

For Senator Humphrey

Business and Government



FOURTH ANNUAL REPORT
to the PRESIDENT *by the*
COUNCIL *of* ECONOMIC
ADVISERS • *December 1949*

For Hubert H. Humphrey,

Whose ever-increasing
capabilities are bringing him
ever-increasing opportunities
for service to his country & to the
world

Business and ^{Sec. of Defense}
Government ^{Atlantic City}
August 27, 1969



FOURTH ANNUAL REPORT
to the PRESIDENT *by the*
COUNCIL *of* ECONOMIC
ADVISERS • December 1949

Additional copies of this report are for sale by the Superintendent of Documents,
U. S. Government Printing Office, Washington 25, D. C.
Price of single copy 15 cents

Letter of Transmittal

COUNCIL OF ECONOMIC ADVISERS,
Washington, D. C., December 27, 1949.

The President.

SIR: The Council of Economic Advisers herewith submits its Fourth Annual Report in accordance with the requirements of Congress as set forth in the Employment Act of 1946.

Respectfully,

Leon Keyserling

Acting Chairman.

John D. Clark

Contents

	Page
I. FREE ENTERPRISE AND FREE GOVERNMENT	1
Communism, socialism, and the American system	1
A new generation needs new ideas	3
II. TRENDS IN GOVERNMENT'S ATTITUDE TOWARD BUSINESS	5
From theory of stagnation to practice of growth	5
From "more for some" to progress for all	6
From social theory to economic "balance"	6
Toward mutuality of interests	9
Regarding business size and practices	10
From mere policing to affirmative facilitation	11
Away from specific controls	11
From "compensatory" theory toward more reliance on enterprise. And a word about Keynes	12
III. TRENDS IN THE ATTITUDE OF BUSINESS TOWARD GOVERNMENT	14
Gains through businessmen in public service	14
Improved appreciation of public policy	15
Rejection of mere slogans—the pension example	15
Enlarged understanding of world conditions	16
IV. FURTHER NEEDS IN GOVERNMENT ECONOMIC POLICY	18
Need for further harmony and consistency	18
Need for more stability	19
Need for correlation of welfare programs, especially social security, with general economic policy	21
Coordination of national economic policy is not "central planning"	23
V. FURTHER NEEDS IN BUSINESS PREPARATION FOR STABILITY AND GROWTH	25
Further acceptance of "maximum" objectives	25
Further realization that public sentiment affects the economy	26
New business attitude toward "politics"	26
Can business action achieve sufficient concert to promote stability?	27
VI. FOCAL POINTS FOR ECONOMIC STUDY	29
The processing of facts	29
Forecasting	31
Defining objectives	32
Policy making	34
VII. RECENT DEVELOPMENTS IN COUNCIL OPERATIONS	36
Work with private economic groupings.	36
Work with governmental agencies	37
Relations with the Congress	38

The Council's First Annual Report to the President discussed the political philosophy of the Employment Act of 1946 and the economic philosophy of sustained employment. The second dealt with the meaning of maximum production and the means of attaining it, and the third considered the environment within which the Council operates. These three efforts brought indication that revelation of our general economic thinking was appreciated. They also provided background for the Economic Reports of the President and the Economic Reviews by the Council, which appear in January and July of each year. In this Fourth Annual Report, we discuss the relations between business and government because we find this subject of significance at all times and close to the forefront of general interest now.

We use the term "business" to refer to business management, recognizing that our system of free enterprise includes also workers, farmers, consumers, and their organizations. They equally are confronted by the system's problems; they too are responsible for its achievements; they too have dealings with government and are concerned about public policy. Before long we hope to discuss their relations with government.

I. Free Enterprise and Free Government

COMMUNISM, SOCIALISM, AND THE AMERICAN SYSTEM

The balanced emphasis which the Employment Act places upon the merits and responsibilities of free enterprise and free government is typically American and yet of universal import at this midpoint in the twentieth century. In the last century the philosophic base was laid for extremist doctrines that these two freedoms were irreconcilable, and that one or the other would give way under the impact of industrial concentration, disparate wealth, and popular communication. More recently, these extremists rose to command in many lands. On the right, powerful economic groupings allied themselves with counterrevolutionary movements to destroy free government. On the left, powerful statist revolutions swallowed up free enterprise. We now know how similar are the weeds growing from these different seeds, and how their pollen stifles genuine economic progress, intellectual inquiry, and spiritual aspiration. These manifestations create international problems. But they do not require much analytic annihilation because they make no appeal to the minds or hearts of the American people.

Then there are the current efforts by other peoples with a long tradition of democracy to combine free government with very substantial diminution of free enterprise. In our view these other free peoples will approach their own special problems according to their own needs or beliefs; but our problems are not theirs and we have different methods which are all our own.

During the nineteenth century there were many thinkers even in the United States who, appalled by the prevalence of poverty in a land of plenty and by the crude manifestations of industrialism in the raw, argued sincerely that neither our people nor their government could remain truly free so long as business enterprise remained free. But there are powerful reasons why this thesis is no longer given serious consideration. Although many of our problems remain unsolved, our unique combination of free enterprise and free government has moved so rapidly toward raising the general standard of living that the fair hope of more progress by the same methods immensely outweighs the costs and risks, the divisions and tensions, and above all the uncertainties, of radical change. All history shows that freedom in the long run may best be safeguarded through moderation in the adjustment of seeming conflicts. And the American system is so fortunately situated that it furnishes to the world a beckoning example of this kind of moderation.

The case for moderation grows in appeal because, whatever the situation in other lands, the only conditions which could seriously undermine free enterprise here would also jeopardize free government and possibly do it irreparable damage. In sober retrospect, not even the great depression of the 1930's altered the basic character of our economic system or reduced the commitment to it by the people and also by our most "advanced" philosophers, economists, preachers, and other social thinkers. It follows that nothing less than another depression even more devastating could break us away from this basic commitment. And any such economic convulsion could unleash forces of social tension, domestic friction, and pure political adventuresomeness which might leave us for a time without the essence of free government. Thus, those whose concentration of interest is upon free enterprise and those whose concentration of interest is upon free government are held together by unseverable bonds. No genuine liberal—and most Americans call themselves that—would welcome an economic crisis in order to have a chance to remold the economic system nearer to his heart's desire. We all know what happened to the liberals elsewhere who waited for or courted that opportunity and got totalitarianism instead.

Many of our domestic problems revolve around the application of moderation, compromise, and reconciliation in defining the respective rights and responsibilities of free enterprise and free government under a popular democracy. There are many ways of stating this root issue. How can enterprise remain free enough to be dynamic without

moving from freedom to license? How can government be strong enough, as Lincoln said, to maintain the essential interests of the people without invading their liberties? How can stability be equated with growth? Liberty with law? Individualism with cooperation? How can we steer between the dangers of absolutistic freedom and the deadliness of absolutistic security? However put, these questions involve business and government and seek to broaden their areas of agreement and to strengthen their complementary interactions.

Nobody can resolve this omnipresent issue with a single formula, symbolism, or definition. But there is room for a broad effort to formulate or restate a philosophy of the relationship between business and government. A philosophy voices that agreement on a few fundamentals, alive in the minds of the people, without which there can be little unity or progress. Without universal accord in America about free speech, for example, we could not benefit by debating our disagreements about so many other things. In our economic life no less than in our political, there is need for some common philosophy to hold us together; and since constitutions and courts are not so well suited to this purpose we must resort to the voluntary projection and constant cross-fertilization of ideas.

Economists may take some initiative here because economic problems occupy or even overcrowd the stage on which the drama of adjustment between business and government is going forward. And this Annual Report of the Council to the President is a convenient location for such discussion, in contrast with the Economic Report of the President and the Annual Economic Review by the Council (both scheduled for early January) which must necessarily be steeped in facts and particularistic points of policy.

What we now say is by definition general. Logical deductions from it will not reveal the content of specific programs which may be proposed in 1950 or any other year. Nonetheless, it is our earnest desire that this report will have some influence upon attitudes both in business and in government, and that it may uncover the solid ground on which they can deal with each other in ever-increasing harmony and trust.

A NEW GENERATION NEEDS NEW IDEAS

The particular urgency of this subject exists because there has now grown to maturity a whole generation of Americans touched by the influence of extremists who look upon conflict between business and government as normal. Conditioned by the depression era, extremists on one side have said that our business system broke down through fatal defects and that government took the whole leadership in putting it together again; while extremists on the other side have blamed government for all the tribulations of business. The new generation of Ameri-

* The underlined² portions state the theme for moderation in 1964 no less than in 1949.

* The case against extremism in 1964 as well as in 1949.

cans should always remember that the breakdown resulted from errors on the part of both government and business; that both joined in forging some of the most practical measures for recovery; and that both must admit imperfection because the recovery was incomplete until the war restored maximum production and employment.

This new generation of Americans has also observed that some of the national programs directed toward economic change have initiated from government and been opposed by some spokesmen for business. But the extremists on either side should not overplay this observation to range either government or business along with the angels or the devils. Rather it should be recognized that it is a primary function of government, representing the whole people, to view the economy as a whole and to propose general measures. It is the function of business, as the main operators of the going economic system, to be conservationist if not conservative and to be wary about discarding workable machinery before better machinery has been clearly tested. In the interaction between these two functions, which is essential if we are to preserve both free enterprise and free government, the clash of viewpoint and the reconciliation of means to ends are in themselves beneficial, particularly when undertaken in good spirit.

We have now moved far enough away from the depression of the early thirties to start looking ahead, and to appraise the heartening evidence that free enterprise and free government have blended their varying strains into a rewarding effort. The conduct of the war was an example never to be forgotten. The moderate character of the 1949 recession, and the upward turn which followed, would have been impossible without business policies as well as public policies based upon greatly increased understanding of economic affairs.

The time has come to develop the prospects of the American economy for further economic progress and human happiness. Unlike other countries we were not decimated by war; we do not suffer from underdevelopment or impoverishment of basic plant and equipment; and we have the operational and financial skills, the splendid labor force, and the solid institutional structure to realize in full the promise of America.

The only thing that could stand in our way—provided that lasting peace is achieved—would be excessive internal discord. This would not stop our economic progress in the long trend, but it could slow it down greatly and leave us subject to costly fluctuations which we probably have the technical know-how to avoid or mitigate.

At this juncture, there may be value in a candid stocktaking of current relations between business and government. We shall place the greater emphasis upon the vast progress which has already been registered and upon the assets which have consequently accrued. But we cannot neglect some of the problems yet unsolved.

II. Trends in Government's Attitude Toward Business

The attitude of government toward business has always been favorable, in the sense that responsible public servants have always wanted our free enterprise system to thrive and prosper. The course of events shows that many of the public policies adopted over the years have contributed toward the strength of the economy, although they are always subject to refinement and improvement. Governmental thinking has never been static, and it may be helpful to try to discern recent trends under the impact of experience.

No one person can speak with absolute certainty or comprehensiveness about these trends. The minds of various men and women in our public service are not melted down and fused into a single instrument. Policies and pronouncements, even when by the President or by the Congress—and many others decide issues and make statements—reflect a range of training, temperament, and viewpoint as wide as those in any other sector of our national life. However, while the Council can speak only for itself, we believe that from our strategic point of observation we can detect a prevailing trend of thinking about our business system and its problems.

FROM THEORY OF STAGNATION TO PRACTICE OF GROWTH

The first trend in the attitude of government toward business seems to the Council to be this: the doctrine of secular stagnation no longer finds place in any important public circle with which we are familiar. During the depression years, a significant body of thought held that the forces of business expansion had spent themselves and that government must provide the dynamic force for renewed growth. The thought may have had some relevance then; and the persons who held it developed some useful devices. But today the doctrine of secular stagnation has been replaced, in our judgment, by the firm conviction that our business system and with it our whole economy can and should continue to grow. This is illustrated by the statement of President Truman that we can achieve a 300 billion dollar economy within a very few years. We regard it as an historic event when the occupant of the most persuasive office in the world acts upon the proposition that our business system has further opportunities which transcend even those it has seized upon in the best previous decades. A member

4
★ the respective complementary
roles of free enterprise & free govt.

5
★ Business & govt must progress
together
★ ★ Businessmen welcome this idea.

of the Cabinet, the Secretary of Commerce, has recently applied the same realistic approach over a longer time span.

This sentiment on the part of important officials would be significant without independent verification, because it would have a controlling effect upon their attitude toward the business world. But we also note the recent corroboration of these growth assumptions by non-governmental economists who are highly regarded by businessmen as being unusually conversant with their problems.

FROM "MORE FOR SOME" TO PROGRESS FOR ALL

A The second important trend which the Council senses in the attitude of government toward business is the realization that efforts to promote expansion of the total production and income of the economy are more significant than measures to "redistribute" the current product. In an economy foredoomed to inability to provide an adequate or rising standard of living for all industrious families, there might be some reason for according the resharing of output priority over efforts to increase output. The rationing resorted to by people in time of famine is an extreme illustration. But the notable expansion in production which our economy has achieved in the past and can certainly repeat or excel in the future, coupled with the observed fact that this so much lifts the general standard of living, should receive foremost consideration in economic programs and policies.

Of course, we cannot postpone efforts to improve the lot of the underprivileged until they can be lifted to reasonable levels by the lever of general growth. And measures directed specifically toward improving the productivity and incomes of low-income groups have favorable impact upon the whole economy. At the same time, primary emphasis upon general growth offers a more workable formula not only for the business community but also, the Council believes, for other groups as well. For once it is appreciated that the general growth of the American economy can create within less than a generation a truly good standard of living for all, then there is reduced to manageable proportions the ancient conflict between social equity and economic incentives which hung over the progress of enterprise in a dynamic economy.

FROM SOCIAL THEORY TO ECONOMIC "BALANCE"

The third important trend in the Government's attitude toward business, as viewed by the Council, arises from fuller realization that the flow of income to different parts of the economy should be viewed as an economic no less than a social problem. Certainly a people's ultimate objectives are social, being concerned with well being, and social thinking will never lose its utility. But the application of more precise

economic analysis to problems of income flow will yield benefit to all by reducing the problems of ways and means to soluble terms.

The use of economic analysis to refine and sometimes reformulate social theory will help to broaden the areas of understanding and agreement, without which the tensions and conflicts in a free economy of large organized groups might in the end become unbearable. That unsocialist George Bernard Shaw argued in one of his famous books written for American women that the only sound income distribution was absolute equality, since nothing else could be called "fair" in the absence of any precise measurement of the relative productivity or relative need of everybody in the community. While this is a *reductio ad absurdum*, it illustrates that contending individuals or groups in a free society could never arrive at viable agreements as to what share of national income each should get by the unalloyed application of social principles. Any effort to apply such principles fully or even excessively would involve the whole nation continuously in fracas and confusion.

Concentration upon the central objective of a stable and expanding general economy identifies more manageable although still difficult approaches to the problem of income flow. It then becomes possible, albeit not easy, for businessmen, workers, and farmers to seek that share of the total product which is most conducive to the progress of the whole economy and thus to their own best interests in the long run. The same approach should be used to evaluate those government programs which channel the flow of income from one spot in the economy to another, to test whether these programs promote general stability and expansion or rob Peter to pay Paul.

The nub of the problem of economic "balance" is to encourage sufficient funds and incentives for the growth of productive facilities which fully absorb our technology and manpower, while promoting sufficient flow of income to ultimate consumers to clear the markets of goods and thus to avoid periodic "overproduction." The Secretary of Commerce has put forward this idea of "balance" so cogently that it deserves repetition:

As we look down the road ahead, what do we see? Standing squarely and obstinately ahead of us on the road to a richer America is one great question mark. How shall we divide equitably among consumers, labor, management, capital, agriculture, and government their shares of our production? People are called liberal, radical, conservative, or reactionary depending upon the way they approach this most difficult of all our economic problems. Some pessimists say that there is no solution to this problem but the one resulting from the struggle between organized groups. They say that capital always wants more than its fair share of production, that labor will never be content until it takes all of the profit out of business, that farmers will not rest until all other groups are supporting them, that government officials will not be happy until they manage the whole economy and become the only privileged class in America. I am not so pessimistic. Many businessmen understand that business success depends upon well-paid, self-respecting workers and upon the ability of the public at large to buy what business produces. Many workers understand that business cannot operate at a loss, and that some return on capital

* a useful theme in 1964. Priority of growth for all over redistribution here or share the wealth.

* Really the theme of President Johnson.

investment is proper. Many farmers realize that other groups are entitled to consideration and that the farmer is not cultivating a fenced-off lot.

We have not yet reached the time when these groups forget their special interests and talk out their differences in a spirit of sweet reasonableness. However, we have made and are continuing to make progress. Most Americans now understand the importance of business investment as well as the importance of mass purchasing power. We have passed the time when intelligent Americans use the word "profit" as a curse. I believe all of us can agree on the fundamental principle that profit is good when it is reasonable and when it is used to produce more of the things we need.

To this problem we must apply the idea of balance. What division at any given time will promote the smooth operation and further the balanced growth of our economy? To answer this question we must know as much as possible about our economy and we must also be willing to abide by the facts. In other words, we should bring to the solution of our problem scientific analysis and a scientific attitude of mind.

When this general idea of economic "balance" is translated into the factual analysis which alone can give it practical significance, it becomes crucial that the business world appreciate the motivation underlying such analysis. We may illustrate by citing some of the previous work undertaken by the Council. During the postwar inflationary boom between 1946 and 1949, we took the position that the bunching of unusually high profits and an unusually high level of business investment, accompanied by price-income developments which did not seem to promise sufficient consumer demand to maintain maximum employment and production when certain temporary props were removed, should not be viewed with equanimity. This did not mean that we were adverse to profits or profit-makers or were throwing partisan weight on the side of the consumer or wage earner.

Such was not our position. We simply foresaw in 1947 and 1948 that the "balance" between investment and consumption, while compatible with a very high level of activity in 1947 or 1948, could not be sustained indefinitely and that a new "balance" would need to be struck for a growing peacetime economy. We were concerned that, as profits declined during the transitional striking of this new "balance," business might have become fearful and contracted investment and employment unduly. This would have accentuated the downward spiral. Instead, we urged recognition that a temporarily lower level of return than the 1947 or 1948 level was inescapable for a while. If this was recognized, then, when the economy had passed safely through the adjustment tests, profits and investment along with consumption could again resume an upward course as the economy in general moved upward on a noninflationary basis.

Nor were our comments about the relationship between prices and consumer incomes during the inflationary boom intended to suggest that consumption between 1946 and 1949 should have been higher when there were no more goods to consume. The point rather was that looking forward to 1949 and succeeding years, when bottlenecks would be broken, productivity increased, and the plant and equipment improvements of the reconversion period fully felt, the price-income structure would have to readjust to the expanding volume of

consumption needed for maximum production, employment, and business opportunity. We advised business that some of these price-income adjustments should be started early and made gradually, for experience indicated that if too long delayed and then subsequently bunched over too short a period of time the consequence would be a dangerous decline in business activity. This in turn would cause profits and investment, the most volatile parts of the structure, to decline even more rapidly.

Fortunately, the practices of more and more representatives of the business community are coming to conform more closely to the tenor of what we have said. In the early 1949 recession, the majority of businessmen did not react to lower profit margins or prospects by the erstwhile traditional acceleration of cutbacks, rapid price deflation, wage reductions, and layoffs. Some occurred, but they generally took place with moderation and discernment. Many businessmen realized that we were working our way toward a better "balance," and that if they maintained steady nerves through a short but perilous phase the fundamental strength of the economy would turn us again upward. This does much to explain what transpired during the second half of 1949, although the march to maximum production and employment is still to be completed.

Our conclusion that in the long run a "balanced" economy would require the expansion of consumption opportunities at an even more rapid rate than the expansion of investment—although both should grow—has been matched by the similar findings of many nongovernmental economists. It is not the Council's purpose here to vindicate its own specific conclusions. We merely point out that our approach departs from the earlier and narrower perspective sometimes applied by economists; and that many of our profession are now in accord with our views.

TOWARD MUTUALITY OF INTERESTS

The fourth advance in the attitude of government toward business, as appraised by the Council, derives from the three already listed. The problems of our economy appear no longer primarily as problems of protecting the shippers of the West from the "interests" of the East, or the farmers of the South from the bankers of the North, or the workers in general from the industrialist class, or the consumer from the farmer. To be sure, government still has the function of preventing any one group from taking unfair advantage of another, and laws and administrative devices are necessary for this purpose. But national economic policy should center mainly upon the basic interdependence of the long-range interests of various groups. If we are to endure and grow as a nation, the things which unite us must become infinitely more important than those which divide. The function of gov-

again, a central theme of Pres Johnson
& broadly welcomed by the business groups

ernment is, without favor or preference, to test each of its own actions by the long-run common good. Moreover, government should stimulate that thinking and analysis by business and other elements in our free-enterprise system which will help them to advance the general economic welfare and thus to reduce the requirements for public supplementation.

In an expanding economy, the lifting of low-income families to a far higher standard of living, the improvement of agricultural programs consistent with the needs of urban consumer incomes and also promoting parity of income for the farmer, the provision of adequate funds for a rewarding level of business investment and profits, and the meeting of our domestic welfare and international security requirements, are not incompatible objectives. Attainment of each objective is inseparable from attainment of the others.

REGARDING BUSINESS SIZE AND PRACTICES

The Council finds the fifth trend in the attitude of government toward business related to the size, structure, and behavior of business organizations. No thoughtful person within government wants to abandon or vitiate the "antitrust policy." The stultifying results of excessive cartelization in some other lands gives renewed evidence of the prescience of those who wrote the Sherman and Clayton Acts and established the Federal Trade Commission. Still, it is important to realize that our industrial problems have changed continually and require recurrent examination. Under our system of law and administration, many adjustments to new situations are made interstitially without organic reconstruction of the legal framework. These adjustments have been going forward over the years. The process is never finished.

In a stable and expanding economy, there is room both for well conducted big business (with its unique facilities for scientific and developmental experimentation) and for small business with its display of individualism and self reliance. Small business should be protected from any predatory practices by its larger neighbors, and all business should be protected against unfair competitive practices by units of any size. Yet the truth at least in part is that small business is threatened not primarily by big business but rather by big instabilities in the economy. When the economy attains full prosperity and is moving upward, small business in general does very well; but when the economy hits the toboggan many small businessmen are ruined not because they are less efficient than big business but because they are weaker and have fewer sustaining resources. An economy that grows steadily, as our economy can, would provide manifold opportunities for small business. Small business has some unique problems of obtaining financing, and more efforts should be directed toward solving these problems.

We are still a long way from having completed the necessary rethinking of problems involving business size and practices. Much more

work needs to be done. It should proceed in a spirit of fair objectivity toward business both large and small.

FROM MERE POLICING TO AFFIRMATIVE FACILITATION

The Council would describe the sixth trend in the attitude of government toward business as being away from the purely negative or policing function and toward the affirmative or facilitative approach. Our economy has become too complicated for government to function best simply by placing "don't" signs all over the lot. Some things, of course, the government must continue to prohibit or regulate—and regulation may be focused in part upon affirmative objectives. But the central problems of economic "balance" require adjustments which cannot be achieved mainly by regulation. For example, regulation is inadequate to correct an economic situation in which business might not receive the incentives to stimulate a high enough level of investment. Yet an inadequate level of investment can probably wreak economic havoc. Consequently, the fiscal, credit, monetary, and other facilitative operations by which government may promote an environment conducive to business expansion are at least as important as the more traditional watchdog functions. Those government policies and programs which affect farm income, industrial wages, or consumer incomes are also of prime importance and call for increasingly thorough and objective analysis.

AWAY FROM SPECIFIC CONTROLS

The seventh trend which the Council observes in the attitude of government toward business relates to specific controls. The war made these controls necessary. In our judgment, they were abandoned too soon and could have been helpful in curbing the inflationary boom, and rent control is still necessary. A better understanding between business and government might even make it possible to have a broader range of restraining measures available in reserve without concern that they would be used prematurely or excessively. However, in the current and foreseeable economic situation, it is far less important even to contemplate the restoration of the specific controls than it is to realize that they do not for the long pull answer the basic economic questions confronting the American economic system. In peacetime, the mere authority to fix prices or wages does not in itself answer the question of what relationship between prices and wages will be fair to all concerned and most conducive to economic stability and growth. The answer resides in improved economic understanding rather than in fiat. Nor, in peacetime, does the mere presence of control authority upon the statute books obtain the popular understanding of price-wage problems essential for their workable adjustment; and if this popular understanding exists, we should in peacetime find better ways than specific controls to translate

10
★ offers an expanding role for business
★★ Reconciles the interests of big & small business

★ The govt is no longer primarily a policeman, but rather a facilitator.

it into action. The Government should use its fiscal and monetary powers to promote economic "balance," and supplement these with such well accepted programs as farm price supports, social security, minimum wage legislation, developmental programs, etc. The other phase of the task of promoting "balance"—which resides in the continuing adjustment of prices and wages and profits—should be left to the actions of managers and workers within our business system itself.

FROM "COMPENSATORY" THEORY TOWARD MORE RELIANCE ON
ENTERPRISE. AND A WORD ABOUT KEYNES

The eighth, and in the Council's judgment the most important trend in economic thinking within government as we observe it bears upon the respective scope and weight of public action and private action in promoting stability and growth. During the mid-1930's particularly, there grew up an influential school which held that our free enterprise system was necessarily subject to violent fluctuations which could not be ameliorated substantially *within* the system. It held that only government action, mainly through enlarging or contracting the volume of taxation and public spending, could fill in the gaps in employment and production when these became large or curb inflation when it became dangerous.

The experience in the 1930's, however, demonstrated that when the private economy ran sufficiently far downhill "compensatory" action by the government became entirely necessary but *was not alone sufficient to restore and maintain satisfactorily high levels of general economic activity*. The reason for this was not simply that the "compensatory" action was not big enough. The fact was—and still is—that the range of useful projects susceptible to undertaking by government cannot be sufficiently voluminous to counteract fully a general depression—even when coupled with tax reduction. Further, public action beyond certain levels or in certain fields may be offset by declines in private spending and investment, so that the net gain is not equal to the total number of public dollars spent. Similarly, in fighting inflation, mere increases in taxation and reductions in public spending, while useful weapons, are difficult to employ fully enough to curb inflation without bringing on an excessive deflation. Nor do these fiscal measures alone deal adequately with the internal maladjustments in the price-income structure which are primary sources of danger in the kind of inflation that we have recently witnessed.

This leads to the conclusion that "compensatory" public action can help to iron out minor fluctuations of the business cycle and must indeed be used if big ones develop, but that complete recovery from a substantial downswing depends primarily upon the revival of private investment. And because that revival becomes progressively harder to accomplish as the economy moves further downward, the main concentration of economic policy should be upon encouraging stability and

growth within our free enterprise system itself. This is doubly true in a prosperous period like the present, when action is feasible before the eleventh hour.

Many government policies, if appropriately designed, can place foremost emphasis upon encouraging steady business expansion and thus minimizing the fluctuations in business activity. This approach is sometimes referred to as creating a climate favorable to business. This is true although the responsibility does not lie wholly with government. Within enormous areas of action and decision, business holds within its own hands the factors which condition its course. This is the essential nature of a free enterprise system, and business should be encouraged when government recognizes this cardinal fact.

Despite all efforts by business and government to promote steady growth, "compensatory" policies form an important part of the techniques to be used for stabilization purposes. The difference between the exaggerated use of the "compensatory" approach and the Council's approach is a matter of degree or emphasis. This problem is further treated in a later section of this report which stresses the need for somewhat more stability in national economic policy.

Sometimes the purely "compensatory" approach is referred to in popular discussion as "Keynesian economics." In fact, Keynes placed more emphasis upon structural problems than upon the cycle. Lord Keynes was too sizable an economist and too enterprising a technician for us to attempt to evaluate his great work in a report of this kind. We shall content ourselves here with saying that, insofar as any popular version of the "Keynesian economics" identifies it with the school which placed exaggerated stress upon "compensatory" action, that school is neither representative of our own thinking nor in our opinion characteristic of any important segment of government thought today.

* Same theme as to the under
role for business itself.

* a very important theme in 1964,
and a very realistic one

III. Trends in the Attitude of Business Toward Government

As government economists, it would be presumptuous for the members of the Council to attempt a description of business thinking as fully as we have attempted an appraisal of the prevailing government attitude toward business. But it may be helpful to sketch briefly our own impression of business attitudes, particularly because public appraisal of these attitudes obviously interacts upon government's attitude toward business. We discern a trend which is distinctly propitious to mutual accommodation and adjustment.

GAINS THROUGH BUSINESSMEN IN PUBLIC SERVICE

American business is highly pragmatic, and its point of view has been vitally affected by the war effort which brought to countless businessmen a new experience in public service. There they observed at close range the operations of the whole economy, the interdependence of its parts, and the common problems of all. True, the war economy and its problems, as well as the solutions devised, were drastically different from anything wanted in peacetime. Yet many businessmen in Washington during the war developed points of view which have immensely influenced their subsequent thinking.

The net result has been an increased appreciation by business that business and government are not enemies but friends; and that persons permanently in the public service have the same virtues and faults as Americans elsewhere and are equally committed to free enterprise as well as free government. The government service needs additional inducements to bring more skilled businessmen into that service in peace no less than in war. The idea that a businessman working for government is "serving two masters" (even when he has divested himself of private interests which might conflict with his public duties) is a relic of the earlier thought that the sole or main purpose of government is to police business. The problems of economic policy have shifted their center of gravity away from this earlier concept toward an area where the problems of business and government interpenetrate and require complementary action. It is therefore desirable that the most practiced exponents of industrial management should participate in government. This is equally true of the practiced exponents of American trade and industrial unionism, as well as of those who have been closest to the problems of the farmer.

* Business is very favorably conscious of this in 1964.

Through the war experience, and in other ways, businessmen have come increasingly to realize the immense influence of public policy upon the American economy. The prevalent view that government should adopt policies which "create a favorable environment" for business is a far step from the earlier notion that government should just "let business alone." For that could happen only if government had no policies which affected the business environment. In addition, there is an increasing measure of agreement about many policies now in effect. Farm price supports, social security, Federal Reserve operations, and Treasury debt management, to mention a few, have passed into the realm where the debate is no longer at the central core but instead on the periphery—dealing with improvements or modifications in detail.

This realism on the part of businessmen about the role of government in modern economic society is accompanied by a mature view concerning the need for a variety of policies blended in just proportion. This has replaced an earlier view that some one trick or gadget would maintain the economy in good health. Very few businessmen now believe that the whole answer lies in some minor change in interest rates, in whether the Government supports its bonds at par, in whether some particular tax reform is adopted, in whether the labor laws are amended or repealed. Instead it is recognized that big government is even more complex than big business, and that the same skepticism of panaceas and the same balanced judgments on a wide range of problems and procedures which characterize the successful business manager are equally necessary on the government scene.

REJECTION OF MERE SLOGANS—THE PENSION EXAMPLE

Recognition by businessmen of the complexity of the modern economy has made a majority of them increasingly distrustful of mere slogans or shibboleths as a guide to the relationship between enterprise and government.

By way of example, mere slogans would lead all businessmen to believe that privately negotiated pension systems are preferable to the expansion of Federal old-age security because the former is "free enterprise" and the latter involves "government." But this is not happening. Many businessmen, on entirely unselfish grounds, are questioning whether the random development of unequal pension systems in scattered industries would really leave the business system more truly free than the systematic development of uniform old-age security. And they are asking other questions. If thoughtful business and labor have both been concerned about the wide disparities in the wage structure, will this problem be lessened as an equal or greater disparity arises in business costs for pension plans developed sporadically? If labor mobility is a prime characteristic

* a useful non-doctrinaire analogy between business & govt.

of dynamic free enterprise, will business or workers have more freedom when nontransferrable pension benefits weld particular workers to particular jobs? If business success depends upon flexible adjustment to changing circumstance, should business entangle itself in cost ventures which necessarily project a generation or longer into the future?

