123.88	140.61	139.50	135.68
TRANSPORTATION AND PUBLIC UTILITIES	6.70	7.21	7.24	7.25	264.65	290.56	292.50	286.38
WHOLESALE AND RETAIL TRADE	4.17	4.39	4.38	4.51	136.78	144.87	146.73	145.67
WHOLESALE TRADE	5.41	5.71	5.77	5.85	208.29	222.12	226.18	224.06
RETAIL TRADE	3.73	3.92	3.91	4.02	116.00	122.70	125.12	123.01
FINANCE, INSURANCE, AND REAL ESTATE	4.52	4.71	4.74	4.84	166.34	172.39	173.01	177.14
SERVICES	4.60	4.87	4.89	4.97	153.18	161.68	162.84	165.00

[1] See footnote 1, table B-2.
p=preliminary.

Table B-4. Hourly earnings index for production or nonsupervisory workers[1] on private nonagricultural payrolls, by industry division, seasonally adjusted

[1967=100]

Industry	JAN. 1977	AUG. 1977	SEPT. 1977	OCT. 1977	NOV. 1977	DEC. P 1977	JAN. P 1978	Percent change from: JAN. 1977-JAN. 1978	Percent change from: DEC. 1977-JAN. 1978
TOTAL PRIVATE NONFARM:									
Current dollars	192.6	199.9	201.2	203.3	204.1	204.9	207.3	7.7	1.2
Current (1967) dollars	109.7	109.1	109.5	110.3	110.2	110.2	N.A.	(2)	(3)
MINING	208.2	217.4	218.8	221.7	221.7	217.8	221.6	6.5	1.7
CONTRACT CONSTRUCTION	191.8	195.8	196.2	197.8	198.5	198.6	201.2	4.9	1.2
MANUFACTURING	192.3	201.2	202.7	204.2	205.4	206.1	208.1	8.2	1.0
TRANSPORTATION AND PUBLIC UTILITIES	205.3	212.3	215.0	217.8	219.1	221.4	221.1	7.7	-.1
WHOLESALE AND RETAIL TRADE	186.2	193.3	194.4	196.2	197.1	198.5	201.2	8.0	1.3
FINANCE, INSURANCE, AND REAL ESTATE	176.7	180.6	181.8	185.2	185.3	185.4	189.3	7.1	2.1
SERVICES	197.5	204.8	205.8	208.6	208.8	209.1	213.0	7.8	1.9

1 SEE FOOTNOTE 1, TABLE B-2.
2 PERCENT CHANGE WAS .8 FROM DECEMBER 1976 TO DECEMBER 1977, THE LATEST MONTH AVAILABLE.
3 PERCENT CHANGE WAS .0 FROM NOVEMBER 1977 TO DECEMBER 1977, THE LATEST MONTH AVAILABLE.

N.A. = not available.
p=preliminary.

NOTE: All series are in current dollars except where indicated. The index excludes effects of two types of changes that are unrelated to underlying wage-rate developments: Fluctuations in overtime premiums in manufacturing (the only sector for which overtime data are available) and the effects of changes in the proportion of workers in high-wage and low-wage industries.

Table B-5. Indexes of aggregate weekly hours of production or nonsupervisory workers,[1] on private nonagricultural payrolls, by industry, seasonally adjusted

[1967=100]

Industry division and group	1977 JAN.	FEB.	MAR.	APR.	MAY	JUNE	JULY	AUG.	SEPT.	OCT.	NOV.	DEC. P	1978 JAN. P
TOTAL PRIVATE	112.3	114.2	115.0	115.4	115.9	115.8	115.8	115.6	115.9	116.8	117.2	117.6	116.3
GOODS-PRODUCING	95.2	98.6	100.1	100.8	101.4	101.8	101.4	100.6	100.9	101.7	102.3	102.3	100.1
MINING	131.3	134.3	140.6	141.6	140.6	142.3	139.9	134.7	142.5	143.9	144.8	113.0	114.3
CONTRACT CONSTRUCTION	95.9	105.8	108.7	111.7	112.4	111.8	112.8	110.8	110.4	112.3	114.0	113.9	107.2
MANUFACTURING	93.9	96.1	97.2	97.5	98.1	98.7	98.0	97.6	97.8	98.4	98.8	99.8	98.4
DURABLE GOODS	93.2	95.2	96.8	96.9	97.8	98.7	98.3	98.1	98.4	99.3	99.5	100.9	99.7
Ordnance and accessories	39.1	39.3	39.2	40.1	40.7	41.0	40.5	39.3	39.1	38.2	38.2	39.3	39.1
Lumber and wood products	101.4	103.0	103.6	103.5	104.1	104.0	105.3	104.0	106.0	106.8	109.5	109.3	109.1
Furniture and fixtures	98.7	103.2	105.3	106.1	107.1	107.9	108.4	107.2	108.3	110.6	111.7	113.0	109.4
Stone, clay, and glass products	96.6	97.4	101.7	103.9	104.2	105.4	104.9	104.1	103.3	103.2	106.7	107.7	105.7
Primary metal industries	85.2	85.9	88.6	89.7	90.7	90.9	89.0	88.2	89.0	89.7	89.5	89.7	89.5
Fabricated metal products	97.3	100.3	101.7	101.3	102.8	104.2	103.7	103.3	103.1	105.0	105.7	107.5	105.1
Machinery, except electrical	95.2	97.9	98.7	98.8	100.2	101.6	103.2	103.5	103.6	105.5	104.9	106.2	105.2
Electrical equipment and supplies	91.9	95.6	96.1	96.3	97.2	97.9	98.3	98.3	97.8	98.8	99.4	100.6	100.2
Transportation equipment	93.4	92.9	96.4	94.7	95.3	96.5	94.8	95.4	96.5	96.2	94.5	97.3	95.4
Instruments and related products	108.7	112.7	111.6	111.7	112.3	113.2	111.7	111.3	112.4	113.2	113.4	114.1	112.2
Miscellaneous manufacturing industry	92.5	96.5	95.5	95.0	94.7	94.6	91.4	91.3	90.3	91.1	91.5	94.5	94.5
NONDURABLE GOODS	94.9	97.3	97.7	98.5	98.5	98.7	97.7	96.9	96.9	97.1	97.8	98.2	96.5
Food and kindred products	94.9	97.5	97.8	98.5	97.3	97.3	95.9	94.5	94.1	92.8	94.2	94.5	93.6
Tobacco manufacturers	76.1	82.4	75.1	80.5	78.2	80.2	77.2	71.7	73.2	72.4	72.2	72.1	70.5
Textile mill products	96.7	98.1	99.4	99.6	100.2	99.7	99.9	98.9	99.4	100.2	101.4	101.2	99.9
Apparel and other textile products	84.1	87.9	86.1	87.7	88.6	89.8	87.6	87.8	87.2	87.8	86.6	89.2	84.8
Paper and allied products	96.2	98.2	98.6	100.8	100.4	101.1	100.3	99.4	99.7	100.2	99.6	101.4	99.6
Printing and publishing	93.4	94.6	94.5	95.2	95.1	95.3	95.6	95.1	95.7	95.7	95.9	95.7	95.5
Chemicals and allied products	100.7	101.6	102.2	102.9	103.3	103.8	103.7	103.4	103.0	102.6	103.0	103.3	103.2
Petroleum and coal products	115.0	114.4	118.4	119.6	119.3	121.6	119.9	120.4	120.8	122.8	124.8	126.0	127.5
Rubber and plastics products, nec	128.0	131.8	132.9	134.8	135.3	133.9	132.5	129.7	129.3	130.5	132.5	134.4	131.6
Leather and leather products	69.1	72.1	71.8	73.4	73.3	72.9	69.9	71.8	72.7	73.8	73.7	71.9	69.7
SERVICE-PRODUCING	124.1	125.0	125.3	125.5	125.9	125.6	125.8	126.1	126.4	127.2	127.5	128.3	127.5
TRANSPORTATION AND PUBLIC UTILITIES	102.7	104.4	104.1	103.8	104.6	104.1	103.1	103.5	103.9	102.9	105.1	105.8	103.5
WHOLESALE AND RETAIL TRADE	119.4	120.3	120.7	121.0	121.4	121.2	121.6	121.6	121.8	122.7	122.4	123.1	121.9
WHOLESALE TRADE	115.4	117.1	116.9	117.3	117.3	117.3	117.5	117.5	117.8	118.7	118.8	118.9	118.7
RETAIL TRADE	120.8	121.6	122.1	122.4	123.0	122.7	123.1	123.1	123.3	124.2	123.7	124.6	123.2
FINANCE, INSURANCE, AND REAL ESTATE	130.1	130.2	131.0	131.0	131.6	131.7	132.3	132.7	133.2	134.2	134.9	134.5	134.7
SERVICES	138.8	139.3	139.8	140.1	140.3	139.6	140.1	140.6	140.9	142.7	142.6	143.9	144.1

[1] See footnote 1, table B-2.

p=preliminary.

Table B-6. Indexes of diffusion: Percent of industries in which employment[1] increased

Year and month	Over 1-month span	Over 3-month span	Over 6-month span	Over 12-month span
1975				
January	15.1	12.8	12.8	16.6
February	15.7	12.8	11.9	17.4
March	25.6	18.6	17.7	17.7
April	39.0	32.3	28.2	20.6
May	51.2	43.9	41.6	27.0
June	40.7	52.3	56.7	40.7
July	58.1	57.0	67.2	50.6
August	73.0	76.2	70.1	63.1
September	80.8	81.7	75.3	72.4
October	66.9	74.1	82.3	77.3
November	62.2	72.4	83.4	80.2
December	74.1	74.7	81.7	82.6
1976				
January	78.5	82.0	83.1	86.0
February	77.9	84.3	81.7	84.6
March	74.1	85.2	79.9	81.1
April	79.4	77.9	79.4	74.4
May	66.6	71.5	70.9	79.7
June	54.1	61.0	68.6	79.1
July	57.3	52.9	57.0	74.1
August	47.1	62.5	57.3	74.7
September	69.8	56.7	63.7	78.5
October	42.4	62.8	69.8	76.5
November	69.5	58.7	73.5	75.0
December	73.0	79.9	78.5	74.7
1977				
January	75.0	79.7	89.0	75.9
February	73.5	86.0	86.6	75.6
March	82.3	85.8	83.1	78.2
April	77.6	84.0	80.5	78.2
May	68.6	73.3	71.5	79.1
June	63.7	70.1	68.0	78.5p
July	65.7	56.1	68.3	80.1p
August	50.0	62.5	68.3	
September	61.3	57.0	73.8p	
October	59.9	73.3	75.4p	
November	75.9	74.7p		
December	75.6p	77.5p		
1978				
January	64.6p			
February				
March				
April				
May				
June				
July				
August				
September				
October				
November				
December				

[1] Number of employees, seasonally adjusted, on payrolls of 172 private nonagricultural industries.
p = preliminary.

U.S. DEPARTMENT OF LABOR
BUREAU OF LABOR STATISTICS
WASHINGTON, D.C. 20212

OFFICE OF THE COMMISSIONER

February 3, 1978

Changes in Procedures for Estimating Labor Force and Unemployment in States and Local Areas

Revised procedures for estimating monthly State and local area labor force and unemployment will be introduced with the estimates for January 1978. The purpose of these changes is to make unemployment estimates more accurate by using more current data from the Current Population Survey (CPS) and improved data from the State unemployment insurance programs. The changes will also bring State and area estimates more closely into line with the national unemployment statistics and reduce the extent of the year-end revisions in the State and area unemployment estimates. It should be emphasized that the changes do not affect the national unemployment statistics published by the Bureau and do not affect the definitions of employment and unemployment.

The national unemployment statistics published monthly by the BLS are obtained from the CPS, a representative survey of households throughout the Nation each month. However, the size of the CPS sample has not been sufficient to generate reliable monthly estimates for all States. Therefore, administrative statistics from State unemployment insurance operations and payroll statistics from establishment surveys, as well as correction factors from the CPS, have been used to calculate monthly estimates for States and labor market areas. Estimates for counties and political subdivisions within labor market areas have been estimated from fixed statistical ratios derived from the 1970 Census of Population.

The major thrust of the changes now being put into effect is to provide more current survey data and more recent statistical ratios as the basis for the estimates--most importantly to rely more heavily on the CPS, from which the official national measure of unemployment is obtained.

Background

Since World War II, estimates of unemployment for States and metropolitan areas have been prepared by State employment security agencies under the auspices of the U.S. Department of Labor. In 1972, responsibility for technical procedures and methodology was assigned by the Department of Labor to the Bureau of Labor Statistics. The estimating system then in place relied primarily on administrative data from State unemployment insurance programs, supplemented by estimates for persons not covered by unemployment insurance (especially new entrants and reentrants into the labor force) to derive State and metropolitan area unemployment data. Estimates for cities and counties within metropolitan areas were derived by applying fixed proportions of employment and unemployment from the 1970 Census of Population.

Because of generally recognized data inadequacies and definitional differences in State UI laws, BLS began a program of data improvement spanning several years. These improvements reflected data needs required by legislation, especially the Comprehensive Employment Training Act (CETA) administered by the Department of Labor.

CETA requires the use of unemployment data as part of a formula to allocate funds to States, prime sponsors (large cities and counties), and areas of substantial unemployment. It specifies that "the determination of whether persons are without jobs shall be in accordance with the criteria used by the Bureau of Labor Statistics in defining persons as unemployed." These are the criteria used in the national Current Population Survey conducted each month for the BLS by the Bureau of the Census.

With the enactment of CETA, several major modifications in the procedures for estimating State and local employment and unemployment were introduced by BLS, including:

1. Adjustment of place-of-work employment estimates (from payroll surveys) to place of residence, the concept used in the national CPS estimates and mandated by CETA.

2. Adjustment of UI based total unemployment estimates to annual State CPS averages to provide definitional consistency and to reduce statistical

bias stemming from the use of UI data from different State programs. The adjustment of the UI based unemployment estimates to the CPS was phased in as CPS sample expansion was completed. By 1976, CPS sample expansion provided annual data for the 50 States and the District of Columbia.

3. Improvement of the UI data:

In addition to the expansion of the CPS sample at the State level, BLS entered into arrangements with States to improve the UI data needed to develop unemployment estimates at the area level. Three major improvements of UI data are being emphasized:

a. Counting claimants by county of residence, instead of where they file.

b. Eliminating duplicate counting of claims because of different processing or reporting procedures.

c. Counting only those claimants who were without any earnings due to employment during the survey week.

Problems With Existing System

Large Revisions

Until now, measures of unemployment for States have been derived by inflating the UI data to account for persons not collecting benefits and linking these estimates to annual measures of unemployment derived from the previous year's Current Population Survey estimates for each State. The system required an annual revision of the estimates when the actual CPS data become available early in the following year. Experience over the past 3 years for the 27 largest States for which CPS data were available has shown that the average revision has amounted to approximately 10 percent.

The revision of unemployment estimates which are used to allocate billions of dollars of Federal funds has proved to be very controversial. This is especially true when the revision is of a substantial magnitude.

Outdated Statistical Relationships

BLS is required to produce monthly estimates of unemployment for about 6000 areas in order to meet legislated requirements. These involve about 275 metropolitan areas, small labor market areas, all counties, and cities of 25,000 or more population. Because of data limitations, employment and unemployment estimates were prepared for the labor market areas as a whole, and estimates of counties and cities within labor market areas were derived by applying fixed proportions applicable to each county and city to the labor market area. These fixed proportions were based on the 1970 Census of Population.

For example, if within a five county metropolitan area, a county had a 20 percent share of total unemployment of the metropolitan area in 1970 and a 30 percent share of the area's total employment, these shares were used to derive the current estimates of unemployment and employment for the county. Implicit in the use of 1970 Census relationships is the assumption that changes in the employment situation in the metropolitan areas were shared equally by all counties and cities within the area. This assumption cannot be supported by the facts. The fact is that there were marked differences between central cities and suburban counties of metropolitan areas in employment and unemployment trends during the 1973 to 1976 period. Total employment in the central cities declined by 2.5 percent, but rose by 7.9 percent in the suburbs. Unemployment in the cities increased 58.7 percent, while it increased 73.4 percent in the suburbs. Thus, the use of fixed proportions derived from the 1970 Census provides erroneous estimates of trends in both employment and unemployment for cities and suburbs within metropolitan areas.

Another example illustrates the errors associated with the use of fixed Census proportions. Under the old procedure, when a layoff occured in a large factory located in a city, the unemployment created by the layoff would be distributed throughout the metropolitan area, even if most of the workers employed by the factory lived in the city. In other instances, emerging population centers in suburban counties were not assigned their appropriate share of resident employment because fixed 1970 Census proportions were used to derive the estimates.

Changes in Estimating Procedures

New Linking Procedure for State Estimates

Over the past 12 months, the BLS has conducted extensive research into alternative ways to link the UI based estimates to the CPS. It was concluded that a 6 month moving average relationship of the CPS to the UI based estimate would result in considerably reduced annual revisions in comparison with the present method of applying a fixed linking factor throughout the year. During its research, the Bureau also determined that the monthly CPS estimates were sufficiently reliable to be used directly in the 10 largest States, New York City and the Los Angeles-Long Beach metropolitan area. For these States and areas, no further revision in unemployment rates will be required because actual CPS data can be used directly each month. Therefore, beginning with the estimates for January 1978:

1) Labor force and unemployment estimates in New York, California, Illinois, Ohio, New Jersey, Pennsylvania, Michigan, Texas, Massachusetts, and Florida will be based directly on the CPS. Two large areas, New York City and the Los Angeles-Long Beach metropolitan area, also will use CPS data directly because these are the only areas for which the CPS sample is large enough to support their use.

2) Labor force and unemployment estimates in the remaining 40 States and the District of Columbia will be developed each month based on the relationship between the CPS and UI based estimates for the 6 month period ending in the current month.

Efforts continue to link the State estimates more closely with the national CPS on a current basis. Under the direction of the Office of Management and Budget, the Bureau of Labor Statistics is now investigating the use of quarterly averages of CPS data for States and the District of Columbia in allocation programs, rather than monthly figures. Sample expansion of the Current Population Survey is now underway to provide reliable quarterly data for all States.

Use of Improved UI Claims Data for Areas

As a result of recent efforts by State employment security agencies, UI data will become more uniform from State to State with regard to such considerations as residency, reference period, treatment of disqualified claims, and counts of claimants who are receiving UI benefits but have reported earnings during the reference period. The improved UI data will be incorporated into the independent estimates of unemployment for labor market areas in 1978, including areas which were formerly adjusted to the CPS area estimate on an annual average basis. Improved UI claims, together with other data to reflect new entrants and reentrants will be used to allocate unemployment within a multi-county labor market area to each of the individual counties. In conjunction with the use of UI claims, current estimates of the population by county will also be used to distribute employment within the metropolitan areas. This will replace the use of fixed ratios based on the 1970 Census of Population.

A comparison of employment and unemployment estimates under the old and the new procedures was conducted in eight States for which current data were available under both procedures.* In 20 of the 43 cities within the metropolitan areas the unemployment rates were raised, in 14 they were lowered, and in 9 they were unchanged. The unemployment rate for the sum of the 43 cities, however, was unchanged. The unemployment rate, of course, is affected by the differential movements in the employment and unemployment levels. In 25 of the 43 cities unemployment levels would have been lowered by use of the new procedures, and in 32 of the cities employment would also have been lowered. These results are consistent with CPS trends in employment and unemployment for all 276 SMSA's.

*Colorado, Connecticut, Florida, Kentucky, North Carolina, Oklahoma, Pennsylvania, and South Carolina have been using the "new procedures" for the past 2 years.

Representative BOLLING. Thank you.

Mr. Levitan, this is your first appearance before this committee as Chairman of the National Commission on Employment and Unemployment Statistics.

We welcome you.

STATEMENT OF HON. SAR A. LEVITAN, CHAIRMAN, NATIONAL COMMISSION ON UNEMPLOYMENT AND UNEMPLOYMENT STATISTICS

Mr. LEVITAN. Thank you, Mr. Chairman.

Although I am appearing here as chairman of the National Commission on Employment and Unemployment Statistics, I hope the record will show that I am talking as a college professor. Regretfully, the Commission has not been duly constituted yet. Therefore, what I say may lack the strength that comes with numbers, but since there is nobody in the Commission to oppose what I am saying there is no danger that my views will be contradicted. I hope the Senate will act soon to appoint the rest of the Commission.

You asked me, Mr. Chairman, to comment on the adequacy of the labor force statistics for indicating "full employment," a concept which relates directly to the pending Humphrey-Hawkins Bill.

With your permission, I would like to submit my prepared statement for the record and summarize it very briefly.

Representative BOLLING. So ordered, it will be included in the printed record.

Mr. LEVITAN. I think, Mr. Chairman, policymakers should be aware that the present employment and unemployment statistics serve two distinct but related purposes. First, how well is the economy performing in terms of the business cycle? Second, how well is the labor force being utilized?

Of course, the data that Mr. Shiskin presents before this committee include different numbers BLS has developed to serve different purposes. Based on their 37-year record, I would say that the current labor force statistics have served very well to indicate overall economic performance. However, I do not think they serve as well in measuring the utilization of the labor force. Permit me to single out several problem areas that have emerged over the years.

First, we are counting a person who works for 1 hour, or who is seeking 1 hour of work as either employed or unemployed. Does it make sense, for example, to count the high school boy who is looking for a few hours of babysitting, or the high school girl who wants to mow a lawn as employed or unemployed if he or she does not get the job? I think one of the challenges before the Commission is to recommend a more rational measurement of employment and unemployment and labor force attachment.

This leads me to a second weakness of current data on utilization of the labor force, namely, the phenomenon of the discouraged worker. Again, this is nothing new to Mr. Shiskin and the BLS; they have struggled with this problem for years. There are hundreds of thousands of people who are not being counted as either employed or unemployed. Instead, they are counted separately as discouraged workers outside of the work force. Yet, those people really want a job. In isolated areas, when people are laid off from one job, they may become discouraged and may not look for work immediately. But according to the official definition, if a person has not looked for a job in the last 4 weeks, he is not counted in the labor force.

It is a very difficult problem. The Commission awaits data being developed by the BLS, which will hopefully be available to us before the end of the year. With the help of the BLS, we may be able to recommend other needed revisions as well.

The counting of the military is a third area to be considered when discussing utilization of the labor force. We presently have a dichotomy in the labor force; if you look at the numbers as they are presented every month, the data pertain only to the civilian labor force. Again, for the first 33 years of the current population survey, the military did constitute a separate labor force. Obviously, it was not always a voluntary labor force, as some of us may have experienced. Thus, it was justifiable not to count the military as part of the labor force.

In the past few years, however, we have had a volunteer Armed Force. The young man or woman can now choose to work for General Brown or for General Dynamics, both of whom are practically being supported by the same source. Therefore, the dichotomy of a separate military and civilian force may not be appropriate any more.

On the national level that may not be so significant, but on the local level, if we count the military force as employed, unemployment would be reduced substantially in certain areas. Counties and cities would lose millions of dollars as a result of this change in the definition.

Finally, and again this is a problem that Mr. Shiskin and BLS have been working very hard on, there is a need for improved data on minorities. It is not enough to have labor force data for the general population, or to provide averages for the whole population. Present data do not adequately measure the status of minorities and especially minority subgroups.

All this is known to Mr. Shiskin and to the BLA technicians. Thus, the question might arise: Why do we need a commission?

I think we need it because the recommendations for change have to come from outside people who represent various groups in the population. It is very hard for a Government official to alter statistical concepts and definitions, because every time the statistics in a given area change by 1 point, the mayor in that city or the people of that city may lose $1 million.

It is not something that the Secretary of Labor would like to take on as his own responsibility. It is easier to be supported in that endeavor by a commission that can at least suggest what changes are needed.

Further, I believe, Mr. Chairman, that national statistics do not suffice for measurements of economic performance and utilization of the labor force. Last year, Congress appropriated $17 billion to be allocated to communities on the basis of individual needs. But right now, the BLS data tell us very, very little about these local areas.

Finally, there is another aspect of the labor force which BLS does not measure now, and which fails, therefore, to meet the needs of the folks designing legislation for full-employment policy. We do not presently have a hardship measurement.

Once a year the Bureau of the Census picks up data to determine how well people made out economically in the labor force. The significance of this is apparent in the full employment issue you are going to face in the Humphrey-Hawkins bill. Suppose we attain 4-percent unemployment but at the same time, millions of people remain in poverty despite the fact that they are working full-time or are in the labor force full-time. Would that constitute a meaningful full employment policy?

I am not posing a hypothetical situation. In 1976, the BLS and the Bureau of the Census reported that there were almost 1 million people in the United States who worked full time year round and were poor.

I think that we do need the development of an additional hardship index. It is essential for what I understand to be the policy enunciated by the Congress. And again, on this point, I think that my thoughts and those of the Bureau of Labor Statistics are coming closer and closer. They are seeing the light of day, and I won't be surprised if before long, the BLS helps us develop this kind of a hardship index.

Of course, that assumes that you in Congress will tell OMB not to act penny wise and pound foolish so as to restrict the Bureau of the Census and BLS in collecting their statistical sample. One of the major problems in the BLS in recent years has been the inadequacy of the numbers, because OMB has repeatedly stopped them from getting needed data.

I do hope that the Congress will see that the BLS–CPS sample can be doubled or tripled. That would give us more accurate numbers. And that is up to Congress, because if you leave it to OMB, they will continue in their penny-pinching ways, despite the fact that Congress based $17 million in appropriations upon these data. Thank you.

Representative BOLLING. Thank you.

[The prepared statement of Mr. Levitan follows:]

PREPARED STATEMENT OF HON. SAR A. LEVITAN

Labor Force Statistics for Full Employment

This is my first appearance before this Committee as Chairman of the National Commission on Employment and Unemployment Statistics. But since the Commission has not yet been duly constituted, the views expressed here should be considered as personal observations of a George Washington University economics professor.

Following its mandate under Public Law 94-444, the Commission is required to undertake a comprehensive review and appraisal of the procedures, concepts, and methods used to measure labor force activity, as well as the application of the statistics. Our hope is that the Commission's labors will prove valuable to this Committee and others in the appraisal and formulation of economic and social policy.

My assignment on this occasion is directly related to the work of the National Commission on Employment and Unemployment Statistics; Chairman Richard Bolling asked me to review the appropriateness of labor force statistics focusing on the ways these statistics "could be improved to provide a better indication of 'full employment.' "

Policymakers concerned with full employment require two distinct but closely related statistical measures of labor market operations. The first should measure the impact of economic performance upon the labor force, revealing both the effect of fluctuating levels of economic activity and the degree of utilization of the available labor force. The second measurement should indicate whether the economy is providing adequately for those who are participating in the labor force.

In regard to economic performance, my judgment is that the labor force statistics are fairly adequate for measuring changes in the levels of economic activity, but are less successful for measuring labor force utilization. The unemployment rates have responded to changes in economic conditions over the past three decades and have consequently been good indicators of overall economic activity. Beyond the aggregate measures of employment and unemployment, the Current Population Survey supplies numerous details about the impacts of economic fluctuation on various sectors of the labor force. In recent years these data have been expanded to include information about minorities, but the sample is only partially successful in measuring labor force activities of component groups, particularly Hispanics. The CPS monthly labor force sample needs to be expanded further in order to provide more reliable information about minorities and other groups, as well as to illuminate other public policy concerns. The Office of Management and Budget has seen fit, however, to restrain the Bureau of the Census and the Bureau of Labor Statistics from applying for the necessary funds.

Turning to labor force utilization, the labor force data have fallen far short of the mark. The Current Population Survey has been in effect since 1940, and its underlying concepts and definitions do not fully reflect current conditions. At present, we count the person working for even one hour per week as employed. Conversely, if the same person is looking for an hour's work, the individual is counted as unemployed.

For example, a student undertaking a full-time course of study in high school or college but looking for a few hours of work is counted among the unemployed. This often evokes questions regarding the credibility of our labor force statistics and with some justification. Considering that nine out of every ten 16- and 17-year-olds are in school, does it make sense to count the boy who is looking for a few hours of babysitting, or the girl who is looking for a lawnmowing job as unemployed, though these youngsters are fully occupied in school? As a teacher, I would maintain that going to school is already a socially useful occupation. The youngster seeking a few hours of work might well be excluded from overall labor force employment and unemployment measurements, perhaps counted alternatively by separate data. Similarly, adults seeking only part-time employment have also contributed to the expansion of the work force. Any consideration of changes in counting part-time workers who are only marginally attached to the labor force would involve the entire age spectrum and not just teenagers.

A minimum number of hours employed or seeking work might be a useful criterion for determining labor force participation and attachment. This step would both refine the unemployment rate as a measure of labor utilization and prevent a blanket exclusion of all part-time workers, many of whom are self-supporting or responsible for the support of others. Of course, any cutoff would be arbitrary, but special tabulations supplied by the Bureau of Labor Statistics suggest that it might be appropriate to exclude persons working less than eight hours, or one day a week, from the work force. Of the millions of people in the work force who do voluntarily seek part-time work, relatively few work less than eight hours. A majority of all 16- and 17-year-olds in the work force are voluntary part-time workers, as are a high percentage of married women. Exclusion of persons working, say, less than eight hours or one day a week from measurements of labor force participation might remove one of the anomalies of the present counting procedures.

Another area which has been bothering labor force statisticians in and outside of government is the so-called discouraged worker phenomenon. A monthly average of a million persons were counted as discouraged by the Bureau of Labor Statistics in 1977 because they failed to seek jobs in their belief that none was available. Discouraged workers are not included in the monthly report of overall labor force participation either as employed or unemployed; they are now counted separately as being outside the labor force and their numbers are reported quarterly.

This is in line with current perceptions that labor force participation status applies only to persons displaying some tangible effort to find a job during the four weeks preceding tabulations by Census investigators and not to those merely interested in working. Here, too, additional data are needed. The Bureau of Labor

Statistics has undertaken an indepth investigation of the characteristics of discouraged workers with the aim of reassessing current discouraged worker definitions. The subject is a difficult one. Clearly, it would be improper to count as unemployed the individual who has not displayed any effort to look for a job for a year or more. On the other hand, the current definition excludes hundreds of thousands of persons who are available and really would like to work. Indeed, these people could be considered a prime concern of policymakers because they have given up searching for a job, even though they would like employment. Here the Commission will have to rely upon the results of a job search survey planned by the BLS for later this year. The results of this survey, I trust, will be available to the Commission before it writes its final report.

In recent months we have seen rapid growth in the number of people employed, and yet the unemployment rate hasn't always fallen to reflect this fact. That is because the unemployment rate is a ratio of unemployed to the entire labor force. If the labor force grows because of the influx of formerly discouraged workers, then employment gains may not change the unemployment rate. Clearly, the unemployment rate is quite sensitive to how we treat discouraged workers.

A third area worth consideration is the counting of the military. The present employment, and particularly unemployment, statistics are based on the civilian labor force, excluding the 2.1 million members of the armed forces. The explanation is easy to find. During the first 33 years of the Current Population Survey we had a conscripted military force, most of whom joined the military by special invitation from the President of the United States, and not always voluntarily. Their compensation, particularly for recruits, was not competitive with the civilian labor force. Under those circumstances it was perfectly justifiable to count the military separately from the civilian work force.

But since 1973 we have had a voluntary armed force that competes with civilian employers for the same workers, most of whom are new entrants into the labor market. A youngster today can choose between going to work for General Brown or for General Dynamics. This is increasingly true not only of young males, but also young females. National labor force measurements could easily be adjusted, but including the military as part of the counted labor force would play havoc with local unemployment rates in many communities with concentrations of military installations. This change would reduce the measured unemployment rates and consequently also cut the share of funds appropriated and allocated to these communities on the basis of unemployment. Given current economic policies these are not miniscule considerations. Last year, Congress appropriated some $17 billion to be allocated to states and communities on the basis of their unemployment levels. Therefore, inclusion of the military in the work force is largely a political consideration, not a conceptual or technical one.

A fourth area that concerns the reporting of labor force utilization is the undercounting of minority groups. This is a general problem faced by the Census Bureau and it especially affects the employment and unemployment statistics of young minority males. For example, nearly one of every five black males aged 25 to 34 years was not counted by the 1970 decennial census.

There are, of course, many other policy and technical problems that the National Commission on Employment and Unemployment Statistics will consider that might lead to recommendations for revising labor force measurements. Of utmost interest for full employment policy might be whether the Commission's reassessment of current labor market realities produces a higher or lower unemployment rate. Clearly, it is premature to second-guess its deliberations and recommendations before the full Commission is even appointed. For example, a Commission recommendation that discouraged workers be counted among the unemployed would have raised the 1977 average unemployment rate from 7 percent to 8 percent. On the other hand, if the Commission recommends the exclusion of workers seeking only part-time work of, for example, less than eight hours per week, the unemployment rate could fall by as much as the addition of discouraged workers would boost it. The important thing is that the Commission address itself to real problems and offer realistic recommendations.

The discussion thus far has focused on labor force statistics as a measure of national economic performance and labor utilization. On this score the current statistics are serving policymakers reasonably well in reflecting business fluctuations, but fall short on measuring labor utilization. There is, however, a need to improve the credibility of the data, close existing gaps, and bring the concepts and definitions of the measures in line with current economic reality.

Sound economic policy and planning for the full and productive utilization of the labor force also require data about local labor markets. On this score, current statistical measurements have fallen short of needs, partly because implementation of legislated policies requires statistical details beyond the capabilities of current surveys, but mostly, again, because the pound foolish, penny wise policies of OMB have precluded BLS from effectively meeting these needs. A crucial responsibility of the Commission is to consider ways of improving the statistical accuracy of state and local data since billions of federal dollars are allocated depending upon these state and local numbers.

But man, and increasingly woman, does not enter the work force in order to measure economic performance or to fit into the utilization concepts of the Bureau of the Census and the Bureau of Labor Statistics. Most people still have to work in order to sustain body and soul. And a policy-oriented formulation of labor force statistics should include a measurement of how well the economy is providing for those who are in the labor force. Clinging to the concepts first developed when the Current Population Survey was initiated in the 1930s, the Bureau of Labor Statistics continues to measure only whether persons are employed or unemployed, with the underlying assumption being that a job is a job, whether or not the job pays a living wage by accepted standards.