The Council is certainly not prepared to censure the drive toward privately operated old-age security, which has arisen from delay in enactment of changes in the Federal system. It seems to us that many workers and employers have had no choice but to do what they have done. Nor do we take the doctrinaire position that some thoughtful combination of public and private insurance against old age may not usefully emerge, although we incline strongly toward immediate expansion of Federal old-age security as the more urgent requirement. Our main purpose is to illustrate that certain functions performed by government may be more consistent with the practical welfare of free enterprise—including both management and labor—than excessive efforts by private business to perform those particular functions. And because more businessmen are adopting this pragmatic view, the prospects are increasingly bright for workable alignment of the functions of business and government.

ENLARGED UNDERSTANDING OF WORLD CONDITIONS

There are also general forces of compelling magnitude which contribute toward a better understanding by the business community of the problems of government. This is evidenced in a statement made by Mr. J. Cameron Thomson (on behalf of the Research and Policy Committee of the Committee for Economic Development) before the Joint Congressional Committee on the Economic Report on November 23 of this year. Mr. Thomson said:

The idea that great economic instability is inevitable in a free society is one of the most dangerous ideas at large in the world today.

Most businessmen in recent years have not denied that *great* instability could be avoided. The debate raged only as to whether such instability was not preferable to even the minimum amount of government action—in addition to extensive private action—conceded to be necessary for its avoidance. We think that this debate is receding, with so many businessmen sharing the viewpoint expressed by Mr. Thomson that we cannot confront the world with another American depression and still maintain our position or security in the world of the future.

The informed businessman of today is acutely aware of the menacing challenge to free enterprise and free government which confronts the West. He knows that this challenge must be met by firm and comprehensive countermeasures, largely in the area of our international economic policy. He knows that the United States must take the leadership in these measures, which are fundamentally economic in

character. He knows that for both historic and practical reasons government must help to mobilize and give leadership to the programs involved. Thus the businessman appreciates that perhaps the most important phase of public policy today is directed toward the literal salvation of the one kind of world in which the businessman can breathe.

In the struggle to preserve freedom, the businessman needs government; and government needs the help of businessmen in the development of practical programs. These are no times for bickering or prejudice. Ironically, the actions of those who believe that free enterprise and free government are incompatible, and that one or the other or both must be destroyed, are prompting free enterprise and free government in America to close ranks and to work together in the supreme cause of human freedom.

* The central theme of
mutuality applied to
the international front.

IV. Further Needs in Government Economic Policy

Despite much progress in the relations between business and government, there are still some gaps in national economic policy as viewed by the Council. The word "gaps" is used advisedly to indicate our belief that improvement in current operations should proceed at least apace with ventures into new fields. This does not mean that no new programs are needed, or that the nation can pause in building upon solid foundations. While this report is not the place for specifics, we have said that measures such as social security should now be expanded. But one way to safeguard progress is to consolidate the gains which have been made.

NEED FOR FURTHER HARMONY AND CONSISTENCY

A cardinal task, as the Council sees it, is to achieve even more harmony and consistency among those outstanding programs of government which greatly affect the whole economy. During the critical mid-thirties, when some of the structure of current national policy was built, there was no time to develop symmetry for the various wings of the structure or to connect them with the center. This was inevitable during an economic emergency, but there is no such emergency now. The privilege of men and agencies within a free government to give differing advice should be cherished. But this does not mean that the final execution of public programs touching upon the whole economy should not achieve that internal consistency and that harmonious relationship to defined common objectives which any large undertaking demands.

In the context of this problem, much good may be derived from the comprehensive work of the Hoover Commission and from the steps which the President and the Congress have already taken to implement it in part. More efficient use of personnel and of instrumentalities can register great gains for the taxpayer and for the country. But administration is an arm of policy, not the heart. For every dollar affected by the use of personnel, there may be a hundred or a thousand dollars affected by basic economic policy. It is here that the most costly mistakes could be made or the most useful services rendered. Here also manifold gains have already been affected, but there is need for still more progress.

This progress toward still further harmony and consistency in governmental economic policy does not in the judgment of the Council call for the establishment of more agencies or committees. It calls instead

for a unifying framework within which each separate economic policy may be tested against its effect upon the general economy and upon the promotion of maximum opportunities for employment and production in free, competitive enterprise. This depends in turn upon the further use of machinery which the Congress has already made available and which the President has always been ready to use—the machinery of the Employment Act of 1946. Progress in this direction is reviewed later in this report.

NEED FOR MORE STABILITY

As government economic policy becomes increasingly consistent, it should also become somewhat more stable. The prudent American family makes some arrangements lasting 20 or 30 years; a moderately large business may look 50 years ahead; and a local government sometimes looks a century ahead. The biggest venture of all, our Federal Government, should strive gradually to modify its habitual practice of carrying almost all of its major policies and programs on a year or year and a half basis. The credit and spending and regulatory and tax policies of the Government are so highly conditioning to the whole economy that the degree of stability of these policies affects the degree of stability throughout the whole business world.

Some short-run shifts, indeed, are necessary to enable the Government to alter its position and thus to "compensate" for changes in the private business situation. But we have already in this report indicated that if the Government moved gradually toward placing somewhat more of its own activities on a somewhat more stable and longer-range basis, this might add greatly to the stability of the whole economy. The placement of some public programs primarily upon this basis rather than upon a "compensatory" foundation would also hold these programs truer to their intrinsic purposes. The intrinsic purpose of public works is not to take up slack in employment, but rather to build up our national wealth by procuring certain end products which the country needs but which cannot be produced in any other way. Similarly, a decision to expand our educational facilities should be related closely to the priority value which we place upon education, rather than to the usefulness of school construction in taking up a business slack. All or some of these programs may to a degree be expanded and contracted in response to variations in private business. But the variation should not be carried so far as to interfere with the primary purpose of these programs.

Our public programs are supported out of the production record achieved by the economy as a whole. We should ask ourselves what is the productive potential and capacity for growth of our economy over a reasonable span of years, assuming that we are fairly successful in maintaining full utilization of our material and human resources. We should then ask ourselves what part of our output of materials,

* Businessmen appreciate this theme
** True economy is based on sound
major economic policies, not just per-
sonnel

* A theme very congenial to
the business world - & valid, for

money, and effort—over a similarly reasonable span of years—we want to devote to specific purposes such as public improvements and education. The Council admits that this involves social as well as economic judgments; but nonetheless the problem has elements which prompt economists to suggest an orderly method of arriving at results although they do not presume to dictate what these results should be.

The Council thus leans toward some further development of reasonably stable policies, in a few major conditioning areas, to cover a moderate span of years. Allowance should be made for the growth potential of the economy, instead of basing policy upon the assumption that the economy will linger indefinitely near a point reached after a half year of recession or fail to move again toward maximum levels of employment and production. This stability and confidence, displayed by government at so important a sector of the economy, might favorably condition also the free enterprise sector.

The argument may be advanced that more stability in some public policies is impractical because "we cannot see that far ahead." The problem is admittedly one of degree. But it is easier to predict safely that our economy will grow in the long run than that it will grow in 1950, although we believe the latter also to be true. This is not to say that short-range adjustments have no place in a rounded economic policy; some of these short-range adjustments may now be needed, but they should not be asked to carry too heavy a load. If, despite the effect of some reasonably constant public policies, serious downturns in general economic activity should occur, it may still be practical to readjust public policy upon observation of the event. Economic downturns do not progress so rapidly that they leave no time for effective changes in policy. However, we repeat the more important consideration that temperate progress toward somewhat more stability in government policy would promote more confidence and stability throughout the whole economy and thus help to hold the manifestations of instability to manageable proportions.

One caution is called for. The foregoing discussion develops principles for gradual application, but it cannot be accepted as a necessary guide to specific policies during the coming year. For example, while we should aim in the long run for reasonable stability in tax policy, the great changes in the tax structure over the most recent years and the double reversal of economic trends in 1949 may make it necessary to alter the tax structure somewhat before a basis for stability in future years will have been laid. But this does not vitiate the principles which we have set forth; it simply proves that the objective cannot be fully accomplished overnight. The Council hopes that the specific policies soon to be announced for 1950 will show some progress toward the goal of improved stability and that this goal will be increasingly pursued in subsequent years.

* more a reasonable
stability of public policy very important

NEED FOR CORRELATION OF WELFARE PROGRAMS, ESPECIALLY SOCIAL SECURITY, WITH GENERAL ECONOMIC POLICY

The need for still more harmony and consistency in national economic policy, and for its placement on a somewhat more stable basis, has cogent applicability to programs such as social security. A still better understanding between business and government would result if the excessive separation were lessened between "economic" and "social" programs—between a government interested in encouraging the growth of the economic system and a government interested in "welfare." Those who quite appropriately raise the question of how much "welfare" is going to cost, or whether our economy can stand that cost, clearly recognize that programs of social security which involve billions of dollars in taxes and in public outlays cannot be divorced from economic considerations.

The support of people who are too old to work or who are unemployed or ill does not create wealth. It is not like the production of goods and services. For the most part, it enables certain individuals to consume wealth which is being currently produced by others. The real question is how much of current production may be diverted to support this particular type of consumption (above a base subsistence level, for that level of support the economy must bear in any event) without sacrifice of relatively more important objectives. This makes social security an economic problem in the same degree as striking an appropriate balance between business investment and ultimate consumption, or between defense and foreign aid programs and the requirements of our domestic economy.

Sometimes it is said that, whatever amount of income may be flowing to the old or to the unemployed, it is economically desirable because it creates purchasing power and thus provides demand for the products of industry. But no *additional* purchasing power is created if this income is simultaneously taken in equal amount from those who are still employed. In fact, there might be future deflationary elements in a social security system which for too long provided a large excess of forced savings going into reserves over current payments to the aged. Payments to the old or the unemployed which resulted from deficit financing would create purchasing power of a sort. But purchasing power generated in this way, while it would be better than no purchasing power at all, would not have equivalent economic value to purchasing power generated by production efforts. For similar reasons, cutting the workweek simply to provide jobs for more people—which is a form of sharing unemployment—would never be as beneficial as obtaining the full use of our productive resources, even though it might be a necessary expedient if we failed egregiously in the more important task. Likewise, the age at which workers retire or the size of the benefits they receive should not be determined by the fallacious idea that this is a good way to create more pur-

* Needs emphasis. Welfare programs may be self-defeating, if not carefully controlled.

chasing power by adding the purchasing power of those who are not working to the purchasing power of those who are working. We should start with the assumption that our economy will be most productive by providing useful jobs for as many people as are able and willing to work. In that event the national policy with respect to the general age of retirement would be based not upon an artificial method of leaving more job opportunities for others, but rather upon a decision that the functioning economy can afford to support people who have reached a certain age without requiring that they work further.

Social security programs are viewed in a distorted perspective unless it is realized that their justification rests upon two grounds. First, that the cost of caring for the old, the unemployed and the sick always falls upon the economy; and that bearing this cost in a systematic way is more efficient than bearing it through charity or improvisation. Second, that as an enlightened nation we are willing and even eager to divert a portion of our annual output away from capital replenishment and away from consumption by current producers in order to make life more livable for those who are unable to produce through no fault of their own. The appropriate test for the size of a social security program is how much of our resources on balance we wish to devote to this humane purpose, taking into account all the competing purposes and needs of our kind of economy. It is true that the social insurance programs make our economy somewhat stronger by cushioning it against fluctuations by their "built-in stability" effects. But the larger question is how much of these programs a strong and rich economy can and should afford.

The true nature of the social security problem being what it is, the concept of "saving" for social security is in one sense useful and in another sense misleading. It is useful to recognize that we must save in order to enlarge our productive equipment. Without such enlargement, our economy would not be able to turn out more goods from year to year and therefore would not be able to afford the progressive expansion of social security. But it is misleading to assume that through any process of bookkeeping, either personal or national, millions of people can "save" the food, and clothing, the medical care and recreational allowances which they will be consuming 30 years from now when they retire. What they consume when they retire will be produced not by themselves but by the working force at that time, and what they save now should be channeled insofar as feasible into current investment opportunity.

The Council strongly favors the national system of social security which involves contributions from employers and from workers on a systematic basis, and which also involves contributions by government. This is the best way to protect people in their old age as a matter of right, and not to leave what may happen to them later on subject to unforeseeable policy decisions in the future. Yet our discussion of the social security problem implies that gradual efforts should be made to

improve the contributory system so that at least part of the contributions would be more nearly on a "pay as you go" basis. By this, we mean the gradual development of a closer balance between social security receipts and payments from year to year. The ultimate objective should be toward making withdrawals from the economy for the purpose of social security roughly balance the contemporary cost of benefit payments, although it might always be desirable to maintain some "reserves" of significant size. We also believe that, as coverage becomes more general, a larger part of social security receipts should be obtained through general revenues rather than payroll taxes.

This gradual development would be sound economics for reasons already given; and it would also provide a better gauge as to the magnitude of future social security benefits which we can afford to enact into present legislation. For if enactment of legislation now involves the commitment that X number of people who will not be working 30 years from now will receive Y number of dollars of old age benefits per month, the real test of whether the nation can afford such a program is not XY dollars per month measured against the *current* size of the economy but XY dollars per month measured against the productivity of the economy 30 years from now. Social security expansion now, insofar as it applies to persons who will not retire for many years, should make considerable allowance for an assumption of continuing secular economic growth. Almost all of our national policies in the long run depend upon the validity of this assumption. For otherwise we face continually rising unemployment, under-utilization of our resources and technology, and increasing disturbance to our whole economic system.

The Council's main reason for offering this analysis is to promote the application of sound economic principles to social security matters. It is not our function in this report to argue for a social security program of any particular size. Yet it seems clear to us that the application of sound analysis reveals that our nation can afford a considerably expanded social security program without impairing our economic stability or weakening our growth potential.

COORDINATION OF NATIONAL ECONOMIC POLICY IS NOT "CENTRAL PLANNING"

The Council's interest in the orderly evaluation and systematic reconciliation of public policies should not be misconstrued as any leaning toward "blueprinting the economy" or "central planning." Except for the reference to social security to clarify certain points in our analysis, we have not here dealt with any specific additions to governmental programs. We have only stressed that, *whatever* the scope or extent of government programs, there should be applied to them those principles of consistency and harmony which are valid in the case of any material undertaking of business as well as government. The use within gov-

Very important to stress this

ernment of that "budgetary" concept which is applied by any large corporation in the measurement of its competing needs and prospects is compatible with the maintenance of a flexible and pragmatic spirit in government as well as in business.

A In the long run, this approach should lead to the simplification rather than to the proliferation of public programs. For the more successful government becomes in weeding out inconsistencies and adapting means to valid ends, the more the taxpayer will be saved in direct administrative costs. And the more effectively government weighs the effect of its established programs upon the whole economy and upon the course of business development, the more confident and prosperous our business system should become. This, in turn, may help to protect us against those serious economic downturns which provide the main impetus for certain types of public intervention in response to public need.

* Doing basic things well will eliminate random efforts, duplication, & overreaching on the part of gov. This is the road to economy & efficiency.

the balance is not so relevant.
V. Further Needs in Business Preparation for Stability and Growth

Along with further progress in those government policies which affect business, the record of recent years leads the Council confidently to anticipate further progress in business thinking and practices. This will help our business system to maintain that major responsibility for the condition of our economy which is ascribed to it under the American combination of free enterprise and free government.

FURTHER ACCEPTANCE OF "MAXIMUM" OBJECTIVES

First of all, our business system needs to embrace even more fully—as its enlightened leadership has already done—the goal of continuous maximum production and employment. This is not to say that so high a goal is readily obtainable. Possibly some periodic setbacks of moderate size are the price we must continue indefinitely to pay for the freedom and flexibility which make our system so dynamic in the long run. But this is entirely different from saying that the setbacks are desirable as well as difficult to avoid. Very few businessmen really believe that the drop in the industrial production index by about 16 percent, and the increase of unemployment by about 1½ million, which took place in 1949, left them with a more confident feeling than if a better balanced expansion in 1948 had prevented this decline. We are recovering from that downturn because of the strong elements in our economy, and not because of the deficiencies which generated the downturn. As our system learns to develop still stronger elements, even if it does not succeed in maintaining continuously maximum levels of activity, the downturns can become more moderate and the upturns can become more certain.

Nobody should confuse the classic theory of how downturns occur with the erroneous belief that they are helpful. Saying that a downturn in production and employment is an adjustment of supply to demand may be true; but supply and demand were thus "adjusted" even in 1932. Saying that a downturn is inevitable, when backlogs of demand accumulated during a war period are worked off, may be a correct observation about the past; but it is simply another way of saying that we have not yet learned how to make full use of our productive capacity in peacetime. It is better to aim constantly toward maximum production and employment, because this will in the long run make our think-

ing clearer and our achievements greater, even though we have not yet learned enough to reach this objective fully every year.

FURTHER REALIZATION THAT PUBLIC SENTIMENT AFFECTS THE ECONOMY

Occasionally it is said that a level of employment below the maximum is desirable because it makes workers more efficient and improves productivity. Quite aside from the lack of scientific verification of this proposition, the Council feels that even more businessmen will come to recognize—as so many now do—that public sentiment toward mass unemployment is just as much a part of our economic life as the public's attitude toward buying particular goods or spending particular portions of its earned income. And whether unemployment is "too high" depends as much upon what the unemployed think as upon what business thinks, just as whether prices are too high depends as much upon what the buyer does as upon what the seller says. Social and psychological considerations will come to enter more and more into business action because they are a part of the environment in which business is done.

Since mass unemployment tends to build up resentment (whether rightly or wrongly) against free enterprise, it injects a threatening element into business life and prospects which is enormously important. Efficiency, even if it could be purchased at the price of so vast a danger to our business system, would not be worth the buying. Our economic system is strong enough to be sufficiently efficient without undergoing this oppressive risk. And because every mass increase in unemployment tends to shift the location of authority and decision from business toward government, business has additional cause to strain every effort towards its prevention.

NEW BUSINESS ATTITUDE TOWARD "POLITICS"

Of course, government is a "political" process, just as the Constitution of the United States is a "political" document. But no businessman should resignedly take the position that it is futile to attempt to influence public policy because he is outnumbered by workers and farmers and "the government counts instead of thinks." Neither business nor any other group can offer any workable substitute for the processes of democracy, because there is none. Further, democracy is the system which affords the best opportunity for those with the qualities of thinkers and leaders to make their weight felt although they are outnumbered. These qualities exist in abundance in the business world.

Some of the best friends of business, who are neither in government nor in business, are now urging businessmen to assume increasing responsibility for participation in public affairs. This is a good thing.

CAN BUSINESS ACTION ACHIEVE SUFFICIENT CONCERT TO PROMOTE STABILITY?

Successful efforts to combat serious economic downturns must be concerted. They must be on a massive scale, because the economy is huge and acquires tremendous momentum when it starts definitely upward or downward. The main advantage offered by government policy in resisting economic fluctuations is that government can act on this massive scale. The extent to which free enterprise can enlarge its necessary contribution to economic stability hinges upon methods whereby business itself may act more effectively and thus deliver a more massive blow against the forces of deflation.

The dilemma is this: businessmen *individually and separately* may react to the beginning of a downturn, or even to its prediction, in sufficient numbers cumulatively to accentuate the downturn. But no sufficiently satisfactory way has yet been found for businessmen *individually and separately* to respond to the beginning or prospect of a downturn in a manner which cumulatively holds the economy stable or propels it upward. This is the real meaning of the importance of "business psychology." Businessmen at certain stages in the economic process take so seriously the first signs or predictions of a downturn that the prediction may become, as the Council said in its First Annual Report, "the engine of its own verification." If businessmen under such conditions could follow in *sufficient numbers* policies contributory toward stability or growth, or at least act in a manner consistent with the proposition that the long-range trend of the economy is upward, this might provide a key to the dilemma.

There are two lines along which such action by business may be facilitated. The first is by more common study and education of how the economy works and what policies may be most salutary at various stages in the economic process. If the results of such inquiry were sound and obtained sufficient acceptance, individual businessmen might act (without the kind of concert which could be against good policy) to cumulate the forces of stabilization and growth instead of cumulating the forces of downturn.

That this is not too much to work toward is demonstrated by the economic history of 1949. The Council finds one explanation of why the recession of the first half-year was so contained in size and duration in this fact: businessmen all throughout the postwar period, and particularly during 1949, exhibited far more economic understanding translated into practice than in those past periods which presented them with somewhat comparable difficulties. To be sure, there were mistakes of price policy and other policy during the inflationary boom. But in contrast with the period following World War I, the management by

business of its inventory and pricing policies was definitely superior. Similarly, the fact that business knew enough not to react to the first signs of the downturn by wage cuts or by layoffs (beyond the minimum in the face of dwindling markets) was a sustaining factor along with the sustaining influence of many public policies. There is no reason why this behavior pattern exhibited in 1949 cannot be accentuated in future years.

However, the Council does not feel that the forces making for a downturn in early 1949 were sufficiently powerful to put our business system or our government policies to as severe a test as may occur at a later period. Consequently, we feel that in order to be safeguarded against the possibility of more ominous danger at some time in future, the process of study and education and understanding needs to be carried much further by every feasible means.

Moreover, we feel that such study and education and understanding may not be enough—even when added to vigorous public policies—unless it is accompanied by improved institutional arrangements which will come nearer to assuring consistent and massive private action on a much broader scale than was exhibited even in 1949. Therefore, as a second line of action, we favor further exploration of how these institutional arrangements may be developed and made most effective to expand business activity without that kind of collaboration in restraint of trade which the Sherman Act wisely condemns. In the final section of this report, we make some reference to meetings of management, labor, and others to explore some guiding principles for private economic policy on a voluntary basis.

These considerations, and in fact all that we have said in this report, shape our thinking about the kind of fundamental study and analysis most relevant to foreseeable economic problems in the United States. We now turn to a somewhat more detailed description of the kinds of economic study which we believe should engage economists, businessmen, labor and farm organizations, and all those most deeply concerned about economic stability in the months and years ahead.

VI. Focal Points for Economic Study

In carrying out its own responsibilities under the Employment Act, the Council has found itself of necessity the carrier and purveyor of the kind of improved economic analysis to which reference has been made throughout this report. We have also been acutely aware of the gaps and deficiencies, because we have been challenged to arrive at judgments upon matters where current facts and analysis have provided only a very partial guidance. Our desire is to stimulate individual and organized research through every available means.

By stating with some definiteness the difficulties which we have encountered or anticipate, we hope to provide further stimulus to those lines of study and education which may be helpful to both business and government. Those who have read the various reports under the Employment Act will have identified some of these difficulties. But many of them are in the future, since the life of the Council has thus far largely coincided with a period of high employment achieved by war-initiated momentum. This period, it is true, has presented serious problems concerned with inflation and its aftermath. But for the problems of the future, these earlier reports have been only trial runs. Largely concerned with immediate problems of postwar adjustment, they have not adequately explored the long-run problems of stability and growth.

THE PROCESSING OF FACTS

Our economy consists of myriad interacting elements. The problem of analysis is to reduce them to manageable categories of thought, to trace the paths of interaction, and to identify strategic points at which particular actions will lead to desired results.

At the base of the pyramid lie numberless facts. The principal way to impound economic facts is through statistics. The effort to carry forward our work would have proceeded in darkness and disorder had it not been for the tremendous programs of collecting statistical data which have been put into effect over the past generation. Many private organizations—business, labor, universities, research institutions—have participated in this development. But in very large measure it has been and must be the statistical activities of the Federal Government which provide the necessary data. The cost and complexity of adequate statistical services far exceed the resources of any private agency.

As soon, however, as our work was initiated, it became clear that existing statistical services although extensive were inadequate. This was indicated in a committee print of the Congressional Joint Committee on the Economic Report, *Statistical Gaps*, issued in 1948. It presented a series of recommendations concerning the need for more complete Federal statistics in several fields, summarized as follows:

(1) Periodic surveys of consumer purchasing power and demand, sufficient to show—

(a) the distribution of income and saving available for expenditures by geographic areas and among various consumer groups and income brackets, and
(b) current and prospective patterns of consumption and expenditures.

(2) Collection of information on wage earnings of employees in activities not covered by our social security system.

(3) Improvement of the information on returns to capital and management of unincorporated businesses.

(4) Collection of more information on employment and unemployment, adequate to reveal geographic differences in employment trends and unemployment rates, and to provide data on occupational and other characteristics of the unemployed.

(5) Development of more complete and current information on financial trends in business, providing industry totals, data on business operations by size of business, and information on business concentration.

(6) Taking of an up-to-date census of wholesale and retail trade and services by means of which the current statistics on business and distribution may be improved and made more reliable.

(7) Development of adequate concepts for measuring productivity and the collection of data to supply information on the course of changes.

(8) Development of data on costs of construction and improvement of data on the volume of new housing and nonresidential construction.

(9) Improvement of inventory statistics by covering a larger and more reliable sample which would permit a break-down of inventories at the various stages in the industrial process.

(10) Collection of detailed information on the relationship of requirements for materials, capital equipment and energy to the volume of production, to permit evaluation of the industrial consequences of production programs.

(11) Collection of fuller information on business intentions with regard to capital expenditures and related data.

(12) Collection of more current and detailed information on expenditures of State and local governments, for use in preparing estimates for the Nation's Economic Budget.

This list is merely illustrative of the wide informational base upon which broad economic policy must be built.

Statistical facts, however, are just the beginning—the raw materials. They must be made to mean something. Thus, the next great step lies in the field of analysis. What relations between particular sets of facts are of strategic importance? How do we relate the past relations to future relations? How should we try to shape the collection of future facts?

In attempting to answer such questions, we come squarely to the functions of economic analysis. And oddly enough, much of the most useful economic analysis is not based upon detailed facts. It is concerned with the molds, or schemes of relationships, into which facts should be poured. A concept of national income, of consumer income, of savings, of investment, of economic input and output—all these and others are necessary before statistical facts can be made to mean anything in relation to one another. We need a clear conception of the nature and role of credit, of the impact of wage changes upon costs, prices,

and incomes. We need clearly to see why a scheme of competitive enterprise works, and wherein its problems lie. The analytical framework can be, and has been, expanded and improved by economic statisticians. But it is largely economists who have devoted themselves to the broader framework of economic relations. Creative scientific thought and investigation precede the ability to build a radio, a bridge, or a bomb. And so it is with economics. In order to be more explicit, and to identify certain respects in which further economic analysis is needed, we shall now consider certain broad areas within which the Council's work falls.

FORECASTING

The first of these areas is the appraisal of current and foreseeable trends, commonly called forecasting. The immediate past is always fairly well visible to the naked eye with the aid of existing, though still inadequate, statistical data. The course of employment, business activity, credit, investment, consumption, etc., can be discerned, and their shifting relations followed for a past period of time. But what of the future? What is to be anticipated? And if the outlook is not satisfactory, with what confidence can preventive remedies be put into effect prior to the event? This is the rock upon which many people have foundered in their effort to see how any generalized economic policy might be made to work.

While it cannot be denied that the art of economic forecasting is far from well developed, this shortcoming may easily be exaggerated. Expert attention to the course of events can give an informed opinion of where they are tending. On this basis, preparation can be made for meeting developments which lie within the range of probability. This is what the Council now has to do, and all those responsible for the development of private or public economic policy cannot avoid formulating some view of the probabilities in the case. Nevertheless, the deficiencies are real and every effort needs to be made to diminish them.

Various useful experiments are now under way. One of the most promising is the wide sampling of business anticipations and of business intentions with respect to investment. Fluctuations in business investment have in the past been very marked and are breeders of instability elsewhere. Knowledge of the prospects in that direction is one of the most important keys to the short-run outlook. It is, of course, true that business plans can be changed rapidly, and prospects as seen by private firms must be checked against all other indicators of trends. But the possibility of a much improved approach to forecasting is undeniable. The Department of Commerce and the Securities and Exchange Commission are jointly engaged in developing improved procedure in these fields, as are also several private agencies, particularly Dun and Bradstreet and the McGraw-Hill Publishing Company. They

promise to become increasingly useful as techniques are perfected and statistical samples broadened.

Another promising type of inquiry is that which samples the financial position and anticipated purchases of consumers. The principal pioneer in this field is the Survey of Consumers' Finance sponsored by the Federal Reserve Board. From it may be inferred changes in the intensity of consumer demand in different directions as, for example, toward housing, automobiles, and other durable consumer goods. As with business investment, consumer plans can change rapidly if income prospects change, that is, if the whole economic situation changes. But in conjunction with other indicators, such information is extremely enlightening. The techniques which are being developed are likely to be found useful by private market research agencies, bringing a marked increase in the available information.

There are a good many types of statistical forecasting systems being experimentally used by private agencies, particularly financial and investment houses. Some of them may be very imperfect, but in the aggregate they include a large amount of intelligent effort to assess the factors which are shaping the future. The more widely such intelligent attention is directed to these factors, the greater will be the opportunity for well informed business decisions.

DEFINING OBJECTIVES

The second broad category of work identified by the Employment Act, and certainly central to economic policy, has to do with defining objectives. The Act calls this setting "needed levels of employment, production, and purchasing power" in order to promote maximum levels. The fields of inquiry implicit in these simple words are so numerous as to be almost beyond description. But what is involved may be indicated by selective examples.

One group of subjects may be called the institutional structure of the American economy and the means to its improvement. This may be illustrated by the structure of the investment markets. One overall fact that seems reasonably clear in regard to the sources of funds is that business and social evolution has wrought some irreversible changes in the mechanism of private investment. The role of the wealthy independent investor is diminished, while the importance of business savings and indirect institutional investment of individual savings is increased. Constructive effort to meet the problems involved in this adjustment calls for intensive research into existing and potential new means by which the savings of the security-minded small saver can be made available for business investment without excessively burdening risky enterprises with debt.

The central importance of this problem is apparent on its face, since one of the surest ways to halt progress and magnify unemployment is

for a large part of the saving of the people to fail to find an outlet in new productive capital. The study of this problem is one which deserves wide attention by economists and by those agencies engaged in administering the people's savings. Such studies can broaden out to include the whole credit structure of the country, including that part which is directly administered by the Government, with a view to adjusting it to the expanding and changing needs of the country.

Problems of institutional structure arise in many other fields, for example, in the labor-management field. The whole economic well being of the country is closely related to the outcome of collective bargaining agreements. The basis for decisions compatible with the public interest, under modern conditions, requires continuing intensive study by economists, by government, and by the parties to the bargaining process. Similarly challenging problems arise also in the field of market structure where the price and production policies of large-scale business have a very direct bearing upon the health and progress of the economy.

Institutions exist for a purpose. One way of stating the purpose is that they are for achieving goals. The primary goal under the Employment Act is that our working population and other resources should be as fully and efficiently employed as possible. But this goal embraces in fact many goals. It comprises all the conditions which are significantly relevant to the central purpose. Consequently, in addition to concern with the improvement of institutional structure, economic study and policy should concern itself with another group of subjects under the broad category of goals, or needed rates of growth in various directions. There are various ways of approaching this subject, and one of them is to assume that, if things can be kept going well in the short run, the long run will look after itself. There is some point in this thought, but not so much that the Council has thought it proper to forego all inquiry into the capacity of the economy for growth. On the contrary, we have felt it important that explorations be made, in quantitative terms, into the productive potential of the economy as time goes on, and into some of the interior adjustments within the economy which that development will entail.