This omission is particularly disconcerting since, on a number of occasions, Congress has urged the Bureau of Labor Statistics to develop some measurements of labor market performance in terms of economic hardship faced by individuals in the work force. Former Secretary of Labor Willard Wirtz has also advocated such a measure, but without success. As was indicated earlier, this is no idle concern, since Congress has seen fit to appropriate some $17 billion to states and localities to alleviate unemployment problems. Most of these funds are then allocated on the basis of family or personal needs. Nonetheless, measurements of labor market-related economic hardship are almost nonexistent. The Bureau of Labor Statistics has shown very little interest and almost completely avoided the challenge of counting persons who are failing or being failed by the labor market.

The hardship statistics are likely to assume increasing significance in the very near future when Congress debates the enactment of a national full employment bill. We could hardly claim to have achieved such a goal at 4 percent idleness, if millions of those working, some of whom work full-time, full-year, remain poor. The fact is that currently there are nearly a million family heads who work full-time year-round and still live below the official poverty threshold.

Indeed, in this context it might be argued that counting only the proportion of the population that is working is a poor measure of economic performance since it fails to provide information on the lot of individuals who are forced into idleness. The pressing need is to design a measure that would indicate adequacy of labor market performance in terms of providing income to individuals who work or seek work. As long as we lack such a measure there remains a gaping hole in the labor force statistics needed for the formulation of policy for tight labor markets.

In brief, my conclusion is that national data about the numbers employed or seeking work fall short of meeting the needs for designing a full employment policy. A realistic approach to planning and assessing tight labor markets requires data about how well individuals are faring in the labor market and not just how many hours or weeks they work. These data are required for national as well as local labor markets.

Representative BOLLING. Senator Proxmire.

Senator PROXMIRE. Thank you.

Mr. Shiskin always gives us a briefing on the significance of the latest unemployment figures.

What you are saying, Mr. Levitan, and I would like to discuss this more later, but my general observation, and correct me if I am wrong, is that the great crudeness of our unemployment figures so far, the fact is we should look at them with some caution, and they are subject to great improvement. They don't measure many things people assume they do measure.

As you point out, they don't measure the degree of need in the economy, or the inadequacy of income, or inadequacy of jobs, and, among other things, they don't measure the fact that many people in the economy are unemployed.

You have a little store, and nobody ever comes in it, and you are losing money.

There are millions of people who are either small business or who are operating on very, very inadequate income, and they are not reflected at all.

So I think your warning tells us we should be very cautious about the way we judge the unemployment figures and, if we get to 4 percent unemployment, as you point out, we can still have a situation in which there is stress and need and a requirement for more sensible and thoughtful policies on the part of the Federal Government.

Mr. LEVITAN. I couldn't put it any better, Senator.

Senator PROXMIRE. Mr. Shiskin, let me see if I understand the meaning of the statistics you gave us this morning on unemployment.

The first big thing that hits me is that this seems to be a confirmation of what some people called an incredible report that we got for December. I think the New York Times called it "implausible and incredible" in one headline.

Now we have the figure for January, which is about the same, one-tenth of 1 percent lower.

Mr. SHISKIN. Yes.

Senator PROXMIRE. And that would seem to confirm what some people thought was an astonishing drop in December.

Mr. SHISKIN. Yes. As Mr. Levitan just said, you couldn't have put it better.

It is strange, but there are a great many people who don't like to get good news. The economy is improving. Employment has grown greatly, with a substantial decline in unemployment. We are having a very good economic expansion. Some people don't believe it, but I think the data for January confirm what we said in December. Naturally, professional economists will always add a caveat, and I would like to add one too: I will be happier if the data for March and April continue to confirm the trend we see now.

Senator PROXMIRE. There are some things that are a little distressing.

One is that the hours are down sharply. You say that is reflective of the weather. How sure are you of that?

Mr. SHISKIN. I can't produce hard data to support this. However, we made a study of the survey weeks. The weather in January 1977 was very bad, but it was not as bad as that in the January 1978 survey week. The survey week in January 1977 came before the severely bad weather in that month.

Senator PROXMIRE. Doesn't seasonal adjustment take care of that? Isn't January always a pretty severe month?

Mr. SHISKIN. No. What the seasonal adjustment takes care of is the average weather.

Weather that is worse than the average or better than the average is not taken account of by our seasonal adjustment process.

Excuse me. May I go on a minute?

Senator PROXMIRE. Yes.

Mr. SHISKIN. This year, the weather in the survey week was very bad; there was a lot of heavy rain. In addition we had problems processing the data. The processing especially affected the payroll survey, because we get those returns by mail, and the returns from the Midwest are very thin this month. So, we are working with a relatively small sample in that area.

Senator PROXMIRE. One of the elements we can see that is affected by that is that the average weekly earnings decline in January, so that the weekly earnings people had in their pocket, their ability to go out and spend and support the economy diminished in January, right?

Mr. SHISKIN. Right. However, the record seems to show, and here again I don't have the kind of hard evidence I would like to have, that when you get bad weather it only affects the situation for a few days, 1 week at most.

Senator PROXMIRE. Your statistics are for 1 month?

Mr. SHISKIN. No; they are not. They are for 1 week.

Senator PROXMIRE. You are saying that the survey was taken in a week when the weather was rather bad?

Mr. SHISKIN. The weather was worse than the average for that week in prior years.

If people are off work because of severely bad weather for 1 day, this would wreck the hours figures. It wouldn't affect the employment figures, but it would wreck havoc with the hours figures and the earnings figures. So I don't see January's hours and earning figures as an indication of the long-term trend.

Let me give you one example we happen to know about, because we were personally involved in what happened during the storms a few weeks ago. The unemployment figures are collected by the Census Bureau, and they are processed in Louisville, Ky.

Now, that office was closed on Friday of the storm week, but employees went to work on Saturday and Sunday, and by the weekend they had made up for the work they missed Friday.

I think that is usually what happens. I don't think bad weather has much of a damaging effect on the overall situation.

Senator PROXMIRE. I think you make an excellent point, and let's accept that for the moment.

The overall earnings figures that you report here for 1 year, the difference between January 1978 and January 1977, you say the hourly index improved by less than 1 percent in real terms.

The very last statement, then, not your statement, but the release that was given to the press earlier this morning, the employment situation in January 1978, in the very last paragraph, says the following:

> During the 12-month period ending in December, the hourly earnings index in dollars of constant purchasing power rose 0.8 percent.

Less than 1 percent, and this is in the recovery period.

Furthermore, the weekly earnings in constant dollars, my assumption is that they rose very little or probably actually declined. Am I right about that, or wrong? You don't give the weekly earnings in constant dollars.

Mr. SHISKIN. First of all, you know there is a problem with the average hourly earnings that concerns the change in the working population mix; as you have more and more part-time workers, the average becomes less and less representative of all workers.

While part-time workers, in my judgment, make their families better off, it appears from these averages that they are worse off.

So I would be very cautions in interpreting that figure.

We do, however, have another figure——

Senator PROXMIRE. Let me follow up on the figures I am talking about.

Can you give us weekly earnings in constant dollars? Do you have a figure for that? December to December; what does that show?

Mr. SHISKIN. Yes; I have it.

The index, which is found in the last paragraph of our release, is our hourly earnings index adjusted for overtime, seasonality and effects of changes in the proportion of workers in high-wage and low-wage industries. It keeps those factors constant.

This index was 1.2 percent higher in January than in December, and it was 7.7 percent above the index of January 1977. I think that the January to January comparison is a better indication.

Senator PROXMIRE. Is this in constant dollars?

Mr. SHISKIN. Yes; this is in constant dollars.

Senator PROXMIRE. I don't think so. That is in current dollars.

Mr. SHISKIN. I have it here. I was mistaken. It grew 0.8 in constant dollars over the 12-month period.

Senator PROXMIRE. That corresponds with the hourly index.

Were the weekly hours, the number of hours worked per week the same? They must have been.

Mr. SHISKIN. The hours worked per week have declined.

Senator PROXMIRE. Then the weekly earnings must have declined, also, in constant dollars. Am I right?

Mr. SHISKIN. Yes.

Senator PROXMIRE. I would like to get into the excellent letter that you wrote me, and I ask the chairman if he will permit us to put this in the record.

It is a letter I have from Mr. Shiskin in response to my letter enclosing an article from the New York Times.

Representative BOLLING. Without objection, so ordered.

[The information referred to follows.]

UNITED STATES SENATE,
Washington, D.C., January 17, 1978.

Hon. JULIUS SHISKIN,
Commissioner, Bureau of Labor Statistics,
Washington, D.C.

DEAR JULIUS: I'm enclosing herewith an article by Leonard Silk, a highly competent economic expert of the *New York Times* who challenges the December 1977 unemployment rate of 6.4 percent as implausible and even incredible.

Because Silk is such an able and competent reporter and analyst I feel that his statement represents a challenge that should be answered.

Any thoughts you may have on this article will be very welcome.

Sincerely,

WILLIAM PROXMIRE, *U.S.S.*

Enclosure.

[From the New York Times, Tuesday, Jan. 17, 1978]

THE ECONOMIC SCENE

Reactions to Jobless Rate: "Implausible" and "Incredible"

(By Leonard Silk)

The unexpected announcement by the Bureau of Labor Statistics that "unemployment dropped sharply" last month to 6.4 percent of the civilian labor force is being challenged as "implausible" by some of the country's leading economists and manpower experts. The reliability of the new employment and unemployment figures has an important bearing on whether and how much economic stimulus, including President Carter's proposed tax cut, will be needed to keep the economy moving toward full employment.

Those who believe the economy is already expanding fast enough—or some think, too fast, given their fears of inflation—put their emphasis on the employment rather than unemployment numbers.

The bureau has reported that total employment, seasonally adjusted, increased by 950,000 in November and by 409,000 more in December, for a two-month gain of 1,359,000.

Many economists find this number "incredible." One such is Otto Eckstein, president of Data Resources Inc., the large economic research firm, who says that the November-December employment increase is the biggest two-month gain in the last three decades, with the exception of April to May 1960, when employment bounced back from a 947,000 decline. But the jump in November-December of 1977 followed a long string of monthly advances, which brought the year's total rise in employment to a reported 4.1 million in December.

It is difficult to find anything in the performance of the United States economy during the last month of 1977 that would account for so rapid a spurt in jobs as the Bureau of Labor Statistics is reporting, according to Mr. Eckstein. Industrial production rose only 0.5 percent in November and was up in the fourth quarter at an estimated annual rate of only 3.7 percent, well below the average of 6 percent during the first three quarters of the year.

Gross national product, corrected for inflation, rose at an estimated annual rate of only 4 percent in the fourth quarter, which was also well below the average rate of gain of 6.3 percent during 1977's first three quarters.

There are seeming inconsistencies in the bureau's data on employment. The so-called household employment data, based on a door-to-door survey of a sample of 47,000 households, indicate that employment went up by more than 1.3 million in November and December, but the payroll data, which most economists regard as more reliable since they are based on the actual payrolls of a sample of 165,000 concerns, shows that employment went up by only 537,000 in the same two months.

For the year as a whole, the household employment figures went up by 4.7 percent in 1977, while the employment based on payroll data rose by only 3.8 percent.

The new seasonal-adjustment factors used by B.L.S. leave some economists dubious. The increase in employment during November and December, not seasonally adjusted, was only 393,000, or less than 30 percent as much as the seasonally adjusted figure.

Doubts about the drop in unemployment also stem from an equation widely used by economists. This equation is known as "Okun's Law," named for Arthur M. Okun, a senior fellow at the Brookings Institution. It relates changes in unemployment to changes in real gross national product above or below the economy's real G.N.P. potential growth trend as determined by rising productivity and the increase in the labor force.

The equation has been remarkably reliable in the last 20 years, accounting for changes in unemployment within a margin of error of only two-tenths of a percentage point.

When real G.N.P. grows just as fast as the potential growth of real national output, which is currently 3.4 percent, unemployment remains unchanged. But when real G.N.P. grows faster than potential, unemployment declines. At present, every 1 percent increase in real G.N.P. above the potential growth trend means a decline of two-fifths of 1 percent in the unemployment rate.

Data Resources calculates that, given the growth of real G.N.P. during the last year, the "true" rate of unemployment in the fourth quarter of 1977 was probably 7 percent, rather than the 6.6 percent average now reported by the Bureau of Labor Statistics.

The seasonally adjusted unemployment rate in December, which the bureau says was 6.4 percent, almost certainly fell within a range of 6⅛ percent and 7 percent of the labor force, according to Data Resources.

Differences in ways of calculating seasonal variations could account for the spread between the 6.4 percent rate in December and the 6⅛ to 7 percent rate indicated by Okun's Law. The bureau reports that in 1976, different methods of calculating seasonal factors for unemployment that it used varied as much as four-tenths of 1 percentage point in some months and averaged three-tenths of 1 percentage point during the year.

Some Administration officials, cheered by the new unemployment figures, have predicted that the jobless rate will drop below 6 percent by the end of this year. But private economists are holding off before they change their unemployment forecasts. For instance, Mr. Eckstein of Data Resources flatly said, "An unemployment rate below 6 percent cannot be expected."

Data Resources, which is forecasting a 4.2 percent growth in real G.N.P. during the year ahead, expects unemployment in the final quarter of the year to average 6.5 percent. Most private economists at year-end, before the bureau's new data were released, were in the same mid to upper 6 percent range for unemployment this year. One leading forecasting firm, Chase Econometrics, which expected a real G.N.P. growth rate this year of only 2.8 percent, put the unemployment rate for 1978 as a whole at 7.4 percent.

"If the laws of statistics continue to hold, the reported unemployment rate will show a significant increase in one or more of the next three months," Mr. Eckstein said. "Perhaps it will still voices questioning the tax cut."

Meanwhile, the big jump in Social Security payroll taxes, starting this month, will be putting a squeeze on consumer purchasing power for most of 1978—until Congress cuts income taxes, if it does.

Department of Labor,
Bureau of Labor Statistics,
Washington, D.C., January 30, 1978.

Hon. William Proxmire,
U.S. Senate,
Washington, D.C.

Dear Senator Proxmire: I received your letter enclosing the article by Leonard Silk in the New York *Times* of January 17. I have delayed in responding because I was away from the office at that time.

Let me first respond to the questions raised about the credibility of the 6.4 percent unemployment rate for December. As far as the seasonal adjustment for December is concerned, the rate of 6.4 percent seems very likely to be correct. As is well known, BLS computes and publishes many alternative seasonally adjusted unemployment rates. This month we used 18 different methods and 16 of the 18 yielded a rate of 6.4. In one case, the rate was 6.5 and in another, 6.3. And, of course, we had a 6.4 both on the old and revised basis.

Another question concerns the declining trend of unemployment throughout 1977 shown by the revised seasonally adjusted figures. The question that I have been asked most frequently is how can you explain the large rises in employment that have been reported in recent months without their making a dent on the level of the unemployment rate? Part of the answer, of course, is that the labor force has been rising almost commensurately with employment gains. However, after the appearance of the December figure and the revisions of the other 1977 rates, we now believe that the unemployment rate was responsive to the vigorous growth in employment by declining more or less steadily throughout the year. I find the revised data for 1977 much more credible than the earlier data, partly because they are more consistent with the employment data and partly because a relatively low figure at the end of a period of decline is more credible than a low figure which is primarily the result of a big drop in a single month. So, I will say in summary that the revised figures have more internal consistency than the unrevised figures and that they are probably closer to the mark.

There is, of course, a strong relationship between output and employment. With no growth in output, one would expect no growth or even a decrease in employment. The employment growth over the year shown by the CPS has been unusually strong. From December 1976 to December 1977, total civilian employment increased by 4.1 million or 4.7 percent. The latest estimates of GNP, released by the Department of Commerce in late January, show a growth in real output of 5.7 percent from fourth quarter of 1976 to fourth quarter of 1977. These estimates are, of course, preliminary and will be revised in February and again in March as more complete information becomes available. In addition, while the growth in employment over the year may be greater than is usually associated with this growth in output, it should be noted that the relationship between the two factors is not a rigid one from quarter to quarter and productivity change is often erratic.

Employment growth in the last two months of 1977, as measured by the BLS survey of households, (1,226,000 on the basis of revised seasonally adjusted data), was indeed unusually large and not fully matched by the increase in the establishment data. Deviations between these two series for particular months are not uncommon. However, the figures are much more consistent over longer periods of time. For example, from December 1976 to December 1977, the payroll series grew by 3.1 million or 3.8 percent, while the *comparable* series from the household survey (nonfarm wage and salary workers excluding private household workers, workers on strike, and others away from their jobs on unpaid leave) grew 3.3 million or 4.3 percent. This comparison, which is based on the data before seasonal adjustment and, therefore, is not affected by any technical limitations in the seasonal-adjustment procedures, indicates that the year-to-year growth shown by the two employment series was of similar magnitude.

It should also be noted that the unusually large growth in total employment during the final months of 1977 followed several months of comparatively slow growth. Taking the second half of 1977 as a whole, the gain in employment from June to December was slightly less than the gain recorded for the first half (2.0 million compared with 2.2 million).

In a second article, in the New York *Times* of January 19, 1978, Leonard Silk criticized the use of the employment-population ratio by the BLS. One of the original objectives in publishing the employment-population ratio was to put the employment increases into perspective as the population increases, just as the unemployment rate is put into perspective as the labor force changes. The employment-population ratio originally was provided as an attachment to my monthly statement to the Joint Economic Committee for 10 months. A comprehensive evaluation of this measure appeared in my article, "Employment and Unemployment: The Doughnut or the Hole?," which was published in the Monthly Labor Review, February 1976. My conclusion was, and still is, ". . . the answer to the question, the doughnut or the hole, is the doughnut *and* the hole."

About a year ago, the BLS consulted its advisory groups and others who received these data on the advisability of including the employment-population ratio in the official BLS monthly release. The majority of those contacted favored inclusion of this ratio in the official release. I can only repeat that the BLS has not, and has no intention of using the employment-population ratio as a replacement for the unemployment rate. Our position is, and has been, that a broad array of data are needed for economic analysis, including labor market analysis. The employment-population ratio is one of many measures which supplement, but cannot supplant, the unemployment rate.

I should like to call your attention to the possibility that we may soon be confronting another seasonal adjustment problem in the data for January. In the past two years, there has been a relatively sharp drop in unemployment and the labor force, after seasonal adjustment, between December and January, and many analysts believe that this is due to a bias in the seasonal-adjustment method and, thus, does not reflect the true change. As I explained in my recent letter to you, we have carried on extensive studies of this particular question and have not found an acceptable alternative method which gives much different results. We have, however, introduced a procedural improvement in the current method. This improvement was made because of the sharp upward trend in unemployment between 1973-75, and it now appears that as a result of this procedural change we have reduced the magnitudes of the declines in the unemployment rate between December and January 1976 and 1977—by 0.1 point each year. We do not yet know what the January data for this year will show, but I plan, in any case, to discuss this problem at our hearings before the Joint Economic Committee on Friday.

I hope this information is helpful to you. I will be happy to answer further questions on Friday.

Sincerely yours,

JULIUS SHISKIN, *Commissioner.*

Mr. SHISKIN. Would you mind saying that you asked me to comment on that, and the letter was in response to that request. Otherwise, I would have written to Chairman Bolling. I have to keep the lines straight. [Laughter.]

Senator PROXMIRE. Well, see if you can summarize for us the reasons why you could justify those unemployment figures which dropped so spectacularly in December and which were questioned by a number, including Otto Eckstein, one of the finest economists in the country, who said there was no development in December, in production or in any other element, that would justify expecting this kind of marked improvement. It startled him.

What is your answer to that?

Mr. SHISKIN. Let me talk 1 minute about Mr. Eckstein, since you mentioned his name. He was a member of the Council of Economic Advisers for years, and we worked together closely on some projects. I have a high regard for him. He produces one of our best services. So I think he is very good.

But you know how difficult forecasting is. Everybody can go back and look at his own record, if he is courageous enough, and point to bad forecasts. I think this is one of Otto Eckstein's bad ones.

I can talk with more confidence today because we have our January figures which tend to confirm what I said in my letter to you, which I wrote on January 30, before we had the new figures.

First of all, there is a question of seasonal adjustment. We compute a great many seasonal adjustments; we try all kinds of measurements.

I would say, and I don't think I can be contradicted in this, that the world's Mecca of seasonal adjustment work is now in BLS.

A person who, as a consultant to BLS, knows as much or more about seasonal adjustment as anyone else, is Stella Dagum, and we also conferred with her. We think we made a very good adjustment in December, and now that is confirmed by January.

Let me now come to the reasonableness of the figures. Before the December figures became available, the question that I was most frequently asked was, "How could you reconcile all these huge increases in employment—record increases in employment—with a situation in which there is no dent in the unemployment rate?" That was a terrible puzzle.

We were trying to figure out answers to that question. Well, the answer is that there were dents in the unemployment rate.

Our seasonal adjustment based on earlier data, which are now revised was not very good. We had substantial revisions, and, although the revision for each month was rather small, the pattern of the revisions was significant. The figures for the unemployment rates for the early part of the year were raised, and the figures for the latter part of the year were reduced.

So now when you look in the chart, you see a more or less steady decline from an unemployment rate of about 9 percent in the spring of 1975 to 6.3 percent in January 1978. This decline is consistent with the very large rises in the employment figures.

We now have a situation in which the figures are internally consistent.

Let me say in parenthesis, however, that the unemployment rate today is still higher than it usually is after 33 or so months of expansion. We still have a high unemployment rate, and it is a problem. I just want to be sure that is in the record.

But it seems to me that the new figures are much more plausible than the unrevised ones. One of the arguments that was made in the article that mentioned Mr. Eckstein was that this was in violation of Okun's law. But there are no iron laws of economics, or even physics.

GNP figures get revised a lot, too. The first quarter figure we got early a year ago was 5.2 percent, and the figures circulating around town before that were even lower. The figure has been 7.5. So we have to expect substantial revisions in GNP figures.

Now, many people are expecting a fairly slow growth in the fourth-quarter 1977 GNP, because of the decline in the inventory change. I am one of them. But real final sales were strong. So many people expect a large inventory accumulation in the first quarter and a good first quarter.

What I am saying at this point is that I don't think the figures on employment are necessarily that far out of line with the GNP figures. I think when we get the first quarter GNP figure and the revisions of the fourth quarter of 1977, they will be more consistent with the unemployment rates.

Senator PROXMIRE. My time is up, Mr. Chairman.

Mr. Shiskin in his letter makes a powerful argument. He points out there are 18 seasonal methods which the BLS uses. Eighteen. I am amazed there were that many. He said this month in December, you use the 18 different methods, and 16 of the 18 yielded a rate of 6.4 percent.

In one case the rate was 6.5, in another it was 6.3, and, as you say, we had a 6.4 on both the old and revised basis.

So it seems to me that from a seasonal standpoint there is just no other answer.

Mr. SHISKIN. It looks that way. It may be that all our seasonal adjustments methods are wrong, but I don't think so.

Representative BOLLING. Congressman Rousselot.

Representative ROUSSELOT. Thank you, Mr. Chairman.

Mr. Shiskin, I am interested in your accompanying memorandum of February 3, 1978,[1] where you described the changes which you provided for us today, the changes in procedures for estimating labor force and unemployment in States and local areas.

On page 3 of that memorandum you mention why you think there have been substantial improvements in the data needed or required by legislation. I think at the bottom of the page you list three points, and on the next page, you say there has been an improvement. And you describe, then, on page 4, the problems with the existing system. When you list these points on page 4, improvement on UI data, (A), (B), and (C), you say:

> Count employment by county of residence, instead of where they file, and discounting of duplicate claims because of different processing and reporting procedures, and (C) counting those claimants who were without any earnings in the employment earnings survey week.

How have you achieved improvement in these areas? It is nice to say that it has occurred, but how do you know that?

Mr. SHISKIN. First, let me say with a few sentences of background that, while I feel overall the unemployment rate for the Nation in the major aggregate and now even in the major States is quite accurate, the accuracy is not as good for the local areas, where our sample is too thin to give us accurate results, and we have to rely on estimating procedures.

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[1] See memorandum of Feb. 3, 1978, beginning on p. 2430.

Each year we do a lot of research to try to improve those estimating procedures. Therefore, we are able to introduce, and we usually do it at this time of the year, the improvements we see on the basis of our research in the previous year.

Now, most of our research is done through a simulation process. We ask ourselves a question: "With these new data, what would have been the results in the past?"

I am not sure I am responding to your question adequately, but we do the research, we make the study, and then simulate the results.

Representative ROUSSELOT. So it is by simulation?

Mr. SHISKIN. Yes. Simulation.

Representative ROUSSELOT. These three items (A), (B), and (C) on page 4 of your February 3 memorandum——

Mr. SHISKIN. Well, let me take them up one at a time.

Page 3, item 1, we had a problem in using the local data; they counted a person where the person works, but not where the person lives.

We have had contracts with the States in the last few years and have put a lot of pressure on them to include a code which indicates where the unemployed worker lives. That is consistent with the national survey, also, and that is the more reasonable way to do it, because the hardship arises mostly where the people live—where the family is, and where the income fails to come.

We have not been able to go all the way on that, but we have gone a considerable amount of the way.

The second problem has concerned benchmarking these UI-based unemployment statistics in a reliable manner.

Over the years Congress has appropriated more funds, although not to the extent Mr. Levitan thinks they should have, and we have been able to improve the estimates, particularly the estimates in the 10 largest States.

So we are now using these data as the controls. The statisticians use the word "benchmark" for the figures I use as controls for the small areas. When we get the data for the small areas, which are based on unemployment insurance data, with allowance for new entrants, we adjust it up to the State total. We now feel we have a reliable State total each month in 10 States, and we have a reliable picture in all the States now once a year. As you may know, and I say this parenthetically, we recommend that Congress join us in an effort to put the whole program on a quarterly basis.

That is the second point.

The third point——

Representative ROUSSELOT. On point 3, you have three subtitles, (A), (B), and (C). How do you know (A), (B), and (C) areas? And you have already commented on residence——

Mr. SHISKIN. On that one, we have instructed the employment security agencies, and we have provided them with funds which were appropriated to us by the Congress 2 years ago, or 3 years ago, to improve those data. We also have instructed them to count the unemployed by county of residence.

Previously, they have made the counts by where the people work. As I said, we haven't been able to go all the way; we haven't been able to do it in all of the States, but we have in most of them.

Representative ROUSSELOT. Let's assume you have a better system of accountability as it relates to residence; (C) is the one I am most interested in—counting those which are without earnings during the survey week.

I guess the question I want to ask here is: How do you know that?

Mr. SHISKIN. All right. I can't answer that question. I can provide an answer for the record, but there are also people in the audience from BLS, either Mrs. Norwood or Mr. Young, who could answer that question.

Representative ROUSSELOT. Can you provide it for the record or have them answer it now?

Mr. SHISKIN. Whatever the chairman wishes. I can do it either way. Mr. Zeigler can answer it.

Mr. ZEIGLER. In the process of claiming benefits, the claimant has to identify the amount of earnings he has made during the survey week, during the week that he is claiming, and we have instructed the States to eliminate through coding any person who has claimed any earnings whatsoever regardless of whether they are entitled to total benefits or not.

So it is a coding process similar to the residency. The claimant identifies where he lives, and whether he has any earnings, and these are coded appropriately and then tabulated.

Representative ROUSSELOT. We have heard a great deal recently that there are a substantial number of people who have earnings that they now call "off book." They do a lot of work on the side; they moonlight. We have no way of knowing that.

Mr. ZEIGLER. Well, each State has an enforcement policy to insure that people who are collecting unemployment insurance are not, indeed, commiting fraud by having employment or deriving earnings and not reporting them. This is something that is part of the process.

Obviously, it is a statistical agency, and we have to rely on the operating people, but it is in the interest of each State, obviously, to enforce the laws in that respect.

Representative ROUSSELOT. Would you have to rely on the State to determine how good their system is in determining off-book or nonrecorded income?

I have seen an article recently in the Wall Street Journal and articles in several magazines, that make estimates over $150 billion a year of so-called off-book, nonreported earnings, mostly in cash transactions, part-time work, and so on. But we have no way of really knowing that.

Mr. ZEIGLER. No, not definitively.

Representative ROUSSELOT. But it is critical to the decision of whether a State pays compensation benefits for unemployment or not, isn't it?

Mr. ZEIGLER. That is correct.

Representative ROUSSELOT. Thank you.

Representative BOLLING. Congressman Reuss.

Representative REUSS. Thank you, Mr. Chairman.

The figures, as I read them, tell the same old sad story—I think it is sad—the soap opera is generally good, unemployment down to 6.3 percent from 7.4 percent a year ago in January of 1977. But then you look at black unemployment, and it goes up from 12.6 percent in

January 1977 to 12.7 percent today, and black teenagers are up from 36.2 percent to 38.7 percent.

We talk about this about once a month, but it seemed more dramatic because now it comes at a time when the administration is going all out on a macroeconomic program, when it becomes plainer every day that the problem is microeconomic and has to do with structural unemployment.

What are your thoughts, Mr. Shiskin?

Mr. SHISKIN. Can you let me answer that in more than one word? I can't answer that accurately in one word, true or false.

First of all, Congressman, you and I had a chat about 6 months or 9 months ago about the two-tier economy. The press gave me credit for that expression, but it was really your expression and you should get credit for it. But that is what it is, a two-tier economy.

There has been no improvement at all for blacks. The overall unemployment rate has improved, but the rate for blacks remains high. It doesn't budge.

The other comment I would make is that I don't think it is true that the administration is neglecting that. BLS is located, as you know, in the Department of Labor, and I think Secretary Marshall and Assistant Secretary Green, in the Employment and Training Administration are very well aware of that.

They talk about it among themselves more than they talk to me about it, but I am present at some of the discussions, and there is no doubt in my mind that the Secretary of Labor and Ernie Green are trying to zero in on that situation.

I think there is a major structural employment problem. So, I agree with what you said on that, but I don't agree that the administration is uninformed.

Representative REUSS. Thank you.

Mr. Levitan, you say in your prepared statement:

> A fourth area that concerns the reporting of labor force utilization is the undercounting of minority groups. This is a general problem faced by the Census Bureau and it especially affects the employment statistics of young minority males. For example, nearly one of every five black males aged 25 to 34 years was not counted by the 1970 decennial census.

I can attest to the validity of your observation there. The 1970 census was a farce, in that people went through the central cities scaring the hell out of the residents, who were, of course, prone not to report themselves.

I am interested that you are able to qualify that as a shocking 20-percent error.

What is the basis of your assertion?

Mr. LEVITAN. It is not an assertion, but rather it was given to the National Commission on Employment and Unemployment Statistics by Prof. Philip McCarthy of Cornell University, an outstanding statistician, and a consultant to the commission looking into the current population survey. I took this number from a section of his report to the commission and, since Mr. McCarthy used it, I think it is an authoritative figure.

However, as you suggested, and this is in line with what Mr. Shiskin just said, we still have very serious unemployment problems.

But at the same time, we should remind ourselves that 6.3 percent unemployment, even if we take into account rising labor force participation, is still far from any definition of full employment. Therefore, aside from the problems to which Mr. Shiskin alluded, I think we are all also rather concerned about aggregate economic activity. We still have an unemployment problem in the United States, particularly for selected groups in the population.

Mr. Shiskin is correct in saying that employment has grown rapidly, but at the same time this growth is a manifestation of (a) government activity; (b) changes in the structure of the labor force and the labor market; and (c) changes in the family structure.

In January of 1978, the employment situation, as effective as it is in indicating economic recovery during the year, still reveals at least 2 million more idle persons than is reasonable in a full employment for this country.

Representative REUSS. It is clear, is it not, that the figure we get of about 500,000 black male unemployed is inaccurate, and that since there was a gross miscounting of black males in the population count of 1970, that the number of actual black male unemployed is considerably greater than that given to us by the Bureau of Labor Statistics?

Mr. LEVITAN. The chances are that that statement is correct.

Representative REUSS. Let me address myself to the larger point I believe you were making. You were making, were you not, the point that the whole problem of unemployment is not structural and that there need to be macroeconomic methods of getting down the total 6.3 figure as well as the structural component of that figure? Is that your point?

Mr. LEVITAN. Yes.

Representative REUSS. I heartily agree with you. My only point is that you can work macroeconomics until every European ally of ours quivers in his boots and the dollar sinks out of sight, and you still won't get many jobs for these structurally unemployed.

The macromethods can't do it. But you need macromethods too. Do you disagree with that?

Mr. LEVITAN. No; that is the point I was trying to make. You do need macroeconomic measures.

I have sympathy for our European friends. We have tried unemployment for a long time. The dollar situation has not improved.

I think it is prudent to try full employment and see what happens to the dollar. I bet our European friends would love us for that, and the dollar situation would also improve.

But at the same time, Mr. Reuss, I would say that the two are not mutually exclusive.

In other words, a tax cut does not necessarily eliminate the need for pursuing the policies that Congress and the President embarked on last year. And I hope they are continued this year, specifically: the expansion of public service employment, focusing particularly upon youth unemployment. The Labor Department is doing that now, through its youth employment program. The program seems to be working very well, and I think that its administrator, Mr. Robert Taggart, has done an outstanding job within a very short time.

Clearly the additional $1 billion and $300 or $400 million that is allocated for the program is a large amount of money, but if you look at the numbers involved, it is not at all excessive. I hope that Congress will continue pushing for these structural programs.

Representative REUSS. I can't agree that it is working all that well when, in this glorious year, black unemployment has gone up, particularly black teenage unemployment. I can't really give the highest marks to a program that produces an upsurge of black teenage unemployment from 36.2 to 38.7 in a year. One more triumph like that and——

Mr. LEVITAN. Mr. Reuss, as a college professor, may I also ask you: Have you given Congress the right mark? Has Congress tried hard enough to reduce unemployment to the 4-percent mark.

I don't think you can put the blame entirely in the corner of Mr. Marshall, or the employment and training programs, though granted, the manpower efforts are not necessarily perfect programs. Nonetheless, I am not sure that Congress has done all it could do.