The Council's own experiments in this field have been conducted in the form of hypothetical projections of the Nation's Economic Budget. But they can be conducted in other ways, and the more ways the better. In any case, they all involve an advance estimate of our productive resources at various stages of development and the amount and character of their productive yield, upon certain stated assumptions. A path-breaking contribution to studies of this sort was the comprehensive volume, *America's Needs and Resources*, prepared by the Twentieth Century Fund.

In a way, it is not entirely satisfying to call the outcome of such projections "goals." They are not like the goals of a Russian five year

plan. They are not "plans" toward the achievement of which every resource of public authority will be directed, and for failure of which heads will fall. In one sense, they are bench marks of progress, evidences of the attainable. But in another sense they are simply an instrument through which we can more carefully study the conditions of progress. Does one anticipate a growing or declining relative place of government in the economy? And why? What factors suggest a changing proportion between the production of capital goods and consumer goods? Is it possible to measure the levels of investment needed to support stable progress? The mere effort to make the projections leads the mind to ask fundamental economic questions. While some of the answers are necessarily very general or tentative, they are not without meaning or utility.

But more is accomplished by this occupation. It moves us toward a closer inspection of the logic of various public programs of a developmental character. Upon what assumptions is the size of programs of resource development based, and how are they related to other assumed developments in the economy? With what state of economic development is a housing program equated? Upon what base of national income can social security obligations be projected? Such tests of relevancy are presented to public programs reaching far into the future.

One further purpose is served. The American economy cannot reach its potential unless its possibilities catch the imagination of those who plan for the future and invest in it. If investment decisions are made on the basis of "experience" alone, the backward view, they may not adequately correspond to what the future can support. The possibilities are not infinite but they are great, and numberless farsighted private decisions will have to be made to capture them.

The adequate exploration of the future calls for the best talents of many minds. Economists and statisticians can work out the models and fill in many details, but the attention of experts in many fields is needed. The improvement of our economic institutions, the patterns of growth in our resources—these are subjects which will repay dividends to detailed analysis in the form of a more comprehending approach over the years.

POLICY MAKING

The third broad category of tasks falling to the Council is that of appraising and recommending policies and programs. The two other categories of our work, as discussed above, are technical in character. While they give rise to disagreement, it is disagreement mainly on technical questions of analysis. But this third category is in vital respects of a different sort. It is public action that is under discussion. These actions in some measure affect everybody, in their self interests, in their most deep seated ideas of what is good and what is not. Economic action in a democratic society is distilled out of varied viewpoints.

The work of the Council necessarily involves controversial issues. But in this report we deal with that primary aspect of the Council's concern with policy which is technical in character. The process of arriving at informed judgments concerning measures which will contribute to economic stability is to a high degree an objective process. It involves economic analysis of the consequences of various lines of action. It requires the choice between alternatives on the basis of that analysis.

The pattern of sound economic policy is not easily discerned. There are other ends of national policy besides economic stability and growth. Some of these have to be accepted as data. The size of the defense program required for national security, for example, involves factors which the economist cannot even weigh, although it involves other factors where his techniques may be useful. Yet even within these bounds the task is complex. Particular measures may have short-run effects of one character and long-run effects of another. Or they may have conflicting types of short-run effects. In an inflationary period the building of more houses may force prices up by competing for scarce materials, but it may also relieve a critical housing shortage. Which consideration has the greater weight? A blend of judgment is constantly needed.

The problems of practical economic evaluation extend even further. How is it best to do the things which ought to be done? Means and ends are almost inseparable in their impact upon economic activity. Enough has been said to suggest, though only broadly and with little detail, that there are almost endless spheres in which the talents and skills of economists and other experts could be brought usefully to bear upon the problems of economic stability and growth. We hope that both with and independently of our stimuli there will be much more effort by others in many fields, and that the results of their work will flow freely for the benefit of all.

The task, however, goes further. Economic policy is not the exclusive province of economists, or of the Council or the Congressional Joint Committee. The impress of facts and of acute and disinterested analysis must be widely felt. It must be felt in the Congress, throughout the executive agencies, in the circles of business and farm and labor leadership, and out into all the byways of the country. The problems must be widely known; technical foundations of policy must be widely understood; the disinterested and professional character of the underlying analysis must be established. If this foundation can be built, economic measures designed intelligently in the public interest should increasingly find their way into the stream of public and private action.

VII. Recent Developments in Council Operations

This report has already made it abundantly clear that work under the Employment Act is a cooperative venture in the broadest sense. It involves business and government because both have basic responsibilities for the stability and growth of our economy in a free society. It involves organizations of workers, farmers, and consumers, which are of equal importance to business management although in this particular report we have stressed the functions of the latter. (On later occasion, as we have said, we may deal in equal detail with the relations between government and these other organizations in our private economy.) It involves the interplay of numerous agencies and instruments of government. It involves the President and the Congress. It implicates the economics profession, whose members prepare so much of the resources of scientific research underlying the practical tasks of the Council. Perhaps the hardest task of the Council as a small body is to develop relationships between itself and others which will keep moving in both directions a constant flow of information, stimulation, and improved thinking. The best way to describe the progress in our operations, therefore, is to outline some of the recent trends in these relationships.

WORK WITH PRIVATE ECONOMIC GROUPINGS

The Council has continued during the year its frequent meetings with representatives of business, labor, agriculture, and consumers. During our first years, these meetings were devoted mostly to general discussion of the economic outlook, supplemented by somewhat random consideration of specific problems which our visitors might raise with us around the conference table. But beginning with the last quarter of this year, we have instituted a new idea for which we have high hope. We have suggested to our conferees that together we undertake to designate one or two special problems for consideration at our next succeeding quarterly meeting, and that in the interval their staff resources as well as ours undertake to work up specific studies which might be circulated in advance of discussion. In addition to the manifest merit of this pooling of resources, we hope that the psychological advantage of *working together* as well as *talking together* will intensify the realization that the purposes of the Employment Act involve the whole nation and certainly cannot be furthered in an ivory tower.

In the course of our development of this plan, some of our conferring groups have suggested that, instead of meeting separately with representatives of various sectors of the economy, we should undertake joint meetings and perhaps joint studies with representatives of industry, agriculture, labor, and consumers functioning as a single team. There are some practical difficulties involved in this method of approach, but the Council does not deem them insurmountable. Certainly the argument that such meetings lead to hot disputation instead of calm analysis can carry little weight among those who realize—as this report has sought to stress—that the reconciliation of conflicting views and seemingly conflicting interests is the hallmark of free enterprise and free government.

We hope that procedures along these lines may be perfected, and that one of the most important collateral benefits will be the encouragement of mutual efforts along the same pattern but on a more decentralized basis throughout the nation. In such efforts the Council will not generally be able to join because of limitations of time and staff, but it is encouraging to note that already in some states agencies somewhat similar to the Council are being considered or have already been established.

WORK WITH GOVERNMENTAL AGENCIES

The network of the Council's relationships with other agencies of government has been described rather fully in previous reports. Particularly during the latter part of this year, these arrangements have been carried further. In the preliminary development of materials for the forthcoming January reports, members of our staff assigned to specific topics have initiated working committees tying in with other parts of the government devoted to research or operations in the various fields. Different groups have been studying the requirements for and the impediments to a high level of business investment; the interrelationship between international and domestic economic policy; the progress of the program for treating spot areas of unemployment; the relationship between agricultural adjustment and the general economy; the coordination and timing of the wide range of public works and developmental activities in the perspective of economic trends both secular and cyclical.

The Council should not be simply a reviewing body which looks over the proposals made by operating agencies and recommends to the President how these proposals may be fused into a consistent and sound economic policy. Our work to be effective must commence at a much earlier stage in the process. It should include participation in the developmental thinking about those policies and programs which are of central concern to the whole economy. Only thus can other agencies receive our assistance at an early enough stage for it to be fully effective; and only thus can we be brought in contact with their work at an early enough stage for us to comprehend it fully and be benefited fully by their thinking and experience. We feel that during the course of the

coming year, encouraged by the splendid cooperation thus far received, we shall be able to move toward the fuller professional service which the reading of the Employment Act and of its legislative history shows so clearly to have been the expectation of the Congress.

Practically every program and policy of government passes at some stage through the Bureau of the Budget; and those matters which importantly affect economic affairs channel also through the Council. This does not involve duplication, because the functions of the two agencies are manifestly different although closely interrelated. Yet the problem of adjusting other economic policies to the hard facts of the budget, and the correlative problem of adjusting the budget to the hard facts about the economy, mean that the Council must maintain closer year-round contact with the Bureau of the Budget than with any other agency. This contact has been greatly facilitated by the cooperation which the Bureau has extended to the Council.

RELATIONS WITH THE CONGRESS

The signatories of this report have never found any reason to believe that our special service to the President under the Employment Act could be inconsistent with that degree of cooperative servicing of Congressional Committees—particularly the Joint Committee on the Economic Report—which has become the traditional practice of policy advisers to the President who are set up under law, entrusted by law with a specific field of study and advice, and responsible under law for explicit participation in reports and recommendations transmitted to the Congress. The “problems” which such advisers face in occupying a confidential relationship to the President while cooperating with the Congress have been exaggerated, and in any event are not peculiar to economists; and it is less important that the Council be spared these “problems” than that the Congress, at least as much as the economic groups with whom we deal, have access to our open and full discussion of economic fact, outlook, and policy.

Our most recent discussions with members of the Joint Committee on the Economic Report have strengthened our belief in this principle and practice. We look forward to exerting every effort toward making our best contribution to the furtherance of one of the most important objectives of a free government—mutual respect and common purposes between those who serve in the executive and those who serve in the legislative branch. The only way to further these ends is to work together on problems confronting both.

JUN 11 1964

[1958]
BULLETIN 1

THE NEW ECONOMICS OF THE MEASURED WORLD

("GNP Economics")

Series On

HOW TO BE YOUR
OWN ECONOMIST

MACALESTER COLLEGE
SAINT PAUL • MINNESOTA

Bureau of Economic Studies
Arthur R. Upgren, *Director*

1958



INTRODUCTION

President Charles J. Turck, Macalester College

I am glad to introduce this first in a series of bulletins to be prepared and issued under the direction of Macalester's new Bureau of Economic Studies.

To nonprofessionals in the field economics has long been known as "the dismal science." There is nothing dismal about this first bulletin.

This first bulletin, "The New Economics of the Measured World," shows the progress economics has made in the use of measurement. The famous scientist Karl Pearson long ago said that we do not know much about something until we can measure it. The American economy is now capable of being described in measured terms, and Dr. Upgren, I think, has succeeded admirably in doing this in short compass. He uses in this first bulletin our successful experience in a colossal war production for the winning of the Second World War and our equally successful reconversion to a free peace time economy contrary to the great preponderance of expert opinion.

A second and third bulletin are also in press. Their titles are "Our Depressions Are Getting Smaller" and "What to do for the Recession of 1958." Because this is the time for national assessment of our economic position and desirable policies for the future as the result of the annual January appearance of The President's Economic Report, the Bureau of Economic Studies has prepared and is issuing all three bulletins simultaneously as a contribution to that wider understanding by which alone we as a nation may come by a sound and informed public opinion.

Readers of these bulletins will appreciate that they are intended to be "communicative economic research." The author of this bulletin and the authors of later bulletins will welcome criticism, suggestions, and comments on how to improve the bulletins and on topics for future studies of the Bureau.

We hope the reader will be impressed that this bulletin in a controversial field is factually based upon a world of measurement. That measured world is new in economics I am informed. I earnestly hope that it produces advances in our understanding. This is the responsibility of Macalester College as a liberal arts college.

DIRECTOR'S NOTE

This "How to be Your Own Economist" series of bulletins is launched with the present bulletin on the subject, "The New Economics of the Measured World." A second and third bulletin also issued at this time are entitled respectively, "Our Depressions Are Getting Smaller" and "What to do for the Recession of 1958."

The purpose of the series of bulletins is to open up economics as a "Do It Yourself" field of activity for all. The first three bulletins are all based upon simple and easily understood measurements easily grasped as they are selected to tell the story of what is happening in the world about us in which we all make and live our living. The language and the construction of the measurements is intended at once to be simple and to be the terminology of the businessman.

Historian Professor William L. Langer of Harvard University spoke out at the recent annual sessions of the American Historical Association by deploing today's want of "speculative audacity." It is hoped that some of this want has been met in the second bulletin affirmatively entitled "Our Depressions Are Getting Smaller" — in an economy which history evidences has seldom been tamed. The third bulletin, "What to do for the Recession of 1958", makes positive proposals which are not based on popular nostrums of the day. In this third bulletin a tax cut is shown to have "a cost of something less than nothing," at a very time when Sputniks I and II have made us emotionally receptive to the idea that by taxation 'till it hurts' we can make up for the deficiencies in our military progress (or lack thereof).

In the present analysis only the economic consequences of tax reduction are dealt with. The reader is invited to give his generous hospitality to the discussion to clinch his control over the new discipline in economics — "the economics of the measured world."

Later bulletins in this series on "How to Be Your Own Economist" will be based on the measured worlds for monetary and fiscal policy, for international economic policies, for the expansion of markets, and for the determination of proper national standards for the compensation of labor.

ARTHUR R. UPGREN,
Frederick R. Bigelow Professor of Economics

Macalester College, St. Paul.
January 7, 1958.

THE NEW ECONOMICS OF THE MEASURED WORLD

PURPOSE: The purpose of this first bulletin in the "How to be Your Own Economist" series of the Macalester College Bureau of Economic Studies is twofold:

1. To provide the simplest of all descriptions of the American economy and what has been happening to it. This description is given in measured terms — the new economics.
2. From that description to lay bare the past "boom and bust" nature of the American economy; to lay the groundwork for the taming of that economy (Bulletin no. 2); and to go on from there to outline policies for the recession of 1958 (Bulletin no. 3).

All this, it is believed, can be done with the new measured world which is now provided for economic analysis. Fortunately the measurements are given in terms and language common to the businessman's daily use.

METHODS: The method of analysis in these bulletins is the simple presentation of the record of the American economy's achievements; in production for war and reconversion therefrom; in the boom and bust of 1929 and after; and in the mild recessions of 1949 and 1954 from which so much can be learned for its own sake and for the purpose of developing desirable policies for the economic recession of 1958.

Most fortunately the record for all business cycles since 1929 can be presented in a single table displayed on a single page without burdensome detail. This is "TABLE I." The reader is most earnestly asked to be sympathetic and alert to this table's contents, from which so much can be learned fraught with ideas "to promote the general welfare" and "to maintain domestic tranquillity" — the twin objectives of our revered American Constitution.

THE NEW ECONOMICS OF THE MEASURED WORLD

"Table I."

"Table I" must deserve the foremost position in any measured reflection of the achievements of the American Economy. It is placed therefore on the opposite page and a duplicate page easily removed from the bulletin is provided for ready and convenient reference as the bulletin is read. This duplicate page provides sufficient blank space to record the progress of the economy until 1960.

GROSS NATIONAL PRODUCT OR EXPENDITURES 1929 - 1960 (all figures in billions of dollars)

YEARS:	I		II				III		IV			
	TOTAL GNP	TOTAL CONSUMPTION EXPENDITURES	GROSS PRIVATE DOMESTIC INVESTMENT		NET FOREIGN INVESTMENT		ALL GOVERNMENT OUTLAYS		Fed. Gov. Defense		State & Local	
			Total	Houses	Construction	Tools	Inventories				Other	
1929	104	79	16	4	5	6	1	1	Both	1	1	7
1933	56	47	1	1½	1	1½	-2	0	Both	2	2	6
1937	91	67	12	2	3	5	+2	0	Both	5	5	7
1938	85	65	7	2	2	4	-1	1	Both	5	5	7
1939	91	68	9	3	2	4	0	1	1	4	4	8
1944	211	110	7	1	2	5	-1	-2	89	1	1	6
1946	209	146	27	4	6	11	+6	5	21	0	0	10
1948 — 4th q.	264	180	42	8	10	19	+5	2	17	6	7	17
1949 — 4th q.	255	183	29	10	9	16	-6	-1	18	7	7	19
1950 — 2nd q.	276	188	49	12	10	20	+7	-2	17	4	4	20
1951 — 1st q.	319	210	60	12	12	24	+12	-3	27	3	3	22
1951 — 2nd q.	326	204	62	11	12	23	+16	-1	35	4	4	22
1953 — 2nd q.	367	231	53	12	14	24	+3	-3	53	8	8	24
1954 — 1st q.	358	232	46	12	14	23	-3	-1	46	8	8	27
1955 — 4th q.	402	260	65	17	16	26	+6	0	41	6	6	30
1957 — 1st q.	427	275	63	14	18	32	-1	4	45	5	5	35
1957 — 2nd q.	434	279	65	14	19	30½	+1½	4	46	5	5	36
1957 — 3rd q.	439	284	65	14	19	30	+2	3	46	5	5	36
1957 — 4th q.	433	283	61	14½	19½	30	-3	2	45	5	5	37
1958												
1959												
1960												

In Table I the dynamic nature of the American economy "on the 'bust' side" appears at once. The starting year for the figures contained in the table is 1929. The succeeding dates which have been carefully selected cover each turning point in the business ups and downs or cycles we have had since 1929. From 1929 through 1946 the calendar year figures are given as will be readily observed by a glance at the table. Thereafter the turning point *quarter* has been selected. (The data are not available by months but only by quarters.)

Across the table, that is horizontally, are given the components of our total *gross national production*, to which the term "GNP" is now so commonly applied. This total for GNP (second vertical column in the table) is made up of production for various "groups" in the nation. Group I contains the total amount of goods produced (and consumed) for consumers.

Group II makes up the goods in the total national output which are produced for, and which therefore make up, "gross private domestic investment." In this group we have residential housing (just "housing" in the table); all "construction" other than housing; "tools" making up all movable producers' goods such as machine tools, trucks and tractors, the equipment in an electric generating plant, etc.

Goods produced for "net foreign investment" are listed as Group III. Finally in Group IV are all goods and services produced and used by all our governments (federal, state and local). The net foreign investment (the single item in Group III) essentially represents the net exports for which we are paid and which are "invested" abroad to the extent we make advances abroad.

The outlays of all governments, Group IV in Table I, are divided into the "defense" and "all other" expenditures of the Federal government. The final column here provides the amount of expenditures of all state and local governments (for schools, hospitals, highways, and other municipal improvements).

NOTE: Two final comments are: (1) all figures are given as "annual rates" for ready comparison and (2) all these amounts are "in billions of dollars."

The "annual rate" figures given in the table are prepared in this manner by the department of commerce. This is most helpful for no juggling of the figures is needed by author or reader. Finally because we, collectively in the nation, can only *buy* what must have first been already *produced*, our gross national *production* is synonymous with our gross national *expenditures*. Thus we *produce* houses and have a national expenditure for this same housing. The analysis may now proceed. With an understanding of Table I, your B.S. in Economics is now conferred upon you. Successful later analysis will win your advanced degrees.

THE NEW ECONOMICS OF THE MEASURED WORLD

When the total gross national production (GNP) fell from 104 billion dollars in 1929 to 56 billion dollars in 1933 and did not regain the 1929 level until the war year of 1941, the decade of the 1930s came to be known as the years of The Great Depression.

Here was a decline of 48 billion dollars in our total production. That measured the amount of product the American labor force was now "not required" to produce. That is a euphemism for "unemployment". And unemployment for the ten years from 1931 to 1941 averaged 9,958,000, not including the massive additional "hidden" unemployment represented by 5,000,000 Americans then living on farms but quite unproductive. That is the number taken off farms in the early 1940s and added to the civilian and military labor supply of the country. Interestingly enough, and to prove this amount of hidden unemployment on farms, total farm production rose at the same time — from 1940 to 1945 — by more than 42 per cent.

Thus the 1929-1933 "bust" was a 48-billion-dollar affair, and the decline may be measured as a 46 *per cent* decline. Its great magnitude led Professor Irving Fisher to declare that we, the entire nation of us, were insolvent. We could not live *and* pay our debts out of a national output now reduced by almost half.

Will Rogers suggested that since we were doing so badly with the country we ought to give it back to the Indians.

There is a great deal to be learned out of that most stupendous economic decline of all.

First there was its process.

That total GNP declined by almost half — by 48 billion dollars — is readily seen from the figures in Table I. Consumption expenditures (Group I outlays) declined at the somewhat lesser rate of 32 billion dollars (from 79 billion dollars in 1929 to 47 billion dollars in 1933).

The total of our gross private domestic investment declined by more than 93 per cent in falling from 16 billion dollars in 1929 to only 1 billion dollars in 1933 (Group II).

Adding to this 15 billion dollar decline the additional 1 billion dollar decline in net foreign investment (Group III) produces a total decline of 16 billion dollars in all "investment."

It is the highly significant relation of this 16-billion-dollar decline in "investment" to the 32-billion-dollar decline in "consumption" or to the 48-billion-dollar decline in gross national production that gives a key to understanding the cause and cure of the business cycle.

When there is doubt about the future, "nothing is as scared as a million dollars". This refers to the act of "investment" by businessmen. And when

there is doubt about the future, families also do not purchase new homes. As a result "gross private domestic investment" contracts sharply. This is the point of origin of a considerable part of all our personal incomes. Then the contraction of this "primary investment" is followed by a second spiral of contraction of "consumption expenditures".

The relation of the decline in "primary investment" to the decline in consumption is called "the multiplier". "Multiplier" is used because the downward spiral *does multiply the decline of investment into a larger decline in consumption*. This grows out of the fact that if houses and factories are not built, then there is that much decline in investment. That decline, however, is then magnified and multiplied into a second decline in consumption. First of all less is spent on investment. Then because this reduces incomes of workers who build houses, factories and tools, the spending by their families in turn falls. Now we have the explanation of what happened from 1929 to 1933.

The decline in investment, as we have seen, was 16 billion dollars from 1929 to 1933. This was multiplied into a further 32 billion dollar additional decline in consumption. This "multiplier" had a value of 2.00, (16 divided into 32). However the data in Table I suggest that we are interested in *total decline* in GNP. Our interest lies here, because GNP totals measure the potential to create jobs and employment. And it is jobs and employment rather than distinctions between "primary investment" declines and further declines in "consumption expenditures" which interest us and dictate economic policies.

So we have this relationship established:

*The causal force in economic recessions is the failure of investment to be maintained.**

This leads to a multiplication into a larger decline in gross national production and employment.

The *multiplier* is the term applied to measure the greater decline. In the 1929 - 1933 Great Depression the decline in GNP proved to be 48 billion dollars or three times the decline of 16 billion dollars in GNP.

We shall at a later point take up from Table I the analysis of later depressions showing how by positive economic policies we have been able, not to change the theory of the multiplier, but to offset its effects. By so doing it has been possible to reduce to one-quarter of its expected size this measure of intensified economic contraction in the (therefore) "mild" recessions of 1949 and 1954. (See Bulletin No. 2, "Our Depressions Are Getting Smaller.")

The multiplier, of course, can measure economic expansion as well as contraction. In the great economic advance of 1954-55, an advance which carried gross national product forward by 44 billion dollars — without price advance or price "puffery" — the rise in gross private domestic investment (plus net foreign investment) was 20 billion dollars, (Table I).

*"Failure of the money supply" can permit still further deepening of the depression.

Thus the economic growth or expansion in housing and all other construction, the rise in investment in tools and inventories, and the gain in net exports — all measured at 20 billion dollars — produced larger incomes to increase consumption purchases by 28 billion dollars. The multiplier had a value somewhat above 2.00.

We shall give attention later to the mild contractive results in the 1949 and 1954 recessions (Bulletin 2). Up to this point we have seen in our analysis the spiral of depression in the 1929-1933 Great Depression and the spiral^o of economic expansion from 1954 through 1955. The third bulletin will conclude with consideration of the price rise of 1956 and 1957, as seen from the vantage point of the GNP analysis, and conclude with the recession of 1958 and recommendations to ameliorate it, as was so successfully done in 1954 and in 1949.

Economic growth or expansion is again (1958) our national objective. We are now failing to achieve it with the presumptive loss of 15 billion dollars in gross national production, accompanied by a probable loss in Federal budget receipts of 3 billion dollars. Such losses as these likewise deserve obviation.

CONVERSION TO AND FROM WAR

The analysis of the war years, from 1939 to the peak of production for war in 1944, and the postwar reconversion is of special interest. That postwar reconversion from military to civilian production was most successfully completed with a decline in total output (GNP) of less than one per cent despite a reduction in expenditures for war (1944) of 68 billion dollars (to 1946) equal by itself alone to wiping out of one-third of the wartime gross national production.

The first publication of the entire GNP tables, leading to these possibilities of "GNP economics" did not occur until the publication of a justly famous "Supplement to the Survey of Current Business — May, 1947". Perhaps owing to the fact that this first publication of the gross national product tables did not occur until a year after the postwar reconversion had been successfully accomplished, the economists of the Federal government may be forgiven for what they later so frankly termed "the great mistake" in forecasting economic recession after the war's end. The forces which produced the full recovery were evident, if not all of the basic statistical material was yet in print.

The rise of 88 billion dollars in production for war from 1939 to 1944 (see Table I) was achieved only one part by reconversion of our industries to war and "nine parts" by what may best be called "extra effort" — meaning the provision of war needs by expanding total production.

Thus between the years 1939 and 1944 we see (Table I) that the Federal

^oAlways called "growth" if there is no subsequent "bust".

government's defense outlays increased from 1 billion dollars in 1939 to a total of 89 billion dollars in 1944. However the figures for total GNP in this same period (second column, Table I) increased no less than 120 billion dollars. The rise was from a total GNP of 91 billion dollars in 1939 to a total of 211 billion dollars in 1944.

Thus did our wartime increase in total output cover the defense needs of our country and allow for 55 billion dollars of lend-lease to spill over to our Allies. We also were able to increase total consumption expenditures by a further 36 billion dollars. This was only in part due to a price advance here; many consumers expenditures for services—travel, entertainment, hotel occupancy, etc.—rose markedly during the war years.

This tremendous wartime growth was the peculiar result of the economic *milieu* of the years just prior to the war. In 1939 there had been the 9,480,000 men and women unemployed and the hidden 5,000,000 unemployed on our farms. The hours worked per week were only 37.7 in 1939 and many women and older men were ready to enter the labor market in response to the patriotic calls and high wages. Then as the pressure for production increased and the 40-hour week became a wartime casualty, hours of work per week increased up to 45.2 in 1944. Calling all these slack resources into employment was the extra effort which produced the 88 billion dollar rise in war production and the 36 billion dollar additional rise in consumption expenditures.

"Conversion of industry" was widely touted as the source of our miraculous wartime production. Government non-defense outlays by state and local agencies as well as by the federal government did decrease by 5 billion dollars in the years of the war. Our import dependence increased by 3 billion dollars as we offered gold for the imports we required (4 billion dollars of our gold hoard was so used). The failure to keep up our exports was explained by our unilateral announcement of the "doctrine of equal sacrifice". This doctrine stated that where we did not produce for ourselves we would not produce for export.

The final area of modest conversion of resources from civilian production to war production took place in housing and in a very modest exhaustion of inventories. Here the net draft for war was 3 billion dollars, a modest figure indeed.

The total amount of war production thus obtained by conversion (instead of by output *expansion* or "extra effort") amounted to 11 billion dollars. Compare that with the total gain in production for war amounting to 88 billion dollars. That should make it clear why it can be said that 12½ per cent of our wartime production for ourselves and our Allies was obtained by conversion and 87½ per cent of the sinews of war were produced by enlargement of production totals.

The exciting period for the use of GNP economic analysis is the period of conversion back from war production to a civilian economy. The "poten-

tials" which created the economic pressures or forces for a successful re-conversion were powerful and should have been far more widely appreciated than they were. Here they are listed for the reader's appraisal of the power they would have. That power is to be related to the 211-billion-dollar economy we had in 1944 and to the 68-billion-dollar defense, or war, production which we would want to replace promptly in the first postwar year, 1946. The forces which were built up were these:

1. Income levels originating, from 1944 to the war's end, in this more-than-two-hundred-billion-dollar gross national product. These incomes were twice the prewar levels. Families thus had to learn, in the post-war period, to be able to spend two dollars where they had never before had more than one dollar to spend. The lesson was easily learned.
2. There was accumulated during the war an extremely large addition to the country's liquid assets. This *addition* was placed at 150 billion dollars of liquid assets owned by individuals and 75 billion dollars held by corporations. Thus there was available for postwar purchasing *additional* liquid assets amounting to 225 billion dollars. This was available to re-inforce such buying as could not be financed out of current income.
3. As a result of the cessation of production during the war of our automobiles, radios, electric refrigerators, electric appliances and many machinery items for industry's peacetime production a huge vacuum of goods was built up. This was commonly called "starved demand." Its size and amount was measured by Professor Sumner H. Slichter of Harvard University just as buying potentials were measured by others. This demand, "deferred demand," measured, before the war's end, well over fifty billion dollars.

Cash incomes and cash in liquid assets hoards abhorred this vacuum as the war ended. Rushing into the vacuum they produced results we can observe in the figures contained in Table I for the years 1944 and 1946. Incidentally, for those who like to acquire "theory," this method of subtraction of the record for 1946 from the like data for 1944 is the method of "first differences".

The following table measures the forces of decline due to termination of war production and the forces of advance which were created out of the "konjunktur" which prevailed as the war came to a successful end.

Reductions in Spending		Advances in Spending	
War production	\$68 billion	Consumers' outlays	\$36 billion
Other Federal outlays.....	1 billion	Gross private domestic investment (primary investment)...	20 billion
		Net foreign outlays*	7 billion
		State and local expenditures...	4 billion
Reductions in expenditures		Total increased outlays.....	
\$69 billion		\$67 billion	

*Here the first "burden" has been placed on the use of algebraic addition inasmuch as this net foreign investment was negative at 2 billion dollars in 1944 (net imports for war use) and positive at 5 billion dollars. The imports, net at 2 billion dollars in 1944 were produced in other countries. The net exports of 5 billion dollars gave rise to production in the United States and thus assisted in the reconversion from war production. For those troubled by algebraic addition the useful key to the conclusion that the rise here was to be measured at 7 billion dollars is to consider the rise in Fahrenheit temperature from 2° below zero to 5° above. The degrees of advance are 7.

Thus we observe that at the war's end the American economy generated advances in expenditures for civilian purposes of 67 billion dollars. These were sufficient to offset all but 2 billion dollars of the 69 billion dollars by which Federal spending was reduced. The net "force for decline" was a mere 2 billion dollars. This decline reconciles with the fall in gross national production as a total from 211 billion dollars in 1944 to 209 billion dollars in 1946. The decline thus was less than 1 per cent — a most remarkable reconversion of the economy of the United States.*

After the remarkable record of successfully achieving an 88 billion dollar production for war and terminating it with remarkable rapidity and yet with a successful reconversion to a full employment civilian economy, the postwar boom of 1946-48 is of reduced interest. In this period, as in the war, there was a second 30 per cent advance in prices. This was caused by the postwar release of the "suppressed inflation" of the war period. With the abandonment of price control and rationing there came a postwar price rise whose causal roots were to be traced to the doubled build up of the money supply in the war.

Here our story ends — for the present bulletin. It has dealt with "The Great Depression" of 1929-1933, with the so-called conversion to war, 1940-1944, and with our astoundingly successful reconversion to a peacetime economy, 1944 to 1946.

The next bulletin deals with the recessions of 1949 and 1954. Its title is "Our Depressions are Getting Smaller." The large earlier recession tendencies have been "tamed" indeed as we shall see.

The third bulletin in this immediate series deals with desirable policies for the "recession of 1958". Much was learned in the successful (Democratic) tempering of the recession of 1949 and the equally successful (Republican) taming of the recession of 1954. Much more should be learned from the great economic expansion of 1954-55. Can we put all this knowledge to good use in ameliorating the recession of 1958?

*The author, at the department of commerce in 1941-42, was assigned the problem of making studies of the likelihood of a successful postwar conversion without reliance upon "a shelf of public reserve" for providing employment in the postwar period. The shelf of "private works reserve", the defensive slogan of the small minority of postwar planners who believed private enterprise "could come through", did prove adequate. However because of the high peacetime military budget of 1946, 21 billion dollars compared to a mere 1 billion dollars in the prewar years, we as a nation were never faced with the rhetorical question then so commonly asked: "What would happen when the Federal government stopped spending one hundred billion dollars a year for war." Quantitatively two-thirds of this question was successfully answered with "a miss" of less than one per cent.

JUN 11 1964

[1958]
BULLETIN 5

PRODUCTIVITY AND WAGES

("GNP Economics")

Series On

HOW TO BE YOUR
OWN ECONOMIST

MACALESTER COLLEGE
SAINT PAUL • MINNESOTA

Bureau of Economic Studies

Arthur R. Upgren,

Frederic R. Bigelow Professor of Economics

1958



MACALESTER COLLEGE

ST. PAUL, MINNESOTA

OFFICE OF THE PRESIDENT

This bulletin, "Productivity and Wages", is the fifth issued this year by the Bureau of Economic Studies of Macalester College. The subject is timely for the nonprofessional person interested in economics who can today sense the importance of this subject.

As a nation we have been struggling to come by a rational wage policy. That is the subject to which Dr. Arthur R. Upgren, director of the Bureau, has addressed himself in this study. It is therefore issued as a contribution by Macalester College to the further understanding of the problems of today.

CHARLES J. TURCK

President

May 1, 1958.

PRODUCTIVITY AND WAGES

Introduction

Everyone knows that the country's production has increased greatly over the years. We like to brag about "gross national product"—GNP. In fact these bulletins have been labelled "GNP Economics". That is not because we like to deal with GNP exclusively. Rather it is because we like to deal in "the new economics of the measured world". These words were indeed the title of the first bulletin in this series on "How to Become Your Own Economist".

It is *measurement* that we like. When the distinguished international Professor I. M. Kolthoff of the University of Minnesota spoke recently on science and education he said that "in science we use numbers a great deal". These were simple words to mark "measurement" as the distinctive feature of science.

In our earlier bulletins we took a hard look at the measurement of the total GNP, its distribution to consumers, business, government and overseas, and to the cyclical swings in GNP which we have experienced and one of which is occurring right now. We pointed out that our depressions are getting smaller or that, in other words, we are succeeding in growing and at a steadier pace.

In this bulletin we propose to look at other aspects of the growth of GNP and particularly at what economists call "productivity". By this term economists mean, generally, *output per man-hour*.

Many people have made the mistake of saying that labor has caused the increase in output per man-hour since we measure productivity in terms of output per man-hour. This is like saying that the thermometer which measures the temperature in a room causes the temperature in the room to rise or fall. We shall say something about what causes output per man-hour to rise and fall a little later but here we can just say massive amounts of capital and a high skill of management, not sweat, have been most important.

This problem of understanding and measuring productivity is one of the most important problems we have. Over the years we have been able to increase the quantity of products we can produce in an hour. Economists refer to the rate of this increase as increase in productivity. The fact that we have succeeded in increasing the amount we can produce each hour makes it possible for us to consume more—this is what we mean by our rising standard of living. Compared with other countries we have a high standard of living. We also have more leisure than workers in other countries have.

All of us want to increase our standard of living as quickly as possible and we try to do this by trying to increase the amount of wages we get each hour. But if the amount we produce each hour does not increase as rapidly as the increase in our wages for each hour of work we have a problem of *excess* wage increases. *The "excess" produces inflation rather than goods.* This has proved to be one of our most difficult postwar problems. Because it is so important for all of us, we want to give it very special attention. It becomes the problem of stopping our persistent postwar threat of continuing inflation.

PRODUCTIVITY, PRICES AND WAGES

A. Per Capita National Product

The GNP for a nation is a measure of the *total* output of that nation. If we want to compare the output of countries of different sizes, we then use output per worker or output per capita. Output *per capita* gives us a measure of how well off the people in different countries are regardless of the size of population. The latest available figures of product per capita for many different countries are for 1952-54. Soviet bloc countries will not give us their figures on a comparable basis so we cannot include them. However, the estimates of independent experts place the per capita product of Soviet Russia at about one-third that of the United States despite the much longer work week in Russia.

Here then are the different per capita products for 12 of the 55 countries studied by the United Nations. The figures are all stated in U.S. dollars.

Country	Annual Per Capita Product
United States	\$1,870
Canada	1,310
Switzerland	1,010
Sweden	950
France	740
Germany	510
Ireland	410
Italy	310
Mexico	220
Japan	190
India	60
Burma	50

When output per capita is low so also is income per capita. Our table which is "production" might be turned around to measure the material well-being of each country. The tragedy in the countries at the bottom of the list, then, is not only that income is so low, but that output also is so low. These differences between the high output and low output countries are mostly the result of immense differences in the amount of tools and power with which each worker has been supplied. That this capital equipment is well supplied is the job of investors willing to take risks. That it is carefully and efficiently used is the job of management and skilled labor.

B. Production and Productivity in the U.S.

The United States has not always enjoyed its present high level of income and output. This high level has come from a long period of economic growth.

There are three dramatic facts which we all should understand:

1. Over the long period we have increased GNP, *our total production, as a nation*, at an average annual rate of 3 per cent. To accomplish this, output per man-hour has increased about 2.3 per cent a year and the output due to growth in the labor force has added slightly under 1 per cent a year to output to make up the 3 per cent. All this has been done and we have also had a significant reduction in the length of the work week.
2. We have had short periods of time in which output per man-hour has actually declined and other periods in which

the rise has been greater than the long-term increase of 2.3 per cent. In the period 1947 to 1953 we had a very high rate of increase in output per man-hour. This was the result of really "stepping on the gas" as we "got going" about two years after the end of the war. More recently, in 1956 and 1957, output per man-hour has been increasing at a rate *below* the long term rate. While we could by no means expect to maintain the 1947-53 short run very high rate of increase in productivity, we should be able to do better than we have done during the recent 1956-1957 period.

3. If we are able to get back to and maintain the long term rate of increase in output per man-hour, our total GNP will exceed 725 billion dollars in 1975 compared with 415 billion dollars in 1956 in dollars of equal purchasing power in both years.

C. Hourly Wage Rates and Productivity

The general proposition we have set up may be stated this way: What each nation can consume depends upon what it can produce. What a nation can produce depends first on its total number of workers—economists call this *the size* of the labor force.

But if the only way we could increase GNP was by waiting for the labor force to grow there would be little or no increase in the well being of each of us in that labor force. In fact the reverse might be the case. Population might grow faster than output could be made to grow so while the total would increase each individual would have less. The great discovery of the industrial revolution was that we could with tools, capital and power make the output of each hour of work grow. And, at the same time that this was being accomplished, we could pay higher wages for each hour of work or we could lower prices. In either case *real* income would rise.

The problem of inflation shows up when we try to push hourly wages up faster than productivity is rising. This was not such a serious problem before the Second World War but with the continued growth of large and powerful unions after the War this has developed into a very real problem which can threaten our economic stability and thus threaten our economic growth.

This is where we have failed in the postwar period. Our failure is measured in the following comparisons taken from a recent study of the Bureau of Labor Statistics:

Fact 1. *Between 1947 and 1956 average hourly compensation in non-farm industry increased 61.4 per cent or 5.5 per cent per year.*

Fact 2. *Between 1947 and 1956 output per man-hour in non-farm industry increased 26.1 per cent or 2.6 per cent per year.*

Here we see that hourly pay rose more than twice as much as the increase in the output of that hour's work. This has been a basic cause of inflation. Chart I pictures this process.

In addition *unit labor cost*—this is the wage cost for one unit of output and directly influences the price of that unit—has increased substantially in every year of the postwar period with the exception of three years. In 1949 and 1950 unit labor cost declined and in 1955 the rise was less than 3/10 of 1 per cent.

Consumer prices likewise have increased substantially in every year of the postwar period with the exception of three years. In 1949 and 1955 prices declined and in 1950 the rise was less than 1 per cent.

A COMPARISON OF THE RISE IN WAGES, THE RISE IN PRODUCTIVITY, AND THE RISE IN PRICES, 1947-1956

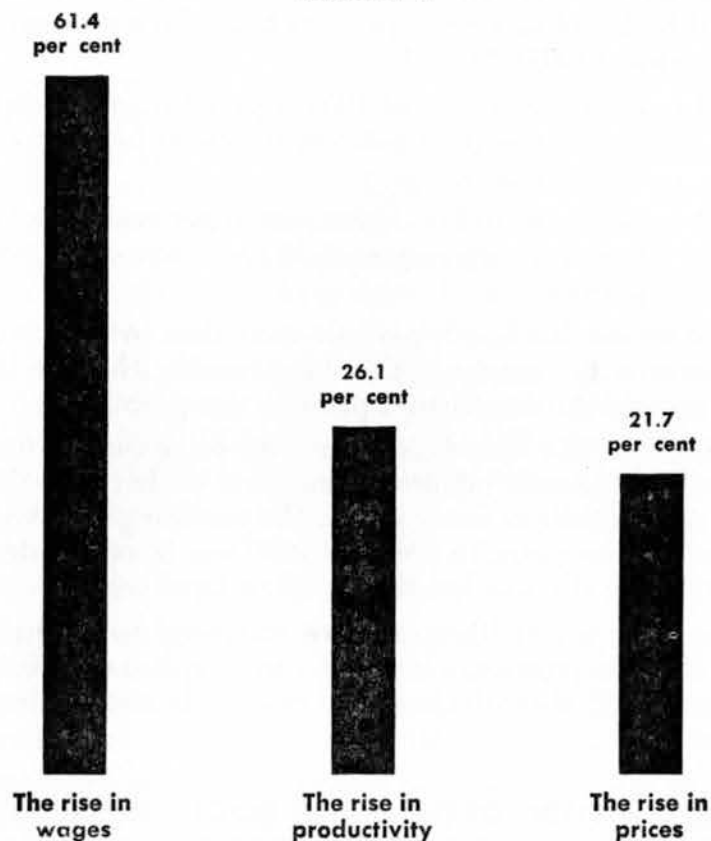
The rise in average hourly wages in industry, the rise in productivity or output per man-hour, compared with the rise in consumers prices, 1947-1956.

The chart at the top of page 8 reveals that the greater rise in wages than in productivity produced a rise of 21.7 per cent in the cost of living.

If output per man-hour does grow at the same rate, or faster, than the rate of increase in wages, there would be no inflation. Prices will then not rise because the increased flow of goods is sufficient to sate and satisfy the increased amounts of wages.

When wages move upwards and output per man-hour does not increase at the same tempo as the increased "beat" for wages, then prices must move up. Chart I.

CHART I



AN ECONOMIC INDICTMENT

Clearly there is enough evidence to sustain an indictment that money wages have increased faster than productivity in the postwar period, and thereby have contributed to inflation.

This indictment can properly be made by the American people because they are the ones injured by the inflation of prices. They should demand that wage increases no longer exceed long-term productivity gains, as they have in the postwar period.

Today we have another round of wage negotiations being entered upon. The public has a vital stake in the outcome. This is particularly true of the fixed income groups. These include members of the teaching profession.

THE POWER TO INCREASE WAGES

The wage-price push has originated in the strongly unionized industries. The force which has caused the increase in wages has been commented upon by many competent authorities including Professor William J. Fellner of Yale University. In a letter published in *The New York Times*, March 25, 1957, at which time we had had a year of rising prices and were then entering upon another round of wage negotiations as we have done again this past March, Professor Fellner wrote:

"We are certainly faced here with the harmful consequences of monopoly power. The reasonable norm (guide for rate of increases in wages) would be that of gearing average wage trends approximately to average output-per-man-hour trends in the economy as a whole. On the realistic assumption this would be a rise in wages at about 2 per cent a year in the long run."

THE ISSUE JOINED

In his statements before the Kefauver Subcommittee on January 28 and 29, 1958, Walter Reuther, Vice President of the AFL-CIO, gave the public both cause for hope and cause for alarm saying: "What we are saying is we will take our minimum demand out of the general level of productivity in the whole economy. . . ."

Now, of course, "productivity in the whole economy" defines what should be the maximum demand—not, as Mr. Reuther suggests, the minimum. At least this is the case if we are to have price stability. To ask for all the productivity gain and more on top of that will be inflationary.

There is another way of looking at this. If Mr. Reuther succeeds in obtaining a larger increase than his members are entitled to under the test of productivity gains, other groups are bound to get less. This is because as a nation we cannot consume more than we produce.

If we raise pay too rapidly, and that means increasing pay faster than we are able to increase output, then we pay higher prices. We all have to pay these higher prices. Only the workers in the strongly unionized industries get enough more money to "break even". If Mr. Reuther's members are enabled by their bar-

gaining power to consume more, and other union members are equally successful, others must consume less. This is precisely what has happened to all groups on fixed incomes or slowly increasing incomes in the postwar period. This is the damage done by the inflationary wage policy which produces wage increases greater than productivity gains.

It is also important to observe that as his wage increase standard Mr. Reuther insists on using by far the highest available estimate of the postwar short-term rate of increase in productivity. On this basis he projects a productivity advance of twice the generally accepted long-term rate experienced by our country.

This brings us to a consideration of the various productivity measures.

THE VARIOUS MEASURES FOR OUR PRODUCTIVITY

Long-Term Measures

There have been a number of studies by various individuals and groups attempting to measure our national long-term rate of productivity gain. Among these are such competent and distinguished research groups as:

Joint Economic Committee Staff,
the Committee for Economic Development,
the Twentieth Century Fund, and
the National Bureau of Economic Research, now headed
by Dr. Arthur F. Burns of Columbia University,
formerly chairman, 1953-56, of the President's
Economic Advisory Council.

While the studies of these groups do not yield precisely identical results, a fair average of their findings is about 2.3 per cent per year increase in productivity. The 1958 Economic Report of the President, also referred to in these studies, preferred to cite a slightly lower figure of about 2 per cent per year.

Short-Term Measures

If the average long run rise in productivity is around 2.3 per cent a year, the question may properly be asked why are there

short-term periods in which the increase in productivity is higher or lower than this.

A glance at the accompanying table provides background to help in the answer to this question.

TABLE I

Average Annual Rates of Change in Output Per Man-Hour
In the Total Private Economy

The Years for Which the Change Occurred	How Long the Period	Direction of Change in Productivity	Average Annual Rate of Change in Productivity
1909-12	3 years	Up	+2.5%
1912-18	6 "	Down	-1.4%
1918-26	8 "	Up	+4.1%
1926-33	7 "	Down	-0.4%
1933-45	12 "	Up	+3.7%
1945-47	2 "	Down	-3.1%
1947-53	6 "	Up	+3.6%
1953-56	3 "	Up	+2.2%
<hr/>			
1909-56	Entire Period 47 years	Up	+2.2%

Source: Calculated on basis of data supplied by the Joint Economic Committee Staff.

This table, based on estimates of the Joint Economic Committee Staff, reveals three periods of falling productivity and four periods of rising productivity with the last period divided into two sub-periods. The periods of falling productivity include the years of the First World War (1912-1918), the years 1925-1933, and the years 1945-1947 immediately following the Second World War. Here we find one war period, one period of postwar reconversion, and the period of the end of the great boom of the 1920's including the first years of the Great Depression of the early 1930's.

The periods of *rising* productivity are four in number: 1909-1912, 1917-1926, 1933-1945, and 1947-1956. The unique feature of all these periods is that of great expansion of total output. This illustrates the double gain of economic growth. We thereby win a gain in total output and as well the gain in productivity as the second dividend.

The final period of marked gain in productivity (1947-1956) divides itself logically into two sub-periods—1947-53 and 1953-56. In the earlier period, to 1953, the trend of productivity increases averaged 3.6 per cent per year. Since 1953, however, the trend has returned to a level of 2.2 per cent per year—very close to the long term trend.

The very high rate of increase recorded from the end of the war to 1953 was the result of very special factors. The process of reconversion from military to civilian production was accompanied by low output and inefficiency. The processes of production were all “messed up” in this period of confusion as we restored civilian production.

In 1947 output per man-hour reached a lower point than at any time during the preceding three years. Measured from 1947, we were now ready for the rise in productivity which came with the “catching up” period.

A recent study by the United States Bureau of Labor Statistics covering this same period wholly confirms this postwar pattern of productivity change although differences in methods of calculation result in estimates higher than those above. According to this method of calculation *the 1947-1953* rate of increase was 4.3 per cent per year and the rate *since 1953* has been about 2.5 per cent per year.

As we observed earlier, the postwar increase in hourly wage rates has exceeded the gain in output per man-hour by about two times. The reckoning would clearly show that wage increases were so far above productivity gains (even at their high average for the postwar decade) that present wages should be reduced, not increased. This would restore justice to other groups who have been injured by the postwar inflation caused by excessive postwar wage increases.

In summary, our productivity measures indicate a long-term rate of increase of about 2.3 per cent per year. The short-term rate of change in productivity has at times been higher and at other times lower than the long-term rate. Currently, since 1953, we have experienced a rate of increase in productivity very close to the long-term average.

HOW SHOULD PRODUCTIVITY GAINS BE DISTRIBUTED?

It has become commonplace to assume that gains in national productivity can be reflected only in wage increases. With the advent of powerful unions this may indeed be the only practical course open that meets the national goals of a stable price structure and a high rate of economic growth. However, union leaders have frequently framed their demands in other terms and we should take note of this. Finally, many economists have had something to say on this subject. Let us look, first, at this.

The first course is to hold wage levels *constant* as productivity rises. This has the great merit, so widely demonstrated in past economic literature, of being precisely the course which results in *all* groups sharing in the fruits of the national gains in productivity. Productivity increases now yield a larger total product. Dividing this larger total product into a constant income level results in prices *declining* in proportion to the productivity *advances*. It is *via these lowered prices* that all groups, especially the fixed income groups and including college professors, are allowed to buy more and thus share in the gains of our rising national productivity.

In the light of our inability for the past 18 years to control the wages-cost-price push towards inflation, this course is most attractive. A drive to achieve it might at least provide the *bias towards price stability* which is so badly needed in all the Western World. In a very real sense the advances we have had in the production and distribution of goods are the result of contributions from all groups in society—management, labor, scientists, technicians and even college professors. What better way is there to recognize and reward this contribution than through making the desirable goods of this life available to all at lower prices?

The second policy is to tie wage increases in *specific industries* to the productivity advances in *those industries*. This proposal will have both inflationary and inequitable results. Workers in industries *not* enjoying marked, specific productivity advances will fight for a wage as nearly as possible in line with the high wage increases in the industries enjoying marked and large productivity increases. The latter are for the most part industries with strong unions which exert both pressure and monopoly power.

(A notable exception to this is agriculture in which the *level* of output per man-hour was very low compared with manufacturing but which has enjoyed a very high *rate of productivity gain* in the postwar period.) If workers in other industries succeed in obtaining increases in wages of larger amount than their productivity rises, the final result becomes inflationary. This follows because now incomes have, in total, risen more than productivity totals have increased.

The third course for national wage policy is to relate wage increases to the *national average* rate of productivity increase. This will result in neither inflation nor deflation and this policy will promote price stability. Now total income derived in all industries equals the general rise in total product. Therefore, the larger increases are adequate to purchase the larger product *at constant prices*.

As between the three alternatives, we must rule out the second both on the grounds of the inequitable distribution of productivity gains and on the grounds of our long-term national economic health. We would like not to rule out the first alternative but in the practical world of large unions it is doubtful that we have any choice. We come then to the third of our possibilities. Wage policy, if it is related to the *nation's* prospective increase in productivity—between 2 and 2.5 per cent per year—is most likely to meet the twin goals of economic policy—price stability and an equitable distribution of the gains from productivity.

SUMMARY AND CONCLUSION

Productivity—output per man-hour—is the key to understanding our high standard of living. The level of output per man-hour depends upon our willingness to supply labor with massive amounts of tools and power and to organize all those efficiently to meet consumer's needs. This is the function of management.

We have succeeded over the long term in increasing output per man-hour about 2.3 per cent per year. There have been short periods of time when the rate has been lower than this and others when it has been higher.

We as a nation cannot consume more than we produce. If wage rates per hour increase faster than output per hour increases, the result will be inflation.

We have seen that in the postwar period the increases in wages have been more than twice the average increase in worker productivity.

This has made our postwar wage policy an inflationary wage policy.

The American people do not want inflation and have the right to demand that those who hold to policies which cause inflation should change those policies.

We could hold wages constant so that as productivity rises all groups share in the gains of rising productivity by all being able to buy more.

In the opposite direction if we increase wages in the industries with powerful unions by amounts equal to the maximum rise in productivity in those industries, other unions will demand like wage increases which will be above their increases in productivity. This sends total incomes up faster than total productivity increases. This is an inflationary wage policy.

Increasing wages therefore must be limited to the pace of *increasing national average productivity*.

This rate of increase over the long run has been about 2.3 per cent a year. This has also been about the rate of increase since 1953. If a little pressure upon managements is wanted at all times, we could hope for wage increases limited to about 2½ per cent a year. This will double wages without inflation in 28 years.

**OTHER BULLETINS AVAILABLE IN THE SERIES ON
HOW TO BE YOUR OWN ECONOMIST**

1. The New Economics of the Measured World
2. "Our Depressions Are Getting Smaller"
3. What To Do For The Recession of 1958
4. Security Against Depressions?
5. Productivity and Wages

JUN 11 1964

[960]

BULLETIN 8

File
Economics
WF

How Affluent Will the Sixties Be?

By **ARTHUR R. UPGREN, Ph. D.**

FREDERIC R. BIGELOW PROFESSOR OF ECONOMICS
AND DIRECTOR OF THE BUREAU OF ECONOMIC STUDIES
AT MACALESTER COLLEGE

A paper given at the
24th Annual Meeting of the
Midwest Economics Association
Minneapolis, Minnesota
April 28, 1960



MACALESTER COLLEGE

SAINT PAUL • MINNESOTA

BUREAU OF ECONOMIC STUDIES

MACALESTER COLLEGE

Office of the President

Macalester College is happy to make available to the friends of the College who are interested in economic problems this address by Dr. Arthur R. Upgren, Frederic R. Bigelow Professor of Economics. The present bulletin is Number 8 in the Macalester College series.

It is a pleasure to read Dr. Upgren's conclusion that the 1960's will be very affluent. He should be competent to make that judgment inasmuch as for twenty years past he has been engaged in measuring the course, past and future, of the American economy. In the latter part of the bulletin, some serious problems are raised which may confront the American people near the close of the decade. Dr. Upgren has had a close acquaintance with, and work in, banking in the United States ever since the formation of the Federal Reserve System. I think it highly significant that he is able to mark out the very important problems of liquidity, especially in the banking area, that we shall face and to do so a good many years before these problems become critical. It is much better to have such an advance warning today than an accomplished post-mortem after the event.

Macalester College is always glad to receive suggestions and comment, adverse or favorable, to help guide it in its publication and research program in the area of economics, banking and business.

Harvey M. Rice, *President*

Macalester College

May 2, 1960

How Affluent Will the Sixties Be?

By ARTHUR R. UPGREN, Ph.D.

FREDERIC R. BIGELOW PROFESSOR OF ECONOMICS
MACALESTER COLLEGE

1. Affluence in the 1960's

The 1960's will be very affluent. In fact the decade will be the most affluent the United States has ever experienced. This next 10 years will be precisely the opposite of the doleful 1930's. In that decade, we lost some \$200 billion of production. In the sixties, we will rise above the present level of production by more than \$200 billion.

In fact, President Eisenhower has told us that by 1970, at the present level for prices, we can achieve a total gross national production of \$750 billion. This will provide an average family income of substantially more than \$8,000 a year; in fact the amount of \$8,300 is often predicted for family incomes in the year 1970.

2. The Production March to the 1960's and 1970's

Total production in the United States has had a remarkable growth. The upward march began after the end of the deeply depressed 1930's. Gross national production at the end of the 1930's was not quite as high as the last year before that decade opened. In fact, in 1939 we had 9,480,000 unemployed compared with the peak figure of 12,830,000 unemployed in 1933.

In addition to these unemployed who were counted, many people were only partially employed, and we had an estimated 5,000,000 hidden unemployment on our farms. In the first half of the 1940's we took 5,000,000 people off farms and farm output rose by 42 per cent (from 1940 to 1945).

The war rather than the New Deal cured the Great Depression and its unemployment. In the six years following 1933, we reduced unemployment by less than 25 per cent from the peak figure of 1933.

The 1930's were all dismal.

So our economic growth in the 1930's was nil. Gross national production at prices then

prevailing was \$104 billion in 1929 and \$101 billion in 1940. In these years there was a decline in prices of about 12 per cent. Thus allowing for the lower price level, there was an 11 per cent gain in real production in the 11 years from 1929 through 1940 but it took until the first year of the 1940 decade to recover the 1929 level again.

From 1940 the march is rapidly upward, with a delightfully even series of \$100 billion steps for each five years from 1940 to 1960. Starting with a gross national production in 1940 at the \$100 billion level, we reached the \$200 billion level in 1944. Then before 1950 had ended, our total production advanced to \$300 billion. The \$400 billion level was reached in 1955 and the \$500 billion level will be reached in 1960, the present year. Thus in the past 20 years we have added \$100 billion to GNP every five years.

This rate of growth will continue. GNP will gross \$600 billion in 1965 and \$700 billion by 1970. (A reservation about 1970 is made later. It is serious.)

3. The Effects of Inflation

We must emphasize that much of the gain from 1940 to 1945 and from 1945 to 1950 was not very real, consisting of price puffery due to the rising price level which was marked in those two five-year periods. Since 1950, the movement of prices has been very much more moderate.

From 1940 to 1945 prices advanced 30 per cent. From 1945 to 1950 the advance was also 30 per cent from the higher 1945 level.

But from 1950 to 1955 the advance in the price level was only 11 per cent, and from

1955 to 1960 the advance has been 10 per cent. For the last year and a half, the price rise has been only one per cent per annum.

Thus the average gain in gross national production of \$100 billion in each of four recorded five-year periods and as estimated for two future five-year periods is a gain which has been growing in real terms. The population also has been growing so that the gain per capita is not quite as large.

This then is the promise for affluence as we shall enjoy it in the 1960's.

4. Rising Family Income and the Businessman

Perhaps the most significant feature of this rapid growth has been the inability of businesses to keep pace with it. In the rapid rise of family incomes from a level of \$4,130 in 1947 to \$4,440 in 1950, \$5,520 in 1955, \$6,260 in 1958, \$6,520 in 1959, and on upward to \$7,200 in 1965 and to over \$8,000 in 1970, the most important fact is the wide margin which has been established above a "subsistence" level of income.

According to the American Federation of Labor (AFL-CIO), something slightly under an income of \$4,000 a year will provide the minimum standard of American living. Now as incomes rise above this figure, the margin which makes up "discretionary," "optional-spending," and "volitional-spending" income

has increased purchasing power with an important "leverage" effect. It has been this very rapidly growing margin of income over subsistence that has made the long distance section of the Bell System such a remarkable "growth" industry. It is what sells more than one telephone in a home and it is what sells the various rainbow-hued colors. It also sells many long distance calls.

With the growth in spending the income over subsistence channeled into luxuries and durable goods, the increase in production in these industries will indeed be very great. Two examples are the swimming pool industry and the power boat industry. It is in this area of spending that many future consumer growth industries will be found.

5. Stability — A Requirement of Sustained Affluence

Affluence, of course, is a state of well-being. Well-being, in the economic sense. We, the American people, committed ourselves to pursue this objective in the Constitution with the words "advance the general welfare." This objective we constantly state and restate in terms of desiring an economy which has a rapid and stable rate of economic growth.

The stability we seek is a stability of the price level, a stability for employment, a stability of income, and a stability for purchasing power. A review of the past two decades will throw light on what we may expect here in the 1960's.

The 1930's were extremely unstable and very markedly *unstable* in a downward direction.

The 1940's were about equally unstable in an upward direction and marked heavily by the inflation that was the product of war. An in-

quiry into the fundamental causes of that inflation is desirable. We certainly can thereby learn if these causes are recurring.

6. Causes of the Instability of Prices, 1930-1950

Two separate and unrelated forces produced the inflation of the 1940's and 1950's. The first force was devaluation of gold by the terms of the Gold Reserve Act approved January 30, 1934. This act lowered the content in gold of the United States dollar by 41 per cent. Lowering that content resulted in our stock of gold on hand at that time being made into many more dollars, in fact 69 per cent more.

Here the increase in our total monetary gold stock was from \$4 billion of gold prior to devaluation to almost \$7 billion for the same weight of gold after the devaluation. As a result of a smaller weight of gold in the dollar, an ounce of gold made more dollars. This produced the well-known higher price for gold of \$35 an ounce after devaluation compared to \$20.67 before devaluation.

Since these changes took place in 1933 and 1934 when our prices and price levels for all commodities other than gold were very low, the opportunity was extraordinarily attractive for the rest of the world to sell us gold and buy what they wanted. As a result, our \$7 billion gold stock of early 1934 advanced to \$17 billion in 1939. Then came the Second World War.

Now Europe became an unhealthy place for gold. An additional \$7 billion of gold was shipped to us, bringing the peak figure for our gold stock to \$24.7 billion. This represented a full sextupling of our original gold monetary stock of 1929 and January 1934.

This larger monetary reserve helped drive down interest rates. Interest rates fell almost to the vanishing point. The larger monetary gold reserves at one time created excess reserves of more than \$7 billion (above the required reserves of approximately the same amount).

With this extraordinary richness of monetary and banking reserves the basis was laid for a tremendous expansion in the money supply. Huge bank credit expansion followed our entry in World War II in 1941. We now financed a very large proportion of the war by the sale of U. S. securities to the banks. All told, about \$100 billion of U. S. securities were sold to the entire commercial banking system. This enlarged total bank deposits subject to check from \$80 billion to \$180 billion.

Here we see in brief the basic causes of the inflation of the 1940's and the 1950's. That inflation, however, has been receding at a greatly diminished rate ever since 1948. It is a pity so few people know this to be a fact.

From 1940 to August 1948, prices rose about 9% per cent a year. For this eight-year period, the total rise in prices was 75 per cent.

From August 1948 up to February 1960, the price rise has been 1% per cent a year or a total price rise of 20 per cent for this 12-year period.

Clearly these figures reveal that the rate of inflation has been cut back by five-sixths in the two periods, first, 1940 to 1948 and second, 1948 to 1960.

7. No "Creeping Inflation" Since 1952 Nor After 1960

To an audience assembled in Minneapolis it is interesting that a savings conference of wide interest arranged by the University of

Minnesota in our city of Minneapolis brought the late Professor Sumner H. Slichter as one of the featured speakers. That was in 1952.

Professor Slichter launched the term "creeping inflation" at that meeting in Minneapolis.

Following the very time the term was coined by him, we had no inflation at all for a four-year period, from March 1952 to March 1956. Then came a typical investment boom described so well by Schumpeter. Plant and equipment expenditures rose by \$9 billion expanding bank credit and incomes without an expansion of total output until the "period of gestation" of this building of new factories and tools was completed in 1958. Here we had an 8 per cent rise in the price level. That price rise was unfortunate, but we see today, in 1960, the advance in total production of more than \$45 billion in real terms and about 11 per cent from the 1958 recession low. This output rise was certainly greatly facilitated by that expansion of industrial capacity from 1955 to 1957.