Representative REUSS. I absolutely agree, and I don't want to single out Secretary Marshall. I think he is one of the best people around on employment, but the fact is that with our total effort, we are producing a greater disaster every month, and I think a little humility on the part of all would be good.

I do point out that to my knowledge Congress has not turned down any structural unemployment alleviating programs forwarded by the administration, and I can think of a number of programs, like the Civilian Conservation Corps, which produced jobs for 3.5 million people in the 1930's, which would be really quite good now.

Anyway, this is our monthly exercise, and I will know a lot more after you have finished.

Representative BOLLING. Senator Proxmire.

Senator PROXMIRE. Mr. Shiskin, the Employment and Training Acts require that an index of economic hardship be developed. Are you breaking a law in not having that done?

Mr. SHISKIN. I don't think so, sir. I never break the law, as you know. [Laughter.]

First of all, the law provided us with enabling legislation, but in order to carry out a program, you have to have something else; namely, an appropriation, and I would like to talk a little bit about that.

I have a record of BLS activities on that item in the law.

Senator PROXMIRE. You asked for appropriations for that purpose?

Mr. SHISKIN. Yes, in June of 1974.

Senator PROXMIRE. Who turned you down, the Budget Bureau?

Mr. SHISKIN. Let me explain. In June of 1974, we asked ETA, the Employment Training Agency, to provide us with funds to support our program, and they did not do so.

You have to bear in mind that in the Federal Government, there is a division of responsibility for the collection of statistics, and the responsibility for the income statistics is with the Department of Commerce.

The Department of Commerce puts out a very comprehensive report on hardship, and they issue it once a year. It has some limitations. I, myself, have publicly criticized their report, but it is a very large and important report.

It is the report on the number of persons under poverty levels in the United States. So the authority in the Federal Government for getting out hardship statistics is in the Department of Commerce—not in the Department of Labor.

Now, what can we do?

Well, besides trying to push that a little bit with some work of our own, we could get out the earnings data, because that is what is relevant. What Mr. Levitan is talking about mostly is job-related hardship.

Here is what we have done on job-related hardship. In our fiscal 1976 budget, which we submitted in 1975, we asked for money to collect additional information on the characteristics of unemployed and on earned income.

We asked for $195,000. Our request was rejected by Congress.

In the fiscal 1977 budget, we had a proposal to collect quarterly earnings data from the CPS. That proposal was supported by the Interagency Federal Government Committee on Economic Statistics, but it did not survive the budget process within the administration.

In fiscal 1978, we had a similar proposal, and it again didn't survive.

Now, for fiscal 1979, we proposed it again. It has not been approved, but OMB suggested that we reexamine our priorities to see if we couldn't make existing programs support this program.

We have done so, and we have shifted the distribution of funds in our total fund for employment and unemployment statistics to allow for this program. We now have scheduled the release of quarterly earnings data for the first quarter of 1979.

Senator PROXMIRE. As I understand it, Mr. Shiskin, you are requesting money to do this for the unemployed. I am talking about the employed, too. There are many, many people in this country who are employed who certainly suffer economic hardship because their income is pathetic.

Mr. SHISKIN. We are talking about the same thing. The earnings data cover the employed. So we will be able to supply data for workers with low earnings. We will do that in 1979.

I don't think we are violating the law. We have made every effort we could to provide information, to get better income data particularly at the low income levels.

Senator PROXMIRE. Mr. Levitan, are you satisfied that the BLS is doing all they can to get this information?

Mr. LEVITAN. The way you initially asked the question, I would not want to see my good friend, Mr. Shiskin, in vain, so I would have to defend him. But what he has fully and vigorously tried to carry out the section you are referring to of CETA, I would say he could have done it a little more energetically what the law provides, without, clearly, being able to fulfill all the requirements, because they were not given the additional funds.

I do think, however—it seems to me, and I am not sure of this in the past, but I think I suggest in my initial statement that BLS is now seeing the light, and I think we will have a hardship index, because I think it is absolutely necessary to carry out the mandate and to implement the programs that Congress has provided in various pieces of legislation.

Senator Proxmire. Mr. Levitan, what seems to be a sharp difference between you and Mr. Shiskin is over the use of the employment-population ratio. It seems to me to be a very usable statistic, one I would like to know about.

I don't think Mr. Shiskin has ever said it should replace the unemployment figures, but he says in his letter, he wants to look at the doughnut as well as the hole. His predecessor, Mr. Moore, talked about the fact that we never looked at the doughnut, but only the hole, that is, at unemployment, not employment.

Why isn't it desirable that we look at both, and have all those statistics before us? Why is it not cause for some satisfaction that we now have a higher proportion of our people at work than we have ever had on the basis of statistics we have.

Why isn't that good and why shouldn't we know that?

Mr. Levitan. There is no question that the employment statistics are useful. My only concern is that we don't get cross-eyed looking at too many things. If you focus on employment, you focus on one aspect of the labor force; if you focus on unemployment, you focus on another.

Obviously we should look at both, but Senator, I am concerned that if we look too much at employment and population, we may ignore unemployment problems, which are still real.

Senator Proxmire. Cross-eyed isn't exactly the kind of thing we like to be, but I still cannot understand why we shouldn't have this information, and why it shouldn't be made available regularly.

It seems to me it indicates progress in the economy that more people are working, and it is wholesome and desirable and something we should look at with the unemployment. I think it may indicate that there are fewer discouraged workers. Maybe not, but that may be some indication of it.

There may be people who instead of remaining idle decide to go to work.

There are a lot of young people in Wisconsin that I know about. There are more in that age group working than there were 10 or 15 years ago. That is a constructive element. Why shouldn't we know that?

Mr. Levitan. I agree we should look at it. Any additional figures about the operation of the labor market are helpful, but again, it is still dangerous to look at that figure too much.

Let's look at what happened in 1977. Undoubtedly, we had a very outstanding year of job growth, possibly the highest one. But at the same time, was it a purely positive development?

I think we ought to know more about the components of employment growth. For example, 400,000 jobs or more were created directly by the Government through public service employment and public works. I am definitely in favor of that, but it was from deficit financing, although it was a necessary measure. Obviously, at least over the short term, we could appropriate billions more and create many more jobs.

Second, 500,000 of the new jobs in the economy were part-time positions. Again, that is part of the development of the economy, and possibly most of those were voluntary part-time jobs, but not all.

Third, a part of the growth of the labor force was due to continued inflation. Again, it is not necessarily a healthy development if households find that in order to maintain their standard of living, another member of the family has to go out to get the part-time job, as suggested before.

And finally, productivity of the economy has declined during the past decade, limiting increases in real wages and salary.

Senator PROXMIRE. You make an absolutely irresistible point, and I would like to get Mr. Shiskin's response to it, that we should include as part of the work force as employed, people who are in the military.

As you point out, it is a voluntary service now, and whether people work for a defense contractor when they are considered employed, or work in the military, where they are considered employed, it seems to me they certainly should be considered employed in both.

Mr. SHISKIN. Senator Proxmire, I would like to answer that question. But I was attacked by Mr. Levitan——

Mr. LEVITAN. No.

Mr. SHISKIN. Yes, I was, by Silk and Levitan, in a published article, and I would like to have an opportunity to respond to that.

Senator PROXMIRE. Yes; but would you first answer my question?

Mr. SHISKIN. Yes. In the military, you are facing a complex problem. Let me give you two examples of how complex it is. We have a much longer explanation of the practical problems, which I can submit for the record, but let me make two points.

In regard to the voluntary army, suppose that there are some waiting lines in some of the offices for people who want to go into the Army. Should we count them as unemployed? That is, you have people that once——

Senator PROXMIRE. If they don't have another job, why not?

Mr. SHISKIN. If they do have a job, are they unemployed with respect to getting into the Army?

Senator PROXMIRE. You know the answer to that, Mr. Shiskin, at least I think what you do under those circumstances. Bill Jones wants to go into the Army.

Mr. SHISKIN. Yes.

Senator PROXMIRE. He is not able to get in because the quota is filled. Under those circumstances, if he doesn't have another job and is seeking work, he is considered unemployed. If he is not seeking work, he is considered out of the work force; isn't that right?

Mr. SHISKIN. But the conceptual point, you see, is that you have people trying to recruit enlistees for the Army, and you have people who want to get in.

Now, this is a special group of people in a special situation. How do you handle them in the light of your ordinary rules for counting people as unemployed?

Senator PROXMIRE. I don't understand why you have any problem at all on this. It seems like it is the same as with any other employer.

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With General Dynamics, if they get a job, they are employed, and if they are looking for a job with General Dynamics, they are considered to be unemployed.

Mr. SHISKIN. Let me drop that then. I don't have a strong answer for that. But let me give you another kind of problem we have.

Mr. Rousselot may be especially interested in this. Suppose you count the people in the Army as employed. OK?

Now, let's go to a county where you have a big military base.

Senator PROXMIRE. Yes.

Mr. SHISKIN. Now, if you include that base, that military base in the employment figures——

Senator PROXMIRE. That is exactly why you ought to do it.

Mr. SHISKIN. Then the unemployment rate——

Senator PROXMIRE. If the Federal Government is going to spend money in a particular area and provide enormous payrolls, that is something we should know about, and consider it as part of the statistics, because it is an enormously important part of the economy to 2 million workers.

As you know, we ought to know about that, and the people should be considered unemployed. Don't we have a discretion on what the economic facts of life are in that situation?

Mr. SHISKIN. We are sympathetic to it, and when we get to the Levitan Commission recommendations, if that is included we will give it very serious consideration.

We are not ruling it out by any means.

The rule we have, which I believe the Gordon Commission recommended because they couldn't find the right cutoff, is that if a person works 1 hour a week, he is counted as employed. That sounds rather silly.

I would like to comment, Mr. Chairman——

Senator PROXMIRE. If you want to do it now, do it.

Mr. SHISKIN. Yes. This article in reaction to the jobless rate was pretty bad, but it wasn't Mr. Silk's worst. The worst he published, that I know about, was on the new employment measures, "Some Economists Are Critical."

What he did in that article was to line up a group of people and he cites here Arthur Burns, Herbert Stein, and Geoffrey Moore, and I think he considers them the bad guys.

Then, on the other side he lines up Arthur Okun and Sar Levitan, and I think he considers them the good guys.

Mr. Silk says in this article that I am in trouble because I have accepted the recommendations of the bad guys.

Representative BOLLING. I want to place a copy of the article in the record.

[The article referred to follows:]

[From the New York Times, Thursday, Jan. 1, 1978]

THE ECONOMIC SCENE

New Employment Measure: Some Economists Critical

(By Leonard Silk)

Some economists are highly critical of the Bureau of Labor Statistics and its commissioner, Julius Shiskin, for accepting and stressing a new measure of the degree of "full employment"—the ratio of total employment, not to the civilian labor force but to the entire population aged 16 or older, whether or not they are looking for work.

A number of economists who have been identified with the Republican Party, including Arthur F. Burns, soon to retire as chairman of the Federal Reserve Board; Herbert Stein, chairman of the Council of Economic Advisers under President Richard M. Nixon, and Geoffrey Moore former Commissioner of Labor Statistics and now director of business cycle research at the National Bureau of Economic Research, have favored use of this new employment-to-population concept.

In an article in the current issue of the Morgan Guaranty Survey, Mr. Moore argues that, by the employment-to-population concept, the United States now has "fuller employment" than in earlier years—1947–48, 1951–53, 1956 and 1966–69, when the unemployment rate was 4 percent of the civilian labor force or less.

Writing before the latest unemployment figure of 6.4 percent of the labor force was released, Mr. Moore said that the United States was already employing more people, relative to the size of the population, than in 1956 or in any other year in which the unemployment rate was at or below 4 percent. "If those were full employment years," he added, "and jobs per capita were the criterion, we have fuller employment now than we did then."

In November 1977, the number of people employed was 57.8 percent of the working-age population, while in those earlier "full employment" years the number employed averaged 55.7 percent of the working-age population.

The latest report of the Bureau of Labor Statistics on employment and unemployment said that in December the ratio of employment to the working-age population "reached a record 58 percent, up from 56.3 precent in December a year ago."

Sar A. Levitan, chairman of a Presidential commission on the employment and unemployment statistics, criticizes Mr. Shishkin and the bureau for "singing hosannas" to the employment-to-population concept.

IS THIS FULL EMPLOYMENT?

[The New York Times, Jan. 19, 1978]

	December 1977 (seasonally adjusted)	Average of 10 full employment years [1]
Percent Employed and Unemployed relative to total population, 16 years and older:		
Employed	58	55.7
Unemployed (seeking work)	4	2.1
Armed forces	1.3	2.5
Not employed and not seeking work	36.7	39.7
Employment and Unemployment relative to civilian labor force:		
Employed	93.6	96.4
Unemployed (seeking work)	6.4	3.6

[1] The years are 1947–48, 1951–53, 1956 and 1966–69, in each of which unemployment as a percentage of labor force was 4 pct. or less.

Mr. Levitan contends that the rise in the proportion of working people to population is not necessarily a sign of improved national well-being. It results, he says, in large measure from inflation, which has been eroding family incomes, and from family breakdowns, which compel many additional women and young people to seek employment.

Mr. Levitan, a professor at George Washington University, suggests that an important factor behind the sluggish rise of national productivity has been the entry into the job market of a rising proportion of unskilled and inexperienced workers.

Arthur M. Okun, former chairman of the Council of Economic Advisers under President Lyndon B. Johnson, contends that, as a labor market indicator, the new concept employed by the Bureau of Labor Statistics "borders on the absurd." He says the ratio of employment to population assumes that there is "no difference between people who want to be and don't want to be in the labor force, between people who want to work, including many discouraged workers, and people who don't want to work."

Analyzing the performance of the national economy, including the impact on wages and prices, Mr. Okun says, means relating the demand for labor to supplies of labor—and only those who want to work constitute the labor supply.

He charges the conservatives who think there is very little unemployment with contending that, "if women and teen-agers, especially blacks, would just pull out of the labor force, there would be no unemployment."

Mr. Shishkin says, however, that the new employment-to-population measure is "important" additional information but it not meant to replace all other measures of labor market conditions. Nevertheless, Mr. Levitan criticizes Mr. Shishkin for allegedly "sweeping unemployment under the rug."

When unemployment is taken as a ratio of the total population of 16 or older, the current unemployment rate still shows up as considerably higher than the same ratio in earlier full-employment years. Mr. Moore, in his Morgan Guaranty Survey article notes that unemployment as a percentage of the working-age population was 4.3 percent in November 1977, more than double the 2.1 percent rate of the earlier full-employment years.

The employment-to-population ratio dipped to 4 percent in December 1977, with the new seasonal adjustment factors, but still remained close to twice the 2.1 percent average level in 1947–48, 1951–53, 1956 and 1966–69.

That was an even wider disparity than the difference between the December ratio of unemployment to the labor force of 6.4 percent as compared with the average jobless rate of 3.6 percent in the earlier full-employment years.

If this is full employment, it remains difficult to prove it by the unemployment figures, whichever ratio is used.

Mr. SHISKIN. I asked Sar whether the following quotation was right, and he replied that it essentially was. The statement says, "Mr. Levitan criticizes Mr. Shiskin for allegedly sweeping unemployment under the rug."

First of all, let me go back to my most recent release, the one before the article was written. In that article, we made a count of the number of lines in which we talk about unemployment and the employment-population ratio.

In our release in January, we had 25 lines on unemployment and 2 lines on the employment-population ratio.

In my JEC statement, we had 7 lines on the employment-population ratio and 38 on unemployment.

Now, in 1 month I had a lot of lines on the employment-population ratio, more than on unemployment. But that is because I was trying to explain the measure. It was a technical statement, not an interpretative one.

In the last 3 months, the references to the employment-population ratio have been a very small part of the releases, which have been dominated by discussions of unemployment.

Also, if you look at the position of the various measures in the statement, we always start with a discussion of unemployment, and the employment-population ratio always comes later. In our January release, we mentioned the employment-population ratio as part of the discussion of employment.

It is mentioned only on one line.

Now, if that constitutes sweeping unemployment under the rug, I wonder about the ability of Mr. Levitan to observe economic facts.

Let me now comment a little bit on the employment-population ratio itself.

Representative BOLLING. Mr. Shiskin, I don't want to interrupt you, but at this point I want to find out if Mr. Levitan wants to say that it is taken out of context.

Mr. SHISKIN. Let him say it. [Laughter.]

Mr. LEVITAN. As you know, Mr. Chairman, a professor never makes a short statement. Obviously, I made a much longer one.

Mr. SHISKIN. Now, let me comment on the employment-population ratio figure itself in a substantive way.

First of all, we have been under a lot of criticism, and although I didn't research it—among other places at this committee—when we used to provide just the employment levels. But how do people judge whether a given rise in employment is good or bad? You need to have a base, just as we have a base for unemployment. We cite the unemployment figure, but mostly we cite the rate, because the rate puts the unemployment figure in perspective.

Now, one alternative that has been kicked around for years is to express the employment figures as the complement of the unemployment figure, but that never was accepted.

The other alternative to the labor force base is the working age population. So we decided—I decided—to provide that kind of a base, and I selected the population for the purpose as the better of the alternative bases, and I think that is helpful.

Second, the Bureau of Economic Research has conducted for many generations research on the reliability of different economic indicators. In 1967, I was the joint author of a book with Geoffrey Moore in which we rated the economic indicators.

We rated them quantitatively, but at that time, we did not have an employment-population ratio, so we did not rate it. Subsequently, Victor Zamowitz, of the National Bureau of Economic Research, rated these indicators, and this is how it came out: The unemployment rate got a rating of 78 and the employment-population ratio got a rating of 76. They are pretty good indicators.

Third, I can see coming a big debate on another question. Which is the better measure of future inflation, the unemployment rate at some level, or the employment-population ratio?

I am not participating in that debate. What I am trying to do is to provide data so that we will have a constructive and productive debate. I am trying to provide data for both groups that will debate. There are some people who say that the employment-population ratio is better for that purpose, and others think the unemployment rate is better. There is a division among the most responsible economists in this country on that issue, and it seems to me that my job as Commissioner of Labor Statistics is to provide data to the parties to the argument. That is what I am doing.

With reference to good guys and bad guys, I would like to close my comments by reading a statement concerning the work of a man you know very well. You can decide yourselves what kind of fellow he is. That is Thomas Dernburg of your staff. [Laughter.]

In an article entitled "Hidden Unemployment," published in the American Economic Review in 1966, Thomas Dernburg and Kenneth Strand attempted to measure cyclical variations in labor force participation.

Their purpose was to measure the level of hidden unemployment, or what we now call discouraged workers. It was their view—and let me stress this—it was their view that, for their purpose, a better measure of overall labor market tightness was obtained by using the ratio of total employment to civilian population to some alternative measure such as the unemployment rate.

In a subsequent paper, Dernburg measured the period of high demand in 1967–69, and found no correlation whatsoever between the unemployment rate and the growth of employment. During that high pressure period, entrants were snapped up by eager employers, so that movements in the unemployment rate were essentially random, during that period. I have a longer example from that paper and I would like to put the whole statement in the record.

Representative BOLLING. Without objection.

[The statement referred to follows:]

In an article entitled "Hidden Unemployment," published in the American Economic Review of March 1966 Thomas Dernburg and Kenneth Strand attempted to measure cyclical variations in labor force participation. Their purpose was to measure the level of hidden unemployment, or what we now call "discouraged workers." It was their view that, for their purpose, a better measure of overall labor market tightness was obtained by using the ratio of total civilian employment to civilian population, than some alternative measure such as the unemployment rate.

In a subsequent paper[1] Dernburg examined the period of high demand in 1967–69 and found no correlation whatsoever between the unemployment rate and the growth of employment. During that high pressure period labor market entrants were snapped up by eager employers so that movements in the unemployment rate were essentially random during that period. Let me quote from that paper:

> . . . fluctuations in labor force participation sometimes cause the unemployment rate to move in a direction quite the opposite from what would have been expected given the growth of employment and the pace of general business activity. The year 1967 furnishes an interesting example. Although the U.S. economy performed sluggishly in the first half of the year, with employment growth limited to an annual rate of 0.74 percent, and with real GNP growing only $3.5 billion between the fourth quarter of 1966 and the second quarter of 1967, the first half average unemployment rate of 3.80 percent was less than one-tenth of a percentage point higher than it had been during the second half of 1966. The revival of the second half of the year was then marked by a jump in employment growth to an annual rate of 3.22 percent and a real GNP gain between the second and fourth quarters of $12 billion. Yet despite this sharp revival the unemployment rate actually increased to an average of 3.89 percent.

Mr. SHISKIN. I am not taking Tom's side, either. I am saying he is a competent economist engaging in this debate, and I say it is our position to provide both sides to the debate with good, detailed data on this subject, and I am not about to suppress any of the figures.

Finally, I would like to say that before we published the employment-population ratio, we submitted such data as part of my statement to this committee for 10 months, and then we took a sample survey of the users of that report. They overwhelmingly supported the inclusion of the employment-population rates in the monthly release.

We have a circulation of 500 people who get copies of my prepared statement to the JEC. Support for including the measure included the then members of the Joint Economic Committee staff.

Representative BOLLING. I think this might be the right time for me to say something.

Years ago I was chairman of the JEC's Subcommittee on Economic Statistics, and after I learned, I guess, the most complicated

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[1] Thomas F. Dernburg, "The Behavior of Unemployment: 1967-1969," in Sheppard, Spring, et al., *The Economics of Public Service Employment.*

and difficult of the dismal particles of a dismal science enough to understand what was happening in terms of Federal support for adequate statistical series, after I had seen time and time again where the technical people had asked for money and had been stopped in the Bureau of the Budget, and after I had seen time and time again how little money was available when the Government was almost totally uncoordinated in terms of its coordinating use for purposes of all of Government, I tried to get two things done.

One was successful and the other wasn't. One was to see to it that there would be a strong coordination, a place somewhere where we would not have an enormous amount of material produced that duplicated in part an enormous amount of material produced by others.

I guess that was moderately successful, because something was set up in the Bureau of the Budget, but I didn't stay on as chairman of that subcommittee, so I don't know if it got better.

The other thing was, particularly in Congress, but also in the Executive, I helped set up a lobby, and it still exists, because statistics tend to get lost in the political process.

I think this situation we have today is absolutely fascinating, because the series that are used on at least some occasions by law to trigger moneys, expenditures, are not accurate enough to be used within the limitations proposed.

Statistical error is larger than the differences between the unemployment rates that are supposed to trigger off more money.

Now, Congress, probably more than the Executive and probably more than the Bureau of the Budget, cuts out statistical money, and they do it because it is politically convenient, and they at the same time say that we have to have the ability to trigger the expenditure of money based on the series; that we won't give them the money to have a big enough sample, in order to make it rational.

I think that the arguments are all good, and I hope that Commissioner Shiskin gets all the money he needs to supply both sides with a lot of ammunition, but the fundamental flaw here is not in the statisticians. It is in the system in the Executive which is not coordinated, and it is in the Congress that doesn't have sense enough to know that a statistical series will probably do it more good than any other single thing.

Finally, some years ago, I went to the United Kingdom, and to France, when they were suffering a more difficult kind of recession than we were at that particular time, and each Government told me specifically that if they had a better statistical series as good as our relevant one, that they would not have gotten into this particular trouble, which confirmed my own set of prejudices, as you can well see, very clearly. And they have since, by the way, developed those series. But I thought that might be a useful addition to the question before us.

Congressman Rousselot.

Representative ROUSSELOT. Mr. Shiskin, would you like to pursue Senator Proxmire's thought about the military force being included as part of the overall employment figures since they really are a part of the labor force—even though you still may consider it as a separate category. How quickly could you convert to including it in the overall statistics of employment?

Mr. SHISKIN. May I defer that question to Mr. Stein? Mr. Chairman, I would like to send to you a much more detailed statement than I made earlier today on problems associated with including the military in the labor force.

Representative BOLLING. Without objection, it will be included in the printed record.

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

THE UNIVERSITY OF CHICAGO,
DEPARTMENT OF ECONOMICS,
Chicago, Ill., August 12, 1975.

Mr. JULIUS SHISKIN,
Commissioner of Labor Statistics,
Bureau of Labor Statistics, Washington, D.C.

DEAR JULIUS: I have just written a *Newsweek* column dealing with the present employment situation. In the course of doing so I had occasion to go over the employment and unemployment figures. I was taken aback to discover that all of the published figures seem to have a bias because of the treatment of the armed forces. This first hit me when I started to calculate the percentage of all persons in the United States 16 years of age and over who had jobs. In order to do this I obviously must include the persons in the armed forces. They clearly have jobs and clearly the percentage that is relevant for this purpose is total employment including employment in the armed forces divided by total non-institutional population 16 years of age and over. I then discovered that Geoff Moore in the work he had been doing had been using a different ratio, namely civilian employment over the total non-institutional population, and that the BLS had used still a different ratio, namely civilian employment over civilian non-institutional population. Frankly I can see no justification for any of these ratios by comparison with a straightforward ratio of total employment over total non-institutional population. It seems absurd that in calculating the employment ratio clerks in the War Department should be counted but career officers should not be. I can see some vague hint of a justification for separating out the military forces during the time when there was a draft on the ground that you could not interpret those employed as voluntarily employed. I believe that excuse would have been far-fetched then; I believe it is even more far-fetched now with an all-volunteer armed force.

Similarly, it seems to me that the unemployment ratio you publish and that receives so much attention is clearly biased. You express unemployment as a percentage of the civilian labor force. As a result the base is too small. I have included in my *Newsweek* column a footnote reading as follows: "The reader should be warned that officially reported unemployment figures overstate the unemployment percentage by about 0.2 percentage points. For some curious reason, the Bureau of Labor Statistics expresses the number of persons unemployed as a percentage not of the total labor force but of the 'civilian labor force' which excludes members of the armed forces. The bias in the reported unemployment percentage is more serious for males and particularly teenage males than for the total."

I tried to check the size of the bias for teenage males but it is difficult to do so because your Table A1 in the "Employment Situation" release permits calculation of the total number of persons in the armed forces by the difference between the total non-institutional population and the civilian non-institutional population, it permits calculation of the number of males 20 years and over in the armed forces, but it does not permit calculation of the number of females separately or the number of males under 20 years of age. Assuming that all 460,000 persons in the armed forces who were not males 20 and over were teenagers would convert the unemployment rate for June, 1975 from 19.2 per cent to 18.2 per cent, or implies a bias of one percentage point in the published unemployment figures.

As you know from a draft article that I believe Michael Darby has sent you, the figures that have been repeatedly quoted for unemployment in the 1930s are defective in a major way because persons employed in emergency governmental employment were treated as if they were unemployed. The defect in the current handling of the armed forces is of the same kind though not as severe since at least they are not counted as unemployed but simply as non-existent.

Do let me urge you to face up to this defect at once and put your published statistics on a defensible basis. I do not see how the present basis can be defended. If for some reason it is desirable to separate those employed in the armed forces from those employed in civilian activities, then by the same logic it would be equally sensible to separate those who are unemployed as those who are attached to the military industry and those who are not. If the concept of a "civilian labor force" makes sense, it should exclude both those employed in the armed forces and those unemployed who are regarded as attached to the armed forces.

Best personal regards and wishes.

Sincerely yours,

MILTON FRIEDMAN.

SEPTEMBER 5, 1975.

Dr. MILTON FRIEDMAN,
Department of Economics,
The University of Chicago, Chicago, Ill.

DEAR MILTON: This is in response to your letter of August 12. On initial review, your idea of tabulating the Armed Forces as part of total employment and basing the overall and age-sex specific unemployment rates on the total labor force appears to be simple, sensible, and straightforward. Upon more intensive study, we find, however, that there are statistical-analytical problems raised by this suggestion, particularly with respect to calculating the unemployment rate. Listed below are some of the problems identified by the staff.

A. At present, persons waiting to enter the Armed Forces, who are not working at a civilian job, are classified as not in the labor force. This treatment is not parallel to that given to persons waiting to enter a civilian job. Civilians are counted as unemployed if they are without a job but expect to have a job in the next 30 days. Current entry rates into the Armed Forces are about 60,000 per month (2½ to 3 percent of the Armed Forces' average) and the rejection experience may be as great as two times that level. If the Armed Forces are to be included in the labor force (or denominator) in calculating the unemployment rate, then it would also seem to be appropriate to include those waiting to enter the Armed Forces in both the numerator and denominator of this calculation. Reliable data for this category are not presently available.

B. At present, residents on military reservations are excluded from the household survey and the Armed Forces figures are based on DOD administrative records. To provide the full range of demographic characteristics, together with our normally collected and published supplementary material, the sample would have to be enlarged, questionnaires redesigned for the particular socio-economic environment of the Armed Forces and the tabulations drastically modified. Knotty questions of compensation-income, migration, hours of work, occupational classification and others would have to be worked out before the summary data on employment could be meaningfully analyzed.

C. Including Armed Forces personnel also would raise serious problems for the sub-national labor force and unemployment rate estimates, presently in use. Would personnel at a military training center be considered part of a local county's labor force? If so, many counties that presently are receiving substantial Federal funds are going to be rudely awakened to the "strength" of the local labor market and the comparative supply-demand situation.

Some of these problems could, no doubt, be resolved by a sufficient investment of statistical resources. I wonder, however, if it is worth the investment, especially in view of the fact that any such modification of the monthly figures, as suggested in your letter, will have an approximately equal effect on the overall unemployment rate for most of the past 15 years (i.e., the rate for males would be .2 percentage point lower for 1968 and .2 percentage point lower for 1974; hence the rise of nearly 2.0 percentage points from 1968 to 1974 would remain the same). It would appear that there is little to be gained by a substantial expenditure of our arduously won and jealously husbanded statistical resources to change the measured rate by a small percentage, even if it could be fully rationalized, when the basic cyclical and secular patterns would remain essentially unchanged, and, therefore, economic and social policy decisions would be unaffected.

In any event, major modifications of concepts, definitions, procedures, calculations and style of the unemployment statistical reports would necessitate changes in the Current Population Survey and are most appropriately made in the context of the recommendations and review of the entire system by a panel of independent experts (a' la the Gordon, Stephan, and Palmer Committees). I am hopeful that my efforts to initiate such a review will be successful by the end of this year. Your suggestion will be on the BLS list of issues submitted for their consideration. In the meantime, I would appreciate any comments you would care to make on the points above.

Sincerely yours,

JULIUS SHISKIN, *Commissioner,*
Bureau of Labor Statistics,
Department of Labor.

Mr. STEIN. Congressman Rousselot, I think if it were just a question of employment aggregates, we probably could do that right away. But there is a great deal of information below the total that we collect.

Representative ROUSSELOT. I understand. But how quickly could you do it, to include the military force in the full employment figures?

Mr. STEIN. I think, sir, again, it would depend on if we pursued the notion that Mr. Shiskin was speaking about earlier, of doing something about including those people waiting to get into the military. That would include some redesigning of the basic questionnaire. We do not ask that kind of question.

Representative ROUSSELOT. Are there really that many who are waiting? Would they affect the unemployment figures that much?

Mr. STEIN. We do not have an estimate at the moment.

Representative ROUSSELOT. So one reason for not doing it promptly is there are a lot of unemployed people sitting around waiting to get into the military and they should be considered as part of this?

Mr. STEIN. I think that is one consideration.

Representative ROUSSELOT. Can you do it one month, six months, what?

Mr. STEIN. Mechanically it is something we could do in a matter of a couple of months. But I think it would be fairly significant. But it is not the kind of thing we can do unilaterally.

Representative ROUSSELOT. Are you prevented by law? I realize that this is a political problem for small communities that may be adjacent to large military bases, it may affect the funding they get for unemployment consideration. I understand that. But that is basically a political problem, it is not a statistical problem, is it?

Mr. STEIN. I think what I am alluding to is the point Mr. Levitan made earlier, that statistics are not the private preserve of the Bureau of Labor Statistics. They are used throughout the economy, the society, and the Government. We really have not made unilateral changes without a fairly broad consensus of support. I do not think it is a very difficult operational thing to do. But I think the fact that it would change the number is something we would be reluctant to do without getting the recommendation of this Commission first.

Representative BOLLING. Which would have to be implemented then by the process. The recommendations of the Commission, even if you agree with them, have to be implemented by that process. You have to get the money through whatever bureaucracy you have to go through before you get to OMB, and then you have to get it through the House and Senate Appropriations Committees.

Mr. SHISKIN. I would agree completely. The local area statistics problem is the main problem politically. We have a tremendous amount of mail and phone calls and criticism of our local area statistics. A lot of criticism is well deserved. But, except for the local area statistics problem, I do not think the military issue is a big issue. It is not going to affect the aggregate unemployment rates very much.

We certainly are not against it. We would be sympathetic to doing it. As Bob just said, on this particular issue we would like to get the point of view of the whole Commission, before moving ahead.

Representative ROUSSELOT. It will not take you long to accomplish it statistically. But the problem is the impact primarily from local communities affected by it.

Mr. SHISKIN. We would do it regardless of the political consequences. That is one of the advantages of being in the BLS. But we would want to be sure we had a strong consensus of the professional people involved before we take that step. One way of demonstrating that is to have such a recommendation from this Commission.

The Commission has not been appointed yet. So it is quite a while away.

Representative ROUSSELOT. I think the members have been appointed.

Mr. LEVITAN. They have been appointed but not confirmed. I think, Congressman Rousselot, if I may just comment on this point, the military statistics are actually a small part of the total. As the chairman just indicated, a much more effective policy for the overall problem is improvement of the State and local data. We are allocating billions of dollars on very, very flimsy data. Mr. Shiskin was the first to warn that he did not know how much unemployment there is in Dry Gulch, but you in Congress force him to come up with the figures anyway.

It becomes very, very difficult to target the funds. Yet you in Congress want us to do it. It is not a question of competence or the ability of the BLS and the Bureau of the Census to get the numbers; it is a question of costs.

As long as Congress decides to appropriate billions of dollars for the unemployed but deny funding to the bureaucrats who collect the statistics, you may have good politics, but not very good economics.