Since mid-1958 the price level, as has been pointed out, has advanced at a rate of barely one per cent a year.

The forces which produced this great inflation from 1940 to 1948 are non-repetitive. They are diminishing very rapidly and have diminished for the past dozen years. The supply of money today is back to the proportions which prevailed prior to 1929 when the economy was not experiencing any inflation. The Federal budget is today in balance. In fact, the only debt which has not increased significantly since the end of World War II has been the Federal debt. The debt of the Federal government and its agencies in the first thirteen years after the war increased only 6½ per cent. In the same period all other forms of debt increased from

200 to 435 per cent. The thrust to inflation caused by a deficit in the budget is non-existent at the present time and has been since 1946 with mild exceptions in 1953 and perhaps in 1958.

The single large deficit of fiscal and calendar 1959 produced incomes and consumption stability rather than serious rise in the price level. That promoted recovery rather than inflation.

The third force operating so strongly against inflation is today's more restricted rate of wage increase. In the recent steel agreement, the rate of wage increase was held down to about a 2.3 per cent cash increase for the workers and to a total increase of from 3½ to 3¾ per cent for the companies. This is according to the recently issued annual report of the United States Steel Corporation for 1959.

In contrast, the three-year steel wage agreement of 1956 raised wages by 8 per cent for each of three years, 1956-1959. That average rate of increase of 8 per cent a year for steel workers' wages also had prevailed for the twenty years ending with the new 1960 agreement which so sharply reduced this rate of wage increase, more than cutting it in two.

The reduction to a maximum figure of 3¾ per cent for the recently concluded agreement is indeed much less inflationary. In fact, it is almost within the range of the average annual increase in productivity of our workers. To the extent that other wage agreements follow this pattern, and they seem to be following it, we have very largely eliminated excessive wage increases from the economic picture thus serving to restrain the rate of inflation.

8. A Deflationary Future?

There is another deflationary force at work. Our bank liquidity has also been declining. The liquidity of banks, as bankers measure it, in 1929 was 23 per cent. After that year, we had tremendous economic difficulty, deflation, and financial collapse in turn producing the Great

Depression. Obviously with our independent banking system this liquidity level of 23 per cent is not at all enough. The two acts of (1) gold devaluation in 1934 and (2) financing at the banks during the war, 1941 to 1945, increased bank liquidity to 83 per cent.

This liquidity of course is not the liquidity ratio which an individual bank might calculate in a manner especially related to its own liability.

Rather it is the liquidity ratio for the entire banking system.

For example, when we pooled individual bank reserves after the formation of the Federal Reserve System, we found that the "pooled reserves" in the Reserve System were no more adequate for a general widespread financial drain than they were when lodged separately in the individual banks.

The liquidity ratio of banks comprises the assets, cash, reserves, and U. S. Government securities in relation to total deposits. These are the assets which will become quickly, and generally without borrowing, available to banks even in emergencies.

While the Federal Reserve authorities today are legally permitted to lend "on any good asset," the question of what are good assets and whether they will be deemed "good" when a time of trouble may come is most important.

In fact, *if the objective of bank policy under conditions of great economic stress is to prevent bank failures and prevent a decline in the total supply of money*, then it would have been better if the regulation or law had stated that in such times the Federal Reserve authorities could lend "on any bad asset." At such a time the maintenance of the money supply should be the most central objective of the Federal Reserve system. All assets other than cash and short-dated U. S. securities may not be good and indeed then may be "bad" assets. Perhaps a compromise in the law to permit lending "on any asset" would suffice. This is what the central banking authorities did not do in 1932-33 despite an earlier legally, "built-in" indemnification designed for just such an emergency. This, of course, is very serious business and it should be studied with its greatest care by the monetary authorities.

The liquidity of our banking system is adequate for some years ahead, but certainly not

beyond 1970. Because the banking system today has large reserves and still possesses about two-thirds of the war-time maximum holding of U. S. securities, the liquidity will suffice for an expanded economy for another seven or eight years. The liquidity ratio at the present time is about 42 per cent or barely one-half of the large liquidity ratio of 83 per cent at the end of World War II, and will fall to the hazardous level of 23 per cent by 1970.

Bank holdings of U. S. securities are primarily short-dated, consequently the prices of these securities will steadily, in the next four or five years, march back to par.

They thereupon become available for conversion (on their own merit rather than on the basis of support by the Federal Reserve System) into reserves or for lending or for both purposes. Consequently, this conversion may be expected steadily to proceed with a resulting enlargement in the loans of the banking system thus lowering the liquidity ratio of the banks.

This whole process produces a very great risk for the American economy. Happily, we can await the report of the Committee for Economic Development's created "Commission on Money and Credit" which should report on adequate measures in abundant good time to avoid the great collapse which may be expected for the banking system by 1970.

Whether, in light of the fact that we have never adequately acted in the past before a crisis, we can now act with this 10 years' notice I give, I do not know. But as an economist, I shall have "done my duty" by pointing out the great danger. In the past, of course, such dangers have never been resolved or fairly met until after a crisis. And, as in 1913, they were not met adequately. We lacked the national courage to compel the state banks to join the (national) Federal Reserve System. States' rights won over monetary good sense.

I do not think we will meet, in advance, this future emergency. As a result, the crisis which I can foresee as coming by 1970 will complete-

ly end the threat of inflation. So I see our decade of the 1960's as producing economic growth so amply as to pose a threat to our ability to maintain adequate liquidity in the

9. Non Financial Causes of Instability

The causes of instability are not solely from the side of finance. Instability can grow out of the ordinary business cycle variation in expenditure of business for new plant and equipment and of consumers for new and consumer durable goods. Such variation can of course be very "unstable" as there may be concern about the inherent stability of the economy as well as concern about the prospects for economic expansion of a sustained character.

In the three distinct business cycles we have had since the end of the Second World War, business has accounted for varying amounts of the decline ranging from about 70 per cent to 155 per cent of the total decline.

By this is meant that business liquidation of inventories added to business reduction in expenditure for new plant and equipment has fully equalled, exceeded, and never been more than slightly short of the decline recorded in gross national production (GNP) in each of our three post war recessions.

It is this decline in GNP which gives us the best single measure of each of our three post-war recessions.

For example, in the recession of 1949 the total of investment by business in new plant and equipment and in inventories declined by \$14 billion whereas the decline in gross national product was only \$9 billion.

Here business accounted for 155 per cent of the decline in total GNP. The recession of 1954 was the natural result of the truce in Korea and the very substantial decline in Federal expenditures for defense subsequent thereto. Yet the decline in business spending was \$7 billion, or 70 per cent of the \$10 billion decline in GNP.

economy to keep the growth continuing for the entire present decade. This is the way we produced the financial collapses of 1933, 1921, 1907, 1893-94, 1884, 1873, 1857, and 1837.

In the third economic recession since the end of the war, that of 1957-58, the decline in investment in new plant and producers' durable goods, and the decline in investment in inventories, taken as a total was \$15.6 billion. Total gross national product declined by \$16.8 billion. If we attribute a part of the \$3 billion decline in net foreign investment to the investment by business abroad, then once again, business accounted for a full 100 per cent of the decline in the 1957-58 economic recession.

The responsibility of business for these economic recessions is further sustained by the fact that in the recessions consumer spending has either advanced or been completely maintained.

In the recession of 1949 consumption increased by \$3 billion.

In the recession of 1954 consumption increased by \$4 billion.

In the decline of 1957-58, consumption was reduced by only \$0.9 billion. This decline was entirely caused by the decline in the sales of automobiles as the result of a natural reduction in the rate of sales following the record-breaking automobile year of 1955. In that year the two finest "gadgets" ever put on the modern automobile came in one year. I refer, of course, to "36 months to pay and power steering."

Now in these three economic recessions with consumption fully maintained, after liquidation of inventory had proceeded, production had to recover. As it recovered to the maintained level of consumption, incomes increased sharply. Economic expansion followed, sending both production and consumption still higher. As a result, production gained much

more. In each of the three economic recessions, in the same period of time as that in which the decline occurred, the subsequent gain in out-

put ranged from 2½ to 4½ times in amount the decline in output in the recession. This reveals remarkable buoyancy in the economy.

10. The Automatic Economic Stabilizers

The automatic economic snubbers, shock absorbers, or stabilizers, as may be preferred, have served very greatly to maintain personal income in face of a decline in production. In periods before 1940, and in accordance with Say's Law, as production declined incomes declined and consumption also declined. Consequently, the economy required 11 years following 1929 merely to regain the level of output which had been reached in that year. That was not good enough. Almost 10 million were still unemployed in 1939.

In the three post-war recessions, the maximum recession duration from high to low has been 12 months. And the latest recession was about eight months in duration from its previous high in 1957 to the recession low in early 1958. In these recessions, as we have pointed out, consumption has been maintained thus forcing a vigorous recovery. The maintenance of consumption, in largest degree, has resulted from rising wages throughout the entire post-war period as the result of the constant increases in hourly rates of pay for workers. These wage rate increases have come as the result of bargaining in a growing but inflationary economy.

The bargaining has been mostly for three-year contracts with accompanying wage increases "dis-regardless" of whether or not a recession might intervene before the expiry of the three-year wage contract.

Wage increases have also come as the result of escalation clauses whereby wage rates have increased in accordance with subsequent increases in the cost of living index. Finally wage rate increases have been granted for the "productivity factor" which has meant an automatic increase in pay being granted by management, because it undertakes, as does General Motors, to raise per worker productivity steadily.

In the last recession, in contrast to a decline of \$16.8 billion in total gross national production, the total amount of wage payments to the employed declined by only \$5.3 billion. As the result of the still further enlarged payment of unemployment compensation to workers losing jobs in the recession, amounting to about \$3 billion, total personal income of *those employed and those not employed* decreased by only \$2.3 billion in face of this \$16.8 billion decline in production.

Finally, as the result of lowered personal taxes and very modestly reduced rates of personal saving, total consumption, the spending out of income, decreased by only \$0.9 billion, as has been pointed out. This was a decline of only 0.3 of 1 per cent.

Thus consumption has been very well maintained in each recession with the result that the recovery has been quick and vigorous. As a result in recovery we quickly solve the problems of the recession.

11. The Responsibility of Businessmen for Maintaining Economic Stability as well as Promoting Affluence

It is earnestly hoped that business leaders will study these built-in stabilizers in the American economy and set to the task of main-

taining with greater stability their investment in plant and equipment and maintaining as well as is practicable their rate of investment in

inventories. This investment has varied greatly.

The three inventory liquidations which have occurred in post-war recessions do not, on balance, seem to have been wise for business itself.

This is still more true of the reductions which have taken place in plant and equipment outlays by business.

In the first two recoveries following the first two recessions construction costs increased by about 10 per cent in each instance. The record for the recovery of 1959-

60 is not yet clear, though it appears construction costs again are rising.

If business were better informed on the inherent stability in the economy, business in turn could contribute greatly to reinforcing still greater stability through a maintained rate of investment. We are all convinced of the very excellent prospects for economic growth for the next five years. This should induce business to provide a steadier rate of expansion of investment in new plant facilities. Timidity can defeat us.

12. Labor Scarcity in the 1960's Will Advance Capital Investment

Because of the inescapable shortage of labor until 1966-67, wages will be high and, of course, labor will be scarce.

We are compelled to await 1967 for the first substantial additions to our labor supply at the lower working ages.

This is the result of the low rate of birth in the 1930's and through the war period.

Only with the sharp rise in the birth rate starting in 1946 and continuing in each year since that date, we are producing the material for additions in the future labor supply.

But these additions will not move into the labor market until about 1966.

The intervening scarcity of labor and high rates of wages will serve excellently to maintain plant and equipment expenditures.

It is these plant and equipment expenditures that are required and that are promoted by the scarcity of labor and the high wages.

The large spending of industry for research and development brings forth new products that also promote expansion.

13. The Automatic Stabilizers in Recovery

The automatic stabilizers have worked as well in the periods of recovery. Putting the record very briefly, since the low point in total production was reached in the first quarter of 1958, the economy recovered by the second quarter of 1959 by a total of \$53.8 billion.

Normally, such a rise in total production would very greatly enlarge incomes and perhaps cause a threat of inflation.

However, of this total recovery all but \$23.9 billion was "sequestered" by the automatic economic stabilizers, snubbers, or shock absorbers.

No less than \$15.6 billion flowed as increased revenues to the Federal government.

It is this increased flow which has so quickly and precipitously diminished the Treasury's borrowing in the capital markets.

Inasmuch as private industry can hardly take up such borrowing with the rapidity with which the Treasury has retreated from the capital markets, we have seen in 1960, as a result, a very substantial easing in interest rates. In fact, there can be concern that this rapid rise in Federal budget revenues may be modestly restraining the economy at the present time. Inasmuch as we wish the budget surplus to be secured and to be used perhaps for debt reduction, the problem is one for the Federal Reserve System now to adopt appropriate

monetary and credit policy if we want budget policy to apply pressure.

In addition to the large increase in tax payments—increases which have completely wiped out the \$12.2 billion deficit of a year or two ago and converted it into an even balance in the present fiscal year and into the \$4.2 billion expected surplus in fiscal 1961—corporate earnings have recovered sharply (by \$21.8 billion) and these funds have flowed to corporations. There they are rather automati-

cally used for the expansion of inventories and accounts receivable in the recovery period.

Finally, consumer savings have increased somewhat by \$1.2 billion and we are now paying into old age security and unemployment reserves an additional \$1.1 billion.

In an appendix table, the figures for the automatic stabilizers are given in detail for the recession of 1957-58 and for the first year of recovery following the low point in the first and second quarters of 1958.

14. "Underwriting Prosperity"

In addition to this appendix table, there has just been issued by the Bureau of Economic Studies of Macalester College a bulletin "Underwriting Prosperity."* This bulletin reviews in considerable detail the record of the recessions and the nature of the structural changes in the economy which have taken place, and particularly the operation of the automatic

economic stabilizers in each of the three post-war recessions. The bulletin was prepared by Professor Harold Lunde. I believe it is the first recording in quantitative terms of the automatic economic stabilizers which have served us so excellently in all post war economic recessions. These stabilizers, automatic in operation, are the greatest feature of the post war era.

15. The Affluent 1960's Can Precipitate a 1970 Depression

Thus the outlook for the 1960's is indeed good.

Perhaps that should be qualified by saying it is indeed and certainly bright for the first two-thirds of the decade, and that a dark cloud may be forming at about that time to threaten the economy as the decade draws to a close. That dark cloud is the inability to maintain, given the inherent lack of strength in the

American independent banking structure, a proper degree of liquidity to finance the very substantial economic growth which will come in the first two-thirds of this decade.

But we shall have ample time at future meetings of the Midwest Economic Association to discuss these problems.

I was not assigned the economic problems of the 1970's.

*Available upon request to Macalester College, St. Paul, Minnesota.

THE AUTOMATIC ECONOMIC STABILIZERS

In Recession, 1957 to 1958

In Recovery, 1958 to 1959

	Note 1 1957-58 Recession (In Billions of Dollars) Decreases	Note 2 1958-59 Recovery Increases
Change in Total Production (GNP)	-16.8	+51.9
<i>Stabilizing Forces:</i>	<i>Maintaining Incomes</i>	<i>Reducing Incomes</i>
Corporate Taxes*	+5.7	-11.7
Corporate Retained Profits*	+5.6	-10.1
Dividends	0.0	+0.3
Government Transfers (Unemployment Compensation)	+3.2	-1.1
Change in Personal Income After Stabilizing Forces	-2.3	+29.0
	<i>Maintaining Spending</i>	<i>Reducing Spending</i>
Personal Taxes	+1.1	-3.9
Personal Saving	+0.3	-1.2
Total Consumption	-0.9	+23.9

NOTE 1: In the recession the decrease in production was \$16.8 billion, but total consumption fell only \$0.9 billion. The stabilizing forces intervened to sustain incomes and consumption almost completely in face of this decline in production.

NOTE 2: In the recovery total production increased \$51.9 billion, but total consumption or spending increase was held down to \$23.9 billion by the automatic "intervention" of the automatic stabilizers as listed in the table.

*Sales of corporations fell in the recession. Expenses of corporations were well maintained. This reduced the corporate tax burden and the corporate retained profits. These "expenses" of corporations are primarily wages and, in fact, total wages or compensation of employees diminished only \$5.8 billion in the recession. This smaller decrease in wages was in part offset by the increase in "government transfers" of \$3.2 billion so that personal income declined only \$2.3 billion. As a result of this decline in personal income, taxes fell and savings were reduced so that the decline in consumption was, as indicated, only \$0.9 billion. In the recovery the taxes and other items are increased again to lower the final increase in consumption outlays (which otherwise could cause inflation) from the very sharp rise in total production.

[962]

BULLETIN 15

WHY THE CORPORATION INCOME TAX SHOULD BE ABOLISHED

By EDWIN S. ELWELL,
Formerly Trustee of Macalester College,
President of Northland Milk Company;
and author of the
Elwell Plan for milk prices

and

ARTHUR R. UPGREN, PH.D.,
Frederic R. Bigelow
Professor of Economics and
Director of the Bureau of Economic Studies,
Macalester College.

Series on

AMERICAN
CAPITALISM



MACALESTER COLLEGE

SAINT PAUL • MINNESOTA

1962

MACALESTER COLLEGE

Office of the President

Macalester College is pleased to present this, another bulletin on an important subject, from its Bureau of Economic Studies. The College is happy to make it possible for our faculty member, Dr. Arthur R. Upgren, to be able to be joined by a prominent businessman, Mr. Edwin S. Elwell, in this proposal of a method to relieve the American economy of a tax which, in the view of the authors, is repressive and wasteful.

The case made against the corporation income tax is a powerful one in that it is shown to be either a hidden sales tax or a double tax upon the stockholders of a corporation.

We, at Macalester College, believe we are discharging one of the important responsibilities of an institution of higher education in making available the talents of our faculty to the general public through the publishing of this and the other distinguished bulletins that have preceded it.

Mr. Edwin S. Elwell has served as a Trustee of Macalester College and for many years has been its true friend. It is our hope that this joint effort may stimulate other businessmen to come forth with suggestions for the improvement of the operation of our economy.

HARVEY M. RICE, *President*

June 8, 1962

Director's Note

Increasingly the burdens, especially taxes, placed upon corporations in the United States compared to other countries, are judged to be the cause of the slower rate of economic growth and gains in productivity that prevail here. The component in our total economic production (GNP) which is persistently weak compared to all other components is business investment in new plant facilities. President Kennedy has recently shown his concern by making legislative proposals to provide some relief and encouragement for business. Incentives to invest in greater productive efficiency must be encouraged. This will be done in part by the abolition of the corporation income tax. However, the main issue discussed in this bulletin is the one of establishing *equitable* taxation. Thus, the proposal made here provides the gain of relieving corporations of inequitable and burdensome taxation, thereby providing incentives for investment and economic growth.

Two background reports are available for those interested in the detailed supporting arguments. The first is "Why the Corporation Income Tax Should Be Abolished" (longer study), and the second, "Abolishing the Corporation Income Tax as a Means to Promote Long Run Economic Growth and Reduce Unemployment." These reports are in mimeographed form and will be available upon request to the Bureau of Economic Studies.

ARTHUR R. UPGREN, *Director and*
Frederic R. Bigelow Professor of Economics

June 8, 1962

WHY THE CORPORATION INCOME TAX SHOULD BE ABOLISHED

PROPOSAL

For a great many business corporations the corporation income tax is substantially the equivalent of a sales tax added to the prices charged in an effort to keep earnings at a level judged to be satisfactory to the owners — those who have provided the capital for the business. In a period of economic growth such as we have had in the United States since the end of the Second World War, the additional capital for industry thereby required would not have been provided by those who supply capital unless the returns earned after payment of the corporation income taxes had been maintained by raising the prices of the products of that industry. As the capital *might not* have been provided, the goods and services produced by corporations would have been accordingly reduced. This hidden restraint in the rate of increase in production, in face of high purchasing power and strong demand, made possible that higher level of prices for the products of corporations. These higher prices, in turn, covered taxes and also avoided further diminishing of earnings in the period after World War II.

Here we see a favorable set of circumstances in the booming economy we have had, for shifting the corporation tax *forward* to consumers in the form of higher prices.

In the case of public utilities allowed to earn a "fair return" on the capital placed in the public service, the fact that the corporation income tax is purely a sales tax is abundantly clear. That "fair return" of course *is to be fair after taxes*. So the rates charged by the public utility are fixed high enough to cover the corporation income tax the privately-owned public utilities pay and yield a fair return after such taxes.

Our purpose is not to argue for or against a sales tax as such. A sales tax is satisfactory if it is

understood to be a sales tax and is voted for by consumers. They are the ones who pay the bill. A sales tax should not, however, be a hidden tax in the form of a corporation income tax, as is the case today. The corporation tax is a substantial revenue producer for the government but in large part it ignores the principle of *ability to pay*.

The obvious unfairness of the corporation income tax is that it takes the same bite, 52 per cent, out of the earnings of each shareholder who has contributed capital, regardless of the income of that shareholder. Some stockholders may have small incomes and thus be taxed only at a 20 per cent rate and other stockholders with large incomes may be taxed at 91 per cent. Yet on the earnings of the capital each has contributed to the corporation, the rate of tax is the same for all shareholders — 52 per cent. Only on such income received as dividends paid out of the remaining 48 per cent of the corporation's earnings, is there graduation in the rate of tax upon the owners — graduated upward as their incomes may be higher and in accordance with the principle of ability to pay.

Where the corporation tax cannot be shifted forward to consumers, it falls upon the owners of the enterprise, and it becomes a double tax. The first levy is upon the corporation. That levy is 52 per cent of income earned by the corporation. Then to the extent that dividends are paid by the corporation out of the earnings which are left after the payment of the tax, there is a second tax upon the owners — the personal income tax paid upon dividend income. Thus, the corporation, which is the stockholders taken together, pays a 52 per cent tax and the stockholder as an individual again pays another tax on those earnings he receives after dividends.

REMEDIES

One remedy might be to eliminate the corporation income tax and in its place levy a 100 per cent tax (or if we have modest doubts, perhaps 90 per cent) against any corporation earnings which are *not* paid out to the shareholders. This would encourage high dividends to shareholders. Then the income these owners would receive would be taxed at the appropriate personal income tax rates ranging from 20 per cent

to 91 per cent. If these rates do not produce as much tax revenue as was formerly produced by the corporation income tax, and more revenue is called for by the budget, these tax rates on personal income could be adjusted to achieve that end. Thus our proposals are made on the basis that there need be no reduction in total tax revenues to the Federal government.

This remedy would place the earnings upon the

contribution of each shareholder (to the capital of the corporation) fully in each shareholder's hands.

Perhaps the simplest method to put the proposal into effect would be to adopt the following procedure:

Substitute for the present 52 per cent corporation income tax a withholding tax levied

upon each stockholder against his share in the corporation's total earnings. This withheld tax would become a credit against the total tax liability of each stockholder as a taxpayer.

This withholding rate might be fixed at some rate between 20 per cent and 52 per cent, as might offer the greatest convenience to taxpayers and to the Bureau of Internal Revenue.

CONSEQUENCES

The objectives of the proposal are to levy taxes according to the principle of ability to pay, and, to release the corporation officials from the enormous wastage of energies stemming from the tax implications of any expenditure, and rather to have those energies devoted to the enlargement of production by the corporation and the reduc-

tion of expenses of the corporation. These double objectives would be served in a greater measure because all the gains, not 48 per cent, would benefit all owners of corporations. This, we insist, is the way to avoid wasteful corporate expenditures. It is the road to corporate efficiency.

NOTE

The authors realize that the larger dividend payments which would naturally and perhaps necessarily be made by corporations would alter the methods of financing of these corporations. The several sources of additional capital are retained profits, depreciation reserves and the sale of capital securities including bonds, preferred stocks and common stocks. It is, however, incongruous to hold the view that larger dividend payments will stand in the way of the ability to acquire, by sale of common stocks, additional funds which were formerly retained by the withholding of corporation earnings from flowing to stockholders as dividends. The payment of dividends, it might be claimed, in the early days of the Ford Motor Company, would have prevented its rapid growth. There is no reason, however, that the senior Henry Ford could not have made dividend credits to himself and have paid for additional stock issues by the use of this credit. In contrast today, a corporation heavily dominated and owned by one man would, because of the taxation of the major share of earnings received in dividends under the terms of the personal income tax, require some sale of common stocks to the general public. If the personal income taxation is eminently fair, then the consequence is also eminently fair. In the case of large corporations, very widely-owned, it also seems eminently fair that small shareholders receive in dividends the full share of the earnings upon the capital that they have provided to the company. This will surely not be any inhibitor to the sale of additional stock to them or to the public generally. It may also well be possible that where corporations offer their shares widely to the public this places them under a greater dividend responsibility. Their consideration must now be for their shareholders rather than taking the easier course of deciding dividend policy in terms of the needs of the corporation alone, or a few individual stockholders, without regard to the vast majority of stockholders for whom corporations were created in the first place.

List of Available Publications of the BUREAU OF ECONOMIC STUDIES

- No. 1 — THE NEW ECONOMICS OF THE MEASURED WORLD — by Arthur R. Upgren
- No. 2 — OUR DEPRESSIONS ARE GETTING SMALLER — by Arthur R. Upgren
- No. 3 — WHAT TO DO FOR THE RECESSION OF 1958 — by Arthur R. Upgren
- No. 4 — SECURITY AGAINST DEPRESSIONS? — Arthur R. Upgren, Harold I. Lunde, *et al*
- No. 5 — PRODUCTIVITY AND WAGES — by Arthur R. Upgren
- No. 6 — LIFE INSURANCE AND INFLATION — by Arthur R. Upgren
- No. 7 — UNDERWRITING PROSPERITY — by Harold I. Lunde
- No. 8 — HOW AFFLUENT WILL THE SIXTIES BE? — by Arthur R. Upgren
- No. 9 — THE NUMBERS GAME — by Frederick L. Deming
- No. 10 — HOW ARE FARMERS DOING? — Arthur R. Upgren and Harold I. Lunde
- No. 11 — THE BIG CORPORATION: WHERE ITS MONEY GOES — by Lloyd J. Buckwell, Jr.
- No. 12 — AMERICAN LIVING STANDARDS: A PROGRESS REPORT — by Marcus Alexis
- No. 13 — IRON MINING AND TAXES IN MINNESOTA — by James B. McComb
- No. 14 — THE GUIDE FOR WAGES TODAY — by Arthur R. Upgren
- No. 15 — WHY THE CORPORATION INCOME TAX SHOULD BE ABOLISHED —
by Edwin S. Elwell and Arthur R. Upgren
- No. 16 — LABOR AND MANAGEMENT — by Harty A. Bullis
- No. 17 — CHALLENGE FOR AMERICA: TRADE OR FADE — by David J. Winton
- No. 18 — MARKETING AUTOMOBILES — by J. Eugene Kangas
- No. 19 — WHEAT PROBLEMS AND POLICIES — by Harold I. Lunde and James B. McComb

MACALESTER COLLEGE
St. Paul 1, Minnesota

JUN 11 1964

BULLETIN 17

[1962]

CHALLENGE FOR AMERICA: TRADE OR FADE

HR9900 and the European Common Market

By DAVID J. WINTON

Vice-Chairman of Macalester College Trustees,
Director of Committee for National Trade Policy,
Director of National Planning Association,
President of Winton Lumber Co.,
Chairman of Kenwood Oil Co.

Series on

AMERICAN
CAPITALISM



MACALESTER COLLEGE

SAINT PAUL • MINNESOTA

BUREAU OF ECONOMIC STUDIES

Arthur R. Upgren, Director and
Frederic R. Bigelow Professor of Economics

MACALESTER COLLEGE

Office of the President

The Bureau of Economic Studies at Macalester College has issued a series of bulletins on various aspects of the American economy. This study is the second one to have been written by a member of the Board of Trustees of the College.

The author, David J. Winton, has been engaged for many years in the lumber business and has been active in public affairs and in the formation of public policy; he is deeply concerned with the successful operation of the American free enterprise economy.

Tariffs are an interference with the operation of such an economy. Whatever place tariffs may have had in the earlier economic development of our nation, they now are an impediment of serious proportion to a free world economy. The present threat from outside the free nations is of such serious significance that it behooves these nations to act in concert if the ultimate economic success we seek is to be accomplished.

It is a privilege for us at Macalester College to be able to present this 17th bulletin in our series on important problems facing our country.

HARVEY M. RICE, *President*

May 15, 1962

Director's Note

Tariff history in the United States became important with the adoption, from about 1870 to 1930, of high tariffs which assisted the industrial development of the United States. The tariff act of 1930, so roundly denounced by the vast majority of economists, brought the highest level: 48½ per cent in our tariff rates expressed as a rate on all dutiable goods. The world-wide response to this surely *uneconomic* act was autarchy and self-sufficiency in many countries of the world, such as in Hitler's Germany and in Italy under Mussolini. In Japan the turn was toward world empire to be achieved militarily.

Beginning with the Trade Agreements Act of 1934, we have persistently reduced tariffs bringing the average rate down to 12½ per cent at the present time.

But now we must speak to the issue of meeting great developments abroad. Foremost of these is the development of the Common Market and our adjustment to it. This is the problem to which David J. Winton addresses himself in this bulletin.

ARTHUR R. UPGREN, *Director and*
Frederic R. Bigelow Professor of Economics

May 15, 1962

CHALLENGE FOR AMERICA: TRADE OR FADE

The Trade Expansion Act: HR 9900

By 1932, aided and abetted by the Smoot-Hawley Tariff Act, the United States had reached the unenviable distinction of having an average 48½ per cent tariff. Actually, it was higher than 48½ per cent because many prohibitive tariffs shut out entire categories of goods. This high tariff wall contributed to a catastrophic decline in foreign trade — both imports and exports, not only in the United States, but world-wide.

In 1934, the Trade Agreements Act was adopted by Congress. It has been renewed in various forms and names for 28 years. It has reduced tariffs to about 12½ per cent on the average today. Again it is not an exact measure of the extent of protection for the United States. Many prohibitive tariffs on specific goods remain today.

The Reciprocal Trade Agreements Act, our present act dealing with tariffs, expires June 30, 1962. HR 9900, the Trade Expansion Act, is now before Congress. The President urges its passage so that he can deal particularly with the problems likely to be created for American trade by the development of the European Common Market.

The European Common Market is an economic union of France, West Germany, Italy, Belgium, Holland and Luxembourg — a union including some 170 million people. At the present time England, Ireland, Denmark and Norway are negotiating to join the Common Market as full members; while Austria, Sweden and Switzerland are seeking associate memberships. If all these countries join the Common Market there will be 325 million people included in an economic union with an industrial growth rate now roughly 2 to 2½ times the present growth rate of the United States. This could be a desirable market for American industry.

The European Market

This past summer the State Department sent the author to Geneva as a public member of the U. S. delegation to the GATT conference there. As a result, I was in Europe much of the summer. I had not been there long before I began to see the significance of the renewed economic strength of our European partners and allies, and what this rich, vast market could mean to us in the United States. I am so impressed that I urge every businessman, every labor leader and every farm leader who can,

Participation without discrimination will be most valuable to us. To gain access to this market is one of the main purposes of HR 9900.

The main difference between HR 9900 and the present Reciprocal Trade Act is found in the tariff changes designed to meet the Common Market competition and permit our U. S. goods to penetrate that market.