Senator PROXMIRE. Mr. Levitan, I understand that about 40 percent of youth unemployment is accounted for by young people going to school, who would like a job but do not have it. Is that about right?

Mr. LEVITAN. That's about the right figure for 16- to 21-year-olds.

Senator PROXMIRE. Could you give us a ball park figure concerning the effect it would be on the January unemployment figures if all the changes that you favor in the unemployment figures were put into effect? Would there be a washout, would it be lower, would it be higher, would it be about the same?

Mr. LEVITAN. This is a very, very difficult question to answer, Senator Proxmire. I would like to shy away from the word "favor." I am alone on the Commission. I certainly would not want to second guess my brothers or sisters by suggesting figures. I was asked the same question by a Mr. Hobart Rowan, of the Washington Post, who is in the room right now. My response at that time was that it is really not so important whether we come up with higher or lower numbers.

What is important is that we address ourselves to the correct issues. I am not sure that I wish to come up with one number. The BLS data is quite good for measuring overall economic activity; not as good for State and local activity. Hardship cases require completely different data. Therefore we may have to live with two numbers rather than one number.

I realize that it presents a problem.

Senator PROXMIRE. We were talking about being cross-eyed a minute ago.

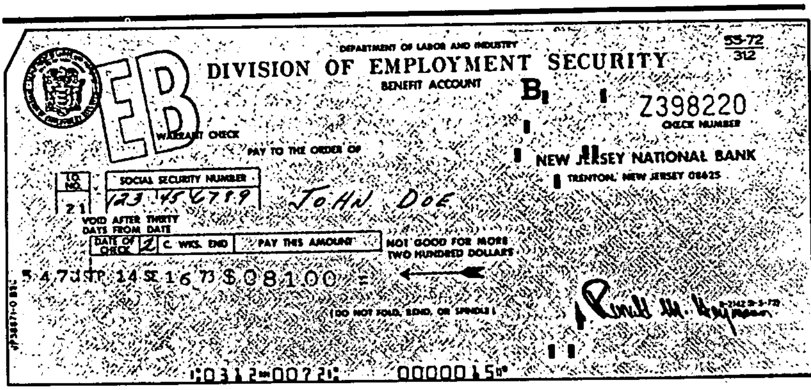
Mr. LEVITAN. It also presents a problem for Walter Cronkite or Barbara Walters or whoever your favorite broadcaster is who has to mention two numbers instead of one. But for the purpose of appropriating and allocating funds for public policy, you may need another number.

Finally, as far as the recommendations of the Commission are concerned, the staff of the Commission is preparing the work of the Commission according to the instructions of the Human Resources Committee in the Senate. The advisers of the Commission include six members of Congress, and seven members of the executive, including the Commissioner of Labor Statistics and the chairman of this committee. Rather than make up our minds in advance, we tried to prepare for them, as best as we can, an objective analysis of the pros and cons. Even before I was appointed, I asked Mr. Shiskin whether he would prepare what we call issue papers with pros and cons, not position papers.

Mr. Shiskin was very hesitant to prepare these papers because he thought that would cause interference with the Commission's work. I persuaded him to do it though and the staff is preparing pro and con arguments on the various major issues to be confronted by the Commission as we begin our deliberations. For example, we are going to have the pros and cons on the military, an issue that Mr. Rousselot was discussing. I really do not know if we shall come up with a higher or a lower unemployment figure. To be candid about it, should the Commission also adopt the hardship measure, that number might be higher than the present number depending on what level of income we recommend. On this note, if I may, I would like to insert an article in the record that I did with Mr. Taggert which says exactly that: the hardship index reflects a higher incidence of labor market failure than do present figures.

Representative BOLLING. Without objection, that article will be included in the record.

[The article referred to follows:]



Photographs by Zvi Lowenthal

The hardship index

The unemployment rate is only one measure of hardship and sometimes it isn't even a measure of that. Here is a proposal for a formula that reflects the realities of the '70's; the Employment and Earnings Inadequacy index

by Sar A. Levitan and Robert Taggart

It is critically important that the economic indicators we compile and use in decision-making accurately portray reality. Current labor market measures, developed at the end of the Great Depression, reflect the primary concern of the time—the availability of jobs for those able and willing to work.

Over the decades, changes in the labor market and in our society have eroded the validity of the unemployment measure as an economic indicator for policy determination. Changes in the structure of the domestic economy have apparently altered the relationship among unemployment, wages, and inflation.

Idleness is increasingly an acceptable and voluntary option whose impact is softened by transfer payments or by multiple family earners. Many workers claim they want jobs but are only halfheartedly looking. More would take jobs if working conditions were favorable, but they are not actively seeking work. Others may feel it prudent and possible to look longer in order to find a higher paying job. Extended unemployment compensation, welfare, food stamps, Social Security, veterans' benefits, and other aid reduce earnings losses and even generate work disincentives; recipients with no interest in work may claim to be able, willing, and actively looking for jobs solely to meet program requirements. Finally, for workers trapped in a "secondary labor market," intermittent employment is the product of low wages, bad jobs, and employment situations in which turnover is accepted and even encouraged.

As a product of these changes the relationship between

Sar A. Levitan, director of the Center for Social Policy Studies, The George Washington University, and Robert Taggart of the National Council on Employment Policy devised the EEI index. This article is taken from their presentation to the American Statistical Association's Annual Meeting in Boston this past August.

unemployment and hardship has been increasingly obscured and unemployment statistics are no longer the valid measures of economic and social health they once were. Joblessness among teenagers rarely affects the well-being of families. Many unemployed have a spouse with very adequate earnings, or the family may have other income sources. But people who do have intermittent work may have low earnings over the course of a year and even full-time work is no guarantee against poverty where there are many mouths to feed. Many full-time and intermittent workers end up with a lesser income than the families of the more affluent unemployed.

The unemployment rate is like the proverbial old shoe: we wear it because it is familiar, even though it has become disfigured and the sole wears thin. We debate minor changes in joblessness and faraway targets without really knowing what the numbers mean. We continue to ignore the realities of a drastically expanded transfer system which provides some support to at least one of every four Americans. We still think in terms of neoclassic supply and demand theory despite the demonstrated interrelationships among low wages, discrimination, welfare, and unemployment in the secondary labor market. In brief, unemployment rates and other official labor market statistics have become inadequate to explain the ever-changing labor market conditions. New concepts and new measures are needed for public policy formulation. Multibillion-dollar programs and new job creation proposals may be riding on misconceptions about labor market operations.

With earnings the predominant and societally preferred source of income, a crucially important concern is the labor market's ability to provide not just a job, but a minimally adequate income. The long-term unemployed are likely to live in deprivation because of their earnings loss, but others besides these unemployed are failed by the labor market. Part-time employees seeking full-time work, intermittent workers, persons withdrawing from the labor force because of limited job opportunities, and, of course, low wage earners may all have deficient incomes.

The Employment and Earnings Inadequacy index, devised by the authors, attempts to count all persons in the labor market who face employment *and* income problems. The prevalence of employment problems is first assessed by a "subemployment" measure defined to include the unemployed, discouraged workers not in the labor force who currently want a job but are not looking because they think no work is available, employed household heads who earned less than a poverty level wage in the last year (including those working full-time full-year as well as those working intermittently), and persons employed part-time involuntarily because of shortened workweeks and other economic reasons. Full-time students age 16 to 21 years are excluded since they presumably are occupied in socially useful activity and therefore seek only part-time jobs, and since their income needs are frequently met from nonwork sources. Persons age 65 and over are also excluded since public pensions are now nearly universal and private pensions are much more widespread, reducing needs and labor force attachments. Only family heads are counted in the two low-earnings categories because other family members may frequently have only a peripheral attachment to the work force and hence limited earnings.

Despite the difficulties they face in the labor market, some of the subemployed may have an adequate personal or family income. In order to screen out these cases, an upper income adequacy test is applied. All persons whose family income for the preceding year was above the average for families are excluded. The same holds for unrelated individuals with income above the average. Since wide variations exist between metropolitan and nonmetropolitan areas, separate averages are applied to residents inside and outside metropolitan areas.

The Employment and Earnings Inadequacy index is calculated as a ratio of the subemployed with below-average incomes to the number of persons in the labor force, defined to include discouraged workers. The index indicates the proportion of people working, seeking work, or discouraged from seeking work who are unable to secure a minimum income and are also not fortunate enough to have other working family members or sources of income which ameliorate their own earnings problems.

In March 1974 the civilian noninstitutional population numbered 148.2 million persons age 16 years and over. A total of 89.6 million were in the labor force and 585,000 were nonstudent, nonelderly, discouraged workers. The adjusted labor force was the sum of the two—90.2 million.

Subemployment was the sum of five categories:

Unemployed. The Current Population Survey counted 3.9 million unemployed workers in March 1974 after subtracting students age 16 to 21 years old and individuals age 65 years and over.

Discouraged workers. There were 585,000 persons wanting a job currently but not looking because of discouragement over the prospects.

Fully employed low earners. There were 1.8 million family heads and 293,000 unrelated individuals who worked full-time, full-year in the previous 12 months and yet did not earn enough to reach the poverty threshold.

"The 1975 recession was the severest economic dislocation since World War II. Unemployment peaked at 8.3 million. Yet, there was surprisingly little public clamor over this slump—no riots, no large-scale marches on Washington, not even much rhetoric. Why?"

Intermittently employed low earners. Another 2.6 million employed family heads and 1.1 million unrelated individuals who had worked intermittently during the preceding year did not earn a poverty level income.

Involuntary part-time workers. There were 2.0 million persons working part-time involuntarily for economic reasons who were not students, were under 65, and were not counted among the intermittently employed low earners.

Adding these components, there were a total of 12.3 million subemployed in March 1974 out of the 90.2 million in the adjusted labor force, yielding a subemployment rate of 13.6%. Among these were 2.7 million persons living in households with above average incomes in the preceding year and therefore with questionable needs. Eliminating these from the subemployed left 9.5 million with inadequate employment and earnings. The EEI index was, thus, 10.5%.

Conditions in March 1974, when the unemployment rate was 5.3%, were more representative of post-World War II experience. Though unemployment substantially exceeded 1960 levels, the unemployed accounted for only a fourth of all persons with inadequate employment and earnings in March 1974. More than a third of the nonstudent, nonelderly unemployed were members of households with above-average incomes and were not counted in the EEI index. Two-fifths of the involuntarily part-time workers were also screened out by the upper adequacy standards.

The low-paid fully employed heads accounted for a fifth of persons with inadequate employment and earnings, while the intermittently employed represented a third. The size of these low-earning groups is explained by several facts. Poverty among full-time working heads results from a combination of low wages and large families; intermittency compounds these difficulties by adding periods with no earnings. Many of the unemployed were affected by two or more spells of joblessness. Where the household heads earned less than poverty wages, it was very rare that earnings of other family members or alternative sources of income lifted the household to an above-average income. In terms of numbers, then, low earnings and intermittent employment accounted for twice as much hardship as did unemployment.

The unemployment rate alone is not a very good measure of hardship. The unemployed in March 1974 (minus students and the elderly) had an average household income in the previous year of $11,443, or only 15% less than that of the total labor force. The average income (for the preceding year) of the unemployed excluded in calculating the EEI was $19,844. This would hardly qualify in anyone's book as hardship. The discouraged and involuntary part-time workers also included many with dubious needs.

The screening process was especially important for wives and other relatives. Many of the unemployed were secondary job-seekers in families with substantial incomes. On the other hand, unrelated individuals with employment problems were more likely to face hardships because there was usually no one else to support them. Overall, the use of an income screen yielded an average annual EEI income of $5,364 compared with $8,446 for the subemployed. The proportion in poverty for the two groups was 41% and 32%, respectively. In contrast, only 17% of all the unemployed were poor.

The incidence of inadequacy varies significantly among different groups. The EEI for blacks in March 1974 was 2.6 times that for whites, or more than the 2.1 ratio of adjusted unemployment rates. The unemployment rate clearly understates the disparity in hardship. Only an eighth of unemployed whites were poor, compared with a third of blacks; two-fifths of the former were in households with above-average income, compared with a fifth of the latter. Blacks were more frequently low earners and discouraged workers. In all categories they were less

The long lines—at a New Jersey unemployment office. "In terms of numbers, low earning and intermittent employment account for twice as much hardship as unemployment."

likely to be in households with above-average incomes. A fourth of the subemployed whites were screened out by the upper income standard, compared with an eighth of blacks. Yet the average household income of blacks with inadequate employment and earnings was a tenth less than that of whites; half of the blacks compared with less than two-fifths of whites were living in poverty. Among black female family heads the EEI was a staggering 56.0%, and among unrelated females 32.5%. With such limited chances of success in the labor market, it is easy to understand why many find welfare an acceptable choice.

According to the EEI, inadequacy is one sixth higher among female than male labor force participants. The difference would be greater if wives were included in the low-earnings categories. Two-fifths of women heading families had inadequate employment and earnings, more than four times the rate among male heads. Women in the adjusted labor force were 36% more likely to be among the unemployed in the EEI, 64% more likely to be employed part-time involuntarily, and 70% more likely to be discouraged and in a household with below-average income.

The 1975 recession was the severest economic dislocation since World War II. The number of unemployed rose from a seasonally adjusted total of 2.7 million in December 1968 to 4.2 million in October 1973 after the relatively mild setbacks at the start of the decade. Unemployment then peaked at 8.3 million in May 1975. Yet, there was surprisingly little public clamor over this slump—no riots, no large-scale marches on Washington, not even much rhetoric. The Republican Administration continued to claim that inflation was the number one enemy, while Democrats, with an overwhelming majority in Congress, introduced only modest countercyclical programs while failing to override the vetoed spending measures. What was the reason for this quiescence?

The EEI offers one explanation. This index suggests that economic hardship did not increase as sharply as unemployment. In 1969 the EEI stood at 9.8% and it was 10.5% in 1974, after recovery from the short recession. In 1975 the EEI rose to 13.5%. But if inadequacy had risen proportionately with joblessness, more than a fourth of the labor force would have faced economic hardship in March 1975.

Overall, the total with inadequate employment and earnings increased by 2.7 million, a fifth less than the increase in the number of unemployed. The proportion of the adjusted labor force with inadequate employment and earnings rose only by a fourth, compared with the 72% rise in the unemployment rate. Even in the most severe business downturn since the Great Depression, the continuing structural problem of hardship far outweighed the cyclical impacts. While headlines focused on the rise in unemployment, the increase in deprivation owing to low earnings was much less and this may explain the limited social unrest generated by the economic downturn. The corollary, of course, is that when unemployment recedes it should not be assumed that the real problems have been eliminated.

In the 1960s there was a concerted effort to improve the employment status of minorities through manpower programs and equal employment opportunity action. The tight labor market provided a conducive climate, since those at the end of the labor queue tend to move up relatively, as well as absolutely, in good times. In the 1970s the government's commitment slackened, or, at least, its rhetoric favored a policy of benign neglect. The gainers in the tight labor markets become the losers in the recession. What, then, has been the end result for minorities?

The official unemployment statistics tell a not too pleasant story. Joblessness declined in 1969 to 3.1% for whites and 6.4% for nonwhites. The respective rates deteriorated to 7.8% and 13.9% in 1975. The nonwhite/white unemployment ratio fell from 2.1 to 1.8, but the unemployment rate differential increased from 3.3 to 6.1 percentage points. If nonwhites had done as well as whites in 1969, 295,000 more would have been employed in 1969 and 553,000 more in 1975.

The victims of unemployment and low earnings even in prosperous times have little to lose in economic slumps. Accordingly, the EEI shows no further deterioration in the conditions of blacks between 1968 and 1975. The index for blacks remained virtually unchanged at 28% compared with a sharp increase from 8.5% to 12.5% for whites. The black/white inadequacy ratio declined from 3.2 to 2.2, while the gap was reduced from 19.8 to 15.3 percentage points. Before the severe economic setbacks of 1974, inadequacy was falling quite rapidly among blacks, reaching a low of 22.2% in 1973, compared with the upward drift of the white rate.

The relative improvement for blacks is related to a decline in low earnings. The percentage of blacks in the adjusted labor force earning less than a poverty level wage fell from 17.3% in 1968 to 13.0% in 1974, while for whites the proportion declined only from 5.4% to 5.1%. The proportion for blacks went down even farther to 11.4% in 1975, but this was probably the result of increased joblessness among the otherwise intermittently employed.

Some blacks who would have had inadequate employment and earnings abandoned the labor force in preference to income support or other activities not counted as work by the Current Population Survey. As defined by the EEI index, the black male participation rate fell from 77.3% in 1968 to 72.6% in 1974, while the white male rate fell by .8 percentage points to 78.5%. If the decline for blacks had been the same as for whites, and the differential had all been added to the ranks of those with employment problems, the black EEI would have been 26.3% rather than 23.3% in 1974. This is an extreme assumption, however, and it does not deny that those leaving the labor force (including, for instance, many males receiving disability insurance or early retirement benefits) were better off than in low-paying jobs. On the whole, then, it would appear that despite the lack of aggressive public efforts in the 1970s, some absolute and relative progress was made before the massive recession.

Based on earlier works by Secretary of Labor Willard Wirtz in 1967 and 1968, by the staff of the Senate Subcommittee on Employment, Manpower, and Poverty in 1972, and previous EEI calculations, Congress recognized the value of a needs index and directed the Department of Labor to "develop preliminary data for an annual statistical measure of labor market related economic hardship in the nation" (Section 312 (c) of the 1973 Comprehensive Employment and Training Act). In the *1975 Manpower Report of the President* the Labor Department reported on its progress: "Considerable conceptual work must be done in the development of statistics on economic hardship. When satisfactory definitions and criteria have been developed, ways to use these in analyzing economic hardship and underemployment can be examined." Translating this bureaucratic jargon: no data had been collected and no new definitions tested. This remains the case today.

It is difficult to rationalize the failure of the Bureau of Labor Statistics to carry out the clear congressional mandate. The "conceptual work" in developing, analyzing, and presenting the EEI for 1968-1975 amounted to less than one-half a man-year.

The lack of progress simply reflects a lack of priority. The Administration was understandably reluctant to admit that conditions might be worse than already staggering unemployment rates suggested (although, paradoxically, the index would have demonstrated that conditions did not deteriorate as severely in 1975 as unemployment tallies indicated). The massive increase in joblessness diverted attention from other issues. But, more fundamentally, Administration economic policy-shapers were apparently opposed to the underlying concepts of a needs index which would focus attention on deep-seated structural labor market problems.

The EEI and other economic hardship measures are based on the notions that: (1) the inadequacy of earnings is as important as the availability of employment; (2) unemployment and earnings problems are interrelated and compounded for a significant minority of all workers; (3) the gravity of employment problems is primarily related to their impact on household income; and (4) those with the most severe problems are the ones who should be given attention. In contrast, the prevailing view of the many policy-makers in the first half of the 1970s seemed to be that any job was better than no job, that low earnings due to intermittent work were a reflection of limited work commitment, and that earnings provided in the labor market could somehow be divorced from family income needs.

These arguments, which tried to explain away hardship, sound disturbingly like the pre-Depression neoclassical theories which dismissed mass unemployment as a transitional phenomenon. Problems do not disappear simply because we refuse to recognize them. Just as a new set of statistics was introduced in the late 1930s to measure unemployment, it is necessary to overhaul and supplement current economic indicators. The unemployment data are not an adequate measure of economic hardship. The need is to attack the problems of wage adequacy and intermittent work by focusing public efforts on work force participants who face economic deprivation in good times as well as in recessions. ☐

Note: The technical flaws and conceptual difficulties involved in the proposed index were spelled out by the authors in *Employment and Earnings Inadequacy: A New Social Indicator* (The Johns Hopkins University Press, 1974), pp. 39-45, and in the *Monthly Labor Review*, Oct. 1973, pp. 24-27. Particularly troublesome is the distinction in the treatment of low earning males and spouses. The problems can be corrected when a more refined measure is developed.

Senator PROXMIRE. The great importance of this for economic policy can hardly be overestimated. Not only that, you have $16 or $17 billion allocated strictly on the basis of these statistics. So we ought to be sure they are as comprehensive and fair as they can be. I think you have made a strong case, and Mr. Shiskin has, over the years, that things can be improved.

It seems to me, if we have to spend relatively little amounts of resources to improve these, then we should do that.

I would like to ask you, Mr. Shiskin, the only bright spot, as so often happens, is when we look at the sex figures, look at the unemployed men and unemployed women. We can see a real improvement this month for women. It is sensational. It is remarkable. I take it this is partly because your sample of women is very big, numbers 20,000 or so in the work force that these figures should be pretty accurate.

Let me just contrast the figures for men and women and show how sensational they are. November 1977, men unemployed, 4.7; December, 4.6; and January, 4.7, no change to speak of. Women, November 1977, 6.9; December, 6.6; and January, 6.1, a remarkable improvement, one of the biggest I have ever seen and in only a 2-month period.

When you have this dramatic change, in your expert experience, what is the explanation of the fact that there was such a sharp, almost unprecedented improvement in the employment for women and no change for men?

Mr. SHISKIN. My answer to that is let us wait for the next month. I would guess that the 6.1 figure for women is not accurate.

Senator PROXMIRE. It is not accurate?

Mr. SHISKIN. That is my guess.

Senator PROXMIRE. Such a large proportion of the total sample?

Mr. SHISKIN. But our month-to-month changes are not that accurate.

Senator PROXMIRE. What would be the elements to cause error?

Mr. SHISKIN. There are errors we do not know too much about. If you put the question in a somewhat different way, I would be able to say more about it—the situation seems to be that the unemployment rates for men are pretty stable and are not improving. I can say the unemployment rates for women are improving without getting into how much.

Senator PROXMIRE. You simply would say we have to wait for another month?

Mr. SHISKIN. No: not on a drop like you mentioned. Manufacturing has been very stable. Heavy industry has been very stable. What we have seen is a very rapid growth in the financial and service industries. It just so happens that those are the industries which use the kinds of skills women have. There is a good match here.

In addition, women hold a lot more part-time jobs. I think you have a match between the kind of growth in the economy and the availability of women for these jobs. That is why you have a steady improvement in the rate for women and less so for men.

Senator PROXMIRE. The only other bright spot is the increase in the jobs of 270,000. But you say that is largely a statistical change and it may not be as encouraging as it looks.

Mr. SHISKIN. Right. We have comparable data for the larger samples, and it shows an increase in nonagricultural employment of 153,000. We have the figure of 250,000 from the payroll service. I would not quite put it the way you did, though.

I think the situation is improving. We are having a very good expansion. Suppose you make, as I did last month, a conservative assumption, a cautious assumption, that the unemployment rate will continue to improve but only half as much as in 1977.

If you have to do it on a month-to-month basis, you would say that the unemployment rate should move down somewhere like a tenth of a point. Well, that is what is happening. I think it is a bright situation. I think the economy is experiencing a very good expansion. It is not one of the best ones we have ever had, but it is certainly not one of the worst ones.

The unemployment figures show a better overall cyclical picture than the real GNP figures do. For example, the employment figures show that we are doing better in this expansion than in the median expansion. The GNP figures show we are not doing quite as well. But overall we are having a good economic expansion, and I would interpret what we have for January as continuing expansion.

I think that is a very bright picture. I do not think it is a bad picture at all.

Senator PROXMIRE. Mr. Levitan, let me ask you a question and either Mr. Shiskin or Mr. Layng to comment. We have before us in the Senate a bill and we had our first big hearings on it yesterday, the Humphrey-Hawkins bill. As you know, in the past it has been very controversial.

The expectation now is that it will have a great deal of support. It has been changed and modified. One element is that while there is rhetoric on holding down prices, there is no specific goal. There is a mandatory numerical goal for unemployment, 4 percent overall by 1983, and the President is called on every year to come forward with his goals, not only for unemployment but for income, for productivity, but not for prices.

Prices you have rhetoric. Unemployment you have good, hard, cold, clear numbers. Why would it not be a better balanced bill if we tried to do both, if we have numerical goals for inflation? We are assured by the proponents of the bill that you can get unemployment down and inflation down at the same time. The objectives are not inconsistent. But it seems to me you have an unbalanced bill if you do not have a numerical goal and do not treat them alike.

Mr. LEVITAN. I would think your suggestion comes at a very bad time. Inflation is still high and presumably it might even rise during 1978.

But I do not believe that we can reduce inflation by reducing unemployment, not until we reach 4.5 percent unemployment. At that point, we would get the best of both worlds. We ought to strive for it.

Senator PROXMIRE. We have deep concern for inflation as well as unemployment.

Mr. LEVITAN. I think it would be an excellent idea to add the inflation goal if you can aim for 2 or 3 percent.

Senator PROXMIRE. Three percent by 1983 as the objective?

Mr. LEVITAN. Yes.

Senator PROXMIRE. And the President could set whatever goals he wishes each year, recommend that to Congress.

Mr. LEVITAN. The President and Congress should look at both parts of the equation, inflation as well as unemployment. Sound economic policy would require both. Since I was just classified as a good guy, I would say that any good guy would not be opposed to less inflation and less unemployment. I would join you in that.

Senator PROXMIRE. Yesterday I ran into a buzz saw and every other member on the committee who was present was bitterly opposed. The UAW testified against it. I was told after the hearing that labor would oppose the bill if we put that in, any goal for inflation. So it is a red hot controversial issue. But I am glad to get your advice.

Mr. LEVITAN. As I read the bill, it is a goal. I do not see where anybody would object to it as a national goal.

Obviously, you would want a national goal to embody both less unemployment and less inflation. However, I could see how people supporting the original Humphrey-Hawkins bill, which would have called for immediate implementation, would be concerned that too little was being done for unemployment since the inflation goal was also included. It is not a requirement though, but only a wish, and therefore we ought to wish for less inflation.

Senator PROXMIRE. Can you tell me, is there any technical reason why you can see why the inflation figure would be less reliable or would be less—more difficult to develop than the unemployment figures?

Mr. SHISKIN. The consumer price index certainly is today, and will be even more so in a few weeks, a very reliable figure. The President has nominated a new Commission on Unemployment. But the work on the CPI is based on the recommendations of a previous commission. It has been researched thoroughly, and I think it is a very first class index.

My own judgment is that it is probably the best economic index in the world. I would see no technical reason for not using it. If you mean by inflation the GNP deflator, then parts of the economy not covered by the CPI are included. For example, the investment sector of GNP. So if you use the CPI——

Senator PROXMIRE. Do you think the CPI would be better than the GNP deflator?

Mr. SHISKIN. I do not say that. But if the CPI is used as setting up the goal, then you have the best index that the present generation of statisticians and economists can produce. It is first class. I might say also, that when we assemble here next month, we will have produced the new index, right, John?

Mr. LAYNG. Yes.

Mr. SHISKIN. I am always a little nervous about that. You may want to think about the questions and discussions that we ought to get into about prices next month, because we will have a new CPI out.

I met a little more than a week ago with the New York chapter of the National Association of Business Economists. It was after the big snowstorm, and the big turnout was amazing. L. Clark of the Wall Street Journal wrote a very good column on this meeting, and he started off by quoting me as saying that all you have to look forward to when the new CPI comes out is total confusion. I think there is a lot to that statement.

The reason is that later this month we will be producing what you may term a brand new CPI. That is, a CPI for all urban consumers. We also will be producing a partially new CPI. That is, the CPI for wage earners and clerical workers with new weights, new samples, new market baskets. We will also be producing 1 month's additional data for the old CPI. The number of human beings that can absorb all this is very limited. So it will need a lot of explanation.

We would like to help you in understanding what we are doing. You may wish to concentrate on that in next month's discussion. We would be glad to come here at any time to tell you more about it.

Representative BOLLING. Thank you.

I have a few questions. First, I would like to comment on the concern of the proponents of the Humphrey-Hawkins bill. I have been working on one or another draft of that, I guess, for 10 years, and for the last 2½ I have put in 300 or 400 hours on it. I know what worries them. I suspect that you do, too.

That is, that the inclusion of a specific inflation target will reduce the emphasis on complete commitment to full employment. I think that is what they are worried about. Personally, I am not. I think we have a different goal than just full employment. I think we have to have full employment without inflation. I think we will lose a lot of votes if we have that in there.

Mr. Shiskin, in today's unemployment figures, BLS has published unemployment rates for 10 large States. Will the estimated information in today's release be published monthly?

Mr. SHISKIN. Yes.

Representative BOLLING. The unemployment statistics published in the release are efficient estimates used in the administration of the Federal fund allocation program.

What is the margin of error in the statistical data?

Mr. SHISKIN. I will supply that for the record.

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

Coefficient of variation of CPS State estimates assuming a 6-percent unemployment rate

California	5.6	Ohio	8.3
New York	6.5	Michigan	9.1
Pennsylvania	8.0	New Jersey	9.9
Texas	7.9	Florida	9.8
Illinois	8.1	Massachusetts	10.0

Representative BOLLING. The next question, do you plan to publish unemployment data for all the States?

Mr. SHISKIN. When we get the data, yes. Hopefully we will be expanding the sample and when we get sufficiently accurate data we will publish such data. We have made a recommendation which is supported by the President and others—the Secretary of Labor, OMB, etc.—to alter the allocation process to a quarterly one. We think that would be much better.

One reason is that the quarterly figures are more accurate. You get more accurate figures by averaging monthly data than by looking at monthly data alone. So we made that recommendation. If that is approved, we may be publishing data for States in a somewhat different way. But we do intend to expand those data to other States.

Representative BOLLING. Thank you.

Then I have one question. As the economy moves toward full employment, the issue of structural unemployment will become increasingly important. Most of the structural unemployment exists in larger central cities and in depression regions of the country. We have reasonably reliable employment and unemployment figures for central cities. We have inadequate information on the labor market conditions in depressed regions.

There is a tremendous need for this information. Where are we on that?

Mr. SHISKIN. We are not moving very fast on that. We have funds in the budget to expand the work—to expand our program of improving the monthly estimates for States. But there are no funds at all for improving the direct CPS estimates for cities or any other kinds of areas. So there I think you might refer back to Mr. Levitan's comments and suggestions, because we do not have any money for improving such data.

In fact, we are planning to drop the data we have using SMSA's. We already have gotten criticism for that. I guess that answers your question.

Mr. LEVITAN. It is quite clear that the state data are improving, but they are still subject to large margins of error. The local data are simply nonexistent in many cases or are guesstimates. I am sympathetic with Mr. Shiskin; the BLS has to estimate. And in doing so, it always states that we lack the data. To some extent, the demands of Congress exceed the capabilities of available technology. You will never get good data for those small areas, and I do not think it is possible to legislate and allocate funds but on a case-by-case basis to a particular area. In other words, if you have high unemployment in a small one-factory town, and the factory leaves, then Congress may choose to provide funds specifically for that town or allow Secretary Kreps discretionary power to allocate the necessary funds.

As you suggested though, in the case of the 400 or so prime sponsors of larger areas, allocations would require a larger sample, as well as improved administration and a formula based on levels of unemployment insurance recipients. Again, all of this can be accomplished.

I do not know the exact amount that will be required to collect a larger sample. But certainly, considering that the CPS costs approximately $18 million, Congress might consider doubling that amount. In my judgment there is no need for Congress to await Commission recommendations on this subject. It should be done as soon as possible, because it is likely that the millions of dollars Congress is appropriating are not being targeted according to congressional goals. If you do get it targeted to the areas you want, it is purely accidental.

I am not implying that Mr. Shiskin and his staff deserve criticism. They are trying to do their best. But they cannot do it with the funds, samples, and limited resources available to them at present.

Representative BOLLING. Thank you. Do any of you gentlemen have any comments you would like to make?

It has been a very stimulating discussion. I thank you all.

[Whereupon, at 12:10 p.m., the committee recessed, to reconvene at 10 a.m., Monday, February 6, 1978.]

THE 1978 ECONOMIC REPORT OF THE PRESIDENT

MONDAY, FEBRUARY 6, 1978

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

The committee met, pursuant to recess, at 10:08 a.m., in room 318, Cannon House Office Building, Hon. Lloyd Bentsen (vice chairman of the committee) presiding.

Present: Senators Bentsen and Javits; and Representatives Reuss, Hamilton, and Brown of Ohio.

Also present: John R. Stark, executive director; Louis C. Krauthoff II, assistant director; G. Thomas Cator, Thomas F. Dernburg, Kent H. Hughes, L. Douglas Lee, Katie MacArthur, Deborah Norelli Matz, and George R. Tyler, professional staff members; Mark Borchelt, administrative assistant; and Charles H. Bradford, Stephen J. Entin, George D. Krumbhaar, Jr., M. Catherine Miller, and Mark R. Policinski, minority professional staff members.

OPENING STATEMENT OF SENATOR BENTSEN, VICE CHAIRMAN

Senator BENTSEN. Good morning. The hearing will come to order.

We are delighted to see that neither wind nor rain nor sleet nor snow kept everyone from their appointed rounds.

We will resume our hearings with three distinguished witnesses who will discuss the economic forecasts. Some years these economic forecasts cover a rather wide range. But I have been interested in seeing somewhat of a consensus develop on what will happen to the GNP for the coming year. Most seem to settle around a 4.5- to 5-percent growth.

I hope that today's witnesses will not be inhibited by that consensus and will give us their own forecasts, whether they agree with it or don't agree with it, and in turn if they disagree, give us some idea as to the weakness they see in that consensus.

There is a second area that the administration has not addressed to the extent I think they should. That is the question of monetary policy—what kind of monetary policy will have influence on reaching that consensus and that projection, and does that mean a slight easing of interest rates or a modestly declining rate?

I would like to have your views on that, on what you think should be done in that regard.

Our first witness will be Mr. Gerard Adams from the Wharton School of Public Finance; and he will be followed by Mr. Jack Carlson, the chief economist for the Chamber of Commerce of the United States; and Mr. Harold Shapiro of the University of Michigan.

If you will, start out, Mr. Adams.

STATEMENT OF F. GERARD ADAMS, PROFESSOR OF ECONOMICS, UNIVERSITY OF PENNSYLVANIA, AND WHARTON ECONOMETRIC FORECASTING ASSOCIATES, INC.

Mr. Adams. I am delighted to be here in spite of the snowy weather. I have provided a 10-page prepared statement which I do not propose to read, so I think maybe the most efficient way is to draw on certain parts of it and to talk about it.

In many respects, as we now know, 1977 turned out to be a pretty good year, and yet, as you know, for most of the year and even now there are significant elements of uncertainty about the economic outlook. There remain serious unresolved issues which represent the negatives of the present situation, and these unresolved issues can be summarized quite briefly as, one, the continued lag of business fixed investment; two, the uncertainty with regard to economic policy; and the third one is the worsening problem with the U.S. balance of trade and the decline of the dollar.

These uncertainties have depressed financial markets and have impaired incentives for business to make new capital investments. Nevertheless, this should not obscure the basically sound fundamental position of the U.S. economy. There is ample capacity, inventories are not excessive, inflation is not accelerating rapidly, and there are few indications of the kinds of imbalances which would normally signal a business cycle downturn.

Consequently, we see the potential for what I would call a stretched economic recovery into 1978 and into 1979. With the stimulus of a tax reduction, the Wharton forecast is a fairly optimistic one. I have looked carefully to see how it compared with the forecast tabled by the Council of Economic Advisers in the economic report, and I find that certainly for the year 1978 the two forecasts are quite comparable. This means, as you know, that we are talking about real economic growth somewhere between 4.5 and 5 percent, possibly, I would suggest, with some slowing in 1979, only moderate reduction in unemployment to about 6 percent by the end of 1978, substantially stable inflation rates at around 6 percent, increases in business fixed investment of approximately 7 percent, a little higher than the number being recorded by recent plant and equipment anticipation surveys, housing starts somewhere near 2 million but beginning to decline, reflecting the reduced availabilities of mortgage finance.

I hate to say this, but we do see continued commodity trade deficits somewhere near the high levels of between $25 and $30 billion, at least during 1978. Thereafter we see some reduction in the trade deficit as the competitive position of American exports improves.

The Federal Budget deficit is likely to remain high, running from $55 to $60 billion on a national income accounts basis. Corporate profits will continue to increase by approximately 10 percent. This is a moderately optimistic picture.

In common with all economic forecasts, it should be seen with a range of uncertainty. I am inclined to say that the risks are somewhat greater on the downside than they are on the upside.

Let me go on to an important aspect of the current outlook which I find troublesome. Most of the current forecasts do envision an increase in interest rates, but they do not envision a significant tightening of money.

Now it is my judgment that we have given up some of our freedom in the management of our monetary policy. The reason we have given up some of our freedom in our management of monetary policy is that increasingly in 1978 we will need to support the international value of the dollar, and that almost inevitably will entail higher interest rates to attract foreign capital flows, higher interest rates than we might justify on the basis of the domestic situation of the U.S. economy. In other words, regardless of what the Federal Reserve might like to do with monetary growth and interest rates to achieve domestic targets, we may see further substantial increases in interest rates in order to help stabilize the dollar.

We have used the Wharton model to test out the impact of higher interest rates on the domestic economy, and these results are summarized in the table. This was a very simple experiment. I simply assumed a tightening of monetary policy such that short-term interest rates would rise by approximately 1 percent as compared to the base forecast. That means also automatically that I obtain an 0.3 percent rise in the long-term rate in the first year and a half, and a 1 percent rise in the long-term rate in the second year.

Those are the numbers on the right-hand side of the table under the heading "Effect." The first number represents the effect on the growth of the money supply, the second line represents the impact on the 4- to 6-month commercial paper rate which, you will notice, is 1.1 in the first year and 0.9 in the second. The third line represents the impact on the long-term rate, 0.3 in 1978, 0.5 in 1979.

The question is what is the impact of such tighter money and higher interest rates on real economic activity. That impact can be summarized simply by pointing out that the level of real GNP in 1979 turns out to be about 1.5 percent lower in the high interest rate solution than it does in our base forecasts. The rate of change of the GNP in 1972 dollars, which is shown on line 6 of the table, is a half a percent lower in 1979 and 1.1 percent lower in 1979. The unemployment rate is four-tenths of 1 percent higher in 1979.

Now this can readily be explained in terms of the components of GNP. The reduction from the base solution in real GNP is of the nature of $22 billion. It consists of a $3 billion reduction in residential construction, amounting to about 200,000 starts; a $5 billion reduction in business fixed investment; and the remainder is the multiplier effect on consumption. This means that the impact of higher interest rates on real economic activity is perceptible. It means moreover that the impact of higher interest rates would fall not so much on 1978, but principally on 1979, which is a point when economic expansion may be slowing down in any case.

I would draw from this point that from the view of the domestic economy higher interest rates would have clearly undesirable consequences even if they may be unavoidable from the point of view of the international position of the dollar.

I want to now ask what kind of policy does this economic outlook call for? One, it calls for a commitment to full employment and price stability, but this should not be empty rhetoric. It does not call for arbitrary rules with regard to monetary growth, budget balance, or unrealistic targets with regard to employment.

Second, it calls for macroeconomic policy actions to stimulate the economy. The magnitude of the tax cut being proposed by the administration for 1978 is probably about right, $25 billion. There may be need for another tax cut in 1979.

Now with regard to the composition of the tax cut, I would like to stress that emphasis should be on providing additional long-term incentives for investments. Special investment incentives, accelerated depreciation, higher investment tax credit, and so on, may be more effective than overall cuts in the corporate tax rate, and such special investment incentives should be directed particularly at industries which have lagged behind or have been hit heavily by safety and pollution control regulations.

There is need for coordination of fiscal and monetary policy. I want to stress that such coordination may be particularly important now since it may be necessary to offset through fiscal policy some of the monetary policy measures made necessary to support the value of the dollar.

I have done a little experimentation with that, not shown here, which says that in order to offset a 1-percent rise in interest rates, we would need an increase in the investment tax credit from 10 to 15 percent plus mortgage financing funds, equal to approximately 150,000 to 200,000 housing starts. It means, in other words, there is the option of countering the impact of tighter money with fiscal policy, but these fiscal policy actions are considerable and must be taken relatively soon.

We need new policy measures to combat inflation. No one has any idea whether the proposed TIP program, tax-based incomes policy, will work, but it should definitely be considered experimentally and tested out to see whether it has a consequence.

We need new measures to provide training and employment. It is quite clear that our unemployment problem is not simply a macroeconomic problem, an aggregate problem that can be solved simply with aggregate economic policy. It requires special programs, and I would urge promoting and subsidizing employment in the private sector.

I would urge a national apprenticeship program, private industry, public financial support.

There needs to be a clear and definitive statement of energy and pollution control policy.

There needs to be a realistic international economic policy with emphasis on free trade. Here I think we should say that stabilizing the dollar will require not only intervention in foreign exchange markets, but also more fundamental changes in trade and capital movements. We must seek to obtain these changes cooperatively with our trade partners. The decline of the dollar has made U.S. goods more competitive in the world markets and has increased the cost of imports. Since trade flows do not respond quickly, we will have to be patient until changes in trade flows occur.

It is highly probable, as I have noted above, that stabilization of the dollar will call for higher interest rates. It would be unfortunate if domestic economic expansion were checked by the monetary measures used to stabilize the dollar.

I think we can conclude on the note that the combination of price stability, full employment and budget balance for the domestic economy will be difficult to achieve and unfortunately it will be even more difficult in a world where we must aim also for stability of the dollar in international economy.

[The prepared statement of Mr. Adams follows:]

PREPARED STATEMENT OF F. GERARD ADAMS

The beginning of a new year is a time for perspective, an occasion to look back at economic performance in 1977 and to look forward to 1978 and beyond.

In many respects 1977 turned out to be a moderately good year. Real gross national product grew almost five percent, a good result in comparison with our major trading partners—only Japan among industrial countries exceeded the U.S. growth rate—though not quite sufficient to absorb our unused capacity and unemployment. Even so, employment expanded by an unprecedented three million workers, many of whom are new entrants into the labor force. Industrial production grew at 5¾ percent; auto sales hit a near record level of 11 million cars, and housing starts averaged almost 2 million. The economy ended the year on an upbeat.

Why then has there been so much uncertainty about the economic outlook? Serious unresolved issues represent the negatives of the current economic situation:

1. *The continued lag of business fixed investment.* In contrast to other business cycle recoveries, investment in new plant and equipment has not come back vigorously. A number of explanations have been proposed—uncertainty about the economic outlook and about government policy, the impact of inflation on price-cost relationships, the unfavorable ratio of debt to equity in corporate balance sheets, and the depressed state of the stock market, for example. But the precise explanation is not known. This shortfall of investment is a source of slowed growth and low gains in productivity at present and poses the threat of insufficient producing capacity and inflationary pressures in the future.

2. *The Uncertainty with regard to economic policy.* In the past year, we have not had a consistent and credible approach to economic policy. Unfortunately, this must be said of numerous dimensions of economic policy making. The energy bill remains enmeshed in Congressional disagreements. When it is passed, it will impose new tax and inflation burdens in the economy. Some of the uncertainty with regard to monetary policy has been alleviated with the appointment of Mr. Miller as Chairman of the Federal Reserve Board which may mean a monetary policy stance somewhat more in tune with the Administration's economic objectives. The uncertainties with regard to tax reform have only partially been resolved by the proposed program of tax reduction for 1978.

3. *The worsening problem with the U.S. balance of trade and the decline of the dollar.* The merchandise trade deficit has been running at an annual rate of almost $30 billion. In addition to expensive imports of oil, the relatively more favorable cyclical position of the U.S. economy as compared to other countries accounts for the unfavorable trade balance. Until mid year, the decline of the dollar was largely offset by still greater declines of the Canadian dollar and the Mexican peso but since then the dollar has fallen sharply—a 50 cent Deutschmark, a 2 dollar pound sterling, and 0.5 cent yen are no longer unthinkable. In the past year, on a trade weighted basis, the dollar has dropped approximately 5 percent, though it has fallen almost 20 percent with respect to the yen. The dollar situation reflects as much a loss of confidence in the dollar as the underlying unfavorable trends in trade. On a purchasing power parity basis the dollar is already undervalued. On a trade competitiveness basis, the position of dollar goods is now considerably improved. But in the aggregate international competitiveness it is

not really the problem since U.S. trade is substantially in surplus after we allow for the $40 billion deficit for fuels. Even after the Treasury-Federal Reserve declaration of the intent to support the dollar, the situation will remain precarious until confidence in the dollar can be restored.

Uncertainties and problems have depressed financial markets and have impaired incentives by business to make new capital investments. Nevertheless, this should not obscure the basically sound fundamental position of the United States economy. There is ample capacity. Inventories are not excessive. Inflation is not accelerating sharply. There are few indications of the imbalances which signal a business cycle downturn.

The potential exists for a stretched economic recovery in 1978 and 1979. But the expansion is not likely to continue at the same rate and to be advanced by the same forces as last year. Consumer saving rate will rise to its historical level near six percent. Purchases of new cars have already shown some softness in recent weeks, as the Index of Consumer Sentiment has shown a modest decline. Housing construction has been well maintained but is likely to peak out from now on. Only a small improvement in the trade balance is likely.

A needed stimulus comes from tax reduction. The Wharton forecast assumes implementation of the President's proposals for a $25 billion tax cut. The tax cut measures will provide stimulus to the economy, but they will be offset by increases in Social Security and fuel taxes. A critical question is whether they will be sufficient to improve business confidence and serve as an incentive to additional business fixed investment.

The following are the principal features of our current forecast of the U.S. economic outlook for 1978 and 1979:

1. Real economic growth above 4½ percent during 1978 and gradually slowing during 1979.
2. Only little reduction of unemployment to around 6 percent at the end of 1978.
3. Substantially stable inflation rates, despite higher food prices and higher energy costs, at around 6 percent.
4. Increase of real business fixed investment spending adjusted for inflation by approximately 7 percent, a little higher than is being recorded by recent plant and equipment anticipations surveys.
5. Housing starts near 2 million but the beginning of a decline in residential construction reflecting reduced availabilities of mortgage finance (Flows of savings into mortgage financing institutions have already declined significantly).
6. Continued commodity trade deficits near high levels of $30 billion at least during 1978. Thereafter, we may see some reduction in the trade deficit as the competitive position of American exports improves.
7. Expansion of money supply (M1) at approximately 7 percent per year, with an increase in short term interest rates of 50 basic points by mid year. Long term interest rates are likely to remain fairly stable.
8. The federal government deficit is likely to remain high, $55 to $60 billion (NIPA basis).
9. Corporate profits will increase by approximately 10 percent in 1978 as compared to 1977.

This is a moderately optimistic picture. In common with all economic forecasts it should be seen with a range of uncertainty. Unforeseen contingencies could sharply modify this prediction.

On the "up" side, we can envision a somewhat greater recovery of business fixed investment—a development which would be highly desirable. Along with greater expansion of plant and equipment would come somewhat greater growth of consumer income and employment, stimulating consumer spending and inventory accumulation. Fortunately, there is ample spare capacity. Greater investment spending could be accommodated with only little increase in inflationary pressures. Moreover, offsetting monetary policy, and perhaps a somewhat smaller tax cut than now planned, would keep other parts of final demand in check. On the whole, faster expansion is desirable and feasible.

On the "down" side, the risks are greater. It is difficult to predict whether the decline in consumer auto purchases will persist in 1978 and how much of a decline it will be. Investment may show even less real growth than we forecast, particularly if energy policy and tax policies are not clarified. Housing may fall off more rapidly than we anticipate, especially if the Federal Reserve sticks rigidly to its monetary targets. The market for U.S. exports may decline if the world economic situation deteriorates further. Finally we may get a speeding up of inflation, as a consequence of higher agricultural prices, as a result of the devaluation of the dollar, or because of a high wage settlement in coal.

An important aspect of the current outlook is the fact that supporting the U.S. dollar may limit our freedom of action with regard to monetary policy. Over the course of the next few months, higher interest rates may be required to attract foreign capital flows. This means that regardless of what the Federal Reserve might like to do with monetary growth and interest rates to achieve domestic economic targets, we may see further substantial increases in interest rates.

We have used the Wharton model to test out the impact of higher interest rates on domestic economic activity. The results, summarized in the following table, involve the assumption of open market operations designed to reduce non-borrowed reserves of the banking system by $2 billion in early 1978 with a consequent increase of short term interest rates by approximately one percent. The impacts take effect fairly slowly but quite perceptibly. The reduction in GNP is of the order of one and one-half percent in 1979. The real growth rate is less by a half percent in 1978 and one percent in 1979. The impact on real demand falls on housing with a reduction in housing of almost 200 thousand after a lag of four quarters. The impact on business fixed investment develops somewhat more slowly but grows over time. The unemployment rate is approximately .5 percent higher. The consequences on higher interest rates on real economic activity become particularly apparent in 1979, a point when economic expansion may be slowing in any case. From the point of view of the domestic economy, higher interest rates would clearly have undesirable consequences even if they may be unavoidable from the point of view of the international position of the dollar.

EFFECT OF HIGHER INTEREST RATES ON ECONOMIC ACTIVITY

	Base forecast		Tight money forecast		Effect	
	1978	1979	1978	1979	1978	1979
Percent change in money supply (M_1)	6.9	8.6	3.3	7.3	−3.6	−1.3
4–6 mo commercial paper rate	7.2	8.0	8.3	8.9	+1.1	+.9
Moody's corporate bond rate	8.7	8.9	9.0	9.5	+.3	+.5
GNP (billions of dollars)	2,101	2,325	2,093	2,298	−8	−27
GNP (billions of 1972 dollars)	1,400	1,456	1,394	1,433	−6	−22
Percent change GNP (1972 dollars)	4.7	3.9	4.2	2.8	−.5	−1.1
Unemployment rate	6.4	6.0	6.5	6.5	+.1	+.4
Business fixed investment (billions of 1972 dollars)	138	150	137	145	−1	−5
Residential construction (billions of 1972 dollars)	59	51	58	48	−1	−3
Net exports of goods and services (NIPA basis) (billions of dollars)	−8	−6	−7	−4	+1	+2

There are thus a number of circumstances which reduce economic growth considerably below 4½ percent. Weakness should be a signal for stimulative policy—a larger tax cut and particularly additional investment incentive programs.

What kind of policy does the economic outlook call for? First, and foremost, it calls for clear decisive economic policy. Uncertainty about economic conditions, even fear, follows to an important extent from uncertainty about economic policy. The Congress must reach a detente with the Administration on the outlines of realistic economic policy. It is hoped that the new tax cut proposals represent a step in that direction. Congress must pass an energy bill. The broad outlines of economic policy planning involve the following points:

1. *A commitment to full employment and price stability.* These must not be empty rhetoric. It does not call for living by arbitrary rules with regard to money growth, budget balance, or unrealistic unemployment targets.

2. *Macro policy actions to stimulate the economy.* The magnitude of the proposed tax cut for 1978 is probably about right, though it could well come on July 1 rather than later in the year. Emphasis should be on providing additional long term incentives for investment. Special investment incentives—accelerated depreciation, higher investment tax credits, etc., may be more effective than overall cuts in the corporate tax rate. Such programs could be directed particularly at industries which have lagged behind or have been hit heavily by safety and pollution control regulations.

3. *Coordination of fiscal and monetary policy.* Such coordination is particularly important since it may be necessary to offset through fiscal policy monetary measures made necessary to support the value of the dollar.

4. *New policy measures to combat inflation.* New emphasis is needed to provide incentives to slow down inflationary pressures. The TIP, tax based incomes policy, plan should be considered experimentally. Additional programs are needed to stimulate competition in agriculture energy, and foreign trade. The inflationary cost of many government regulations must be recognized and minimized.

5. *New measures to provide training and employment.* Programs for employment and training particularly for urban youth must be extended and enlarged. Emphasis should be on promoting and subsidizing employment in the private sector. A national apprenticeship program in private industry with public financial support would be a step in this direction.

6. *A clear and definitive statement of energy and pollution control policy.* Resolution of the impasse on energy policy is important not only in its own right but because failure to pass energy policy has been a contributing element to the instability of the U.S. dollar. Energy and pollution policy questions must be settled once and for all and hopefully in ways which will minimize hardship and uncertainty on specific industries and the tax and inflation impact on the economy as a whole. The depressing impact of such policies must be offset with appropriate economic stimulus.

7. *A realistic international economic policy with emphasis on free trade.* Stabilizing the dollar will require not only intervention in foreign exchange markets but also more fundamental changes in trade and capital movements. We must seek to obtain these changes cooperatively with our trade partners. The decline of the dollar has made U.S. goods more competitive in world markets and has increased the cost of imports. Since trade flows do not respond quickly, we will have to be patient until changes in trade flows occur. Additional economic stimulus by our trade partners would also help. The adverse trade balance should not serve as a justification for protectionism. It is highly probable, as we have noted, that stabilization of the dollar will call for higher interest rates. It would be unfortunate if domestic economic expansion were checked by the monetary measures used to stabilize the dollar.

The combination of price stability, full employment, and budget balance for the domestic economy and stability of the dollar in the international economy will continue to pose difficult challenges for economic policy.

Senator BENTSEN. Thank you, Mr. Adams.

I think we will go ahead with the other witnesses before we go to questions. I thought that was a good statement and I want to talk to you more about that.

Mr. Carlson.

STATEMENT OF JACK CARLSON, VICE PRESIDENT AND CHIEF ECONOMIST, CHAMBER OF COMMERCE OF THE UNITED STATES

Mr. CARLSON. Thank you very much, Mr. Chairman. We are pleased to comment on the economic outlook and policies recommended by the President.

The President appropriately proposes slowing down the growth of Federal spending to make room for tax cuts to offset huge tax increases. However, his proposed growth in the budget is excessive, his budget deficit remains too high, the size of the tax cut is too small to offset tax increases, and too little to stimulate much-needed, job-creating investment.

The President undermines the economic health of the Nation by his proposal to greatly increase resources to be spent for new Government regulations and enforcement. The economic impact of Federal policies was ignored at the time of enactment during 1977. Consequently, the administration and the Congress passed legislation that is the cause of new inflationary pressures, losses of job opportunity, loss of family income, and lower investment per worker in 1978, 1979, and beyond.

ECONOMIC OUTLOOK

The Carter administration is more optimistic about the economic outlook than the economic indicators merit. The same was true last year when the administration underestimated inflation and overestimated economic growth, as shown in table 1 of my prepared statement.

The administration's forecast for 1978 and 1979 appear from our view to overestimate growth of physical output, investment and the reduction in the unemployment rate and somewhat underestimate the rate of inflation.

Also, the administration expects too much stimulus from the proposed tax cut. The administration estimates a 1 percentage point gain in real output in 1979 and the Chamber and many other forecasters expect a 0.7 percentage point or somewhat lower improvement. The administration expects a 0.5 percentage point reduction in unemployment, and we expect only a 0.2 percentage point, as shown in table 2 of my prepared statement.

However, both the administration's and our forecast reveal a need to stimulate the economy during the second half of 1978. By then housing expenditures, State and local government outlays, consumer durables, and business investment would be unable to keep the economy healthy and growing fast enough to reduce unemployment, or keep it from increasing.

With the tax cut consumer expenditures can be expected to grow at about 4 percent and housing starts to drop no lower than 1.8 million units. Employment should continue to expand and create 2 million new jobs in 1978 and nearly as many in 1979, a better record than in the four previous recoveries, as indicated in graph 1 of my prepared statement.

This is a much better record and forecast than past and forecast job creation in other major industrial countries, as shown in graph 2 of my prepared statement.

The job-creating capacity of the U.S. economy has provided and is forecast to provide more jobs as a proportion of the population than at any other time in U.S. history, including the so-called full-employment years since World War II, as indicated in table 3 of my prepared statement.

Job creation would have been much greater than forecast if the administration and the Congress had not enacted legislation during 1977 that destroyed jobs, as shown in table 4 of my prepared statement.

Even with the tax cut, the forecast for investment continues to be disappointing, at about 5 percent real growth during 1978 and 7 percent during 1979, well below the 10 percent plus that is needed to improve productivity, provide the tools for the larger work force, and boost the growth of real wages and incomes.

Growth in real business fixed investment has been much lower following the peak of previous business cycles and will not reach the same level until spring 1978, as shown in graph 3 of my prepared statement.

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The deficiency of investment growth is most pronounced in the slow growth of structures, as shown in graph 4 of my prepared statement.

The only modest growth of investment is forecast in 1979 in part because Federal policies are discouraging investment. Just a partial list of investment-destroying policies reveal that investment per worker will be $19 less because of legislation passed in 1977 alone, as shown in table 5 of my prepared statement.

U.S. trade will remain a problem with huge deficits expected in 1978 and 1979. Imports are forecast to continue to grow slowly through 1978 and match levels achieved during past business recoveries, as shown in graph 5 of my prepared statement.

However, the slow growth of real exports during this recovery and particularly during 1977 reveals the reason for the huge U.S. trade deficit in 1977 and a major reason why the huge trade deficit will persist. Our major trading partners are growing relatively less during this recovery than during past recoveries. Also, the new wave of protectionism in the U.S. is fueling protectionism abroad against U.S. exports, as shown in graph 6 of my prepared statement.

Monetary policy up to now has not been a major difficulty in this recovery and one would not expect it to be a difficulty during the next few months. However, I do share, as Mr. Adams shares, a concern with the impact on domestic interest rates with the support of the dollar abroad and with the possibility of the deficits we are looking at, there could be some crowding out later this year going to next year.

If the tax cut were doubled to $50 billion or roughly equivalent to the relative size of the tax cut of 1964, Americans would still be required to increase their payment of taxes. Moreover, the President has designed his tax changes so as to increase taxes in the future caused by either inflation or growth in real income. Clearly, the growth in taxes must be curtailed now and in the future or it could set new records every year and cause a drag on the economy.

Less than one-fourth of the net tax cut would directly encourage investment ($5.8 billion). This reflects too low a priority for encouraging job-creating and capacity-expanding and productivity-increasing plant and equipment investment, given the low growth of real total investment and per labor hour in recent years, as indicated in table 7 of my prepared statement.

The $1.3 billion net tax cut would extend the "10-percent investment tax credit to structures" and should stimulate the weakest category of investment. Each dollar of investment tax credit extended to structures should cause at least $1.25 growth of investment and within 4 years generate enough additional taxable income to fully offset the tax cut now. Unfortunately no increase in investment tax credit was proposed for equipment. Nor did the administration propose changes in depreciation allowances that could reduce the gap between replacement costs and capital cost recovery. For example, the administration should have considered liberalizing depreciation from 20 percent of ADR to 40 percent of ADR. Even this improvement would close only one-third of the gap.

We strongly urge the Congress to increase the proportion of the tax cut for directly stimulating investment.

Also, we urge the Congress to defer consideration of the President's proposal to increase taxes on activities that encourage exports (DISC and deferral) until the U.S. trade deficit has been greatly reduced.

We think it is time for the Congress to consider a tax credit for employment tied to those who find difficulty finding employment even in good times. Congressman Ullman has something along those lines and I think experimentation along those lines is called for. The increase in minimum wage created a number of people that are unemployable and something must be done to counter that.

BUDGET INCREASES

The President proposes increases in Federal spending of 8 percent, $38 billion, or equivalent to $637 for the average American family. This is the second largest annual spending increase in U.S. history. The priorities are roughly observable by noting changes in proposed outlays, as indicated in table 8 of my prepared statement.

BUDGETARY INCREASES FOR FEDERAL REGULATIONS

Evidently the highest Presidential priorities and certainly the largest budgetary growth are proposed for Federal regulatory authorities, those which most directly affect business operations. For example, the Environmental Protection Agency's enforcement budget is proposed to increase by 26 percent, Occupational Safety and Health Administration by 1.7 percent, Mining Enforcement and Safety Administration by 27 percent, and so on for the dozens of Federal regulatory authorities. The largest increases are proposed for those regulatory authorities creating "serious or very serious" problems for American business to operate and create jobs in the future, according to the latest Chamber-Gallup Business Confidence Survey. These same regulatory authorities, according to the same survey, caused substantial increases in costs and thus consumer prices during the last 2 years, as shown in table 9 of my prepared statement.

FEDERAL DEFICIT

The President proposes continuing with a $60 billion deficit for another year. However, State and local governments are expected to continue with large surpluses, so that the total Government deficit should reach only $28 billion, as shown in table 10 of my prepared statement.

Nonetheless, increases in the deficit above these levels could add to the competition for loanable funds by the end of the year and cause interest rates to increase and slow the growth of housing and business investment. So a growing deficit should be avoided. Given the huge increase in taxes, a preferable approach would be to hold down the growth of spending and thereby hold down the deficit rather than reducing the size of tax cuts, particularly to stimulate investment.

VOLUNTARY WAGE AND PRICE CONTROLS

The President's voluntary wage and price controls or "standard of behavior" calls for reducing "* * * the rate of wage and price increases in 1978 to below the average of the past 2 years." The administration hopes to reduce inflation by one-fourth to one-half percentage points annually.

Rather than focusing on American business and labor, the President should recognize that the Federal Government has become the source of new inflationary pressures. Just the legislation enacted during 1977 will cause 1.8 percentage points higher prices by 1979. A "standard of behavior" must be applied to the Federal Government if inflation rates are to subside, as shown in table 11 of my prepared statement.

ECONOMIC IMPACT OF ALL FEDERAL POLICIES

The economic health of the Nation is continually affected by the policies of the Federal Government. Jobs, inflation, income, and investment must be simultaneously considered when considering any policies, including regulations, minimum wage, energy, social security, Federal pay, and labor law reform. Apparently this is not done or the Congress would not have handicapped the economy. For example, during 1977 the administration and the Congress enacted legislation that will cause 1.8 percentage points higher consumer prices by 1979, the loss of 800,000 jobs, loss of $102 of real family income, increase Federal taxes an average of $154 per family and cause $19 less investment per worker. This can be worsened by policies now before the Congress, including energy policy, as shown in table 12 of my prepared statement.

In summary, we recommend the following:

Support for at least the magnitude of the President's tax cut;

Steps to slow down the growth of taxes in future years;

A larger proportion of tax cuts for job-creating and capacity-expanding investment;

A smaller growth in Federal spending, particularly resources for new regulations and enforcement;

Abandonment or no further intrusion of the Government in the private sector through the President's voluntary wage and price controls; and

Government refrains from crippling the economy by new legislation and regulations.

I would be pleased to respond to any questions.

[The prepared statement of Mr. Carlson, together with attachments, follows:]

PREPARED STATEMENT OF JACK CARLSON

I am Jack Carlson, Vice President and Chief Economist for the Chamber of Commerce of the United States, and I welcome this opportunity to comment on the economic outlook and policies recommended by the President in his Economic, Taxation and Budget Messages, and as more fully described in the *Annual Report of the Council of Economic Advisers.*

SUMMARY ASSESSMENT

The President appropriately proposes slowing down the growth of Federal spending to make room for tax cuts to offset huge tax increases. However, his proposed growth in the budget is excessive, his budget deficit remains too high, the size of the tax cut too small to offset tax increases, and too little to stimulate much needed job-creating investment.

The President undermines the economic health of the nation by his proposal to greatly increase resources to be spent for new government regulations and enforcement.

The economic impact of Federal policies have been ignored at the time of enactment during 1977. Consequently, the Administration and the Congress passed legislation that is the cause of new inflationary pressures, losses of job opportunity, loss of family income, and lower investment per workers in 1978, 1979 and beyond.

ECONOMIC OUTLOOK

The Carter Administration is more optimistic about the economic outlook than the economic indicators merit. The same was true last year when the Administration underestimated inflation and overestimated economic growth (see Table 1).

TABLE 1.—CARTER ADMINISTRATION AND CHAMBER RECORD ON FORECASTING

[In percent]

	Forecasts made February 1977 for 1977		Actual for 1977	Differences between forecast and actual	
	Carter [1]	Chamber		Carter [1]	Chamber
Real GNP increase	5.4	4.9	4.9	+0.5	[2]
Consumer price increases	5.1	6.5	6.9	−1.8	−0.4

[1] "Fiscal year 1978 Budget Revisions," February 1977.
[2] None.

The Administration's forecast for 1978 and 1979 appears from our view to overestimate growth of physical output, investment and the reduction in the unemployment rate and somewhat underestimate the rate of inflation.

Also, the Administration expects too much stimulus from the proposed tax cut. The Administration estimates a one percentage point gain in real output in 1979 and the Chamber and many other forecasters expect a 0.7 percentage point improvement. The Administration expects a 0.5 percentage point reduction in unemployment and we expect only a 0.2 percentage point (see Table 2).

TABLE 2.—CARTER ADMINISTRATION AND CHAMBER FORECASTS

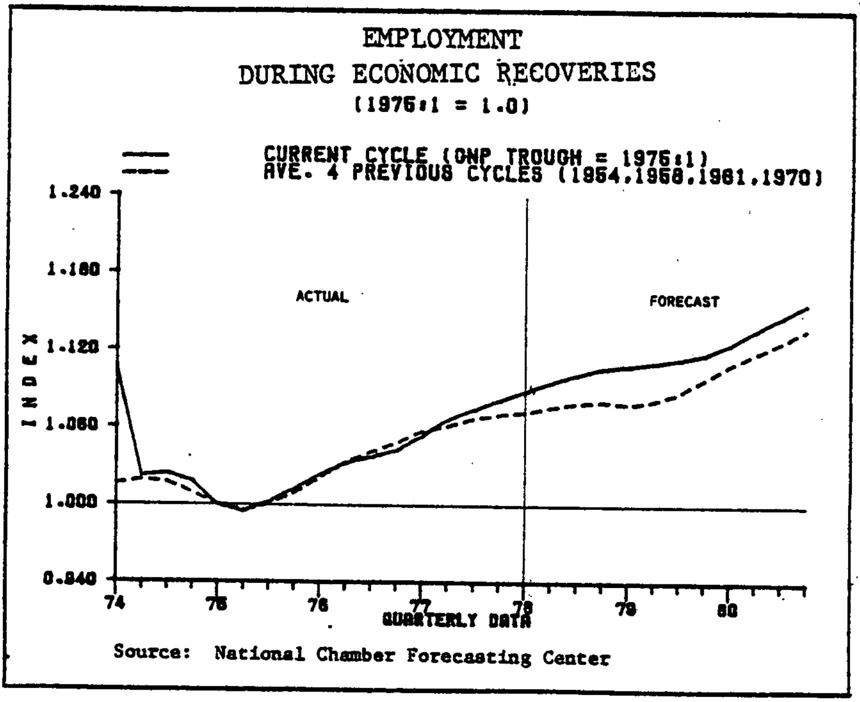
[In percent]

	1978			1979		
	Without tax cut—Chamber	With tax cut		Without tax cut—Chamber	With tax cut	
		Chamber	Carter		Chamber	Carter
Gross national product (GNP)	10.4	10.7	11.0	9.4	10.3	11.2
GNP deflator	6.2	6.4	6.1	6.3	6.5	6.2
GNP, adjusted for inflation	4.1	4.3	4.7	3.2	3.9	4.8
Business fixed investment, adjusted for inflation	5.0	5.2	7.0	5.5	7.2	9.0
Unemployment rate	6.6	6.5	6.3	6.6	6.4	5.9
Consumer Price Index	6.0	6.2	5.9	6.3	6.5	6.1

However, both the Administration's and our forecast reveal a need to stimulate the economy during the second half of 1978. By then, housing expenditures, state and local government outlays, consumer durables and business investment would be unable to keep the economy healthy and growing fast enough to reduce unemployment, or keep it from increasing.