Here are the main changes. HR 9900 permits reduction of tariffs up to 50 per cent on entire categories of items gradually over a five-year period in place of the present Act's maximum of 20 per cent tariff reduction on an individual item by item basis. Under HR 9900, jointly and gradually over a five-year period, tariffs can be eliminated completely on those goods 80 per cent of which are produced in the United States and the Common Market. Further, under this bill, tariffs against raw materials from the newly developed and emerging countries can also be eliminated by the President. Because HR 9900 is a recognized instrument of foreign policy and since some domestic industries may be hurt by tariff reduction under the Act, it contains trade adjustment features such as compensation for employees, companies or industries harmed as the national welfare is advanced.

This paper discusses particularly two questions in connection with HR 9900 about which there has been much misunderstanding: First, can the U. S. compete with foreign wages and costs? Second, how will the external tariffs and the internal tariffs of the Common Market discriminate against their imports and particularly their imports from the United States, or our exports to these European countries?

to go to Europe and see this remarkable economic transformation for himself. Europe is on the make industrially. This is the kind of development that American businessmen who believe in the private enterprise system can appreciate and enjoy.

One of my earliest memories of France many years ago, is of a workingman dressed in a blue smock and riding a bicycle with a long loaf of bread and a bottle of wine sticking out of a (musette) bag hung over his shoulder. This same

chap has continued through the years. His day may not be completely over yet, but it is passing fast. For the bicycler is reaching for a motor scooter; the man with a gasoline engine on two wheels is reaching for a three-wheeler; and the three-wheeler for four wheels. And the four-wheeler Frenchman today, occasionally has a boat on a trailer behind. France in the early 1960's looks more like my home state of Minnesota two decades ago than the France and Europe one may have known in the recent past.

Installment buying is just starting in Europe. Recently I saw figures that showed installment debt in England to be \$32 per person, Germany \$27 and France \$18. In the U. S. it is \$212! We in the United States have 105 television sets per 100 families; Germany has 26 television sets per 100 families. As European living standards go up, a large demand is being created for television and many other kinds of durable goods which American business produces so efficiently. This European Common Market is growing and expanding 2 to 2½ times as fast as our U. S. markets, and it will eventually include 325 million people. This is the kind of potential market American businessmen are always dreaming about finding.

Look back for a moment on the France and Italy of 1948. Production and income were at poverty levels. They were overshadowed by the threat of Communist domination. Then came the industrial growth of the last decade and a half. Today these nations are enjoying rapidly rising standards of living and economic growth. We can take honest satisfaction in the comparison, for American aid stimulated the resurgence of industrial life in Europe after the Second World War. Our generosity here, an excellent example of enlightened self-interest, wrote one of the most glorious pages in American business history and in the record of Congress. For it was largely business that paid the taxes and Congress that voted the funds making the Marshall Plan possible. In Western Europe it is fair to say we have helped run Karl Marx off the main street and up the alley.

A short time ago, February 22, 1962, to be exact, the *Saturday Evening Post* quoted a spokesman for the Kennedy Administration. He said: "Our main battle point in the Cold War is not Berlin or Cuba. It is the economic front. If we lose there, we lose everywhere. The President is asking for tools to fight for our survival." I believe this to be true.

Further, I believe in healthy business competition between our industries and those of Western Europe. We businessmen, labor leaders and farm

leaders can understand this. The flow of goods both ways will raise living standards both in America and in Europe.

So far, for the vast majority of the products we make, we have been able to compete successfully with foreign producers. And I believe we can continue to hold our own very well in international markets, even though we live in an increasingly competitive world — a world experiencing rapid technical advance and economic growth.

One thing is abundantly clear: Exports create jobs for workers, markets and profits for businessmen and farmers. What is not so widely known is that foreign trade between the United States and the rest of the world provides all important markets for every single one of the 50 states. The accompanying chart at the end of this section shows how much businessmen, workers and farmers in each and every state of the United States all benefit from our foreign trade.

More workers gain jobs than lose their jobs through foreign trade. According to a recent report by the AFL-CIO, the number of workers whose jobs depend on foreign trade is ten-times the number of jobs lost through imports. (See: "Foreign Trade", AFL-CIO, page 14.)

Lionel D. Edie and Company of New York is a firm of practical economists. They make their living giving economic advice to their clients. They have allowed us to quote from their copyright release of January 26, 1962 — telling how the Detroit automobile industry met the competition of imported foreign cars — and also from their release of February 28, 1962 about the comparison of the quantity of electrical power per worker in the U.S. and in Europe. The most important parts of these two releases follow:

POINT AND COUNTERPOINT

"In 1955 we imported 57,000 cars. In 1957 and in 1958 imports rose steadily. Plot the monthly figures on a chart and the line goes up and up. Then in 1959 the blow really came. We imported more than 665,000 foreign cars. Foreign cars had by then obtained more than 10% of the market.

But American industry had become aware of the challenge. They were getting ready to compete with the foreign cars. The American people wanted smaller and more efficient cars, okay, American industry would provide them.

In 1959 we produced 755,000 compact cars. In 1960 we really went to town; we produced almost two million compact cars!

The rise and demise of imports. . . . We reacted late, but when we did react we beat the competition hands down. As we reacted, foreign car imports declined. We met the competition. . . .

Year	Thousand Units	
	Foreign Car Imports	Compact Car Production
1955	57	249
1956	108	179
1957	259	180
1958	431	273
1959	668	755
1960	445	1,945
1961	250	1,990

Points to be made. This very brief review of the way American Industry reacted to foreign competition has some very interesting facets to it that should be realized by those who underestimate our ability or inclination to compete:

- (1) The importation of foreign cars although marginal was threatening. At no time were foreign car imports more than 11 per cent of total car registrations.
- (2) Foreign cars sold at prices substantially lower than American cars. Pricing competition was a major factor.
- (3) Maintenance costs of foreign cars were below American cars. They burned gasoline more efficiently and required less lubrication.
- (4) There was little comparable to foreign cars on the domestic market. American Motors was the only organization producing a domestic compact car. American industry had to gear up in order to compete. It had to design from scratch, and produce from scratch. It had to put in place entirely new assembly lines. To put it simply, they had to make tremendous capital investments to compete. It made them.
- (5) Exports of American cars fell from 1955 to 1959, but since 1959 have risen moderately. This is particularly noticeable in the face of the extremely high tariffs and other obstacles levied against American cars by foreign countries.
- (6) This case study encompasses almost all those negative factors that people use to claim we can't compete with foreigners. But compete we did, compete we can, and compete we will."

There is a strong relationship between the way Detroit met the imported small car competition and the power back of each worker in the U.S. and Europe. Let's see what Edie says about that.

PRODUCTIVITY AND POWER

"The Findings. Let us present our findings in two ways: First we compare energy utilization levels in industrial production and then in civilian employment.

Kilowatt-Hours Produced Per Point of Industrial Production (Indices)

Year	Billion Units		U.S. as a Multiple of Common Mkt.
	U.S.A.	Common Market	
1954	5.80	1.55	3.7
1955	5.93	1.52	3.9
1956	6.26	1.53	4.1
1957	6.51	1.54	4.2
1958	7.10	1.58	4.5
1959	6.91	1.59	4.3
1960	7.06	1.59	4.5

Kilowatt-Hours Produced Per Civilian Employee

Year	Thousand Units		U.S. as a Multiple of Common Mkt.
	U.S.A.	Common Market	
1954	9.0	2.6	3.5
1955	9.9	2.7	3.7
1956	10.5	2.9	3.6
1957	11.0	3.1	3.6
1958	11.3	3.2	3.5
1959	12.1	3.5	3.5
1960	12.7	3.8	3.3

Both these tabulations indicate the same things: The relative utilization of electrical energy is higher in the United States than in the Common Market and there is no material change taking place in the relative trend of U. S. consumption (of electric power in industry).

What do these tabulations mean to us? They mean that there is a solid basis for assuming a substantially higher productivity in the U. S. than in the Common Market. We can compete on a cost basis."

Here is one more basic reason why American industry can meet successfully the competition of foreign costs and wages. Because our workers have more power and tools to work with.

Another instance of meeting competition was pointed out to me at a recent Chamber of Commerce meeting. Each winter the National Chamber of Commerce recruits speakers to tour the country and explain the Chamber's position on important pieces of legislation before the Congress.

This year officials of the National Chamber of Commerce travelled to 15 cities in three weeks and explained six pieces of proposed legislation at each place. The National Chamber of Commerce stands firmly behind HR 9900 with only one reservation. This reservation is in connection with that portion of the "trade adjustments" part of the Act covering longer payments to employees of industries adversely affected. The Chamber feels that payments to laid-off employees should be limited to payments made and determined by the individual state involved. At the invitation of the National Chamber, I explained HR 9900 to business men in New York, Providence, Syracuse, Columbus and Charleston, West Virginia.

The third morning at breakfast in Syracuse Virgil Day, Vice President of General Electric, who was part of the Chamber Aircade volunteered: "Winton, I have a good example of our ability to compete. Our company has a plant at Utica making radios. Three years ago we were down to 300 employees. We considered abandoning the plant. Instead we studied how the Japanese made their radios. We decided we couldn't do it exactly their way, but gave the problem another hard look — more research, redesign and automation. Today we can meet the Japanese competition here in the United States and next year we think we can meet their competition abroad."

I said: "That's wonderful. How many employees do you have at your Utica plant today?"

Virgil Day replied: "That's the best part of the story. We now have 1900 employees at Utica!"

Much of our confusion about our ability to compete comes from equating wage rates with costs. They are not the same at all. It is costs we must

compete against, not wages. The more one studies the problem of foreign trade and foreign competition, the more sure you are that America not only can, by and large, successfully compete, but we are competing successfully, and we are going to continue to compete successfully in world markets, not on every item but on the vast majority of products.

WORKERS, FARMERS, CONSUMERS, AND INDUSTRIES OF EVERY STATE BENEFIT FROM OUR EXPORT TRADE

(Figures Located on the Map Show the Totals of the Exports of Each State in 1960)



Trade Adjustment Provision

Of course, there are cases where we can't compete, such as the extreme example of artificial flowers where it is all hand labor. The same is true of trout flies and, of course, some more important items. Occasionally, for example, we have lost a sale of heavy electrical equipment to England or Germany. But sometimes, in fact often, an industry that reacts fearfully about imports, or the threat of imports, is already "sick" from the competition of substitutes made in America, or changing whims

in our consumer choices, or a dozen different and local competitive conditions. However, industries harmed by enlarged imports via HR 9900 will not on balance, adversely affect our total economy. In fact, quite the reverse is true. We have a favorable trade balance of some 4 to 5 billion dollars now — exports twenty billion dollars, imports fifteen billion dollars. We have many more jobs because of our present export-import picture than we would have under a restrictive trade program

because many "export" jobs would disappear. According to the AFL-CIO, the Brookings Institution and a host of other agencies down through the years, reducing and eliminating trade restrictions world-wide will improve living standards everywhere and will increase employment in the United States. We can't enjoy a favorable balance of trade if we don't accept imports. Otherwise how can

External-Internal Tariff Problems

Our exports to the Common Market countries have increased 100 per cent in the past seven years, while the rest of our exports to other countries have increased only 30 per cent. So we are talking about a very important market for us. To continue to enjoy this greatest of all overseas market, we must give the President power to penetrate the external tariffs of that market — to bargain for lower tariffs against our goods. This is exactly what HR 9900 is designed to do.

As things are now we are in jeopardy. We stand to lose a substantial amount of this vast and growing market. This is because the original tariffs of the Common Market countries — that is the old tariffs between these countries — gradually, over some seven years, will be reduced to zero. But the tariffs of the Common Market countries as a union against the rest of the world, including the United States, will be averaged from the individual tariffs of the member countries. The result: a big area of free trade among the Common Market members and a restrictive wall of protection around these same nations against the world, including the United States.

The President must have unusual powers to negotiate penetration of this wall. That is what HR 9900 is designed to do. The squeeze on U. S. business caused by the present structure of the internal and external tariffs of the Common Market is very important to understand, and then, to see how the President plans to meet the problem. We must remember the internal tariffs between Germany, France, Italy, Belgium, Holland and Luxembourg will gradually evaporate and they

foreign countries buy our exports?

HR 9900 is more than a Trade Act. It is a key instrument of our foreign policy. It is important to remember this. If in the larger welfare of the nation some are harmed, it is proper that both workers and employers receive adjustment assistance. The bill provides for this in specific detail.

will be on a free trade basis with each other in the near future. But the external tariffs of these same countries will be maintained against the United States unless something is done about it. Again we come to the solution, HR 9900.

Let us take fishing rods as a hypothetical example. A manufacturer in Chicago could price his fishing rods at \$40, and prior to the Common Market, sell them in Hamburg, Germany for \$50, including a tariff of 25 per cent. A similar rod could be made in France and priced there at \$40 to sell in Hamburg for the same \$50, again including the 25 per cent tariff. But when the internal tariff between Germany and France disappears, the French producer could sell his rod in Germany for \$40 without duty. And if the present external tariff on fishing rods is 40 per cent for France, 30 per cent in Italy, 25 per cent in Germany, 10 per cent for Holland and Belgium and 5 per cent for Luxembourg, the Common Market's external tariff on this item would be the average of these old tariffs — 120 divided by six or 20 per cent. Our American manufacturer would be priced out of the Common Market. He would have to get \$48 (\$40 plus \$8 duty) for his fishing rods in Hamburg in order to keep his net price of \$40.

This external-internal tariff squeeze on U. S. exporters has already started on a number of items, and we will feel steadily growing pressure on our exports to Europe in the months ahead. Tariff discrimination against our goods caused by the Common Market will grow gradually but forcefully unless we give the President the wherewithal to negotiate away this discrimination.

Conclusion

This study is based on a fundamental belief in our ability to successfully compete in the world market. Also it is hoped that this statement will clarify some of the dangers inherent in the existing structure of external and internal tariffs of the Common Market. We must act now. Europe is moving ahead at a rapid rate.

We must not overlook the forces at work in the international scene. There is a new resurgence of Russian aggressiveness; including prolonged tension over Berlin, bomb testings, subversion in Latin American and Southeast Asia.

Russia is doing, and will continue to do, all in her power to foster a trade war between the United

States and the rest of our Allies, to sever Western Germany from the Western Alliance and destroy NATO. Should Russia succeed, we in America face not only business stagnation and recession, but the loss of our freedom and our way of life.

On the other side, HR 9900 offers a peaceful means of retaliation against World Communism coupled with an immense opportunity to bind the free world together in economic abundance. With the power to reduce our own tariffs, the President has the best tool with which to bargain and get our goods into Western Europe. Thus, we can enlarge world trade with fewer restrictions both to and fro, and with great economic and security advantage to

both our allies and ourselves.

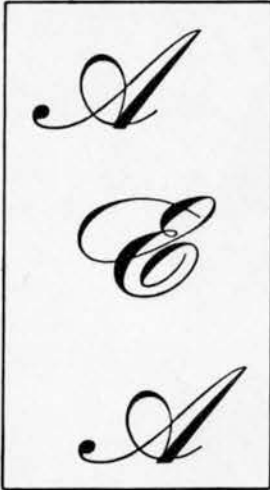
The Trade Expansion Act through increased world trade will help boost the rate of America's industrial growth. It will assist in re-employing our unemployed workers, and ease our balance of payments position. As our allies grow in strength, they will grow in their ability to pay their full share of NATO and other defense costs. This, combined with their, and our, foreign aid to the newly-founded and underdeveloped countries will strengthen and unify the free world as a whole.

HR 9900 is the indispensable agent in this plan for progress.

List of Available Publications of the
BUREAU OF ECONOMIC STUDIES

- No. 1 — THE NEW ECONOMICS OF THE MEASURED WORLD — by Arthur R. Upgren
- No. 2 — OUR DEPRESSIONS ARE GETTING SMALLER — by Arthur R. Upgren
- No. 3 — WHAT TO DO FOR THE RECESSION OF 1958 — by Arthur R. Upgren
- No. 4 — SECURITY AGAINST DEPRESSIONS? — Arthur R. Upgren, Harold I. Lunde, *et al*
- No. 5 — PRODUCTIVITY AND WAGES — by Arthur R. Upgren
- No. 6 — LIFE INSURANCE AND INFLATION — by Arthur R. Upgren
- No. 7 — UNDERWRITING PROSPERITY — by Harold I. Lunde
- No. 8 — HOW AFFLUENT WILL THE SIXTIES BE? — by Arthur R. Upgren
- No. 9 — THE NUMBERS GAME — by Frederick L. Deming
- No. 10 — HOW ARE FARMERS DOING? — Arthur R. Upgren and Harold I. Lunde
- No. 11 — THE BIG CORPORATION: WHERE ITS MONEY GOES — by Lloyd J. Buckwell, Jr.
- No. 12 — AMERICAN LIVING STANDARDS: A PROGRESS REPORT — by Marcus Alexis
- No. 13 — IRON MINING AND TAXES IN MINNESOTA — by James B. McComb
- No. 14 — THE GUIDE FOR WAGES TODAY — by Arthur R. Upgren
- No. 15 — WHY THE CORPORATE INCOME TAX SHOULD BE ABOLISHED — by Edwin S. Elwell
and Arthur R. Upgren
- No. 16 — LABOR AND MANAGEMENT — by Harry A. Bullis
- No. 17 — CHALLENGE FOR AMERICA: TRADE OR FADE — by David J. Winton

MACALESTER COLLEGE
St. Paul 1, Minnesota



LEGISLATIVE ANALYSIS

THE PROPOSAL TO INCREASE THE NATIONAL DEBT CEILING

PUBLISHED AND DISTRIBUTED BY THE
AMERICAN ENTERPRISE ASSOCIATION
1012 FOURTEENTH STREET, N.W., WASHINGTON, D. C.
EXECUTIVE 3-8205

THE AMERICAN ENTERPRISE ASSOCIATION, established in 1943, is a nonpartisan research and educational organization which studies national policy problems.

Association publications take two major forms:

1. LEGISLATIVE AND SPECIAL ANALYSES—factual analyses of current legislative proposals and other public policy issues before the Congress prepared with the help of recognized experts in the academic world and in the fields of law and government. A typical analysis features: (1) pertinent background, (2) a digest of significant elements, and (3) a discussion, pro and con, of the issues. The reports reflect no policy position in favor of or against specific proposals.

2. LONG-RANGE STUDIES—basic studies of major national problems of significance for public policy. The Association, with the counsel of its Advisory Board, utilizes the services of competent scholars, but the opinions expressed are those of the authors and represent no policy position on the part of the Association.

ADVISORY BOARD

Herrell F. DeGraff, Chairman Babcock Professor of Food Economics, Cornell University	
Karl Brandt Food Research Institute Stanford University	Felix Morley Editor and Author
Milton Friedman Professor of Economics University of Chicago	Stanley Parry, Chairman Department of Political Science University of Notre Dame
Arthur Kemp, Professor of Money and Finance Claremont Men's College	Roscoe Pound Professor Emeritus Harvard University
Paul W. McCracken, Professor School of Business Administration University of Michigan	E. Blythe Stason Dean Emeritus, Law School University of Michigan

OFFICERS

President Allen D. Marshall	
Vice-Presidents	
Walter C. Beckjord Henry T. Bodman	Carl N. Jacobs H. C. Lumb
Treasurer Henry T. Bodman	
William J. Baroody Executive Vice-President	Thomas F. Johnson Director of Research
David M. Abshire Director of Special Projects	Joseph G. Butts Director of Legislative Analyses

TABLE OF CONTENTS

	Page
SUMMARY.	1
BACKGROUND	2
Origin of the Ceiling.	2
Current Federal Debt	3
Other Debts in the Picture	5
LEGISLATIVE HISTORY.	6
ANALYSIS OF THE ARGUMENTS.	9
Federal Budget Control.	9
The Advocates of a Tight Ceiling	9
The Critics of a Ceiling	11
The Annual Review.	15
The Effects of the Debt	18
The Advocates of a Tight Ceiling	18
The Critics of a Ceiling	18
THE ALTERNATIVES	20
QUESTIONS RAISED BY THE PROPOSAL	21
* * *	
AEA Publications	Inside back cover

THE PROPOSAL TO INCREASE THE NATIONAL DEBT CEILING

SUMMARY

The present ceiling on the national debt is fixed by law at \$298 billion. President Kennedy has indicated that he will ask the Congress to increase the ceiling to \$308 billion for a period extending to July 1 of next year.^{1/}

The national debt ceiling originated during the first World War and from time to time in recent years has become an instrument for controlling federal fiscal policy. The ceiling states the limit on the amount of government securities that may be outstanding.

On many occasions in recent years, the administration has requested and received an increase in the ceiling. Its position has been as follows:

(1) The administration must have funds to pay for the programs that Congress has authorized. If Congress does not vote adequate tax revenue, the only other proper source of funds is government borrowing.

(2) When the national debt ceiling is tight, it hampers the ability of the Treasury to manage the national debt with a maximum of efficiency and a minimum of cost. The administration, therefore, requires a margin between the debt outstanding and the ceiling.

The opponents of increases in the national debt ceiling view the ceiling as a potential device for bringing greater economy to government. They recognize that discussions and debates over the ceiling occur usually after Congress has made appropriations. However, they point out that a firm stand on the debt issue emphasizes the importance of economy in the budget-making process. They view the ceiling as an important instrument of federal fiscal policymaking and prefer to see the gap between the ceiling and the existing debt held to a minimum. In this way, they believe, we can halt and perhaps reverse the long-run upward trend of national debt.

In view of the nature and brevity of this Analysis the usual detachable Summary of Pro and Con Arguments has been omitted.

^{1/} Press Release by Sen. Harry F. Byrd, Chairman of the Senate Committee on Finance, January 16, 1962.

BACKGROUND

Origin of the Ceiling

Prior to World War I, Congress passed a new law each time an increase in the national debt was planned. In this way, it fulfilled the responsibilities of Article 8 of the Constitution, which gives Congress the power "to borrow money on the credit of the United States." Before 1917, Congress generally played a much more intimate role in the management of the public debt, setting interest rates and maturities, and identifying the types of securities which were to be sold by the Treasury. With the coming of World War I, this intimate relationship to debt management began to deteriorate under the pressure of large financing and the increasingly complex financial structure in the economy.

In the Second Liberty Bond Act of 1917, the basic debt limit Act, Congress pulled together a number of unused authorizations and added an additional amount to be borrowed. The Act gave the Treasury authority to borrow an amount "not exceeding in the aggregate \$7,538,945,460." Then, as the war progressed, congressional authorization took the form of increasing this amount (and also authorizing certain changes in the types of securities and in the allowable interest rates that could be paid by the Government). Through this process, Congress maintained its legal control over the amount of public debt outstanding and, within the latitude of the alternatives offered to the Treasury, also controlled the types of securities which the Government might issue.

The debt ceiling at this early date was viewed primarily as a means of increasing the flexibility of the Treasury in meeting the unusual financial demands of war. After the war and postwar financing had been accomplished, the debt ceiling virtually dropped from legislative sight. The size of the public debt declined throughout the 1920's and the ceiling did not again become an issue until, in the midst of the depression, the public debt again began to rise.

In the 1930's, amendments to the Second Liberty Bond Act authorizing increases in the national debt continued to approach the form in use today. That is, attention continued to shift from authorization of specific amounts of specific securities to authorization of a total debt, with more and more of the choices about debt instruments being left to the discretion of the Treasury Department. In 1941, the amendment to the Second Liberty Bond Act, establishing a \$65 billion ceiling for the national debt, created the type of debt ceiling which exists today: it lumped all securities together and simply set a top limit.

The principal formal change in national debt ceiling legislation since 1941 has been in its amount. During World War II, in response to the financial demands of the war, the limit increased from \$65 billion

to \$300 billion. After the war, the limit was cut to \$275 billion to fit more closely the financial needs of the moment. This is why the debt ceiling was not a matter of major public or legislative concern in the postwar years until 1954. The \$275 billion ceiling left room to finance the postwar deficits and the deficits for the Korean War. It was not, however, adequate to finance the deficits that came with the post-Korea recession.

Since 1954 the national debt ceiling has played an entirely new role in federal fiscal affairs. In this period the Congress has maintained a tight ceiling on the national debt and in most years has allowed only temporary increases to meet the financial needs of the moment. One of the notable effects of the tight ceiling during this period has been that it has drawn considerably greater attention to increases in the national debt when they have occurred. In 1954, for example, an increase of \$3.5 billion caused considerably more attention and public discussion than an \$8 billion increase that had occurred two years earlier within the then existing debt ceiling.

During the seven-and-a-half years in which a tight ceiling has been maintained on the national debt, mounting discussion of the role of the debt ceiling has occurred. Pressure for its modification has grown and only gradually has its new role in fiscal affairs become apparent. Contributing to the debate is the fact that on more than one occasion unpaid claims on the Federal Government have been allowed to accumulate. Certain government programs have been temporarily curtailed and from time to time various financial maneuvers have been employed by the administration to circumvent the fiscal restraint imposed by the ceiling. It has, at times, been a source of considerable public confusion that Congress, through the ceiling, has refused to permit the Government to obtain funds to carry out programs that Congress itself has approved.

Current Federal Debt

The federal debt of December 31, 1961 was \$296,499 million. All but \$438 million of this has been borrowed under the authority of the Second Liberty Bond Act, and therefore is subject to the federal debt ceiling (see Table on next page).

The federal debt ceiling applies to the gross federal debt. It does not change when government securities are acquired by the Government itself, as in the case of the special issues and other securities held by the Social Security or other trust fund accounts. Thus, although the federal debt is approximately \$296 billion, it does not give an accurate picture of the amounts owed to the public. A substantial volume of government securities (\$83.7 billion on September 30, 1961) are owned by the Government itself, but under the debt ceiling, this self-held debt is treated the same as that owed to the public.

PUBLIC DEBT AND GUARANTEED SECURITIES OUTSTANDING

December 31, 1961

Class of Security	Amount (millions of dollars)
Public Debt:	
Interest-bearing securities:	
Marketable:	
Treasury bills	43,444
Certificates of indebtedness	5,509
Treasury notes	71,526
Treasury bonds	75,486
Total marketable debt	<u>195,965</u>
Non-Marketable:	
U.S. savings bonds (current redemption value)	47,458
Other non-marketable	5,747
Total non-marketable	<u>53,205</u>
Special issues to Government agencies and trust funds	<u>43,520</u>
Total interest-bearing securities	<u>292,689</u>
Other (interest-free) debt	<u>3,042^{1/}</u>
Total public debt	<u>295,730</u>
Guaranteed Securities:^{2/}	
Gross public debt	<u>330</u> <u>296,061^{1/}</u>

Source: Daily Statement of the United States Treasury, December 29, 1961, p.5. Totals will not agree due to rounding.

^{1/} \$438 million is not subject to the Debt Limit.

^{2/} Held outside the Treasury.

Other Debts in the Picture

In addition to the "Gross Federal Debt" which is governed by the debt ceiling, the Federal Government has, outstanding, a variety of other contingent claims. Among these are approximately \$54 billion in loans and mortgages which are insured or guaranteed by agencies of the Federal Government, \$251 billion of other government insurance and guarantees of various types, and an amount in excess of \$250 billion of trust fund contingent liabilities. These obligations of the Federal Government are, in many cases, offset by clearly defined marketable assets and, therefore, cannot be readily combined into a total debt figure for the Government. Moreover, most of these obligations are contingent on something more than the mere passage of time. The likelihood of all these contingencies occurring is extremely small. Hence, the total figure must be used with caution. Yet they are a part of the federal financial structure. The important point is that the federal debt ceiling applies to only one part of this vast complex of federal obligations.

Private debt is also a part of the total financial structure within which the federal debt fits. In 1961, the total of public and private debt amounted to something over \$1,000 billion; that is, one trillion dollars. In addition to the federal debt, this consisted of approximately \$70 billion of state and local government debt, corporate debt of about \$350 billion, and individual debt of about \$290 billion. The Federal Government's relative portion of this total has been shrinking fairly steadily since the end of World War II. At the end of World War II, it was 58 percent of all debt and in 1961 it was 30 percent of all debt: Private debt, which grows most rapidly in periods of prosperity, and public debt which grows most rapidly in periods of recession (and war), must be serviced from the same total national income, however.

The following table shows a summary of federal debt legislation since the passage of the Second Liberty Bond Act of 1917. The new element that was introduced in 1954 was the practice of creating a one-year temporary increase in the ceiling. The "temporary approach" has required the administration to request an additional increase the following year when the debt did not drop to the permanent ceiling level.

The most recent legislation affecting the debt ceiling was H.R. 7677 in the First Session of the 87th Congress. This bill was signed into law on June 30, 1961. The text of the law (P.L. 87-69) is as follows:

AN ACT

To increase for a one-year period the public debt limit set forth in section 21 of the Second Liberty Bond Act.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That, during the period beginning on July 1, 1961, and ending on June 30, 1962, the public debt limit set forth in the first sentence of section 21 of the Second Liberty Bond Act, as amended (31 U.S.C. 757b), shall be temporarily increased by \$13,000,000,000.

Approved June 30, 1961.

Debate on this legislation concerned many of the issues outlined below, but a central theme in the debate was the question of whether the Nation should have a tight ceiling or a loose ceiling on the debt. Relatively little discussion has been given to the question of abolishing the debt limit entirely. For many, the implications of outright repeal would appear to be too alarming; moreover, the existence of the ceiling appears to conform more nearly with the constitutional authority granted to Congress. Thus, legislative discussion has tended to center around the issues of the role of the debt ceiling as a control over the fiscal affairs of the Government.

The Current Proposal. The present debt ceiling, including the temporary increase granted last year, is \$298 billion. Sen. Byrd, of Virginia, Chairman of the Senate Committee on Finance, stated recently that he had been advised by the Secretary of the Treasury "that the debt limit must be raised immediately to approximately \$300 billion if we are to meet current bills, and beyond that the limit must be raised to \$308 billion for a period extending through June 30, 1963." At the same time Sen. Byrd stated:

I shall support temporary legislation raising the limit to the minimum immediate requirement. As to raising the limit to \$308 billion through fiscal year 1963, I shall ask the Senate Finance Committee to undertake a full scale investigation into the fiscal condition of this country in all of its aspects.^{1/}

Related Proposals. Various bills have been introduced during the current Congress dealing with reduction of the national debt, limitations on expenditures and obligational authority, budget procedures, etc.^{2/}

^{1/} Press Release by Sen. Harry F. Byrd, January 16, 1962.

^{2/} For a list of such bills see Digest of Public General Bills, 1961, Library of Congress, Index, p. I-50.

FEDERAL DEBT LIMIT LEGISLATION, 1917-1961
(In Millions of Dollars)

Date of Act	Debt Affected	Limitation ^{a/}
September 24, 1917	Bonds	7,539 ^{b/}
	Certificates	4,000
April 4, 1918	Bonds	12,000 ^{b/}
	Certificates	8,000
July 9, 1918	Bonds	20,000 ^{b/}
March 3, 1919	Certificates	10,000
	Notes	7,000 ^{b/}
November 23, 1921	Notes	7,500
June 17, 1929	Bills, Certificates	10,000
March 3, 1931	Bonds	28,000 ^{b/}
January 30, 1934	Notes	10,000
February 4, 1935	Bonds	25,000
	Bills, Certificates	20,000
May 26, 1938	Bills, Certificates, Notes, Bonds ^{c/}	45,000
July 20, 1939	Bills, Certificates, Notes, Bonds	45,000
June 25, 1940	National Defense Series	4,000 ^{d/}
February 19, 1941	Total	65,000
March 28, 1942	Total	125,000
April 11, 1943	Total	210,000
June 9, 1944	Total	260,000
April 3, 1945	Total	300,000
June 26, 1946	Total	275,000
August 28, 1954	Total	281,000 (275,000)
June 30, 1955	Total	281,000 (275,000)
July 9, 1956	Total	278,000 (275,000)
July 1, 1957	Total	275,000
February 26, 1958	Total	280,000 (275,000)
September 2, 1958	Total	288,000 (283,000)
July 1, 1959	Total	295,000 (285,000)
July 1, 1960	Total	293,000 (285,000)
July 1, 1961	Total	298,000 (285,000)

^{a/} Limitation on outstanding securities unless otherwise indicated. Bracketed figures show permanent limit when a temporary limit is effective.

^{b/} Limitation on issue.

^{c/} Bonds limited to \$30 billion.

^{d/} Limitation on issues less retirements.

ANALYSIS OF THE ARGUMENTS

Federal Budget Control

The Advocates of a Tight Ceiling

According to those who favor it, a tight debt ceiling will accomplish a greater degree of overall budgetary control. The difficulties of maintaining some overall budgetary control over federal fiscal affairs is, they say, becoming increasingly apparent and the difficulties apparently stem from three major conditions:

1. Congress has in fact yielded considerable control over annual expenditures arising from prior appropriations and obligational authority. Each year the Congress grants the Departments and agencies of the Government "obligational authority" to commit the Government by orders, contracts, and so forth, to make future expenditures. It was estimated in January 1961 that unspent obligational authority on July 1, 1961 would be \$74 billion. The President requested \$80.9 billion of new obligational authority for fiscal 1962 making a total of \$154.9 billion. However, the President estimated that \$72.7 billion of this would be used for expenditures in fiscal years after fiscal 1962. Congressional enactments generally give the President broad discretion to determine the rate at which obligations will be incurred. As Sen. Harry F. Byrd has pointed out, "In general, there is no effective facility under present legislative procedure or appropriation bills to exercise full and direct annual expenditure control."^{1/}
2. The practice of providing federal agencies with the authority to spend what are called "Public Debt Receipts" has also diminished congressional control over annual spending. This process, known sometimes as "back door financing," provides a greater degree of flexibility to the agencies involved and in the view of the advocates of the ceiling can only be controlled through the use of limitations on new public debt issues.

"Back door financing" involves the process of borrowing from the Treasury to finance government programs and doing so without going through the normal appropriations process. The Treasury, in turn, then borrows the funds needed to finance these operations. Rep. Howard W. Smith of Virginia argued as follows:

What are you going to do this year about back-door spending? It is getting to be a very popular pastime, particularly in the other body. As you know, appropriations under our rules initiate in this body. But that is a way to get them initiated in the other body, through back-door spending; and a great many bills are coming over with that type of financing.

^{1/} Congressional Record, 85th Cong., 1st Sess., 1957, p. 5074.

Here is what we have done this year under what are termed politely "Treasury transactions." That is where you pass an authorization bill authorizing somebody to go down to the Treasury, give them a note, and get all the money he wants. It never comes to the Committee on Appropriations. A number of us have been trying to get something done about it, but the House will not do anything about it.

* * *

We may well be coming back here with another bill just like this before the session is out, asking for another increase. When are you going to stop shadow boxing and get down to business?^{1/}

3. Control over spending is also restricted by the size of the federal budget and the processes by which it is reviewed. Describing this problem, Sen. Byrd stated:

...once the President's budget is submitted in January, Congress never again sees it as a whole until after the appropriations are enacted. The first thing Congress does is to split the appropriation requests of the President into a dozen or more bills. Then it proceeds to consider them separately over a period of 6 months or more.... There is never an opportunity in Congress, in action on appropriation bills, to consider them in terms of annual expenditures in view of estimated revenue.^{2/}

In the view of its advocates, a tight debt ceiling is the only final control that Congress can exercise over the range of spending permitted by congressional procedures. It is only at this point, it is argued, that congressional control can be exercised on the total volume of federal outlays. Curtailing taxes will not do the task unless there is also a limitation imposed on the amount that the Government can borrow. Holding the tax line and restricting the amount that the Government can borrow can bring about a curtailment in spending. The process by which this can work was described by Sen. Byrd in 1954 as follows:

It was a year ago that the President requested Congress to increase the debt limit from \$275 billion to \$290 billion. A bill making this increase was passed by the House of Representatives and sent to the Senate. The Senate Finance Committee heard the testimony of

administration spokesmen who said unless the debt limit were raised by \$15 billion at that time the Government would be unable to pay its bills and a panic would result.

After full deliberation, the Finance Committee, 11 to 4, refused to report the \$290 billion debt limit bill. What happened? The heavens did not fall; panic did not occur. The administration reduced its spending and stayed within the statutory debt limit.^{1/}

The process, thus, is one in which the debt limitation is viewed as a device to bring down federal expenditures to a level that is deemed more appropriate.

The core of the rationale for the tight budget ceiling is that it can control federal spending. It is, in the view of the advocates of the ceiling, almost the last remaining opportunity for economy-minded legislators to strike a blow for fiscal discipline. With the growing complexity of budgetary control, the debt ceiling provides the only opportunity for Congress to view the results of its past actions and to assess fiscal implications. A tight ceiling, which says, in effect, that money will not be spent, is one way in which economy measures can be made effective.

The Critics of a Ceiling

According to the critics of the debt ceiling, this legislation is not an appropriate nor an adequate device for imposing budgetary control. Many of the critics are aware of the difficulties involved in maintaining some type of annual control over federal spending, but they argue the debt ceiling is not the way to attempt this. The reasons they offer are as follows:

1. A tight debt ceiling will not necessarily yield the kind of expenditure cutting that Congress, by itself, would prefer. A debt ceiling which says, in effect, "the Administration cannot have the money for the programs that Congress has approved" is telling the President to choose where he would cut spending. There is, they argue, nothing to prevent the President from using these cuts for political purposes or to curtail those programs which his Administration does not particularly favor (although Congress may rank them of high importance).

According to its critics, the ceiling yields to the President something comparable to the "item veto," a privilege which Congress has jealously kept to itself. As Rep. Mills of Arkansas stated:

^{1/} Congressional Record, 87th Cong., 1st Sess., June 26, 1961, p. 10386.

^{2/} Congressional Record, 84th Cong., 1st Sess., 1955, p.5694.

^{1/} Congressional Record, 83rd Cong., 2nd Sess., 1954, p.14376.

I think we are treading on dangerous ground if we contemplate rejection of this proposal. Are you certain that you are acting in the interest of the people of the United States when you say that you want the President of the United States to cut rather than the Congress doing it, wherever he says he can? Do you think his judgment might be better in this respect than the Congress set up under the Constitution to do the job?^{1/}

Critics say expenditure cuts coming from this type of action tend to yield dangerous or costly repercussions. They point out that one of the areas for "last minute" expenditure cutting is in the Defense Department. In fact, in the latter part of 1957, new defense orders were curtailed substantially, though the effects upon spending were relatively moderate. The consequence was observed from abroad as follows:

A unique fiscal limitation sneered at by economists and deplored by generals, is imposing a form of unilateral disarmament upon the United States. Unbelievable as it may seem, the single most important reason for the recent cutbacks in defense spending--which, incidentally, reduced outlays on research just as the Soviet satellite began to whirl overhead--is the legal ceiling above which the national debt may not rise. The device appears to be peculiar to the United States; moreover, it actually has meaning.^{2/}

Moreover, according to opponents of a tight debt ceiling, certain programs in research and development that were temporarily slowed down were then subsequently, at greater cost, placed on a "crash basis." The debt ceiling, say its critics, forces such hasty cutbacks, which in turn require a later burst of speed with higher costs.

They point out that one consequence of the 1957 cutback was a rash of unpaid bills and considerable publicity about the slowdown in payments to Defense Department contractors. Many of these contractors whose business affairs were closely linked to their work for the Defense Department were forced to curtail operations and lay off workers. One strange and interesting consequence of this operation was noted by a prominent businessman as follows:

One of my friends who was doing quite a lot of business with the military last year was faced with a policy

^{1/} Congressional Record, 87th Cong., 1st Sess., June 26, 1961, p.10390.

^{2/} "Up Against the Debt Ceiling," The Economist, October 19, 1957, p.217.

that the military were going to stop paying their bills until January 1st. This was in the early Fall. He quickly looked over his financial affairs, finding he would have to borrow \$25 million. So you can see what happened by reducing the public debt by \$25 million, this was simply transferred to private debt.^{1/}

Critics state that a further consequence of the rapid cutback in government spending occasioned by the debt ceiling in 1957 was its role in deepening the recession of 1957. On June 28, 1958, Business Week stated:

In the next few weeks, before Congress adjourns, the Administration will have to make its recommendations for raising the debt ceiling. As a matter of common sense, it should ask for enough leeway to make sure that the ceiling will not act as a ruinous and arbitrary determinant of government policies--as it sometimes has in the past.

In the second half of 1957 the debt ceiling forced the Administration to cut back programs needed for long-term national security. And the resulting slash in defense expenditures was an important contributing cause of the recession.^{2/}

Opponents of a tight ceiling point out that the subsequent attempt to speed up programs contributed to the large deficit of fiscal 1959. According to the critics of the tight ceiling, it was thus the ill-timed and ill-considered attempt to curtail spending that played an important part in bringing about this long-run increase in the debt.

2. The critics of a tight ceiling argue that the spending restraints created by the ceiling have often forced the Administration into fiscal subterfuge. Confronted by a tight ceiling, they point out that the Administration is forced to use circuitous devices to obtain funds for the payment of bills that come due. This is done without going through the usual congressional appropriation process and without increasing the debt subject to the debt ceiling.

On several occasions in the past seven years, these subterfuges were used openly to circumvent the ceiling. These devices require the Federal Government to use its secondary line of credit--and as a result, to pay a higher cost for this credit. In 1954, for example, the Commodity Credit Corporation went into the money market and

^{1/} Robert C. Sprague, "Are U.S. Security Policies Adequate," Industry, January 1959, italics added.

^{2/} Business Week, June 28, 1958, p.124.

borrowed slightly over \$1 billion on short-term notes and turned the funds over to the Treasury. Because it was the Commodity Credit Corporation and not the Treasury that was doing the borrowing, the interest charges for these funds were higher than the Treasury would have paid on its own notes. According to one estimate, the additional cost of this roundabout operation was approximately \$10 million.^{1/}

In 1957 and 1958, during the debt ceiling crisis of that period, the Federal National Mortgage Association was called upon to provide cash for the Treasury to pay its bills. FNMA borrowed by issuing its own notes: in this case, the cost was said to amount to approximately \$24 million more than would have been paid if the Treasury had done the borrowing itself.^{2/}

From time to time, the Treasury also turned some of its gold into new money in an effort to meet the debt ceiling fiscal crises. This occurred in 1953 and again in early 1958.

According to the critics of the debt ceiling, these kinds of costly and roundabout manipulations of federal finances are improper to achieve the fiscal discipline needed for the proper operation of government. They note that, in an effort to solve one problem, the Government has been forced to engage in activities which create new problems.

3. The critics of a tight ceiling point out that it severely hampers the Treasury in the management of our large federal debt. Debt management for a volume of securities as large as the federal debt is, they say, a sophisticated and extremely important affair. Billions of dollars of securities mature every year and must be replaced with other securities. The American financial markets are accustomed to these government securities and, indeed, for certain investment purposes, show great preference for them. The key to proper debt management, the critics point out, is to make the most of these preferences by issuing the right kinds of securities at the right rates of interest at the most appropriate times.

Fiscal experts point out that debt management is complicated by the Treasury's inability to know the precise form and interest rates that should be offered at a given moment. If the Treasury offers too low an interest rate, the new securities will not be purchased in full and then another issue must be hurriedly introduced to obtain the cash to pay off whatever securities are

^{1/} M. A. Robinson, The National Debt Ceiling, (Washington: Brookings Institution, 1959), pp.47-48.

^{2/} Ibid., pp.49-50.

maturing. If the rate is set too high, the issue will be sold, but at an unnecessary cost to the Government. Many such experts feel that the practical way to handle the problem is for the Treasury to offer securities in advance of the maturity date of the old issue and in this way, "try out" a rate which is deemed sufficiently close to the market. It can pick the best time to do its selling and give itself enough leeway in time. Then if the issue does not meet with full success, the Treasury will have time to issue another carefully designed block of securities.

When the debt limit is tight, however, the Treasury cannot follow this practice because it would result in a "doubling up" of a portion of the debt for a brief period of time. When the debt ceiling is tight, the Treasury, therefore, must issue securities at precisely the time that an old issue is retiring. It cannot make any mistakes in assessing the market or it will not have enough cash on hand to redeem maturing securities. As a result, when the debt ceiling is tight, the Treasury is forced to offer interest rates that are more certain to be successful; that is, it must offer higher interest rates than might otherwise be necessary to be certain that the sale of new securities will be successful.

According to its critics, the debt ceiling in this setting forces the Treasury to manage the debt with less economy than would be the case if it were given more freedom. The freedom required here is not of an unlimited nature; it merely argues for a sizable gap between existing debt and the ceiling.

The debt ceiling, say its critics, also hinders effective debt management because it reduces the Treasury's flexibility in setting the timing of long-term issues. Efforts to lengthen the average maturity of the debt have held a position of high priority in federal fiscal affairs for some time, yet a tight debt ceiling tends to hamper this task. The Treasury must plan carefully and often wait for the precise moment when long-term securities can be sold. Unless there is room under the debt ceiling at that moment for such sales, they cannot be made. And to wait until older securities are maturing and there is room under the ceiling may mean a less favorable market.

On balance, then, the critics of the ceiling agree that it is capable of curtailing spending when other funds are not available. They argue, however, that the ceiling is a costly and dangerous way to bring about this type of budget control.

The Annual Review

The Advocates of a Tight Ceiling. The ceiling's supporters argue that it forces an annual review of the budget and focuses public attention on deficit fiscal policies. This, in part, was what Rep.

Thomas B. Curtis was suggesting in the following statement during the Committee on Ways and Means hearings last year on H.R.7677:

...I am about at the point, disagreeing, as I do, with the economic philosophy of deficit spending, of trying to figure out where I can, from a practical standpoint, join in political debate with those who disagree and who do believe in deficit financing.

I think this administration, in spite of its words, is pretty much on record as adopting the Keynesian philosophy of deficit financing. I want to challenge that as a politician. I want those who disagree with that to be able to conduct national debate on the subject. It looks like to me that we are forced into only one spot where we can join it and that is possibly by refusing to go along with the debt limitation.

Former Secretary of the Treasury George M. Humphrey was saying the same things when he stated:

I have fought to hold to the present debt ceiling because I think that the restraint the present debt ceiling gives to the Executive, to the Congress, to everyone concerned is a very wholesome thing to have, and I think that it is like breaking through a sound barrier; there is an explosion when you go through it, and there ought to be one.

It has weight with public sentiment, and I think it is a deterrent to spending over and above that amount. So, I am in favor of it.^{1/}

According to the advocates of the tight ceiling, the ceiling supplies a psychological barrier to the growth of spending. It is the focal point for a major debate on fiscal policies and, even though it must focus on the fiscal decisions of the past, the advocates of the ceiling maintain it can have a long-run beneficial effect on spending. The debate it fosters provides an occasion when the long-run issues of fiscal affairs are finally faced.

The hope expressed by the advocates of a tight debt ceiling is that the public attention brought to federal fiscal affairs by the annual debate on the debt ceiling will encourage public reaction against excessive spending. Economy in government, it is maintained, can only be achieved effectively when the public demands it. If the public debates

^{1/} Financial Condition of the United States, Hearings Before the Senate Committee on Finance, 85th Cong., 1st Sess., p.258.

over the debt ceiling can encourage the public to make such demands, then, according to its advocates, the tight ceiling will perform a highly desirable fiscal function.

The Critics of the Ceiling. According to its critics, the "annual review" concept of the ceiling provides an opportunity for some members of Congress who have voted for spending in excess of the ceiling to record a vote for economy. The fact that the two votes may be inconsistent is, they argue, often overlooked. This, essentially, was the view expressed by Rep. Wright Patman of Texas when he stated:

There were many things which went into this bill for which I did not vote, but I am in part responsible for them. as I am a member of Congress. We must have fiscal responsibility. We cannot have a policy of voting for appropriation bills and then of voting against tax bills to pay the costs or voting against raising the debt limit to borrow the money to pay our just and honest debts. We must pay them.^{1/}

Even those who have opposed the easing of the debt limit have noted the potential duplicity in this legislation which deals with fiscal affairs after the fact. For example, Rep. Alger of Texas stated:

Mr. Chairman, I would like to call the attention of the Members to the minority views...where the gentleman from California and I joined in pointing out what a gimmick this temporary debt limit is. The gentleman from California and I feel it is just a gimmick. It tends to give us an aura of responsibility to an area that is absolutely irresponsible. Let us throw it out of the window, because it has no restraining effect whatsoever in limiting the spending money.^{2/}

According to the critics of the debt ceiling, the annual debate over the ceiling does not produce fiscal results which are useful. It does, they say, provide an opportunity for members of Congress to shrink away from the hard, cold reality of fiscal discipline. According to the critics of the ceiling, the problems of fiscal discipline will only be handled effectively when Congress makes an effort to raise the taxes required for spending proposals and exercises adequate and continuing restraint on spending proposals.

^{1/} Congressional Record, 87th Cong., 1st Sess., June 26, 1961, p. 10398.

^{2/} Ibid., p. 10399.

Most people, they say, are aware of the fact that there are times when the federal debt must increase; wartime and periods of falling national income are frequently mentioned as such periods. But, they point out that deficits of this sort are not necessarily reflections of a lack of fiscal discipline. Rather, they maintain that it is the many spending proposals for enlarged and new programs and purposes that must be given greater consideration; but for this purpose, according to its critics, the debt ceiling offers no help. Rather, they argue, it provides an opportunity for some members of Congress to say that they have been proposing economy, when, in fact, they have done just the opposite in the preceding months.

The Effects of the Debt

The Advocates of a Tight Ceiling

The supporters of the ceiling maintain that one of its effects will be to limit the expansion of a national debt whose size is dangerous and harmful to the American economy. Basically, they regard the debt as a source of inflationary pressure on the economy and as a threat to the Nation's solvency. It is often regarded as a consequence of waste and, to some extent, it is also considered a reflection on the fiscal morality of those who govern the affairs of our Nation.

The arguments of the advocates of a tight ceiling draw primarily on the financial analogy between the National Government and the individual household or business firm. They see the growth of debt as the imposition of an increasing burden of interest payments on future generations and a step toward the destruction of the economic values of our society.

Those who view the national debt in this manner support a tight debt ceiling on the grounds that it constitutes a limit on what they believe to be a dangerous economic development. The debt ceiling, in other words, is not only an instrument to achieve something that Congress cannot otherwise achieve; it is a direct and frontal assault upon a dangerous element in our economic affairs.

The Critics of a Ceiling

According to its critics, the debt ceiling is not an effective device for curtailing the debt and, even if it were, the debt is not necessarily a matter of first importance at all times. They argue that the burden of the debt on the American people is relatively light in view of the large income of the Nation, and they point out that many times in the past, the cost of debt has represented a considerably larger share of our total income than it does at present.

They disagree with the charge that the federal debt is necessarily a contributor to the forces of inflation. They point out that this notion, which became popular during World War II, when the Nation's

resources were being used to their fullest, was correct at that time. However, in recent years, increases in the debt have not, they argue, played the same inflationary role.

According to the critics of the ceiling, an arbitrary limit on the growth of the federal debt is, from time to time, an arbitrary limit on the growth of the Nation's income. They point out that debt growth helps to stimulate the growth of national income in our kind of economy and over the decades our private debt and public debt have shared in this stimulus. Most of the debt stimulus in recent years has stemmed from our rapidly growing private debts. In the future, however, they say when private debt growth slows down (as it does periodically), government debt can fill the gap as it has in the past--but not if the ceiling prevents it.

THE ALTERNATIVES

Alternative proposals from time to time have related primarily to the question of whether increases in the ceiling should be permanent or temporary. Other alternatives which have been made in the past have not formally related to the ceiling, but do have a bearing on many of the same issues.

(1) Abolish the ceiling entirely. This would mean that Congress would be required to return to its pre-1917 practice of authorizing new borrowings whenever they became necessary. This practice would more clearly link the intent to borrow with specific spending proposals.

(2) Establish a permanent "gap" between the existing debt and the ceiling. A gap of perhaps \$10 to \$15 billion which would always provide the Treasury leeway for fulfilling any demands made by Congress is what is conceived here.

(3) Reduce the ceiling by a specific amount each year. This, in effect, is what is sought by some of the bills which have proposed a statutory debt reduction to be included as a part of the budget. This alternative would require a matching of spending proposals with tax proposals at the time that the total budget is approved.

(4) Leave the ceiling where it is and adjust it from time to time by either temporary or permanent changes to meet the fiscal needs of the moment. This is the practice that has been followed for the past several years.

QUESTIONS RAISED BY THE PROPOSAL

1. Does the ceiling represent the most effective way to curtail spending under present procedures?
2. Does the ceiling represent a "second look" at the total budget and provide an opportunity for re-examining the actions of the past?
3. Is it the debt or the growth of the Government's role in the economy that the debt ceiling is seeking to control?
4. Is growth in the national debt harmful to the economy under all circumstances?
5. Is the concept of the debt ceiling applicable to spending (a spending ceiling) or to taxes (a tax ceiling)?
6. What is the relationship, if any, between the debt ceiling and fiscal responsibility?
7. If the debt ceiling should be eliminated, what other legislative measures might be desirable?

AMERICAN ENTERPRISE ASSOCIATION

Recent Long-Range Studies

Morley, Lorna, and Morley, Felix. THE PATCHWORK HISTORY OF FOREIGN AID.
April 1961.

Haberler, Gottfried. INFLATION: Its Causes and Cures, Revised and
Enlarged Edition. June 1961.

Benson, George C. S., and McClelland, Harold F. CONSOLIDATED GRANTS: A
Means of Maintaining Fiscal Responsibility. December 1961.

Van Cise, Jerrold G. THE FEDERAL ANTITRUST LAWS.
January 1962.

One dollar per copy

Discounts: 25 to 99 copies-20%; 100 to 299 copies-30%
300 to 499 copies-40%; 500 and over-50%

COPY

*File
Work File
Disturbed
Areas*

Memo to Bill
cc: Senator
Dave Nelson

From John Stewart

March 14, 1963

I had an interesting telephone conversation with a Bob Arnold, Stanford Research Institute, who has been doing a study of the Appalachian Region for ARA.

He has completed the study and wanted our office to know the results prior to its publication in several months.

Briefly his results are these:

The short-term unemployment problem is simply beyond the reach of ARA. He was very enthusiastic about the impact of the accelerated public works program and feels that this is the only answer for the short-run. This obviously backs up our own conclusions quite concisely.

But Arnold also feels that the public works program should be viewed and should be sold as more than a short-term answer. He feels that it should stand as the first step toward a long term answer, namely the opportunity to clean up the facilities of many towns, communities and regions where unemployment is a serious problem. He quite emphatically stated that the APW program is not a boon-doggie, but was making some very fine fundamental changes in the economic base of these areas. He felt it would be a serious mistake to simply view APW as a short-term answer.

He also feels that the persons in ARA do not truly appreciate the extent of unemployment that exists in such areas as Appalachia. He suggests that a forecast of unemployment in June, 1963, be made for these areas of current high unemployment.

He also suggests a survey of the financial resources available to States for matching purposes in the public works program. He feels these resources are rapidly drying up and that this factor should be taken into account before Congress reauthorizes the program. Perhaps more lenient provisions would be helpful in many areas.

COPY

Arnold gave me the name of Whisman who is on the staff of Governor Coombs in Kentucky as the person best acquainted with the problem of matching funds and State financial resources.

March 6, 1963

Memo for John S.

cc: Bill
Senator

From Senator

*File
with*

new memo

I have been thinking about tax legislation for depressed areas, something along what was done for Puerto Rico when it was in such a serious condition. We ought to examine what the program was in terms of tax incentives for investment in Puerto Rico. Can we get the Library of Congress to do something on that? You may want to discuss this with Neal Peterson.

COPY^{ed}

March 19, 1963

Legislative Reference Service
Library of Congress
Washington 25, D. C.

Gentlemen:

Senator Humphrey would like you to undertake a study to suggest possible legislative measures granting special tax incentives to stimulate investment in economically distressed areas similar to the tax incentives created to encourage investment in Puerto Rico.

I imagine this study should include, at a minimum, a full description of the tax incentives existing for Puerto Rico, an analysis of the economic problems of Puerto Rico in relation to selected distressed areas on the mainland, the possibilities of attacking the long-term economic problems of these areas by a similar tax incentive approach, etc. Please feel free to suggest additional factors that should be considered in this study.

Senator Humphrey would like to receive a preliminary report on this study by Wednesday, March 27. This could be a brief memorandum on the outlines of the broader study, together with some tentative conclusions drawn from initial investigations.

Please call me if any questions arise in regard to this request. My extension is 2424.

Sincerely yours,

John G. Stewart
Legislative Assistant to
Hubert H. Humphrey

bcc: Neal Peterson

AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS

EXECUTIVE COUNCIL

GEORGE MEANY
PRESIDENT

WM. F. SCHNITZLER
SECRETARY-TREASURER

WALTER P. REUTHER
WM. C. BIRTHRIGHT
DAVID J. McDONALD
JOSEPH CURRAN
JOSEPH D. KEENAN
RICHARD F. WALSH
JAMES A. SUFFRIDGE
PAUL L. PHILLIPS
PAUL HALL

GEORGE M. HARRISON
JAMES B. CAREY
EMIL RIEVE
MAURICE A. HUTCHESON
JACOB S. POTOFKY
LEE W. MINTON
O. A. KNIGHT
PETER T. SCHOEMANN
HERMAN D. KENIN

HARRY C. BATES
DAVID DUBINSKY
WM. L. McFETRIDGE
A. J. HAYES
A. PHILIP RANDOLPH
JOSEPH A. BEIRNE
KARL F. FELLER
L. M. RAFTERY



EXECUTIVE COMMITTEE

GEORGE MEANY
WALTER P. REUTHER
GEORGE M. HARRISON
JAMES B. CAREY
HARRY C. BATES
DAVID J. McDONALD
DAVID DUBINSKY
WM. F. SCHNITZLER

815 SIXTEENTH STREET, N.W.
WASHINGTON 6, D. C. NATIONAL 8-3870

July 8, 1963

File

The Honorable Humbert H. Humphrey
Majority Whip
United States Senate
Washington 25, D. C.

Dear Hubert:

It is my understanding that the question of extending the accelerated public works program will come before the leaders' meeting on July 9. I thought you would be interested in seeing the letter which President Meany sent the President on May 23, 1963. You can see from the text of this letter how strongly the AFL-CIO feels that the extension of this bill is absolutely necessary to the economic welfare of this country.

Sincerely yours,

Andy
Andrew J. Biemiller, Director
DEPARTMENT OF LEGISLATION

enclosure



FOR RELEASE IN A.M. PAPERS, THURSDAY, MAY 30, 1963

AFL-CIO President George Meany has appealed to President Kennedy to support extension of the Public Works Acceleration Act through 1964, with a \$2 billion appropriation to finance it.

"A federal program of this magnitude, plus the approximate \$1 billion which would be added by state and local matching funds, would create about 300,000 badly-needed jobs, would help thousands of communities obtain public improvements of permanent worth and would substantially stimulate the national economy," Meany wrote on May 23.

The need for the program and the eagerness of state and local governments to utilize it is illustrated by the response to the original measure, signed into law last September, Meany said.

"By the end of January, 3,756 projects absorbing all of the \$400 million initially appropriated had been approved," he pointed out. "By April an additional 6,200 projects requiring a federal outlay of about \$1.2 billion had been received...I am advised that this backlog now approximates \$1.7 billion. Yet only \$450 million in additional funds is available...; unless the program is extended, apparently \$1¼ billion in public improvement requests already received must be shelved."

The true backlog far exceeds these figures, the AFL-CIO leader noted, since some applications have been delayed pending arrangements for local matching requirements, and new submissions have generally been discouraged by Washington since February, when it became apparent that the number of applications already on hand far exceeded the available funds.

"Unfortunately, the Congress has now cut the \$900 million in federal funds initially authorized for a 12-month accelerated public works program to an \$850 million appropriation to be stretched out to January 31, 1964," Meany said. "If action to extend the program for another 12 months is not undertaken during the present session of Congress, its expiration at the end of January is almost inevitable."

Meany recalled that a one-year term for the original act was supported by the AFL-CIO with the understanding that there would be an extension if unemployment remained at a high level.

"All evidence indicates that unemployment will exceed...5% during...the year ahead," he said.

The text of Meany's letter follows:

Because of continuing high-level unemployment and the prospect that it will not be substantially reduced in the immediate future, the AFL-CIO urges extension of the Public Works Acceleration Act through 1964.

When you signed this Act last September, one of the most effective programs to meet the problem of unemployment was launched. Thousands of workers in areas of substantial labor surplus have returned to work building essential public facilities of long-term worth, and additional thousands have also left the ranks of the unemployed to supply the material and equipment required for these projects. At a time like the present, when the private sector of the economy is failing to fully utilize the manpower and productive resources of the country, no better program to put people to work and to permanently enrich the nation could possibly be conceived.

-more-

The value of this Act to the jobless, to the communities that are obtaining lasting public improvements, and to the national economy is so evident, it clearly should be continued as long as unemployment remains abnormally high.

The tremendous response to this program is demonstrated by the fact that by the end of last January, 3,756 projects absorbing all of the \$400 million initially appropriated had been approved. By April an additional 6,200 projects requiring a federal outlay of about \$1.2 billion had been received and awaited approval. I am advised that this backlog now approximates \$1.7 billion. Yet, only \$450 million in additional federal funds is available to accommodate these projects; unless the program is extended, apparently \$1½ billion in public improvement requests already received must be shelved.

It has been estimated that these projects alone -- if undertaken -- would create about 125,000 man-years of work. What is more, I am advised that at least double this volume of essential public works, on which planning is completed or soon could be, could quickly be gotten underway in areas of substantial unemployment if funds were available. Many projects have been delayed by time consumed arranging to meet local matching requirements, and the submission of others has been discouraged by Washington since February because of the shortage of funds.

Unfortunately, the Congress has now cut the \$900 million in federal funds initially authorized for a 12-month accelerated public works program to an \$850 million appropriation to be stretched out to January 31, 1964. Moreover, if action to extend the program for an additional 12 months is not undertaken during the present session of Congress, its expiration at the end of January is almost inevitable.

A year ago, when the AFL-CIO testified in behalf of the Public Works Acceleration Act, we supported a one-year program, with the proviso that it should be extended if the national unemployment rate continues to exceed 5 percent. Moreover, in adopting a one-year program, Congress and the Administration implied that it would be extended if unemployment remained at high levels. All evidence indicates that unemployment will exceed a 5 percent rate during the course of the year ahead.

The AFL-CIO therefore asks you now to urge the Congress to extend the Act through 1964 and to appropriate \$2 billion for that purpose so an adequate program can be assured. This request is in line with the unanimous decision of the AFL-CIO Executive Council, at its recent meeting in St. Louis, to urge the Administration and the Congress to support an extension of the Act through 1964 and a \$2 billion appropriation to provide a significant job-creating program.

A federal program of this magnitude, plus the approximate \$1 billion which would be added by state and local matching funds, would create about 300,000 badly needed jobs, would help thousands of communities obtain public improvements of permanent worth, and would substantially stimulate the national economy.