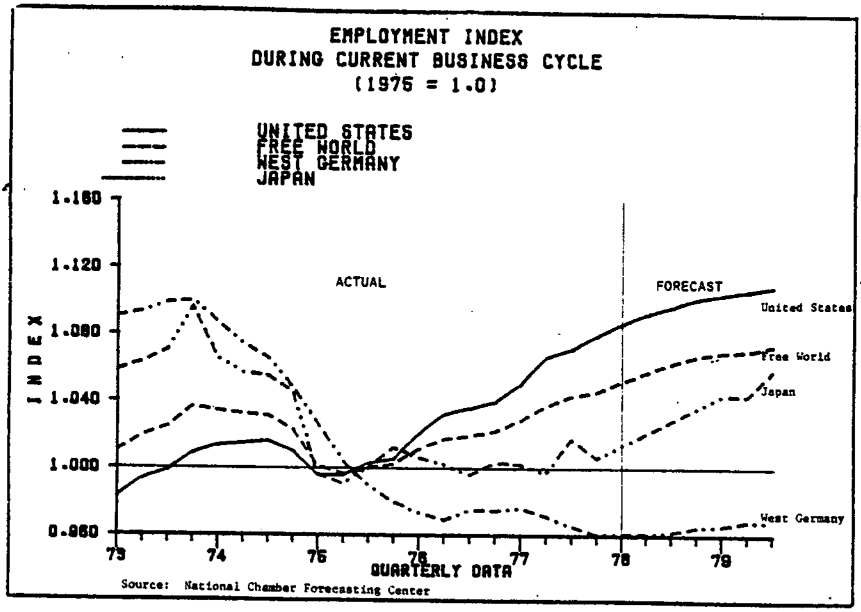
With the tax cut, consumer expenditures can be expected to grow at about 4% and housing starts to drop no lower than 1.8 million units.

Employment should continue to expand and create 2 million new jobs in 1978 and nearly as many in 1979, a better record than in the four previous recoveries (Graph 1).



GRAPH 1

This is a much better record and forecast than past and forecast job creation in other major industrial countries (Graph 2).



GRAPH 2

The job-creating capacity of the U.S. economy has provided and is forecast to provide more jobs as a proportion of the population than at any other time in U.S. history, including the so-called "full-employment" years since World War II (see Table 3).

TABLE 3.—EMPLOYED AND UNEMPLOYED AS A PROPORTION OF TOTAL POPULATION

[In percent]

	Average of 10 yr with unemployment at or below 4 percent [1]	January 1978 [2]	Forecast January 1979 [3]
Employed	55.7	58.1	58.7
Armed Forces	2.5	1.3	1.2
Unemployed (seeking work)	2.1	4.0	3.8
Not employed or seeking work (labor reserve)	39.7	36.6	6.3
Total	100.0	100.0	100.0

[1] Geoffrey H. Moore, National Bureau of Economic Research; the "full employment" years are 1947, 1948, 1951, 1952, 1953, 1966, 1967, 1968, and 1969.
[2] U.S. Department of Labor, "Unemployment Situation," December 1977.
[3] U.S. Chamber of Commerce Forecast Center.

Job creation would have been much greater than forecast if the Administration and the Congress had not enacted legislation during 1977 that destroyed jobs (see Table 4).

TABLE 4.—IMPACT ON EMPLOYMENT BECAUSE OF THE CARTER ADMINISTRATION'S PROPOSALS AND CONGRESSIONAL ENACTMENT OF LEGISLATION DURING 1977

[Change in levels; 1978–85]

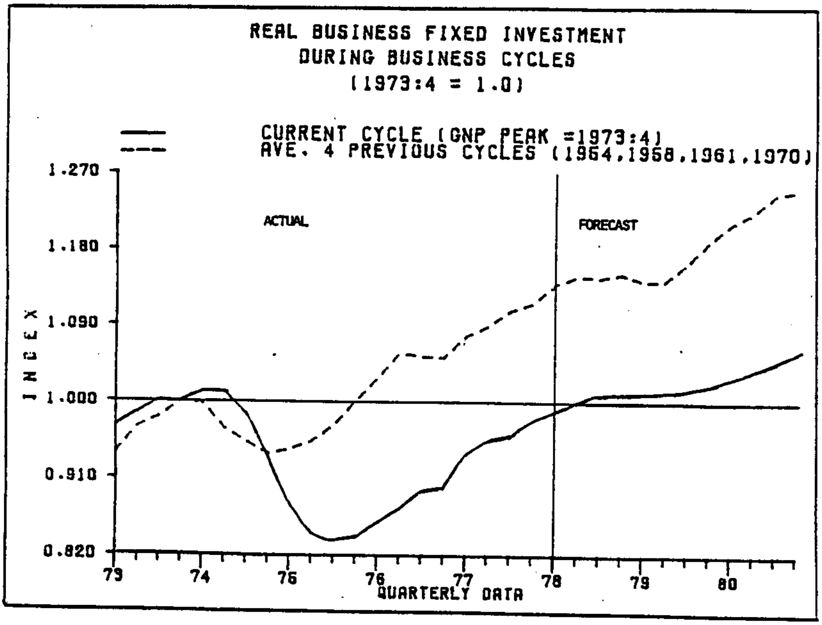
	Employment: Gains(+) or losses(−) (thousands of jobs)			
	1978	1979	1980	1985
Enacted:				
(1) Economic stimulus	502	206	103	100
(2) Minimum wage	−605	−1,230	−1,815	−1,926
(3) Social security taxes	0	−108	−305	−1,284
(4) Farm support	−108	−109	−110	−111
(5) Federal pay increases	−102	−110	−110	−209
Proposed but not enacted:				
(6) Energy taxes	−110	−640	−735	−1,890
(7) Regulation of intrastate natural gas	−50	−105	−156	−215
(8) Cargo preference	0	0	−61	−91
(9) Labor law reform	0	−109	−202	−703
(10) Gross impact of administration's proposed or accepted legislation.	−473	−2,205	−3,390	−6,239
(11) Gross impact of enacted 1977 legislation	−313	−1,350	−2,236	−3,430
(12) Net impact of enacted 1977 legislation (adjustment of (11) for overlapping effects).	−203	−844	−1,445	−2,516

Source: Dr. Jack Carlson and George Tresnak, U.S. Chamber of Commerce, the Forecast and Survey Center; Data Resources, Inc. and Chase econometrics modeling and data; the National Planning Association data.

Even with the tax cut the forecast for investment continues to be disappointing at about 5 percent real growth during 1978 and 7 percent during 1979, well below the 10% plus that is needed to improve productivity, provide the tools for the larger work force, and boost the growth of real wages and incomes.

Growth in real business fixed investment has been much lower following the *peak* of previous business cycles and will not reach the same level until Spring 1978 (see Graph 3).

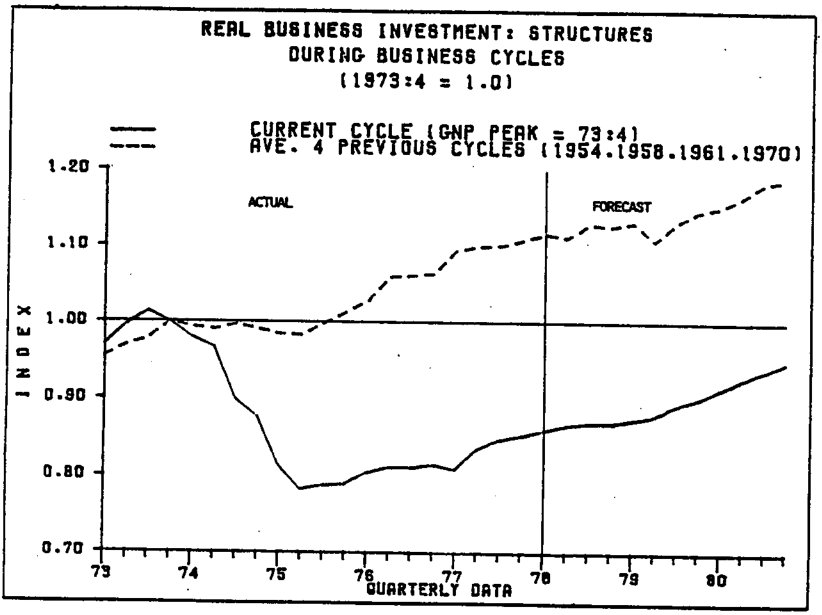
GRAPH 3



Source: National Chamber Forecasting Center.

The deficiency of investment growth is most pronounced in the slow growth of structures (see Graph 4).

GRAPH 4



Source: National Chamber Forecasting Center.

The only modest growth of investment is forecast in 1979 in part because Federal policies are discouraging investment. Just a partial list of investment-destroying policies reveal that investment per worker will be $19 less because of legislation passed in 1977 alone (see Table 5).

TABLE 5.—CHANGES IN INVESTMENT PER WORKER BECAUSE OF THE CARTER ADMINISTRATION'S PROPOSALS AND CONGRESSIONAL ENACTMENT OF LEGISLATION DURING 1977

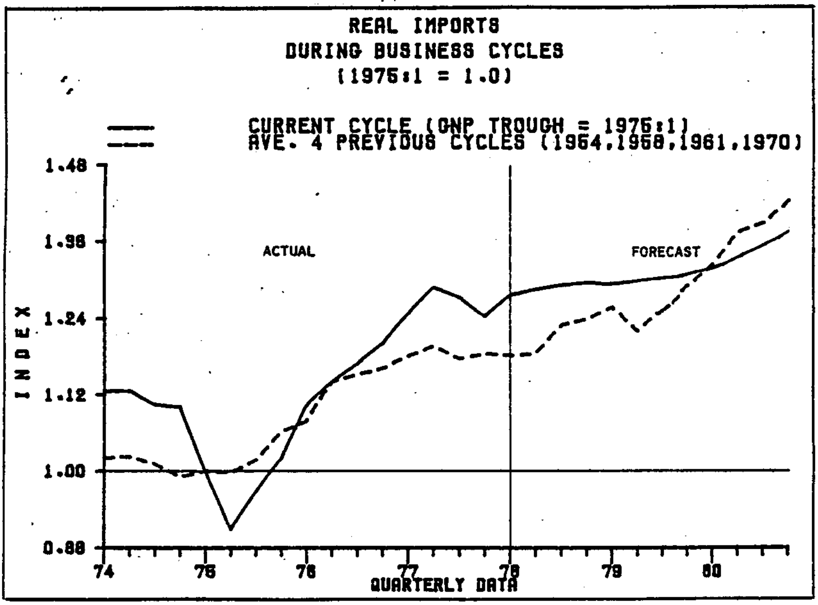
[Change in levels: 1978–85]

	Gain (+) or loss (–) investment per worker (1977 dollars)			
	1978	1979	1980	1985
Enacted:				
(1) Economic stimulus	29	17	7	5
(2) Minimum wage	–3	–47	–52	–48
(3) Social security taxes	–1	–4	–12	–55
(4) Farm support	–3	–5	–4	–5
(5) Federal pay increases	–1	–2	–2	–2
Proposed but not enacted:				
(6) Energy taxes	–5	–26	–40	–103
(7) Regulation of intrastate natural gas	–12	–16	–23	–47
(8) Cargo preference	0	0	–1	–2
(9) Labor law reform	0	–2	–11	–72
(10) Gross impact of administration's proposed or accepted legislation	3	–85	–139	–329
(11) Gross impact of enacted 1977 legislation	20	–41	–64	–105
(12) Net impact of enacted 1977 legislation	11	–19	–40	–65

Source: Dr. Jack Carlson and George Tresnak, U.S. Chamber of Commerce, the Forecast and Survey Center; Data Data Resources, Inc. and Chase econometrics modeling and data; the National Planning Association data.

U.S. trade will remain a problem with huge deficits expected in 1978 and 1979. Imports are forecast to continue to grow slowly through 1978 and match levels achieved during past business recoveries (see Graph 5).

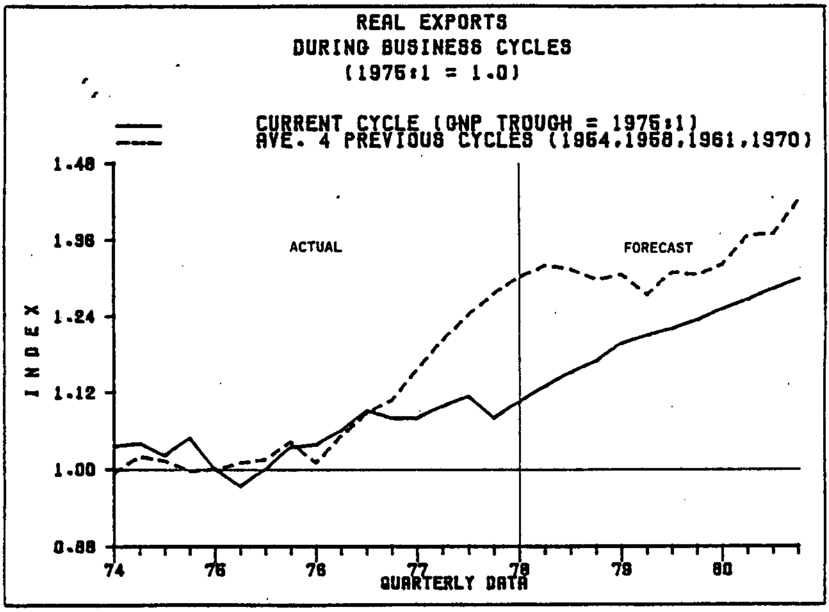
GRAPH 5



Source: National Chamber Forecasting Center.

However, the slow growth of real exports during this recovery and particularly during 1977 reveals the reason for the huge U.S. trade deficit in 1977 and a major reason why the huge trade deficit will persist. Our major trading partners are growing relatively less during this recovery than during past recoveries. Also, the new wave of protectionism in the U.S. is fueling protectionism abroad against U.S. exports (see Graph 6).

GRAPH 6



Source: National Chamber Forecasting Center.

TAX CUT

The President proposes tax cuts to reduce the burden of tax increases and stimulate the growth of the economy. Even with a net tax cut of $25 billion, Federal taxes are proposed to increase by 10%, $39.2 billion, or $653 for the average family, and the third largest annual increase in Federal tax dollars in the history of the United States (see Table 6).

TABLE 6.—PRESIDENT CARTER'S PROPOSED INCREASES IN FEDERAL TAXES, FISCAL YEAR 1979

	Billions of dollars	Percent change from fiscal year 1978	Dollars for average family
Social security taxes	17.8	14	297
Personal income taxes	11.3	6	188
Excise taxes	5.3	26	88
Corporate income taxes	3.6	6	60
Customs, estate, gift and others	1.2	7	20
Tax increases	39.2	10	653
Total taxes fiscal year 1979	439.6		7,327

Source: Fiscal year 1979 budget.

If the tax cut were doubled to $50 billion or roughly equivalent to the relative size of the tax cut of 1964, Americans would still be required to increase their payment of taxes. Moreover, the President has designed his tax changes so as to increase taxes in the future, caused by either inflation or growth in real income. Clearly, the growth in taxes must be curtailed now and in the future or it could set new records every year and cause a drag on the economy.

Less than one-fourth of the net tax cut would directly encourage investment ($5.8 billion). This reflects too low a priority for encouraging job-creating and capacity-expanding and productivity-increasing plant and equipment investment, given the low growth of real total investment and per labor hour in recent years (see Table 7).

TABLE 7.—GROWTH IN INVESTMENT IN PLANT AND EQUIPMENT AND PRODUCTIVITY

[In percent]

	Real investment growth	Capital per labor hour	Productivity growth
1948 to 1966	3.4	3.1	3.3
1966 to 1973	3.0	2.8	2.1
1973 to 1977	.3	1.8	1.5

Source: "Economic Report of the President."

The $1.3 billion of the net tax cut would extend the "10 percent investment tax credit to structures" and should stimulate the weakest category of investment. Each dollar of investment tax credit extended to structures should cause at least $1¼ growth of investment and within 4 years generate enough additional taxable income to fully offset the tax cut now. Unfortunately no increase in investment tax credit was proposed for equipment. Nor did the Administration propose changes in depreciation allowances that could reduce the gap between replacement costs and capital cost recovery. For example, the Administration should have considered liberalizing depreciation from 20% of ADR to 40% of ADR.[1] Even this improvement would close only one-third of the gap.

We strongly urge the Congress to increase the proportion of the tax cut for directly stimulating investment.

Also, we urge the Congress to defer consideration of the President's proposal to increase taxes on activities that encourage exports (DISC and Deferral) until the U.S. trade deficit has been greatly reduced.

BUDGET INCREASES

The President proposes increases in Federal spending of 8%, $38 billion, or equivalent to $637 for the average American family. This is the second largest annual spending increase in U.S. history. The priorities are roughly observable by noting changes in proposed outlays (see Table 8).

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[1] The Small Business Council of the National Chamber recommends such a proposal for stimulating investment for small business—see Attachment 1 to this testimony for more details on small business proposals for long-run stimulating of investment.

TABLE 8.—PRESIDENT CARTER'S PROPOSED INCREASES IN FEDERAL SPENDING, FISCAL YEAR 1979

	Billions of dollars	Percent change from fiscal year 1978	Dollars for average family
Income security	12.9	8	215
International and defense	11.1	10	185
Interest	6.2	12	103
Health	5.4	12	90
Education, training, employment and social services	3.5	13	58
Energy	2.1	28	35
Civilian pay raises	1.9	6	32
Transportation	1.1	7	18
Natural resources and environment	0.5	4	8
Science and space	0.3	6	5
Community development, commerce and housing	−1.3	−10	−22
Agriculture	−3.6	−30	−60
Other	−1.9		−30
Total spending	38.2	8	637
Totals:			
Taxes	439.6		7,327
Spending	500.2		8,337
Deficit	60.6		1,010

Source: "Special Analysis," Budget of the United States, fiscal year 1979.

BUDGETARY INCREASES FOR FEDERAL REGULATIONS

Evidently the highest Presidential priorities and certainly the largest budgetary growth are proposed for Federal regulatory authorities, those which most directly affect business operations. For example, the Environmental Protection Agency's enforcement budget is proposed to increase by 26%, Occupational Safety and Health Administration by 17%, Mining Enforcement and Safety Administration by 27%, and so on for the dozens of Federal regulatory authorities. The largest increases are proposed for those regulatory authorities creating "serious or very serious" problems for American business to operate and create jobs in the future, according to the latest Chamber-Gallup Business Confidence Survey. These same regulatory authorities, according to the same Survey, caused substantial increases in costs and thus consumer prices during the last two years (see Table 9).

TABLE 9.—THE IMPACT OF GOVERNMENT REGULATIONS AND REQUIREMENTS TODAY ON EMPLOYEES' TIME AND COMPANY'S MONEY COMPARED TO 2 YEARS AGO

[In percent]

	Much more	Somewhat more	About the same	Somewhat less	Much less
Small business	63	31	6	0	0
Large business	77	18	5	0	0
All business	72	23	5	0	0

FEDERAL DEFICIT

The President proposes continuing with a $60 billion deficit for another year. However, state and local governments are expected to continue with large surpluses, so that the total government deficit should reach only $28 billion (see Table 10).

TABLE 10.—GOVERNMENT FISCAL YEAR DEFICITS

[In billions of dollars]

	1977	1978	1979
Unified budget bases	−45	−62	−61
National income accounts bases:			
Federal	−48	−49	−53
State and local	28	26	25
Total government	−20	−23	−28

Nonetheless, increases in the deficit above these levels could add to the competition for loanable funds by the end of the year and cause interest rates to increase and slow the growth of housing and business investment and thus a growing deficit should be avoided. Given the huge increase in taxes, a preferable approach would be to hold down the growth of spending and thereby hold down the deficit rather than reducing the size of tax cuts, particularly to stimulate investment.

VOLUNTARY WAGE AND PRICE CONTROLS

The President's voluntary wage and price controls or "standard of behavior" calls for reducing ". . . the rate of wage and price increases in 1978 to below the average of the past two years." The Administration hopes to reduce inflation by ¼ to ½ percentage points annually.

Rather than focusing on American business and labor the President should recognize that the Federal government has become the source of new inflationary pressures. Just the legislation enacted during 1977 will cause 1.8 percentage points higher prices by 1979. A "standard of behavior" must be applied to the Federal government if inflation rates are to subside (see Table 11).

TABLE 11.—CHANGES IN INFLATION BECAUSE OF THE CARTER ADMINISTRATION'S PROPOSALS AND CONGRESSIONAL ENACTMENT OF LEGISLATION DURING 1977

[Change in levels: 1978–85]

	Increase (+) or decrease (−) in consumer prices (percent)				Gain (+) or loss (−) purchasing power for average family (1977 dollars)			
	1978	1979	1980	1985	1978	1979	1980	1985
Enacted:								
(1) Economic stimulus	0.1	0.2	0.2	0.2	−30	−59	−62	−72
(2) Munimim wage	1.1	2.0	2.7	2.7	−298	−554	−764	−830
(3) Social security taxes	.1	.1	.3	.3	−24	−40	−93	−104
(4) Farm support	.4	.5	.6	.8	−119	−148	−183	−261
(5) Federal pay increases	.1	.1	.2	.2	−38	−41	−50	−75
Proposed but not enacted:								
(6) Energy taxes	.6	1.7	3.2	5.4	−171	−471	−905	−1,660
(7) Regulation of intrastate natural gas	.0	.0	.1	.4	0	0	−34	−126
(8) Cargo preference	.0	.0	.1	.1	0	0	−27	−17
(9) Labor law reform	.0	.6	1.3	3.7	0	−152	−353	−1,138
(10) Gross impact of administration's proposed or accepted legislation	2.5	5.3	8.7	13.9	−679	−1,465	−2,472	−4,283
(11) Gross impact of enacted 1977 legislation	1.9	3.0	4.1	4.4	−509	−842	−1,153	−1,342
(12) Net impact of enacted 1977 legislation	.8	1.8	2.5	3.0	−222	−501	−713	−908

Source: Dr. Jack Carlson and George Tresnak, U.S. Chamber of Commerce, the Forecast and Survey Center; Data Resources, Inc. and Chase Econometrics modeling and data; the National Planning Association data.

ECONOMIC IMPACT OF ALL FEDERAL POLICIES

The economic health of the nation is continually affected by the policies of the Federal government. Jobs, inflation, income and investment must be simultaneously considered when considering any policies, including regulations, minimum wage energy, social security, Federal pay and labor law reform. Apparently this is not done or the Congress would not have handicapped the economy. For example, during 1977 the Administration and the Congress enacted legislation that will cause by 1977 1.8 percentage points higher consumer prices, the loss of 800,000 jobs, loss of $102 of real family income, increase Federal taxes an average of $154 per family and cause $19 less investment per worker. This can be worsened by policies now before the Congress, including energy policy (see Table 12).

TABLE 12.—INCREASES IN INFLATION AND TAXES AND LOSSES OF JOBS, INCOME AND INVESTMENT BY 1979 BECAUSE OF THE ADMINISTRATION'S PROPOSALS AND CONGRESSIONAL ENACTMENT OF LEGISLATION DURING 1977

[Changes in level in 1977 dollars]

	Higher consumer prices (percent)	Job losses (million)	Loss of family income	Increases in Federal taxes per family	Loss of investment per worker
Gross impact of administration's proposed or accepted 1977 legislation	5.3	2.2	$390	$490	$85
Gross impact of enacted 1977 legislation	3.0	1.4	177	161	41
Net impact of enacted 1977 legislation	1.8	.8	102	154	19

SUMMARY

We recommend:

Support for at least the magnitude of the President's tax cut.

Steps to slow-down the growth of taxes in future years.

A larger proportion of tax cuts for job-creating and capacity-expanding investment.

A smaller growth in Federal spending particularly resources for new regulations and enforcement.

Abandonment or no further intrusion of the Government in the private sector through the President's voluntary wage and price controls.

Government refrains from crippling the economy by new legislation and regulations.

I would be pleased to respond to any questions.

ATTACHMENT 1

FEDERAL TAX REFORMS PROPOSED BY THE SMALL BUSINESS COUNCIL, CHAMBER OF COMMERCE OF THE UNITED STATES

The Small Business Council has recommended several Federal tax reforms (Attachment 1.1). Individually, each of these would result in small tax cuts with small losses of Federal Revenues, and modest changes for the entire economy, but larger changes and incentives for small businesses.

If all of the recommendations were accepted, the gross reduction in taxes and revenues would be $19.3 billion, $15.0 billion reduction in corporate income taxes and $4.3 billion in personal income taxes (Attachment 1.2). If adjustment is made for the overlapping effect of each recommendation, the net tax cut would be less than $19.3 billion.

The stimulus to the economy from these proposals would result in greater output, employment, income and investment. Consumer prices would be slightly higher. Because of the resulting faster growth of personal and business income, government revenues would offset the initial tax cut in time.

Specifically, if all of the recommendations were enacted during the third quarter of 1978, then by 1982:

Gross National Product would be $48 billion higher.

Employment would be 1.1 million higher.

Average family income would be $585 higher.

Business Fixed Investment would be $17 billion higher.

Consumer prices would only increase by 0.7% or about one-tenth of one percent per year.

Federal revenues would increase and offset the initial $19.3 billion tax cut (Attachment 1.3).

ATTACHMENT 1.1

SMALL BUSINESS TAX REFORM POSITIONS

The Chamber of Commerce of the United States believes that it is in the best interest of the country to encourage a vibrant, enthusiastic and responsive small business community, and that consideration of the needs of small business is a necessary ingredient of the Nation's tax system. In order to meet the needs of small business, it is the view of the National Chamber that Congress should facilitate capital formation and the growth of small business by increasing the corporate surtax exemption, lowering the income tax rates for individuals and corporations, providing a more realistic capital cost recovery system, encouraging outside investment in small enterprises and permitting the continuation or orderly disposition of small businesses on the death of their owners.

CORPORATE SURTAX EXEMPTION

To permit the needed internal capital growth of small business enterprise we urge an increase in the corporate surtax exemption. The National Chamber urges that the corporate surtax exemption be increased to at least $200,000, with a 15 percent normal tax on the first $50,000 subject to the surtax exemption, and 22 percent on the next $150,000.

TAX REDUCTION FOR INDIVIDUALS AND CORPORATIONS

Small business would greatly benefit from individual and corporate income tax rate reduction. The Chamber favors corporate tax reduction to permit and encourage reinvestment of earnings in sufficient amounts to promote healthy economic progress. The Chamber favors lower and less steeply graduated tax rates on personal income. The maximum rate should be under 50 percent. The Chamber urges that an across-the-board tax reduction for individuals and corporations be made a major part of tax revision legislation.

DEPRECIATION AND CAPITAL COST RECOVERY

The present depreciation provisions in our tax laws are inadequate, still tied to an outmoded system of useful lives, and in great need of overhaul. We urge that Congress substitute for the present provisions a capital cost recovery allowance system. Such a liberalization of our depreciation laws would provide greater flexibility for small businesses.

A. Additional First Year Depreciation

Of particular interest to small business is the provision of the tax law which permits additional depreciation to be taken in the first year of an asset's life. In addition to the regular deduction for depreciation taken in the first year of an asset's life, taxpayers may elect to take an initial deduction of 20 percent of the cost of tangible personal property. This extra 20 percent deduction applies only to the first $10,000 ($20,000 for married couples filing jointly) of investment. The National Chamber is of the view that the useful life the asset must have to qualify for additional first year depreciation should be reduced and the dollar limit of property that qualifies should be increased to $20,000 ($40,000 for joint return).

B. Fast Depreciation Methods

Present law provides for depreciation methods other than straightline. The Chamber supports the retention of the existing provisions in the tax law and opposes changes that would eliminate or abridge the present methods of fast depreciation. Liberal capital cost allowances stimulate the modernization and expansion of the Nation's productive plants—especially in the case of small or new businesses which have difficulty in obtaining capital for long-lived property.

INVESTMENT TAX CREDIT

The National Chamber supports enactment of a permanent 12 percent investment tax credit, on an expenditure basis, without limitations based on tax liability, and with an increase in the limitation for used equipment to $200,000.

CAPITAL GAINS

Current law provides for deduction from gross income of 50 percent of the excess of net long-term capital gains over net short-term capital losses for individuals. Expansion of the capital gains deduction would encourage greater capital formation through equity investment, and would assist small business in obtaining venture capital. The National Chamber supports modification of the rate of taxation of capital gains by providing for reduced taxation of capital gains proportionate to the length of time a capital asset is held, with the reduction being gradual and continuous. In addition, we believe the existing Code provisions which provide an alternative tax on long-term capital gains for individuals and corporations should be retained.

MINIMUM ACCUMULATED EARNINGS CREDIT

The National Chamber urges Congress to increase the minimum accumulated earnings credit to $500,000. Small businesses are particularly affected because the tax is generally applied to small closely-held corporations. The threat of the tax makes it difficult for such businesses to raise capital and to accumulate capital out of earnings.

DEDUCTION FOR NONBUSINESS INTEREST

The National Chamber opposes any changes in the tax law that would eliminate or reduce the present deduction for nonbusiness interest. Our society is built largely on credit. If the deduction for nonbusiness interest on such credit is eliminated or further curtailed, the general use of credit could be markedly reduced, causing irreparable harm to small business.

NET OPERATING LOSS CARRYOVER

New businesses often experience a period of losses in the early years of their existence. The Chamber favors a net operating loss carryback of three years and a carryforward of eight years.

CLOSELY HELD BUSINESS ROLLOVER

The National Chamber favors permitting owners of a closely held business to defer the tax on the sale of the equity of the business if the proceeds are reinvested within a specific time in other small business investments.

REFUND OF OVERPAYMENT OF ESTIMATED INCOME TAX

Under current tax law a corporation that has overpaid its estimated income tax does not receive a refund until the end of the taxable year. It is the view of the National Chamber that refunds for overpayment should be made when they are claimed rather than at year end.

SECTION 1244 STOCK

Individuals who experience losses on small business stock should be able to treat $50,000 of such losses per taxable year as ordinary losses which can be used to offset ordinary income, rather than as capital losses. The maximum amount permitted under present law is $25,000 per taxable year. The definition of a small business corporation under section 1244 should be amended by increasing the equity capital limitation from $1 million to $2 million and increasing the permissible amount received by the corporation for its stock from $500,000 to $1 million.

ATTACHMENT 1.2

TAX AND REVENUE REDUCTIONS FROM SMALL BUSINESS TAX REFORM POSITION

[1977 billions of dollars]

	Tax and Revenue Reductions		
	Corporate income taxes	Personal income taxes	Total tax cut
Tax change recommendations:			
Increase in corporate surtax exemption to $200,000 with 15 pct normal tax on first $50,000 and 20 pct on next $150,000	5.0		5.0
50 pct maximum tax on all personal income		2.0	2.0
Liberalized depreciation from 20 pct ADR to 40 pct ADR	4.0	1.0	5.0
Additional 1st year depreciation on small business	.2		.2
Increase investment tax credit to 12 pct	2.0	.5	2.5
Change in capital gains tax to take into account longer holding period	2.4	.6	3.0
Increase minimum accumulated earnings credit from $150,000 to $500,000	.2		.2
Operating loss carry forward of 8 yr	.8	.2	1.0
Deferral of tax on closely held business if reinvested within a specific time period	.1		.1
Refund of overpayment of estimated income tax	.1		.1
Section 1244 stock increase permissible loss from $25,000 to $50,000	.2		.2
Total gross tax and revenue reductions [1]	15.0	4.3	19.3
ADDENDUM			
No change recommendations—Deduction of nonbusiness interest:		8.6	
Interest on consumer credit		2.6	
Mortgage interest		6.0	

[1] Adjustments for the overlapping effect of one recommendation on another were not estimated but would undoubtedly reduce the totals by at least 25 pct.

ATTACHMENT 1.3

ECONOMIC IMPACT OF THE SMALL BUSINESS TAX CUTS

[Assumed enacted 3d quarter of 1978]

	1978	1979	1980	1981	1982
GNP (percent)	0.2	0.9	1.6	2.0	2.0
GNP (billions of dollars)	3	19	35	46	48
Employment (thousands of jobs)	100	300	700	1,000	1,100
Family disposable income (dollars)	70	260	425	545	585
CPI (percent)	.1	.4	.6	.7	.7
Business fixed investment (billions of dollars)	1	5	9	14	17
Federal taxes (billions of dollars)	−10	−15	−10	−5	0

Source: National Chamber Small Business Council, DRI and Chase econometric macroeconomic models, National Chamber Forecasting Center, Jack Carlson and George Tresnak.

Senator BENTSEN. Thank you very much.
Mr. Shapiro, please proceed.

STATEMENT OF HAROLD T. SHAPIRO, PROFESSOR OF ECONOMICS AND PUBLIC POLICY; CODIRECTOR, RESEARCH SEMINAR IN QUANTITATIVE ECONOMICS; AND VICE PRESIDENT, ACADEMIC AFFAIRS, UNIVERSITY OF MICHIGAN

Mr. SHAPIRO. Thank you very much for the opportunity to be here today and once again discuss with the committee my views regarding the short-term economic outlook for the U.S. economy.

Before beginning with my comments proper, I do want to indicate roughly where I stand on some of the issues you raised at the beginning of today's session.

First of all, with respect to the consensus forecast, as you will see in a moment my own forecast is less optimistic than that. We are in comparison to the 4.5- to 5-percent growth rate you spoke of, but our own outlook is for something closer to 3 and 3.75 to 4 percent. So it is somewhat on the downside of what you describe as the consensus.

With respect to some key issues of policy, that is, whether economic stimulus is called for in 1978, we certainly think it essential to have some economic stimulus, that the President's program is certainly acceptable, but is minimal in size, and I would agree with both Mr. Carlson and Mr. Adams that it ought to be redirected to have somewhat more stimulative effect on investment.

With respect to monetary policy, I think we are now facing in the coming year a very difficult situation whereas in a kind of first-round effect you would think that the domestic economy would call for a more expansionary monetary policy and lowering of interest rates, and I think that is important. There is a key issue of what kind of feedback that will have on world commodity prices if the U.S. dollar should devalue any further than it has now.

So there is a very subtle difficulty there and a careful balancing act is called for in the coming year. I will have more to say about that in just a moment.

ECONOMIC OUTLOOK

As I look out at the American economy today, it is quite clear that the general confidence regarding the outlook for the U.S. economy during the coming year seems to have developed a rather uncertain tone in the closing weeks of 1977, and the opening weeks of the new year. This is very much a repeat of our experience of last year.

In both 1976 and 1977 the economy rose rapidly in the early quarters of the year only to then settle down some, and thus generate considerable nervousness about the continued strength of the economic recovery. In both years, for example, this mood was reflected in a decline in the Index of Consumer Sentiment—a widely cited yardstick of consumer confidence—in the November/December survey.

In part, these effects may be due to inappropriate seasonal adjustment factors in the data, but they do illustrate that our confidence in the year ahead is heavily influenced, at times too heavily influenced, by particular developments at the time we make our analysis. Although there has been some "bearish" economic news such as disappointing level of new car sales, a coal strike that could have a serious impact if it is prolonged much longer, a declining value of the U.S. dollar and a difficult winter in the Midwest, the rate of growth of real GNP was considerably stronger at the end of 1977 than in 1976, and the unemployment rate dropped to under 6.5 percent by yearend. The primary difference was that in 1976 the economy experienced a rather severe inventory adjustment at year-end.

Second, I think the decline in the Index of Consumer Sentiment and consumer attitudes in general is somewhat more significant this year than last year, and it is in part responsible, in my own view, which is a little less optimistic than what your describe as the consensus.

If one thinks for a moment about where the economy has been during the expansion, it is widely held that the consumer-household sector has really fueled the household expansion. These have been the leading sectors in the economic expansion. Looking at two other major sectors, Government and business fixed investment, as Professor Adams has already said, the performance of business fixed investment has been very disappointing in the current expansion. It has lagged the economy for the most part, especially in the structures section, as Mr. Carlson pointed out. It is also true the Government sector has been a drag on the economy during that expansion. At the Federal, State, and local levels they have simply not kept pace with the economy whereas the Government revenues have increased as the portion of GNP throughout this period.

I guess Federal revenues are once again back up to 20 percent of GNP and State and local roughly 15 percent or so, so the Government sector has been in a drag, the business fixed investment sector has been disappointing and it is the household sector that has brought us through the expansion so far.

My own view of the economic outlook, as I will explain in more detail in a moment, is heavily influenced by the fact that we can no longer expect the household sector to contribute very significantly to the continued expansion, and my own view is that it is not very optimistic in the business fixed investment sector either unless there are some changes in the economic policy.

The nature of the current expansion to date is roughly summarized in table 1 of my prepared statement, which you have in front of you, which just indicates the leading sectors in this area and which sectors have been more or less a drag on the economy during the current expansion.

Let me turn now to the economic outlook over the next 1 to 1½ years.

The outlook for economic activity in 1978 and 1979 will, of course, also be shaped in an important way by the economic policies of the Federal Government. Of particular interest at the moment is the effect on the economic outlook of a tax cut or a tax cut/tax reform package such as that recently proposed by President Carter. In order to highlight this particular issue, I will present, as briefly as possible, three different forecasts for 1978–79.

The first forecast—entitled "The Control Forecast"—assumes no new tax legislation beyond that already enacted. The second forecast—entitled "the Carter Proposal"—assumes that President Carter's proposals are passed in the form recommended by the administration and effective October 1, 1978. The third and final forecast—entitled "Expansionary Alternatives"—assumes a more expansive fiscal stimulus program by eliminating the tax reform measures suggested by the President, which are estimated to increase tax revenues by some $6 billion, and raising the investment tax credit to 15 percent.

All three forecasts assume Federal expenditures consistent with the administration's budget and a modest acceleration of State and local government purchases. Also incorporated in each of these forecasts is an assumption of a turning toward a somewhat easier monetary policy.

Specifically, we have assumed that the discount rate will drop by 25 basis points in the second quarter of 1978, and a further 25 basis points in the third quarter of the current year, and that the annual rate of growth of unborrowed reserves will accelerate from 4 percent in early 1978 to 4.50 percent in the spring, and 5 percent after midyear. These forecasts, however, make no provision for the effects of any energy bill that might be passed by the Congress in the next year or so. If a bill similar to that recently passed by the House were finally enacted this quarter, by mid-1979 our forecast of the rate of inflation would be higher by about one-third of 1 percent and our forecast of the rate of growth in real GNP lowered by about one-third of 1 percent.

So an energy policy in our view such as that passed by the House is slightly inflationary and slows down slightly also the rate of growth of real GNP. Its primary effects are not on aggregate economic activity, but on prices in energy markets.

Let me turn now to the forecasts themselves.

THE CONTROL FORECAST

Table 2 in my prepared statement contains key economic indicators from "the Control Forecast." Within this framework the outlook is simply not very optimistic. The annual rate of growth or the GNP declines from 3.3 percent in the first half of 1978 to 1.8 percent in the first half of the next year. For 1978 as a whole, real GNP rises by 3.75 percent to a level of $1,387.7 billion (1972). This, together with a rate of price inflation of over 5.75 percent, yields a forecast of GNP in current dollars of just over $2 trillion, at $2,075.4 billion.

Further, the slowdown is rather well-balanced except for the residential construction sector where actual declines are registered from early 1978 through 1979. The unemployment increase is perhaps surprisingly modest—the aggregate unemployment rate reaching the level of just 6.7 percent in mid-1979—but this is largely the result of the rather poor productivity performance anticipated in the contest of a sharp slowdown in the rate of growth of output. Given recent difficulties in forecasting labor force participation rates, however, all forecasters must be less certain about their capacity to forecast movements in unemployment rates.

The most obvious implication of this forecast is that the economy is in need of further fiscal stimulus. As you know, this has, in fact, been proposed by President Carter, and I turn now to look at the effects of President Carter's tax proposals on the economic outlook over the next year to year and one-half.

If you take a look at table 3 in my prepared statement, which is really the same set of figures, only this time assuming that the Carter administration proposals are, in fact, enacted, you can see that they have, as one would expect, very little effect on calendar 1978 figures because they are only enacted late in 1978. However, they do have a substantial effect on growth rates in the end of the year, in the last quarter, and in early 1979, and they have the effects that have by and large been commented on already and I don't think I have to spend any more time on that.

Table 4 in my prepared statement contains some economic outlook under a more expansionary program. That has the effects one might expect. It stimulates the economy slightly more than the Carter proposal and has a somewhat greater effect on investment since the investment tax credit is increased from 10 to 15 percent. I have not been able in these forecasts to trace out the ultimate inflationary impact of such a proposal because the forecast horizon is really too short, the price effects will make themselves felt further on, but I would be glad to respond to that question if you have any questions about that.

Finally, let me say that there has been a growing skepticism in the economics profession about the usefulness of discretionary economic policy and a growing skepticism, both inside and outside the profession, about the capacity of economists to provide useful information to those charged with the ultimate responsibility for implementing economic policy.

I believe that this skepticism has played a useful role in making us all more aware of the limitations we face in our current capacity to control our economy. There is some danger we may carry this notion too far.

It is true that an earlier optimism centered on a policy based on a longrun inflation unemployment tradeoff augmented by a certain amount of fine tuning through temporary income tax cuts has been somewhat discredited by the events of the seventies. There is, however, still a critical role for Government policy, though perhaps acting through shifts in subsidies, sales taxes, payroll taxes, and various wage tax proposals in addition to the careful use of aggregate tax and expenditure policies.

Just as adverse supply shifts such as a sharp increase in OPEC oil prices in 1974 caused a once-and-for-all simultaneous increase in both inflation and unemployment, a decrease in payroll taxes, for example, causes the reverse effect to take place. It seems to me, therefore, that the current and proposed shift from income taxes to payroll taxes is at least from this point of view not very helpful.

If one thinks of the recent tax cuts plus the proposed tax cuts, proposed income tax cuts, while simultaneously having a sharp increase in social security taxes, as you know, this does represent a very sharp shift from income taxes to social security taxes, and I think from the point of view of price stability that this is not very helpful.

It is also time, in my opinion, to reevaluate various Federal grant programs to State and local governments. Many of these were designed to stimulate local activity seem in my opinion not to have been very effective.

In summary, the design of appropriate and effective economic policies remains a difficult and challenging task, but I think we have learned a lot from recent experiences and we are in a position now, I believe, where the Government can issue appropriate economic policies which will have a beneficial effect on economic activity.

Let me finish up by summarizing where I stand on economic policy issues.

With respect to the economic stimulus, I look at the $25 billion tax cut as minimal. I think it entirely appropriate to have a larger tax cut providing a greater amount of that is directed toward stimulating investment activity.

I also agree with Professor Adams that for any given dollar of Federal revenue foregone, the investment tax credit is much more effective than a decline in the corporate tax rate, which is what President Carter proposed. I think there is a very useful aspect to the present proposal in this area and that is increase in the coverage of investment tax credit to include public utilities.

If you look at the sectors of investment which have really lagged in this expansion, some of those, in any case, are simply not covered by the investment tax cut, so the increasing of the coverage is useful, but I also think it would be useful to simply increase it, for example, from 10 to 15 percent. I think the possibility of doing something more on depreciation allowances, as suggested by Mr. Carlson, is something which also should receive very serious attention.

Monetary policy, in my view, is the most difficult issue before us. On the one hand, we have some desire to stabilize the U.S. dollar. That is bound, as Professor Adams indicated, to increase interest rates. That is counterproductive regarding the domestic economy.

At least in the first-round effect, if we give up defending the U.S. dollar, so to speak, to spur some other objectives, interest rates will undoubtedly fall, the dollar may devalue further and that may have an effect on international commodity prices, particularly oil prices, and that is the uncertainty in the area, and I think the planning for monetary policy over the next year or year and a half is going to be a very difficult job indeed.

I would be happy to respond to any questions you might have.

[The prepared statement of Mr. Shapiro follows:]

Prepared Statement of Harold T. Shapiro

The U.S. Economic Outlook for 1978–79

INTRODUCTION

I am pleased once again to discuss with this committee my views regarding the short-term economic outlook for the U.S. economy. As you know, the Research Seminar in Quantitative Economics at The University of Michigan has been producing forecasts of the short-term outlook for the U.S. economy for the last 25 years. Throughout this period these forecasts have been generated with extensive, though never exclusive, reliance on the Michigan econometric model of the U.S. Economy. The economic forecast and analysis that I will present to you today continues this tradition and is the result of a joint effort of my colleague and co-director of the Research Seminar in Quantitative Economics, Professor Saul Hymans, and myself, using the Michigan econometric model as a basic organizing framework of our analysis.

General confidence regarding the outlook for the U.S. economy during the coming year seems to have developed a rather uncertain tone in the closing weeks of 1977, and the opening weeks of the new year. This is very much a repeat of our experience of last year. In both 1976 and 1977, the economy rose rapidly in the early quarters of the year only to then settle down some, and thus generate considerable nervousness about the continued strength of the economic recovery. In both years, for example, this mood was reflected in a decline in the Index of

Consumer Sentiment—a widely cited yardstick of consumer confidence—in the November/December survey. In part, these effects may be due to inappropriate seasonal adjustment factors in the data, but they do illustrate that our confidence in the year ahead is heavily influenced, at times too heavily influenced, by particular developments at the time we make our analysis. Although there has been some "bearish" economic news such as disappointing level of new car sales, a coal strike that could have a serious impact if it is prolonged much longer, a declining value of the U.S. dollar and a difficult winter in the Midwest, the rate of growth of real GNP was considerably stronger at the end of 1977 than in 1976, and the unemployment rate dropped to under 6.5 percent by year-end. The primary difference was that in 1976 the economy experienced a rather severe inventory adjustment at year-end.

It remains true, however, that the pace and shape of economic activity in the next 6-8 quarters is influenced in an important way not only by the nature of the current business expansion which began in early 1975, but also by particular characteristics of the current economic situation. I would like to begin, therefore, be reviewing certain salient aspects of the current state of the economy.

THE CURRENT STATE OF THE ECONOMY

The current economic recovery (now beginning its 4th year) found most of its strength in the household sector. In particular, it has been the strong growth in the demand for consumer durable goods and housing that has provided the critical fuel to the current business expansion. Purchases of consumer durables reached record heights in 1977, with real expenditures on furniture and household equipment far exceeding previous peaks, and auto sales in mid-1977 coming close to earlier record levels, after the unusually deep decline of a few years ago. Likewise, home building activity has risen dramatically since 1975, with single-unit housing starts exceeding 1.4 million for 1977, well above the record set in 1972. Multi-family starts have also risen sharply in the last 3 years, but have failed to return to the peak levels experienced in 1972. Thus, while the overall pace of the recovery of the last 2 years resulted in an average growth rate of 5.5 percent in real terms, household purchases of durables and residential construction activity experienced average growth rates of 10.6 percent and 21 percent respectively (see table 1).

TABLE 1.—SELECTED RATES OF GROWTH IN ECONOMIC ACTIVITY, 1976-1977

[In percent]

	1976	1977
Gross national product	6.0	4.9
Household sector:		
Durable goods	13.1	8.3
Residential construction	23.2	19.1
Business sector (investment):		
Structures	2.2	3.6
Produces durable equipment	4.2	11.3
Government purchases:		
Federal	-.2	5.0
State and local	1.0	1.1

Note.—Data in table represents real growth rates.

The expansion of demand in the business investment sector has been much less buoyant. Activity in non-residential construction is still well below peak levels experienced in 1974, and business purchases of producer durable equipment have only just matched (in the 4th quarter of 1977) the peak level of activity they attained in mid-1974. There is no question that the contribution of this sector to the current expansion has been disappointing. A great deal has been written on the disappointing recovery in business fixed investment during the current economic expansion. This has raised both short-run and long-run concerns. In the short-run it has prevented us from eliminating excess capacity as quickly as we might, and there are long-run concerns about what this means for the future efficiency and capacity of the American economy. I would like, therefore, to take a rather closer look at this issue as I think it is critical for economic policy.

Investment activity in the manufacturing sector has not been a particular problem. The behavior of durable manufacturing investment does not appear to be significantly out of line with our experience in previous recessions and expansions. Further, relative to prior experience, non-durable manufacturing seems to have barely noticed the 1974–75 recession. The same can be said about investment activity in the transportation sector. Thus, the weakness in the investment sector cannot be traced to activities in manufacturing or transportation.

Investment activities in other sectors, however, (communication, commercial construction, utilities and "other"), have been far more depressed than in prior recessions and post-recession periods. Economic policies designed to remedy the short-fall in investment activity, therefore must be specific enough to address special problems which may characterize investment activities in these particular areas. A case in point is the investment tax credit which has not been applicable to public utility investment. I think there is a strong case, therefore, for the President's recommendation that the investment tax credit be extended to the utility industry. In general, we need to learn not only why aggregate investment has weakened, but rather what factors are most responsible for the sluggish behavior of investment in public utilities, commercial cosntruction, and the surprisingly large "other" (e.g. non-profit institutions) sector.

Overall, the government sector has been a drag on the economy during the past 2 years. Government expenditures (see table 1) have simply failed to keep pace with GNP. This is particularly true in the State and local sector. Over the last 2 years, Federal purchases and State and local purchases have averaged growth rates in real terms of only 2.4 percent and 1.0 percent respectively. At the same time government tax receipts have risen noticeably in proportion to GNP. Indeed Federal government receipts in mid-1977 were back to their 1974 mark of 20 percent GNP after a temporary decline to about 18.75 percent of GNP as a result of the 1975 tax cut. Further, as you are aware, the Social Security bill just passed amounts to a 2-year tax increase of approximately $15 billion.

Monetary policy reflects a more ambigious stance. While interest rates have risen sharply in the final weeks or 1977, and the early weeks of 1978, they had maintained rather surprisingly low levels throughout most of the last 2 years. Even the interpretation of the monetary aggregates is somewhat clouded. M1 has risen by less than 12 percent since 1975, and unborrowed reserves have barely risen at all. M2, on the other hand, has been rising considerably faster and has been maintaining a relatively constant ratio to the aggregate level of economic activity. Even M2, however, has risen rather more slowly in the final quarter of 1977, and the Federal Reserve discount rate is now back up to 6.50 percent, after a decline to 5.25 percent in 1976, and has pulled the prime rate and short-term rates up along with it. Thus, at the moment monetary policy seems to be taking a turn to a more restrictive stance.

What seems clear to me from this background is that we cannot rely on the household sector to continue to keep the economic expansion moving strongly ahead. Car sales have weakened and are unlikely to do any more than remain on a high plateau even if the recent "slowdown" is reversed. Further, my own interpretation of recent movements in the Index of Consumer Sentiment indicate that the downturn in consumer attitudes is considerably more significant than the turndown of late 1976. Home-building activities seem to have peaked and are perhaps beginning to feel the impact of greater monetary restriction. Continued monetary restriction will not spare the domestic construction sector just because it may be motivated by the desire to support the dollar abroad. In addition, I see no evidence that business capital spending is about to make up for the slowed growth expected in the household sector.

After a long series of continuous frustrations on dealing with the rate of inflation, it is difficult for many economists not to seem out of touch with reality. The final quarter of 1977 was characterized by an inflation rate in the six percent range, with unit labor costs rising at about the same rate. Given that, the full adverse affect of the declining value of the U.S. dollar has yet to be incorporated into domestic price levels, the outlook regarding inflation remains troublesome. The good news, however, is that the pace of inflation has decelerated and that negotiated wage settlements expected in 1978 are highly concentrated in the second and third year of their contracts.

THE ECONOMIC OUTLOOK

The outlook for economic activity in 1978 and 1979 will, of course, also be shaped in an important way by the economic policies of the Federal Government. Of particular interest at the moment is the effect on the economic outlook of a tax cut or a tax cut/tax reform package such as that recently proposed by President Carter. In order to highlight this particular issue, I will present, as briefly as possible, three different forecasts for 1978-1979. The first forecast (entitled "The Control Forecast"), assumes no new tax legislation beyond that already enacted. The second forecast (entitled "The Carter Proposal"), assumes that President Carter's proposals are passed in the form recommended by the Administration and effective October 1, 1978. The third and final forecast (entitled "Expansionary Alternatives") assumes a more expansive fiscal stimulus program by eliminating the tax reform measures suggested by the President (which are estimated to increase tax revenues by some $6 billion) and raising the investment tax credit to 15 percent. All three forecasts assume Federal expenditures consistent with the Adimistration's budget and a modest acceleration of State and local government purchases. Also incorporated in each of these forecasts is an assumption of a turning toward a somewhat easier monetary policy. Specifically, we have assumed that the discount rate will drop by 25 basis points in the second quarter of 1978, and a further 25 basis points in the third quarter of the current year, and that the annual rate of growth of unborrowed reserves will accelerate from 4 percent in early 1978 to 4.50 percent in the spring, and 5.0 percent after mid-year. Those forecasts, however, make no provision for the effects of any Energy Bill that might be passed by the Congress in the next year or so. If a bill similar to that recently passed by the House were finally enacted this quarter, by mid-1979 our forecast of the rate of inflation would be higher by about 1/3 of 1.0 percent and our forecast of the rate of growth in real GNP lowered by about 1/3 of 1.0 percent. Let me turn now to the forecasts themselves.

The Control Forecast. Table 2 contains key economic indicators from "The Control Forecast." Within this framework the outlook is simply not very optimistic. The annual rate of growth or the GNP declines from 3.3 percent in the first-half of 1978, to 1.8 percent in the first-half of the next year. For 1978 as a whole, real GNP rises by 3.75 percent to a level of $1,387.7 billion (1972 dollars). This together with a rate of price inflation of over 5.75 percent yields a forecast of GNP in current dollars of just over two trillion at $2,075.4 billion. Further, the slowdown is rather "well-balanced" except for the residential construction sector where actual declines are registered from early 1978 through 1979. The unemployment increase is perhaps surprisingly modest—the aggregate unemployment rate reaching the level of just 6.7 percent in mid-1979—but this is largely the result of the rather poor productivity performance anticipated in the context of a sharp slowdown in the rate of growth of output. Given recent difficulties in forecasting labor force participation rates, however, all forecasters must be less certain about their capacity to forecast movements in unemployment rates.

TABLE 2.—THE CONTROL FORECAST

	1977.4–1978.2	1978.2–1978.4	1978.4–1977.2	1976–77	1977–78
Annual rates of growth (percent):					
Real GNP (1972 dollars)	3.3	2.6	1.8	4.9	3.7
Consumption	3.3	2.9	2.3	4.8	3.8
Durable goods	1.9	1.8	.9	8.2	3.0
Business fixed investment	4.4	3.2	1.6	8.9	5.1
Residential construction	−7.9	−11.2	−5.7	19.2	−.6
Government purchases	3.8	3.1	2.2	2.6	4.4
GNP deflator (1972=100)	5.6	6.4	5.9	5.6	5.8
Consumption deflator (1972=100)	5.4	5.7	5.8	5.6	5.3
Levels in terminal quarter or year:					
Aggregate unemployment (percent)	6.4	6.5	6.7	7.0	6.4
Personal saving rate do	5.8	5.7	5.4	5.2	5.8
90-day Treasury bill rate do	6.2	6.7	6.3	5.3	6.6
Corporate Aaa rate do	8.2	8.4	8.4		
Auto sales (millions of units)	10.88	11.05	11.19	11.2	10.9
Private housing units do	2.14	1.98	1.87	2.0	2.1

Source: Research seminar in quantitative economics, the University of Michigan, Jan. 28, 1978.

The most obvious implication of this forecast is that the economy is in need of further fiscal stimulus. As you know, this has in fact been proposed by President Carter, and I turn now to look at the effects of President Carter's tax proposals on the economic outlook over the next year to year and one-half.

The Carter Proposal. Table 3 contains data summarizing the economic outlook over the next 6 quarters under the assumption that Congress enacts President Carter's recent tax proposals and makes them effective in the 4th quarter of 1978. These figures can be compared directly with those of *The Control Forecast* in table 2. Obviously the Administration's tax plan would have very little impact on calendar 1978 data. It would, however, have a significant impact on the rates of growth registered in the final quarters of this year, and in the first-half of 1979. However, as is clear from the data presented in table 3, the proposed tax reduction is neither large enough, or so structured as to produce an expansion of major magnitude. Net of reform induced tax increases, the President is proposing a personal tax cut of only $17 billion—only slightly more than the combined 1978–1979 Social Security Tax increases and almost equal in magnitude to the tax cut of 1964–1965 when nominal GNP was about ⅓ of what it is today. The proposed cuts in business taxes are also modest and much of that reduction is concentrated in the 3 percentage point drop in the corporate tax rate. Most of the evidence of which I am aware suggests that for a given dollar of Federal revenue foregone, more investment spending will take place via the route of an increase in the *investment tax credit* than via a reduction of the corporate tax rate. Since taken as a whole, the investment sector has not responded well during the current expansion. I would opt not only for a bigger total tax cut, but for more emphasis on tax relief tied to higher investment spending. Alternatively, a tax cut of the size proposed would be far more effective if combined with substantially more stimulative monetary policy which would have major positive effects on business investment and residential building activities. Whatever policy is selected with respect to the domestic economy, I hope we shall not come to the situation in which domestic monetary policy is severely constrained by international factors despite the "abandonment" of fixed change rates.

TABLE 3.—THE CARTER ALTERNATIVE

	1974.4–1978.2	1978.2–1978.4	1.9784–1977.2	1976–77	1977–78
Annual rates of growth (percent):					
Real GNP (1972 dollars)	3.3	3.2	3.0	4.9	3.8
Consumption	3.3	4.0	3.5	4.8	4.0
Durable goods	1.9	2.4	5.7	8.2	3.1
Business fixed investment	4.4	3.2	4.3	8.9	5.1
Residential construction	−7.9	−11.2	−5 2	19.2	−.6
Government purchases	3.8	3.1	2.3	2.6	4.4
GNP deflator (1972=100)	5.6	6.3	5.8	5.6	5.8
Consumption Deflator (1972=100)	5.4	5.7	5.7	5.6	5.3
Level in terminal quarter or year:					
Aggregate unemployment rate (Percent)	6.4	6.4	6.4	7.0	6.4
Personal saving rate do	5.8	6.3	5.9	5.2	6.3
90-day Treasury bill rate do	6.2	6.8	6.4	5.3	6.8
Corporate Aaa rate do	8.2	8.4	8.4	------------	8.4
Auto sales (millions of units)	10.88	11.05	11.95	11.2	11.0
Private housing units do	2.14	1.98	1.87	2.0	1.98

Source: Research seminar in quantitative economics, the University of Michigan, Jan. 28, 1978.

The Expansionary Atlernative. The final forecast I wish to present contains a fiscal stimulus package significantly more expansionary than that proposed by the President. With respect to personal taxes, I have simply eliminated the "reform" components of the Administration's proposal. On the corporate side, I have also increased the investment tax credit to 15 percent. These are substantial additions to the Administration's proposals but the overall tax cut would, relatively speaking, still be far less than the 1964–1965 tax cut. The data in table 4 summarizes the short-term outlook under these assumptions. The result, not surprisingly, is to simply reinforce the effects of the Administration's stimulus proposal, particularly in the area of business investment. Growth rates in real output are somewhat higher by mid-1979 and the unemployment rate has moved somewhat lower. There is little noticeable effect on the rate of inflation, but it is perhaps too early for this particular effect to be realized.

TABLE 4.—THE EXPANSIONARY ALTERNATIVE

	1977.4–1978.2	1978.2–1978.4	1978.4–1979.2	1976–77	1977–78
Annual rates of growth (percent):					
Real GNP (1972 dollars)	3.3	3.6	3.1	4.9	3.9
Consumption	3.3	4.6	3.4	4.8	4.1
Durable goods	1.8	2.8	6.5	8.2	3.1
Business Fixed Investment	4.4	3.2	6.7	8.9	5.1
Residential Construction	−7.9	−11.2	−5.1	19.2	−.6
Government Purchases	3.8	3.1	2.3	2.6	4.4
GNP deflator (1972=100)	5.6	6.3	5.8	5.6	5.8
Consumption deflator (1972=100)	5.4	5.7	5.7	5.6	5.2
Level in terminal quarter of year:					
Aggregate unemployment rate (percent)	6.4	6.4	6.2	7.0	6.4
Personal saving rate do	5.8	6.6	6.0	5.2	6.0
90-day Treasury bill rate do	6.2	6.8	6.5	5.3	6.6
Corporate Aaa rate do	8.2	8.4	8.4	8.0	8.3
Auto sales (millions of units)	10.88	11.05	12.08	11.2	10.9
Private housing starts do	2.14	1.98	1.87	2.0	2.1

Source: Research seminar in quantitative ecomomics, the University of Michigan, Jan. 28, 1978.

For your convenience table 5 summarizes, in terms of three principal indicators, the short-term economic outlook in the alternative policy environments I have outlined.

TABLE 5.—COMPARISON OF ALTERNATIVE FORECASTS: GNP (1972 DOLLARS), PRICES, UNEMPLOYMENT RATES [1]

[In percent]

	1977–78	1978.4–1979.2
Gross national product (1972 dollars—) Annual rate of growth:		
The control forecast	3.7	1.8
The Carter proposal	3.8	3.0
The expansionary alternative	3.9	3.1
Prices (the GNP deflator)—Annual rate of growth:		
The control forecast	5.8	5.9
The Carter proposal	5.8	5.8
The expansionary alternative	5.8	5.8
Aggregate unemployment rate—Level in terminal quarter:		
The control forecast	6.5	6.7
The Carter proposal	6.4	6.4
The expansionary alternative	6.4	6.2

[1] All forecasts are consistent with the administration's current budget recommendations, but make no allowance for the effect of any energy bill.

Source: Research seminar in quantitative economics, the University of Michigan, Jan. 28, 1978.

Finally, there has been a growing skepticism in the economics profession about the usefulness of discretionary economic policy and a growing skepticism both inside and outside the profession about the capacity of economists to provide useful information to those charged with the ultimate responsibility for implementing economic policy. While I believe that this skepticism has played a useful role in making us all more aware of the limitations we face in our current capacity to control our economy, there is some danger that we may carry this notion too far. It is true that an earlier optimism centered on a policy based on a long-run inflation-unemployment tradeoff augmented by a certain amount of "fine tuning" through temporary income tax cuts has been somewhat discredited by the events of the 1970's. There is, however, still a critical role for government policy though perhaps acting through shifts in subsidies, sales taxes, payroll taxes, and various wage/tax proposals in addition to the careful use of aggregate tax and expenditure policies. Just as adverse supply shifts (such as a sharp increase in OPEC oil prices in 1974) cause a once-and-for-all simultaneous increase in inflation and unemployment, a decrease in payroll taxes causes the reverse effect to take place. It seems to me, therefore, that the current shifts from income taxes to payroll taxes is, at least from this point of view, not very helpful. It is also time, in my opinion, to re-evaluate various Federal grant programs to State and local government. Many of those grants which were designed to stimulate local economic activity seem, in my opinion, not to have been very effective.

In summary, the design of appropriate and effective economic policies remains a difficult and challenging task, but I believe we have learned a lot from the experience of the 1970's, and are in a position where the government can implement appropriate economic policy in a way that will have a beneficial impact on the evolution of economic activity. We are far, however, from any capacity to eliminate all of our problems.

I would be happy to answer any questions you may have.

Senator BENTSEN. Thank you very much. Would you clarify a point for me in your testimony where you talk about extending the investment tax credit to the utility industry.

Mr. SHAPIRO. Yes.

Senator BENTSEN. I thought we had done that. One of our problems is that utilities pay virtually no taxes, is that what you are referring to, or are you talking about going to a refundable tax credit? What do you mean?

Mr. SHAPIRO. The general comments I was trying to make there is it is my understanding that there are sectors in which are not covered by the investment tax credit and the sectors that have lagged in this area in this recession are areas such as commercial construction, the other sectors, so-called residual sector, and I thought public utilities were not covered.

Senator BENTSEN. I will check my memory, but I seem to remember we specifically did provide it for them. The question is, do you want to go to a refundable tax credit, which is quite different?

Most utilities pay a very low effective tax rate and they have been able to utilize the credits to the extent of that.

Mr. Carlson, you made the point about the impact of legislation in the past. My Subcommittee on Economic Growth is planning to hold hearings on the impact of regulations on business, and the ultimate cost to consumers. Washington University in St. Louis put out a report showing that there is an $82 billion in costs to companies of business regulations, and in turn about a $3 billion cost to the Government in imposing those regulations and enforcing those regulations.

So we plan to be a little more definitive about regulation in our hearings and see what can be done to cut back on the impact. So I appreciate the point that you made.

I must also say, though, when you talk about protection, which I understand is a concern of yours, I must also say that many businessmen come in to see me all the time wanting protection from imports.

Mr. CARLSON. Yes; that is a difficult problem with the slowing down of growth abroad and, perhaps, a little slower pace in this country everybody is looking for expedient solutions which they think will help their particular problem but overall hurt somebody else.

Protectionism is one of the most serious problems we have during the next 2 years. Hopefully, the multilateral trade negotiations in Geneva will be able to stem some of that tide.

Senator BENTSEN. As long as I can remember, a major business concern has been eliminating double taxes on corporations. I don't see the United States Chamber pushing for that legislation or the small business recommendations you made pushing for that legislation.

What I have found is a sudden abandonment of that by many people in business because of the great disparity in impact on whether it is a growth company or a mature company, what happens to the stock, and a difficulty in finding one mode of application that would accomplish the objectives of the diversity of interested corporations.

Mr. CARLSON. I think that is part of it. The other part is that right now we find ourselves relatively speaking in an investment short economy and if you have only so many dollars to cut and you want to stimulate investment, I think you should cut the tax burden on investment.

The most powerful places to stimulate investment are in the investment tax credit area and also depreciation allowances.

Senator BENTSEN. Have you looked at this new administration proposal? If I remember right on the accelerated depreciation preference tax, you would have the elimination, for example, of the half credit for taxes paid. If anything, it heads in the other direction, insofar as accelerated depreciation is concerned.

Mr. CARLSON. The problem on the depreciation side is that people are not recovering through capital allowances depreciation allowances enough for replacement costs. I think in the third quarter of last year it was an $18 billion gap.

Clearly, in particular, improved depreciation allowances would have a big impact in industries such as steel.

More specifically to your problem on double taxation, over the long run that is a desirable objective and maybe if there are some small steps taken like Congressman Ullman has talked about that would be appropriate. But if large tax cuts are made in that area as a tradeoff with some other areas we think you will have less stimulus for investment.

Senator BENTSEN. Double taxation is way down on the list of priorities where it used to be a very high one in the business community. They just don't come in and talk to me about that any more.

Mr. Adams, I thoroughly agree that businesses have been hard hit by safety and pollution regulations and that we ought to have almost an immediate writeoff of those investments. But what do you do about companies that are lagging because of not being competitive or not having sales—both go together—and not using the investment tax credit. They just feel it is a no-win deal for them. If you want to use the credit to modernize them, those firms are some of the most difficult ones to get to do it.

Mr. ADAMS. Of course, we have to be careful. One of the risks in intervention in the economy is to provide support where support should not be provided. Some companies are lagging simply because in a competitive world some people come out on top and others for reasons of lack of entrepreneurship, lack of efficiency, high costs do not come out on top, and we want our economy to operate in such a way that we provide incentives but not that we protect the inefficient.

This is true with regard to an investment tax credit, this is true clearly also with regard to international trade policy and protection. We do not want to protect industries that are not modern, that are not efficient. We want to provide the incentives for modernization and efficiency.

I think one point can be made and it comes directly under what you are suggesting, is that in order to take advantage of investment tax credits, you must be making profits and paying taxes.

Senator BENTSEN. Let me ask you about your statement. You say we have plenty of capacity, our inventory is about right, yet we sure need an investment tax credit. Explain to me that kind of a statement.

Why do we need all of this investment tax credit if we have plenty of capacity?

Mr. ADAMS. I think what we do need is to look ahead. The question that I think my colleagues and I have addressed ourselves to is on the one hand the need for demand and stimulus in 1978, and what we are saying is we have capacity enough so we can stimulate the economy so we can put in place new capital equipment.

I think the second point we are looking to is into the future, 1979, when I think we will need that additional capacity.

Senator BENTSEN. You don't want a repeat of what we had in the early 1970's, where all of a sudden we end up in short supply in various commodities or manufactured goods and which begin to give us a problem. Is that what you are trying to avoid?

Mr. ADAMS. That is what I am trying to say. Furthermore, I would like to make a second point that you will note that again and again we hear about the lag in productivity, in the growth of U.S. productivity.

I think that is very closely related to the lag of investment.

Senator BENTSEN. That is part of modernizing America. When you talk about capacities, another point is how effective and efficient that capacity is. One of my concerns is with the problems of the Northeast in trying to modernize their capacity.

When we talk about the investment tax credit and accelerated depreciation, I don't see much support from northern businessmen. Some of them say to me, all that does is help the sunbelt. Doesn't that help them modernize their plants if they will utilize them?

Mr. ADAMS. Yes. I think that the modernization is an essential element and the investment tax credit goes in the direction of providing support for modernization. And it is clearly a problem that is nationwide, but it is clearly a problem that is most apparent in the older industrial areas in the Northeast.

Senator BENTSEN. For years I have heard Congressmen say that we don't have to worry too much about Federal deficits because in fact we owe it to ourselves. But I hear a different story now because we don't just owe it to ourselves now, do we?

We have a lot of foreign investors coming in here now and much of our debt is owed to foreigners. Isn't it a real concern if we continue deficits of this magnitude?

Would one of you speak to that?

Mr. CARLSON. It is true that about $20 billion of our additional debt is picked up by foreigners each year and probably going over $100 billion at the present time, so it is no longer owed to ourselves.

For this phase in the economic recovery and also being concerned about the funds flowing to foreigners, one would have to be concerned about continuing with the $60 billion deficit in future years.

It turns out the President's proposals on taxes will make the tax system more progressive so taxes will grow much more quickly from inflation or from real growth in the future so moving toward a lower deficit becomes relatively easy compared to the past.

So I think, personally, this coming year that $60 billion deficit is not going to be all that out of line, though we like to see it come down somewhat and have it come down through spending not increasing quite so much.

In 1980 and 1981, you have to be concerned about it on both accounts.

Senator BENTSEN. I would like to add for the record that we have checked the investment tax credit and it is definitely applicable to utilities.

Congressman Hamilton.

Representative HAMILTON. Thank you, very much.

Mr. Carlson, I want to have the privilege of quoting you on that deficit comment of yours before local chambers of commerce, if I may.

I think you said the $60 billion figure is not all that out of line, and that is not the line I usually get at chamber of commerce meetings.

Mr. CARLSON. We have fairly high surpluses in State and local government budgets at the present time and that is why that statement can be made. However, the trend downward is clearly the way to go with the expanding economy.

Representative HAMILTON. I appreciate that and I did hear the rest of your comment.

I was struck by the similarity to some degree in the testimony of Mr. Carlson and Professor Adams. You both said that the tax cut in the neighborhood of $25 billion, perhaps more, was appropriate, and all three of you, I think, put great emphasis on the need to encourage more investment.

It did seem to me, I noted some differences with regard to anti-inflation policy. Professor Adams, you spoke of wanting to encourage at least experimentally the type of approach called the tax base income policy. Mr. Carlson, you seem to suggest in your statement that the President ought to focus a lot more in his economic message on the inflation caused by the Government, and you seem to suggest that maybe we ought not to do very much with regard to prices and wages in the private sectors insofar as Government pressure is concerned.

I would like you to comment on anti-inflation policy, each of you a little more elaborately than you were able to do in your statements.

What really is right and what is wrong with the President's anti-inflation policy? What do you think we ought to do that we are not doing?

Mr. ADAMS. I think that you will find that I agree quite substantially with what Mr. Carlson said. I did not make a special point in my statement about the Government policy impact on inflation.

I realize that some of it is unavoidable but it is terribly important for Congress to realize and the President to realize that many of the regulatory measures which have been imposed on the economy do have inflationary impact.

It may be that we want to carry them forward anyway. We need an energy policy and I, for one, would stand behind energy policy even if it does have a modest inflationary impact, but we must recognize that it does and we must measure the tradeoffs.

I must confess that I am very skeptical of voluntary price wage guidelines or whatever you may call them, it is no longer fashionable to call them guidelines, but whatever we call them, I am very skeptical that they lead anywhere, and I am even more skeptical of price-wage ceilings or freezes or anything else.

Representative HAMILTON. How do you use a tax base income policy experimentally, what is your idea there?

Mr. ADAMS. There are a number of possibilities. One possibility would be simply to begin with a relatively modest program, and to see if it works.

Representative HAMILTON. But apply it across the board, put it into our tax policy?

Mr. ADAMS. Yes. I think, probably, you would want to do something across the board. You don't have to. There are ways of experimenting in particular industries. I think it is time to consider the alternatives on such a program very carefully, and I suspect we will find that it may do more good than harm, and it is certainly a step in the direction of trying to keep down prices and wages.

If we do not provide appropriate incentives we will not bring the inflation rate.

Representative HAMILTON. Mr. Carlson.

Mr. CARLSON. On that approach, I think Gardner Ackley has an article out showing the great limitations on the Henry Wallich proposals in that direction. In fact, they are going back to a phase II type of operation that we had in our mandatory wage and price program during the early part of the 1970's.

I share the view that wage and price controls do not bring down long-term interest rates and only momentarily reduce short-term rates. I talk from the standpoint of having been a deputy member of the Cost-of-Living Council during the early part of the 1970's and involved with the guidelines in the late 1960's when I was with the Council of Economic Advisers.

Table 11 in any prepared statement shows the inflationary impact of Government policies just in 1977 alone. The first five items, and really the last four items that are the cost-push elements, the minimum wage, social security taxes, farm support, Federal pay increases, show the resulting significant increases in cost-push inflation. I also would like to draw your attention to the energy taxes that are still being considered and what the cost-push elements can be there.

Clearly, the new inflationary pressure we have now is coming from government and to use the private sector as a scapegoat by setting up a voluntary wage and price control program and shifting the spolight in that direction is, I think, taking our attention away from an area we should work on.

Representative HAMILTON. What bills coming out this year do you think have a potential inflationary impact?

Mr. CARLSON. I have identified the ones I could measure. The energy taxes you are now considering will obviously have an impact, the deregulation of natural gas will have far less of an impact over the longer run than continued regulation of natural gas, the cargo preference if that should come up again this year, labor-law reform, just to name a few.

And in the case of regulations, the new regulations on trucks will undoubtedly have a cost-push inflationary pressure there as well as many other regulations.

Representative HAMILTON. The President's economic message actually seemed to me to have a pretty good balance on this question of inflationary policy. He emphasized quite a bit the same points you are making about the impact of regulation on inflation as well as his voluntary program of restraint.

Both of you seem to reject that approach outright. There is just no sense in fooling around with it, is that right, as an anti-inflationary policy?

Mr. ADAMS. Well, rejecting it outright may be putting it more strongly than I would. I don't think it will do very much for us and it has not in the past and it is hard to visualize why it should do more for us now than it did in earlier periods.

Representative HAMILTON. You feel very much the same way, I take it, from observations?

Mr. CARLSON. Yes; and I think it sets up an incentive system to move toward more controls and the people involved in making recommendations in this area have testified before the Congress that they support prenotification as well as more controls over the private sector so I think once you start focusing on private sector price movements, even if they represent Government imposed costs, they are going to come through wages and prices and consequently people will ask for more controls, not less.

So we are moving down toward more mandatory wage and price controls and I think the payoff is very small. The President has said that he is opposed to regulations that do tend to cause costs to go up. However, if you look not at the rhetoric but at his budget proposals, he is talking about 25 percent increases in some of his regulatory authorities and clearly he is very much pro additional regulation, not antiregulation.

Representative HAMILTON. The chairman was suggesting this too, when you do bring up a new deregulation bill the opposition to it comes from industry and labor, that is true in trucking, the airlines, in the railroads.

The push for deregulation of those industries is coming from Government, the push for maintaining regulation is coming from the private sector.

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Mr. CARLSON. I was really talking about growth in regulations, 25-percent increase in some of the budgets is growth, not talking about deregulation or actually having negative growth. Clearly, the transitional problem is a key one and if one can find transitions to a more competitive situation and make those transitions over a longer period of time it would be more helpful.

Representative HAMILTON. My time may be running out, but I did not notice any comments on the crowding out problem we have heard about a lot in Congress.

Do you foresee that problem in 1978, and if you foresee it, how serious a problem is it? What if the tax cut is larger than the President's proposals, then are we going to run into a crowding out problem?

Mr. ADAMS. We do not really see a crowding out problem in an economy where we are operating significantly below full employment and full capacity. To a substantial extent the crowding out problem represents a shifting of financial flows which I believe our economy is able to accomplish.

Mr. CARLSON. Let me just add to that, Congressman. I think the threat on crowding out is not large but there will be some as the year goes on, and one analyst, Henry Kaufman, has presented figures that suggest some risk later on this year. Instead of going with a higher deficit with a larger tax cut, it would be better to hold down spending so the deficit isn't trending upwards. Either to have the spending plateau or trend downward during the next 2 years would be a preferable policy.

Mr. ADAMS. The problem is known as disintermediation. That is a very specific situation which means that given the kinds of interest rate ceilings that apply in the world of banks and savings and loans, we still face the problem that when interest rates go up the financial flows shift, and they shift out of the channel of the savings and loans in mortgage finance into other parts of the economy, and that, I think we agree, is a very real risk in the course of the next year if we have high interest rates and tight money.

Senator BENTSEN. Congressman Brown.

Representative BROWN of Ohio. Thank you, Mr. Vice Chairman.

I want to cite a possibility which I know is not exactly what has happened, but it is an example and I would ask you to respond to it.

Inflation has pushed income levels up and increased the marginal tax rates as income increases. We have that little bonus built into the Government tax system. The President has proposed cutting the lower income tax rates so that the incomes of those people who will have to pay nothing will be higher, if you understand what I am saying.

I said that badly. The nontaxpayers' income will edge up. That has been historically true. Now it seems to me that if the Government increases its spending, even though we have not always covered it with traditional taxes, what we have is a situation like this.

Some years ago, $10,000 incomes paid 10 percent taxes, and now those people are making $20,000 a year and they are paying 20 percent taxes on the $10,000 of income between $10,000 and $20,000.

What is the impact on that in terms of the growth of our society with reference to its productive facilities and its consumption patterns?

Is it healthy for us or is it a depressing or unhealthy aspect? Could each of you comment on that? Do you understand my question?

Mr. SHAPIRO. I believe I understand the question. As I understand it, we do have, if nothing else, changes due to this increasing tax burden just as a result of inflation since we make no correction in our tax rates as inflation increases.

Representative BROWN of Ohio. It is more than that. We have made a correction at the bottom end. We have been dropping people off at the bottom end. It is my contention that we haven't been dropping them off as fast as, perhaps, we should have to keep up with where we were back in 1936, say, when the income of the average family was, maybe, $3,600 a year and they didn't pay any taxes.

Now, the overage income family, I think, is around $12,000 or $13,000, and that family does pay taxes. So we haven't been quite keeping up on that end but we have been getting the tax to an increasing degree from the middle class at a much higher rate than we did formerly, if that is clear.

Mr. SHAPIRO. First of all, let me indicate that my response—this really doesn't have a big impact on the current economic situation over the next year or so but it may have a substantial impact as you look at the basic structure of the economy for a longer period of time.

My own view is that it is really quite appropriate to consider adjusting tax rates in some way so that this extra bonus, as you have indicated, does not flow into the Federal Treasury.

Now, I think we do have a significant problem here with the group of our population you have identified as the middle class, because as you get further up the income scale there are so many provisions built into the income tax laws that in my opinion people at the higher levels of income are able to ameliorate this kind of increase through deductions and so on.

So, it is a problem. I don't think it has had a significant impact on the economy to date, but it will have if we are interested in long-term adjustments.

Representative BROWN of Ohio. I assume there is an impact. It has been referred to as the middle-class poor by some people. You are suggesting that the upper income levels—I don't know where that begins in your mind; if you can quantify it in dollars, I would appreciate it—can escape the impact of the higher marginal tax rates, but what about the middle income people?

Your version of middle and my version of middle might not be square, so if you could tell me where you divide the line between middle income and upper income, it might be helpful.

Mr. SHAPIRO. I don't know where to draw the line either, but if we drew it at $35,000 or something like that in today's prices, maybe that would be where it is. I don't want to argue over that.

I think it is true that the middle income people are taking a bigger share of the tax burden and that is what has happened and I guess if you are asking just what the impact of that is, I think, myself, that it adversely affects the incentives in that area, incentives and attitudes toward work and so on, but these are longrun changes.

I think they are only happening very slowly and I don't think there has been any very significant impact so far but I think if we continue to operate in this way, it is likely to occur over some period of time.

Representative BROWN of Ohio. How long would you say we could operate on that basis?

Mr. SHAPIRO. In a serious way, probably 10 years, 10 or 15 years.

Representative BROWN of Ohio. Mr. Carlson.

Mr. CARLSON. Obviously, with inflation having the same impact on the progressive tax structure as real growth and inflation representing two-thirds of the growth of receipts and real growth, maybe one-third, it makes it easier for government to grow than it did before.

For every 1 percent increase in inflation you get 1.55 percent increase in personal income tax receipts from the Federal Government, so it can carve out of one's hides some real resources, not just talking of the margin. So, it encourages government growth.

Second, you do have the fiscal drag problem, you have to worry about the need for tax cuts or encouragement of huge increases in spending each year now instead of over a longer period of time. Third, more resources are going to the government. The government is generally going for consumption as opposed to investment, so you are tending to slow down the growth of your economy and become proconsumption oriented instead of proproduction.

Representative BROWN of Ohio. Do you have any way of assessing the impact on individuals? You have given me the macro impacts as you see them but what about the micro impacts on the individuals?

I understand that is the nature of the studies Mr. Shapiro has done. Do you have any way to assess that?

Mr. CARLSON. The administration attempted to show the impacts at different income levels. However they just looked at the tax increases last year as opposed to total tax increases that are occurring from legislation from previous years and from inflation.

We can make an attempt to provide that for you, Congressman Brown, if you would like.

Representative BROWN of Ohio. But the real wages figure we have for the average worker and so forth, I would like to know whose real wages are most adversely impacted by this practice that Mr. Shapiro said we have been at in a serious way for 10 years, but in fact we have been going about it for some time beyond that.

In other words, I would like to have, not just the average, but to have it done at various income levels if we get the opportunity someday.

Mr. ADAMS. The exact number on that is something that can be figured out and should be figured out.

My reaction is that what really is happening, another way of describing the process is that we are in some sense changing the progressivity of the income tax and we are bringing in the process a larger number of middle class people into the areas of taxation where the marginal tax rates are very high.

Representative BROWN of Ohio. Do the Wharton Models take that into account?

Mr. ADAMS. Yes, the Wharton Model does take it into account, it does it quite explicitly. But the fact is that is something that is apparent as Mr. Shapiro pointed out only over the long run.

It may nevertheless be very painful and particularly to what you refer to as the middle class poor. It seems to me though that is an option which the Congress can do something about.

The Canadian model of adjusting the whole scale of income tax rates as inflation occurs is an appropriate way of doing that. There is no necessary reason why when inflation occurs we reduce taxes at the bottom of the end of the scale and not elsewhere.

Representative BROWN of Ohio. There is a good political reason which may or may not prove out.

Let me ask a final question. My time is up but just to complete the point, if the chairman will be generous enough with me, do you think the result of this higher marginal tax rate is that, let's say, the middle and upper middle income people actually tilt their spending and investment patterns in such a way that they really are reducing savings?

In other words, I mentioned to somebody that on our house out here in the suburbs, we have a very low interest rate. We picked it up when we first moved to town and we are beginning to get the mortgage paid off. One of my friends said, "Well, it is time for you to invest in a more expensive home." I thought it was a sort of ridiculous comment, because I don't think we need a more expensive home, and he said, "But at these interest rates and so forth you had better do that, or you won't have the tax shelters that you have had."

Frankly, that had not occurred to me. Maybe I am not sophisticated enough, because I don't think we need it. But can you suggest to me whether or not that is having an impact on people?

Mr. ADAMS. It is not at all clear. This is one of the things that needs to be looked into. It is not at all clear which way incentives are affected by these high marginal tax rates.

I tend to agree with Mr. Shapiro when he says work incentives may be reduced, but I am not sure. They may well be increased in the sense that in order to achieve a certain standard of living, you have to do more.

Similarly, it is not clear what happens to savings and consumption. For one, I think you will find, as you are suggesting that there is a substantial incentive under these circumstances to take on large mortgages and buy bigger houses.

Representative BROWN of Ohio. Which is consumption rather than investment, isn't it?

Mr. ADAMS. That is not clear in that sense.

Representative BROWN of Ohio. I can stay where I am and buy a rental property downtown to get income.

Mr. ADAMS. You will in a sense with a larger house have a larger flow of household services which you will be consuming. There is another side to it, though. There is a strong incentive to go into tax-sheltered investments and particularly into retirement plans which allow you upfront tax shelter on some of your income stream.

So, I am not at all sure what an empirical analysis would show as to how this precisely affects consumption and savings behavior.

Mr. CARLSON. Our small businessmen tell us that it does disadvantage small business because many of them are not incorporated and consequently, with a progressive, even more progressive tax on the personal income tax side, they become disadvantaged in comparison to where they were in previous time periods, so it tends to be antismall business.

Second, it does tend to discourage investors, at least the best one can tell through the surveys. In one survey that was completed by the Gallup organization, for consumers with incomes above $20,000 it was reducing their willingness to save and make those investments.

The third point, the higher inflation was one of the reasons why people tended to refinance their homes last year to gain additional funds to make expenditures either on cars or other items they may have wished to have spent on, and our measure of savings was inaccurate because it didn't measure that phenomenon.

So people are tending to get additional funds now to spend, and quite clearly last year it was primarily for consumption, not for business fixed investments in any case, be it either housing or consumption for automobiles or others that occurred with additional funds that they did raise through that technique.

Mr. SHAPIRO. We have tended to do some studies precisely on this problem, looking at individual households.

Over the last 10 or 15 years, sort of an interesting result comes out of that. One is that, if you look at only men, you seem to find the kind of effect that has been suggested here that there is some disincentive to saving, some disincentive to invest in further training and invest in human capital.

However, if you look at the household as a whole, you don't see those effects because there is greatly increased participation of women in the labor market.

It's very hard. We have found that we cannot separate out these effects very easily and satisfactorily yet to give you a clear answer to your question. So we are still somewhat puzzled about it, but I would be happy to supply you with what we have found so far.

Senator BENTSEN. Senator Javits.

Senator JAVITS. Thank you.

Gentlemen, I am sorry I was not here for your testimony. I had to attend another hearing.

I have been briefed on what you said. I would like to focus on one question about the President's tax cut: Is it misdirected?

First, I notice that you all agree that there should be a tax cut, notwithstanding the material increase in the deficit. What troubles me is, should we even have a tax cut if it is not going to be targeted to the problems?

The 10-percent investment tax credit is a tax credit only if you make money. Should it be refundable? In other words, should the tax credit represent a rebate even if you don't make money because you have reinvested it to stimulate your business?

Would you try your hand at that, Mr. Carlson?

Mr. Carlson. Yes, sir. I think with carryforward and carryback provisions, the investment tax credit should not be made refundable. However, I do agree with my colleagues that it's the investment side that is weak, disproportionately investment stimulus should be provided at certainly not less than the one-fourth the President has provided.

To be specific about your general question, antitrade provisions for DISC and deferral, I think they should be deferred until a future year when the trade deficit is not so great, and then, too, I know you are concerned about the deficit.

I would argue for holding down the rate of increase of Government spending and going for the healthy tax cut as a preferable route and thereby not letting the deficit get out of hand.

One last point in an area that is of interest to you, I do think with the increase in minimum wage and the increase in social security, we have made people unemployable. As a result, we have a larger number of structurally unemployed people we have to do something about.

If Congress is not willing to go back and provide a youth differential on minimum wage and other things, then the second best approach is Congressman Ullman's approach of maybe having an employment credit given for structurally unemployed people and limited to that group, and let's get these people employed in jobs that have a future, not dead-end public sector jobs.

Senator Javits. I have already introduced a bill to that effect. I would appreciate your studying it and expressing your views on it as a targeted use of tax-cut money.

I ask unanimous consent, Mr. Vice Chairman, that if there are any replies of the witnesses that they may be made for the record.

Senator Bentsen. Without objection, so ordered.

Senator Javits. I also introduced a bill for a subsidy to go through the Community Development Corps. for businesses which they engage in, in order to break youth into the employment process. I am one of the prime opponents of a youth differential in the minimum wage because I believe there is no reason for breaking down the wage structure in order to accomplish what targeted subsidy and tax credits will accomplish. Therefore, as an old friend of mine used to say, "There is a right way to do right."

I am not against using the money, but I see no reason for breaking down the total wage structure when you should do what needs to be done and what can be done without it.

The other question I would like to ask: Would either of you gentlemen like to comment on what Mr. Carlson testified to as to the investment tax credit?

Mr. Shapiro. I would certainly support the comments on the investment tax credit. My own view is that it ought to be increased.

Senator Javits. Increased to what? We have to be very specific.

Mr. Shapiro. Fifteen percent. I think that would be highly beneficial because investment is lagging so I would certainly support those comments of Mr. Carlson.

Senator Javits. What about refundability?

Mr. Shapiro. I am not in favor of refundability.

Mr. ADAMS. I do think the investment tax credit is very important. I am not in favor of refundability. I am in favor of increasing it to, say, 15 percent. I think that the tradeoffs should be in favor of more direct stimulus to investment such as investment tax credits and/or accelerated depreciation, as against across-the-board changes or reductions in the corporate income tax rate.

I think it is the investment tax credit that gives far more bang for the buck. I think we should look very carefully at the industries in our economy, recognize that some of them have lagged behind and are desperately in need of modernization, recognize that some of them have been badly impacted by Federal regulations with regard to pollution control and with regard to safety, recognize that certain ones, energy, is very important for the long-run growth and development of our economy, and we should provide special incentives.

Some of them, by the way, are in a fourth category, which is equally important, and I think everybody would agree with me, those that have relation to the big cities and the rebuilding of the urban economy.

It seems to me those preferential areas should get preferential treatment with regard to investment tax credit. That is terribly important.

The second thing, I would like to join in supporting what you have talked about, which is a subsidy for employment. I think that here we ought to seriously think about a nationwide apprenticeship program in private industry.

I understand in other countries, in Germany, for example, apprenticeship is a widely accepted, highly effective means for taking kids who do not go on to university education and providing training and the kinds of skills that are needed in private industry and business. Part of a subsidy employment might be an organized apprenticeship program that is targeted on these kids who need additional training and development before they are going to be useful employees.

Senator JAVITS. Mr. Adams, you touched a very sensitive point with me. I think it is ridiculous that we have 1 million apprentices in this country when we should have 5 million. The reason for this gap ranges all the way from nepotism to a violation of the antitrust laws in spirit, if not in fact. This problem is terribly hard to solve. I doubt that it can be done within the time parameters allowed us—not because I don't agree, for I thoroughly agree with you, but I have been beating this drum for years, and you can see how little has been accomplished. As a result, I have had to join in the more liberal investment tax credit and subsidization of tax credits for employment routes.

You are absolutely right: We are voices in the wilderness until there is some trade union leadership that says the best interest of the trade union movement is in expanding its youth base.

Union leaders are crying about the fact that they are losing members, but what are they doing about getting new members—except for the effort to organize more intensively? It's a sad picture, I assure you.

I would like to ask you gentlemen one further question. Do I gather that, in terms of the 15 percent nonrefundability and carryback and carryforward, we have a fair consensus of view among you?

Mr. CARLSON. I think, given the political realities of how much tax cut could be given, I would say something like 12 percent is what you would look at.

Senator JAVITS. I want to ask you about that figure, particularly because I was one of the most ardent defenders of the ADR when the rate was increased. I believe in it thoroughly. I believe in the Swedish system where you can charge it all off the first year if you want to, because I think the rate of obsolescence of capital stock is occurring at a great rate in this country. I think we are falling behind in terms of plant and equipment very rapidly, which is why we are "in the cellar," as they say in baseball, on productivity.

I can assure you, as liberal as I am—and I am—I am appalled by the erosion of America's strength in productivity; that's the real McCoy.

Therefore, I would like to ask, if you feel strongly about the depreciation allowances, why doesn't the chamber of commerce step up to bat? I don't sense that the Chamber feels so strongly about them.

Dr. CARLSON. Our small business council came down very strongly, I identified in my testimony, on liberalizing the ADR rate which would be helpful to small business as well as large business, and we very strongly support that.

Senator JAVITS. Can you suggest any other proposals that we could implement, because I will carry the ball for them in the Senate even if I am defeated?

Mr. CARLSON. We will be pleased to do that.

Senator JAVITS. My time is up. I thank you gentlemen for this.

Senator BENTSEN. Congressman Brown.

Representative BROWN of Ohio. It has to be a great deal more serious than that if Senator Javits is willing to go to defeat.

Thank you, Mr. Vice Chairman.

Let me pursue one question, Mr. Shapiro, because I am fascinated by your confidence surveys, but I want to get more precise answers from you on a couple of things.

I have had contacts over the last few weeks with several foreign politicians and businessmen, some from overseas, some from the Western Hemisphere.

The message I am getting from them is not quite as severe as the message that Michael Novak wrote in his column about the President last January 31. But it was that the decline of the U.S. dollar abroad in its relationship to other currencies is made up of a number of things. One, it is, of course, our trade balance and the specific dollar relationships of exports and imports. Another one is confidence in the administration or in the President personifying the administration, and in a very real sense personifying the will of the whole country in some of these areas. And then divide that confidence into two separate aspects. One is his inability, apparently, to get some of his programs, as they originally were enunciated, through the Congress—the energy program is one recent example—and the second one is a lack of confidence in the programs as enunciated.

If he got through a program they viewed as bad, at least they would have some confidence in his ability to get programs enacted, which might balance things out. But the failure to get bad programs passed is a double whammy on confidence.

My question is: In domestic confidence polls such as you conducted, Mr. Shapiro, do you take readings on any of these aspects of leadership, and people's viewpoints about the programs, as well as the economic impact of what we were just discussing in my last round of questions about the marginal tax rates having a depressing effect on investment and a stimulating effect on consumption?

Mr. SHAPIRO. Yes, we asked specific questions regarding attitudes toward confidence in Government and Government programs. We do not ask questions about specific programs, but we ask questions about performance of the Government, and our experience is that, as in the latest surveys, we have noticed when we ask questions about consumers' confidence in the long run—in their long-run financial position—that that is directly related to their confidence in the Government and the Government administration in particular.

We are finding in the November-December surveys, for example, that there is a significant drop in both the confidence in the Government and the confidence in their own long-run financial position.

When asked to explain this, they point exactly to the factors you just mentioned—the programs and the fact they can't be moved forward is really quite critical.

Representative BROWN of Ohio. This really is not a partisan committee, and I don't want to leave it as though my question were a totally partisan question. It occurs to me that lessened confidence may always occur about this time in a new administration. There is another aspect, I think, that goes into it, too, and that is not just the current attitude about Government, where the expectations are rising and falling, but perhaps the sort of long-range view of Government that has been declining or depressed over a series of events—Viet Nam, the Watergate, the fact that we had Lyndon Johnson a one-term President in effect; before that, the assassination; President Nixon resigning in disgrace, and President Ford not reelected to a second term. That all adds up to a negative attitude about Government.

I sense it in my mail. It is not just Government. It is Congressmen and everything else.

Could you quantify in any way the long-range viewpoints, the long-range confidence, the short-range confidence, and the economic impacts and give me a rough idea of what the percentages of those things are, how much of it is economic and how much of it is sort of general feeling of confidence?

Mr. SHAPIRO. I think I probably cannot quantify it in a way that would be a satisfactory response to your question. I will try, however, just one response, and that is, if we would have consumers today responding to our surveys that they held the same level of confidence they held in the mid-sixties, for example, in the Government, that the index of consumer sentiment itself would be rising rather than falling, that is, the index is made up of a composite of a number of responses to various questions and, if they were responding as positively on the issue of confidence in Government today as they were roughly speaking 10 to 12 years ago, the index would be rising rather than falling.

That is not directly responsive to all the questions you have asked, but I don't have that.

Representative BROWN of Ohio. It indicates to me that the long-range confidence factor may be dragging down the short-range, whatever that short-range is.

If I can, I would like to broaden this question a little bit into the more specifically economic area and ask Mr. Adams and Mr. Carlson to comment on this, and you are welcome, of course, Mr. Shapiro, to throw in your viewpoints on this.

From the early 1600's to 1888, the United States had a trade deficit, so there is nothing new in trade deficits, but during that time the dollar enjoyed great confidence because we were a rapidly growing nation, and our market was increasing and people were willing to extend us the credit and so forth because they always knew they would be able to catch up and get paid off.

Implicit in the President's energy program, as an example of a specific policy, and our zero population growth advocates, as an example of something that is in development, maybe not as a policy matter, but in terms of what is happening to our society, and our limited productivity as another aspect that seems to have developed in the last few years, it seems to me that foreign investors looking at our country might say it doesn't look to us as if there is going to be quite as dynamic growth in the future.

Could you relate those features and specific policies to this no-growth or underscaled growth syndrome which seems implicit in some of those things?

Mr. Adams. I would very much like to comment on that.

I think we can pick up from your earlier comment that, as seen abroad, the problems of the administration in presenting programs and in getting them through Congress have certainly imposed a burden on the dollar.

I think the first thing that must be done to try to stabilize the dollar is not just interest rates; it is to pass a reasonable energy bill, reach some agreement on it, and do it.

Clearly there is perhaps a lack of understanding abroad. I think we understand our economy better, and in some sense even though we are impacted by, and we are worried about, the problems of policy, we are still fairly content with the movement of our economy. It is not going to hell in a handbasket.

Now, indeed, I think we ought not be overwhelmed by trade deficits and by slow growth. As compared to the rest of the world, we are doing astonishingly well and, moreover, there are a fairly large number——

Representative Brown of Ohio. Quantify that in time, will you? We obviously are not doing as well as the German economy or the Japanese economy over a period of the last dozen or 20 years, but in terms of the recovery of the recession, we are doing better; is that what you are saying?

Mr. Adams. Yes. But I would go on to say I think that even over the next 10 years, we may do as well or better than the Germans, for example. Remember that these are economies that had a recovery after World War II that began from scratch. They began with modern industry. I am not at all sure that in the long run we will do less well than they do. We certainly have a potential to do as well as these economies.

Representative Brown of Ohio. Isn't it true that those economies are somewhat different from ours in that they are built heavily on foreign trade and have become, as England once was, the manufacturing center for vast geographic areas; whereas our vast geographic area is almost entirely domestic?

Mr. ADAMS. That is certainly true. But again, and obviously it makes a big difference. They are oriented toward seeking out foreign markets, toward designing their products for foreign markets. We are not.

But I want to stress the fact that it is very easy to say American industry is not competitive. We are lagging behind, but I want to stress the fact that were it not for a deficit on oil of $40 billion, our trade balance would be in surplus. All other industries are showing a net plus.

If we look at our aircraft industry and our computer industry, it's very efficient, and an extremely important element is that many foreign firms are buying into the American economy, perhaps at bargain prices. Many foreign firms are beginning to manufacture in the United States because they find it is cheaper to manufacture here.

The rough approximation I had heard was that the wages are higher in the United States, yes, but productivity is sufficiently higher to offset the higher wages.

I, for one, don't underestimate the productivity of the American economy now nor do I think we should underestimate its probable long-run growth.

Senator BENTSEN. Mr. Carlson, before you respond, I understand Professor Shapiro has to catch an airplane. If that is the case, you are certainly excused, and we very much appreciate your testimony this morning. Thank you very much.

Mr. SHAPIRO. Thank you.

Mr. CARLSON. Let me add to the comments. The United States is a good place to invest, will be for the foreseeable future; the forecasts show that our trade partners abroad, especially West Germany, Japan, and other European countries, will not grow nearly as much during this period of recovery as they have in other recoveries and the United States will do very well.

If you will look at graph 4, in my prepared statement, you will see what a fantastic job the United States is doing in creating jobs and will continue to do in relation to other countries.

As with economies that are oriented toward foreign trade, clearly they have an adjustment problem, and they will have to look inward more toward orienting their futures.

The third point I would like to make, on business confidence. You talked about consumer confidence—we have also taken a survey of business confidence. The business confidence is very low, 20-percent chance of recession within the next 12 months, 50-percent chance of recession within the next 24 months was the view last October and November when the survey was taken. However, 5 years out, one-third of the businessmen responding expect to have good times, one-third neither good nor bad, and one-third bad times.

So the outlook over the longer run is actually better than it is over the shorter run.

Another point, when we asked them about Federal Government economic policies, what did they expect during the next 12 months, only 1 percent said good policies, and we had something like 40 percent who said the Government was doing only a fair job, and roughly 60 percent who said the Government was doing a poor job with its economic policies.

I think business confidence is very much tainted by the policies that were debated or passed. They think they tend to foul up the economy, and high on their list are Government regulations, even before Government taxes, as causing them more concern, especially as Government talks about changing them or actually does change them.

Representative BROWN of Ohio. I do think that is significant. I have to say I was at Harvard Business School, however, in the 1948 election, and they took a poll of who was going to get elected, and according to that poll, I think 93 percent of the population would vote for Thomas Dewey, something like 4 percent would vote for Strom Thurmond, there was 1.5 percent for Henry Wallace, and Harry Truman got 0.5 percent; the other percent was undecided.

So I am not sure that the business confidence reflects totally any more than the consumer confidence where we are headed, although it does impact on investment and upon commercial activity; so more clearly maybe it does have a more significant impact.

There is one thing I want to ask the whole group, and I hope we could get the staff to write to Mr. Shapiro and ask him this question. I would like to have some idea of when the zap that I think we are going to get from social security taxes is likely to be felt. The political zap is being felt now by some of us.

In their questions at home, they were beginning to understand there was a social security tax increase passed, and we are getting a lot of nasty questions; I fortunately am able to answer them in a very positive way because my vote was negative. I want to know what the economic impact of the social security tax increase is likely to be and when we can expect it.

I am under the impression that the sociological impact may be now but the economic impact may not be until later this year and next year, and I don't ask you to comment on this now, but if you could send us a written note or some figures or something on it, I would like to get that.

Senator BENTSEN. Thank you very much.

Gentlemen, we thank you for your appearance.

This concludes the hearing.

[Whereupon, at 12:05 p.m., the committee recessed, to reconvene at 10 a.m., Tuesday, February 7, 1978.]

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