U.S. DEPARTMENT OF COMMERCE
AREA REDEVELOPMENT ADMINISTRATION
WASHINGTON 25, D.C.

OCT 19 1962

OCT 22 1962

*June - File -
How we have a
general ARA file?
Send copy of letter
to Neal & Bill.*

Honorable Hubert H. Humphrey
United States Senate
Washington 25, D. C.

Dear Senator Humphrey:

Secretary Hodges asked me to transmit this report in response to the letter you signed with 16 other Senators and Senator Randolph, dated February 15, 1962. You requested that the Department of Commerce consider the degree to which the Area Redevelopment Administration's program might be enhanced by accelerating the Title II road building program in those rural areas which qualify for redevelopment because of severe unemployment or underemployment under P. L. 87-27. You pointed out that in these areas "...there are resources--timber, recreational facilities or recreational potentialities, and mineral wealth--which await only new or improved roads to make them economically useful."

The report, which was prepared with the assistance of those Bureaus with responsibilities for the roads programs, points out that not only will such an accelerated program afford productive work for some of the excess labor force in these areas of need, but the program will improve accessibility to the natural resources of these areas and will thus substantially enhance their opportunities for permanent economic growth. Furthermore, by making the natural resources of these areas accessible, we are going a long way toward making it possible for these areas of chronic economic distress to make an optimum and continuing contribution to the national economy.

The report shows that there are more than \$1.6 billion of unmet road building needs on those public lands which are within or immediately adjacent to counties eligible for assistance by the Area Redevelopment Administration. If we were to accelerate present programs by providing an additional

Honorable Hubert H. Humphrey
Page 2

\$90 million per year, we could employ 25,000 new workers, almost half of them directly connected with the road construction itself, and the remainder added throughout the economy. Most important, however, such an accelerated program would accrue for the Nation the inestimable continuing benefits deriving from a fully developed resource base.

We did not release the report in view of the consideration of the Accelerated Public Works Act. An addendum has been added citing the applicability of the new Act.

Sincerely,


Administrator

Enclosure

ACCELERATING THE PUBLIC LANDS ROADS
PROGRAM IN AREAS OF ECONOMIC HARDSHIP

Report Prepared for the Senate Committee on Public Works
by the U. S. Department of Commerce
Area Redevelopment Administration
July 1962

ACCELERATING THE PUBLIC LANDS ROADS
PROGRAM IN AREAS OF ECONOMIC HARDSHIP

ADDENDUM

The "Public Works Acceleration Act," Public Law 87-658, as signed into law by President Kennedy on September 14, 1962, was enacted by the Congress in furtherance of a finding that certain communities and areas suffering from unemployment and underemployment have failed to share in recent economic gains and that Federal action is necessary to provide immediately useful work for the unemployed and underemployed of these communities as well as aiding these communities to develop industrially through the improvement of their facilities.

Funds which the Congress shall appropriate for the purposes of the Act may be used under the direction of the President by various departments and agencies of the Federal Government (1) for the Federal Government's own public works projects, or (2) for loans or grants to states and local governments for public works projects.

Thus funds may be made available to the Federal agencies cited in this report to accelerate the construction of roads in the redevelopment areas as described herein.

Work on forest highways could be accelerated under the Public Works Acceleration Act inasmuch as funds could be allocated over and above the forest highway authorization and without regard to the limitations imposed by the existing forest highway apportionment formula based on area and value of National forest lands.

Also, under the jurisdiction of the Bureau of Public Roads, a limited number of major road projects in areas under the administration of the National Park Service could be accelerated with funds made available under this Act.

(over)

Road building projects on lands under the jurisdiction of the Department of the Interior's Bureau of Land Management and Bureau of Indian Affairs will be eligible for acceleration with funds made available under the Public Works Acceleration Act as will the forest roads and trails projects of the U. S. Forest Service.

ACCELERATING THE PUBLIC LANDS ROADS
PROGRAM IN AREAS OF ECONOMIC HARDSHIP

Summary

There is a need for the construction of park and forest roads and highways in the public domain of the United States in or adjacent to areas eligible for assistance under the Area Redevelopment Act (Public Law 87-27) amounting to more than \$1.6 billion. The total requirements are shown on the following page.

Approximately \$43 million is being expended in these areas today by the National Park Service, the Forest Service, and the Bureau of Indian Affairs, as well as an unknown part of \$27 million which the Bureau of Public Roads allocates amongst the 29 states and Puerto Rico for forest highways construction. If the Congress were to accelerate these agencies' long range programs by authorizing an additional \$90 million per year, to be expended only in redevelopment areas, it would provide 5,000 new jobs directly on the road work, 6,000 new jobs in associated industries, and another 14,000 new jobs throughout the economy stimulated by the accelerated program.

SUMMARY OF PRESENT AUTHORIZATIONS AND TOTAL ESTIMATED NEEDS
FOR ROAD BUILDING ON PUBLIC LANDS IN OR ADJACENT TO AREAS
ELIGIBLE FOR ASSISTANCE UNDER THE AREA REDEVELOPMENT ACT

Agency	Present Authorizations	Total Estimated Needs
Bureau of Public Roads	N.A. <u>1/</u>	\$986,238,000
National Park Service	\$23,000,000	200,000,000
Bureau of Indian Affairs	12,669,000	207,283,000
Forest Service	7,320,000 <u>2/</u>	220,134,000
Bureau of Land Management	N.A. <u>3/</u>	N.A. <u>3/</u>
Total	\$42,989,000	\$1,613,655,000

- 1/ Bureau of Public Roads allocates approximately \$27 million to 29 states and Puerto Rico for forest highway construction. The states' allocation amongst their counties is not available.
- 2/ Estimate: 18.3 percent of \$40 million total authorization (see Appendix 3).
- 3/ Bureau of Land Management allocates \$1 million and estimates needs totaling \$1.1 billion, but its reporting procedures do not reveal intrastate, small area data.

Background

In his special messages to the Congress on natural resources and agriculture in 1961, President Kennedy urged the acceleration of all forest development to insure adequate forest resources in the future. In the letter of February 15, 1962, addressed to the Secretary of Commerce by a group of interested Senators, it was pointed out there exist on many Federal lands latent resources which need only improved roads to make them economically useful. These lands include the National Forest and Parks, Indian Reservations, and the miscellaneous holdings of the Bureau of Land Management, much of which lands coincide with or are adjacent to counties with unemployment greater than the Nation's average (See Appendix 1).

Senator Randolph asked the Secretary to determine the economic effects of increasing the road building monies available in these special areas, and the data for this report was supplied by the five Federal agencies which have substantial road building programs on public lands: the Bureau of Public Roads, the Forest Service, the National Park Service, the Bureau of Indian Affairs, and the Bureau of Land Management.

The Bureau of Public Roads

The forest highway system is administered by the Secretary of Commerce through the Bureau of Public Roads. Forest highways are parts of Federal-aid, state, county, and other public highways in and adjacent to the National Forests. They are of primary importance to the states, counties, and communities for intra and interstate traffic and transport. These highways also provide primary access to and outlet from forest development roads and trails, and they are heavily used by persons visiting the National Forests for recreation and other purposes. Most of the products of the Forests move over these highways enroute to mill or market.

There are more than 24,000 miles of roads on the designated highway system, and 28,000 more miles have been cited by the Bureau of Public Roads as possible additions to the system. At the present time the Bureau of Public Roads allocates to the 29 States and Puerto Rico -- for those areas cited in Senator Randolph's letter (see Appendix 5) -- nearly \$27 million for road building and maintenance on the designated forest highway system. The amount of allocated monies allotted by the states to the redevelopment areas is not now available. At the

present time there is no authority to assure the channeling of monies into the redevelopment areas.

The Forest Service

Forest development roads and trails, as distinguished from "forest highways," provide access to national forests lands for the protection, development, and multiple-use management of the forests, including resources on which communities in and near the forests are dependent. This system of roads and trails is administered by the Secretary of Agriculture through the Forest Service. In the present system there are nearly 180,000 miles of roads and 107,000 miles of trails; it is estimated that when completely installed this total system will consist of 542,000 miles of access roads and a trail network reduced to 80,000 miles.

For the redevelopment and labor surplus areas cited by Senator Randolph, the Forest Service is at present allocating \$7.3 million of its \$40 million appropriation for the total system of roads and trails (7.3 million is an estimated figure, as a precise reporting was not possible in time for this report). The estimated total need for the roads and trails in or near these special areas is \$220 million.

The National Park Service

The present authorizations for National Park Roads and Trails and National Parkways work total \$34 million annually, and it is estimated that \$23 million of this amount is being expended in those areas shown on the map Redevelopment Areas, November 13, 1961 (see Appendix 8). Under the National Park Service's present program the \$200,000,000 estimated total needs for these special areas could be met in six years. (See Appendix 4).

The Bureau of Land Management

The Bureau of Land Management is responsible for the conservation, management and development of some 447 million acres of the Nation's public lands. For ten western states and Alaska the Bureau estimates that its long range road construction program will amount to approximately one billion one hundred million dollars, and it is intended to accomplish 14 percent of that program amounting to \$164 million, during the next decade. Present authorizations for the Bureau's road program amount to less than \$1,000,000. (See Appendix 7).

The Bureau of Indian Affairs

This Bureau is responsible for maintaining a Federal-aid road system of more than 16,000 miles, serving some 60 million acres of land: this includes the Indian Reservations, all of which have been designated eligible for assistance under the Area Redevelopment Act. The Bureau estimates that its total needs amount to more than \$207 million; its present authorization is \$12 million.

Redevelopment and Labor Surplus Areas

The Area Redevelopment Act provides the means by which the Federal Government, in cooperation with State and local governments and private enterprise, can help areas of substantial and persistent unemployment and underemployment plan and finance their economic redevelopment. The Secretaries of Agriculture, Labor and Interior provide information which the Secretary of Commerce uses to determine which areas may be designated as redevelopment areas under the Area Redevelopment Act (Public Law 87-27). An area's potential eligibility is determined by a complicated set of statistical indices of employment and income. (See Vol. 26, No. 205, Federal Register, October 24, 1961). An area may be a single county, part of a county in a few unusual cases, or several counties as in the major labor market areas.

In this report the agencies programs are presented in terms of costs primarily, with road mileages indicated where these data are readily available. It was not possible, however, for every agency to report its program for areas smaller than States.

The employment-cost ratio figures have been derived from ratios developed by the Bureau of Labor Statistics (see Appendix 2).

National and Local Benefits

What benefits can be expected from the expenditures required to provide the new roadways?

At the outset it should be noted that local road building programs such as proposed here have benefits beyond usual contra-recession type programs and are not subject to some of the latter's weaknesses. It has been stated that public works programs launched as contra-cyclical measures may sometimes be inflationary if they take too long to initiate and if they extend beyond the time it takes for the economy to return to normal. However, in areas of chronic and persistent unemployment and underemployment, labor and facilities remain slack even when the national economy has reached prosperous levels again. Furthermore, if these areas are to make a lasting contribution to the national economy, rather than to remain a drag on it, fundamental measures must be taken to make it possible for the economies of these areas to function properly. A major road building effort in these areas will take considerable time to accomplish, but this is the only means by which these areas' useable resources can be made accessible for better management and for fuller development.

In the normal practice, justification usually takes the form of offering a show of "benefits" expected to be derived from the proposed construction which can be balanced against the cost. In developing this balance in the case of the normal highway construction programs, emphasis is usually placed on benefits to the user of the projected highway, i.e. "user costs" saved. This procedure or emphasis is generally accepted in the normal roads programs since the money for the work actually comes chiefly from the motor vehicle operator in the form of taxes on his fuel.

Much highway construction, however, is of a multi-purpose nature, the costs of which must in turn be balanced against a whole series of benefits by the citizens of the affected area and even beyond. This is true in the case of roads under Title II of the Federal-Aid Highway Act, which includes forest highways and development roads, parkways and park development roads, and the Indian Reservations and public land roads. The "justification" for these roads should be considered in terms of a wide range of benefits.

The National Forests

The National Forests are a source of direct financial revenues to the Federal Government. It is estimated that these revenues will increase to approximately \$230 million annually in ten years. Moreover, they will continue to be in excess of the annual operating expenses.

It is estimated also that the ten-year program sponsored by the Department of Agriculture will increase the capital value of the National Forest systems by about \$2 billion. It is estimated further that for every \$1 of stumpage sold, \$20 in end-products results. This means that the annual sale of 13 billion board feet of saw timber expected to be reached at the end of the ten-year period will have a total consumer value of over \$4 billion. The relevance of these national figures to redevelopment areas is indicated by the fact that of the total of 186 million acres of National Forest lands, 80 million acres (43 percent) are in or near areas of high unemployment or underemployment.

In addition to the asset value of the National Forests, numerous other benefits can come from their development. As recreation areas they have very real value, even though this value is difficult to measure in dollars and cents. It is expected that recreational visits to all national forest areas will reach 195 million annually by 1972, involving indirect benefits through estimated expenditures of about \$15 billion for sporting equipment, transportation costs, etc. The trend toward longer vacations, moreover, will tend to foster increased travel.

On the other hand, it should be noted that our forest resources sustain considerable losses annually from inability to market mature timber because of lack of access roads. Destructive agencies, such as disease, insects, fire, animals and even weather, combined to create a loss of roughly 44 billion board feet of timber in the year 1952 alone. Quicker, more effective control action is needed, which calls for additional forest roads. The Forest Service estimates that a loss of \$40 to \$60 million occurs annually from insects and disease because of "inaccessibility."

In a special report on the Pacific Northwest's forest resources, John Fedkiw, forest economist with the U. S. Forest Service, states that "the big timber management task of the future lies in accelerating the advance roading program in currently undeveloped forest areas... Advance roading ought not wait on market development. Properly conceived and planned public and private investment not only must anticipate

market development, it must also recognize that advance roading is the first step in market development."

Natural Resources on Indian Reservations

The Bureau of Indian Affairs, Department of Interior, exercises authority over nearly 60 million acres of land, including 13 million acres of forest lands and 41 million acres of range lands. The 1963 estimated value of saw logs at the mill from these lands is \$37,050,000. The estimated value of 1963 stock production is \$23 million and of other crops is \$103,673,000. Current income from oil and gas is \$44,396,000 and there is in addition a substantial production of coal, uranium and other minerals. The total potential production from these lands is, therefore, of considerable economic significance.

The conservation, production and marketing of the basic raw materials on Indian lands are to a large extent dependent on road transport. The Department of Interior has set up a schedule of road construction deemed necessary over the next 20 years to sustain and advance the Indian reservations to a level of self-sustaining economy and at the same time protect these resources as trustee.

There is a critical need for the reconstruction and maintenance of forest management and protection of roads on Indian reservations. The present method of providing these timber access roads is to include the construction and maintenance of certain access roads in the timber sales contract. This is satisfactory until completion of the contract which also stops maintenance. Lack of reconstruction and maintenance of these roads is causing a loss on the initial investments and the inability of the Government to carry out its responsibilities for management of the Indian forest lands.

The total road construction scheduled by the Bureau of Indian Affairs over the next 20 years amounts to 21,865 miles, at a total cost of \$207,283,000. The Bureau proposes to spend \$60,669,000 during the next 5 years, leaving \$146,614,000 as the amount required to complete the schedule.

Other Benefits

Apart from the benefits which accrue directly from the construction and extension of forest roads already indicated there are many benefits to others than the user as such which may be derived from the construction of highways of a more general character.

Education

The construction of improved highways has generally, and in rural areas particularly, provided substantial benefits. It has facilitated the trend toward fewer, larger, better-equipped schools with specially trained staffs enabling higher standards of instruction. The number of one-teacher schools has declined from 190,000 to 25,000 in the past 40 years. School attendance has also greatly improved during this period. School bus travel cost per pupil has declined 20 percent at the same time that average daily bus mileage has increased from 22 miles to 40 miles. The effectiveness of library services also has been improved, partly through development of "Bookmobiles," as well as increased accessibility.

Public Health

Public Health is advanced through highway construction by increasing the effectiveness of services in making it easier to reach areas of need and likewise easier for those in need of service to travel to health centers. Fewer, strategically located, completely equipped hospitals can serve a larger public better.

Recreation

Recreation has already been referred to in connection with the proposed development of our forest roads and the increasing extent of travel, both vacation-inspired and other as the automotive vehicle is improved as well as its right-of-way. It is reported that 95 percent of the visitors to our national parks come by private automobile. Estimates indicate that between \$10 and \$20 billion are spent annually on vacations. The expenditures are spread over a wide front. A survey conducted by the American Automobile Association in the early 1950's covering 53 million tourists indicated an average period of trip of 10 days and an average distance traveled of 1,000 to as much as 4,300 miles for somewhat longer periods. Evidence has been offered that adequate highway facilities have tended to popularize recreational areas generally, e.g. between Yorktown and Jamestown, Virginia, and the Bay Bridge in Northeastern Maryland, which resulted in doubling the traffic over that route. The Garden State Parkway in New Jersey is reported to have completely reversed a downward trend in retail trade and resort business in the area along its route, and the Pennsylvania Turnpike, it is stated, has had a similar effect.

Protection

Benefits accrue also through increased efficiency of both police and fire protection. The number of acres of forest burned has declined from 30 million to 3 million in the past 16 years, much of which reduction has been attributed to the provision of more and better access roads.

Appendix 1

Description of Special Areas Used in This Report

1. Senator Randolph's letter to Secretary Hodges includes a list of counties originally prepared by the Forest Service for its own program. This list was used by the Bureau of Public Roads and the Forest Service in preparation for this report. It does not include all the areas eligible for assistance under the Area Redevelopment Act, as it lists only counties in or adjacent to National Forests. (See Appendix 3).
2. The National Park Service prepared data for this report on the basis of the Area Redevelopment Administration's map entitled Redevelopment Areas, November 13, 1961. (See Appendix 8).
3. The Bureau of Indian Affairs reported for the areas under its jurisdictions, all of them having been designated eligible for assistance under the Area Redevelopment Act.
4. The Bureau of Land Management under its present reporting techniques cannot supply data for small areas.

Derivation of Estimates for New Jobs Added by
Accelerated Road Building Program

1. Every \$1,000,000 for road construction represents 55 workers per year working directly upon the road building program, and 60 workers per year in associated industries.
2. Every \$1,000,000 of construction activity generates \$1,250,000 more expenditures, or, in other words, represents a contribution to GNP of \$2,250,000.
3. Every \$1,000,000 contribution to GNP represents approximately 125 new jobs.

Thus; a \$90 million road building project represents the following:

\$90 x 55 workers (on the roads)	=	4,950
\$90 x 60 workers (associated)	=	5,400
\$90 x 1.25 (GNP addition) x 125 workers	=	14,062
Total New Workers		24,412

FOREST SERVICE - U.S.D.A.

Appendix 3

ESTIMATE OF ROAD CONSTRUCTION AND RECONSTRUCTION
IN THE DEVELOPMENT PROGRAM FOR THE NATIONAL FORESTS
IN COUNTIES IN REDEVELOPMENT AND LABOR SURPLUS AREAS
FOR FISCAL YEARS 1963 THROUGH 1972

<u>State</u>	<u>County</u>	<u>Miles</u>	<u>Cost</u>
Alabama	Etowah	0	\$ 0
	Walker	0	0
	Calhoun	25	400,000
	Franklin	0	0
	Talladega	45	600,000
	Montgomery	0	0
	Jefferson	4	82,000
Alaska	Anchorage	61	6,496,000
California	Stanislaus	0	0
	Mendocino	93	1,769,000
	Tuolumne	268	6,042,000
	Glenn	67	1,292,000
	Los Angeles	547	18,946,000
	El Dorado	293	6,181,000
	San Bernardino	428	11,608,000
	Riverside	283	6,706,000
	Humboldt	142	5,200,000
	Orange	54	810,000
Colorado	Pueblo	26	290,000
Florida	Franklin	0	0
Georgia	Habersham	39	292,000
Idaho	Latah	34	745,000
Illinois	Saline	6	100,000
	Alexander	14	220,000
	Williamson	0	0
	Gallatin	5	84,000
	Pope	38	585,000
	Union	18	273,000
	Massac	2	30,000
	Pulaski	0	0
	Jackson	17	266,000
	Hardin	10	160,000
	Johnson	5	73,000
Indiana	Lawrence	9	151,000

<u>State</u>	<u>County</u>	<u>Miles</u>	<u>Cost</u>
Kentucky	Laurel	19	380,000
	Rowan	8	157,000
	Whitley	14	282,000
	Clark	0	0
	Jackson	26	520,000
	Rockcastle	6	113,000
Louisiana	Rapides	40	436,000
Maine	York	11	77,000
Michigan	Delta	68	1,135,000
	Marquette	2	33,000
	Iron	61	1,105,000
	Goegbic	98	1,787,000
	Houghton	55	1,002,000
	Newaygo	20	339,000
	Muskegon	2	40,000
	Wexford	17	291,000
	Schoolcraft	46	772,000
Minnesota	Cass	101	1,891,000
	Itasca	123	2,294,000
	St. Louis	167	3,973,000
Mississippi	Hinds	0	0
	Harrison	10	179,000
	Washington	0	0
Missouri	Iron	24	393,000
	Madison	11	179,000
	St. Francois	1	16,000
	St. Genevieve	3	41,000
	Washington	19	308,000
	Phelps	12	192,000
	Ripley	23	378,000
	Butler	12	188,000
	Carter	22	357,000
	Shannon	22	353,000
	Dent	16	264,000
	Greene	0	0
Montana	Flathead	138	4,500,000
	Lincoln	304	11,950,000
	Silver Bow	21	920,000

<u>State</u>	<u>County</u>	<u>Miles</u>	<u>Cost</u>
North Carolina	Buncombe	83	4,767,000
	Henderson	37	1,818,000
Ohio	Athens	4	70,000
	Hocking	10	168,000
	Jackson	0.2	3,000
	Scioto	2	37,000
	Vinton	1	17,000
	Lawrence	20	331,000
	Perry	8	137,000
	Morgan	1	20,000
	Washington	5	84,000
Oklahoma	Le Flore	51	1,682,000
Oregon	Multnomah	34	1,156,000
	Clackamas	341	11,559,000
	Douglas	662	22,425,000
	Coos	55	1,849,000
Pennsylvania	Elk	39	650,000
	Forest	56	1,057,000
	Warren	44	1,233,000
Tennessee	Greene	9	329,000
	Carter	17	427,000
	Sullivan	19	953,000
	Washington	6	209,000
Texas	Angelina	27	482,000
Utah	Utah	272	4,331,000
Virginia	Lee	7	130,000
	Wise	0	0
	Bland	9	183,000
	Dickenson	0	0
	Montgomery	0	0
	Pulaski	4	104,000
	Roanoke	0	0
	Scott	7	132,000
	Tazewell	4	77,000
	Washington	0	0
	Wythe	0	0
	Alleghany	46	834,000
	Bath	66	1,122,000

<u>State</u>	<u>County</u>	<u>Miles</u>	<u>Cost</u>
Washington	Skagit	182	6,115,000
	Whatcom	154	5,155,000
	Grays Harbor	118	3,943,000
	Clallam	1	34,000
	Jefferson	77	2,572,000
	Yakima	113	3,795,000
	Pierce	62	2,080,000
	Lewis	266	8,927,000
	Chelan	396	13,294,000
	Douglas	0	0
	Stevens	37	1,550,000
	Pend Oreille	76	3,100,000
West Virginia	Greenbrier	15	364,000
	Randolph	161	2,573,000
Wisconsin	Price	66	1,208,000
	Oneida	4	84,000
	Florence	38	716,000
Puerto Rico	Puerto Rico	30	2,000
TOTAL		7,797	\$ 220,134,000

Excerpts from National Park Service Letter 1/

"As a result of that meeting and further discussion between you and Mr. Bayliss we are submitting herewith the enclosed program of road and trail projects in National Parks and Parkways within or contiguous to distressed areas as shown on the Area Redevelopment Map of November 13, 1961. Based upon figures compiled a year ago, this program totals over two hundred million dollars and represents all future road and trail work which has not already been financed through the 1963 fiscal year. At that time it represented approximately 52 percent of the total road work currently left to be accomplished within the National Park System, and included everything proposed as a part of MISSION 66 and subsequent years.

"We have listed the various parks and parkways by States and have included the list of counties for each area, although we have not been able to break down the amount of work by counties since that information is not available to us."

"Our experience has been that we have never been able to provide sufficient facilities to accomodate all the potential visitors to the National Parks. We would estimate that the accomplishment of the work outlined in the enclosed program would increase the capacity of the existing parks and provide road facilities in newly authorized parks to the extent that we could accommodate about 122 million visitors when these facilities are completed as compared to the 78 million visitors now accomodated."

"Of course all of this work could not be placed under construction in a very short space of time. The present authorizations for National Park Roads and Trails and National Parkways work total \$34,000,000 annually. At that level it would require about six years to complete financing of the above-mentioned program (\$200,000,000), and about eleven years to complete all construction (\$381,000,000). We estimate that this work could be accelerated so that the benefits of this construction and the long range realization of increased tourist potentials throughout the National Park System areas that are included in the distressed areas would be accomplished in about half that time."

1/ Letter to Mr. Kraft, ARA, from Mr. A. Clark Stratton, Assistant Director, NPS, dated April 5, 1962.

BUREAU OF PUBLIC ROADS
ESTIMATED FOREST HIGHWAY IMPROVEMENTS
FOR REDEVELOPMENT AND LABOR SURPLUS AREAS
1962 - 1970

<u>State and Forest</u>	<u>Estimated Cost</u>	<u>Mileage</u>	<u>County</u>
Alabama			
Talledega	\$ 2,901,000	119	Montgomery
Talledega	5,408,000	175	Calhoun, Talledega
Bankhead	<u>2,641,000</u>	<u>137</u>	Jefferson, Franklin
Total	\$ 10,950,000	431	
Annual apportionment of Forest highway funds \$ 94,496			
Alaska			
Chugach	<u>\$ 33,815,000</u>	<u>231</u>	Anchorage Area
Total	\$ 33,815,000	231	
Annual apportionment \$ 2,876,474			
California			
Stanislaus, Tuolumne	\$ 8,840,000	26	Stanislaus
Mendocino	3,665,000	47	Glen
Angeles, Los Padres	146,302,000	267	Los Angeles
Eldorado	57,948,000	168	Eldorado
San Bernardino	50,653,000	170	San Bernardino and
			Riverside
Six Rivers, Cleveland	<u>28,022,000</u>	<u>156</u>	Humboldt, Orange
Total	\$295,430,000	834	
Annual apportionment \$ 4,726,004			
Colorado			
San Isabel	<u>\$ 627,000</u>	<u>19</u>	Pueblo
Total	\$ 627,000	19	
Annual apportionment \$ 2,369,837			
Florida			
Apalachicola	<u>\$ 2,257,000</u>	<u>51</u>	Franklin
Total	\$ 2,257,000	51	
Annual apportionment \$ 191,697			

<u>State and Forest</u>	<u>Estimated Cost</u>	<u>Mileage</u>	<u>County</u>
Georgia			
Chattahoochee	\$ 530,000	17	Habersham
Total	\$ 530,000	17	
			Annual apportionment \$ 116,261
Idaho			
St. Joe	\$ 1,850,000	18	Latah
Total	\$ 1,850,000	18	
			Annual apportionment \$ 3,359,886
Illinois			
Shawnee	\$ 25,930,000	498	Saline, Alexander, Williamson, Gallatin, Pope, Union, Massac, Pulaski, Jackson, Hardin, and Johnson
Total	\$ 25,930,000	498	
			Annual apportionment \$ 38,033
Indiana			
Hoosier	\$ 10,073,000	163	Lawrence
Total	\$ 10,073,000	163	
			Annual apportionment \$ 22,121
Kentucky			
Cumberland	\$ 27,607,000	495	Laurel, Rowan, Whitley, Clark, Jackson, & Rockcastle
Total	\$ 27,607,000	495	
			Annual apportionment \$ 67,835
Louisiana			
Kisatchie	\$ 258,000	4	Rapids
Total	\$ 258,000	4	
			Annual apportionment \$ 76,147

<u>State and Forest</u>	<u>Estimated Cost</u>	<u>Mileage</u>	<u>County</u>
Michigan			
Hiawatha	\$ 26,168,000	188	Delta, Marquette, and Schoolcraft
Mainstee	42,903,000	533	Newaygo, Muskegon, and Wexford
Ottawa	20,696,000	379	Iron, Gogebic, and Houghton
	<hr/>	<hr/>	
Total	\$ 89,767,000	1,100	

Annual apportionment \$ 354,108

Minnesota			
Chippewa	Improvements will progress		Cass, Itasca
Superior	satisfactorily under normal		St. Louis
	appropriations.		
			Annual apportionment \$ 456,357

Mississippi			
Desoto	\$ 4,162,000	86	Harrison and Washington
	<hr/>	<hr/>	
Total	\$ 4,162,000	86	
			Annual apportionment \$ 155,671

Missouri			
Clark	\$ 7,550,000	264	Iron, Madison, St. Francois, Ste. Genevieve, Carter, Ripley, Shannon, Butler, Washington, Dent, and Phelps
Mark Twain	<hr/> 720,000	<hr/> 19	Phelps
	<hr/>	<hr/>	
Total	\$ 8,270,000	283	
			Annual apportionment \$ 168,659

Montana			
Flathead	\$ 12,058,000	127	Flathead
Kootenai, Kanitan	15,508,000	162	Lincoln
Deerlodge	<hr/> 6,877,000	<hr/> 86	Silver Bow
	<hr/>	<hr/>	
Total	\$ 34,443,000	375	
			Annual apportionment \$ 2,630,481

<u>State and Forest</u>	<u>Estimated Cost</u>	<u>Mileage</u>	<u>County</u>
North Carolina Pisgah	\$ 5,422,000	108	Buncombe and Henderson
Total	\$ 5,422,000	108	
		Annual apportionment	\$ 203,316
Ohio Wayne	\$132,982,000	1,021	Athens, Hocking, Jackson, Scioto, Vinton, Lawrence, Perry, Morgan, and Washington
Total	\$132,982,000	1,021	
		Annual apportionment	\$ 18,072
Oklahoma Quachita	\$ 560,000	27	Leflore
Total	\$ 560,000	27	
		Annual apportionment	\$ 22,759
Oregon Suislaw, Siskiyou Umpqua, Rogue River, and Willamette Mt. Hood	\$ 31,947,000 14,582,000 8,188,000	132 115 79	Coos Douglas Multnomah, Clackmas
Total	\$ 54,717,000	326	
		Annual apportionment	\$ 4,545,904
Pennsylvania Allegheny	\$ 18,867,000	207	Forest, Warren
Total	\$ 18,867,000	207	
		Annual apportionment	\$ 88,074
Tennessee Cherokee	\$ 7,472,000	120	Carter, Sullivan, Washington, & Green
Total	\$ 7,472,000	120	
		Annual apportionment	\$ 110,622

<u>State and Forest</u>	<u>Estimated Cost</u>	<u>Mileage</u>	<u>County</u>
Texas			
Angelina	\$ 918,000	59	Angelina
Total	\$ 918,000	59	
			Annual apportionment \$ 104,462
Utah			
Unita	\$ 1,085,000	16	Utah
Total	\$ 1,085,000	16	
			Annual apportionment \$ 1,095,914
Virginia			
Jefferson	\$114,793,000	1,461	Lee, Wise, Bland, Dickerson, Montgomery, Pulaski, Roanoke, Scott, Washington, and Wythe
George Washington	21,282,000	437	Alleghany, Bath
Total	\$136,075,000	1,898	
			Annual apportionment \$ 214,589
Washington			
Mt. Baker	\$ 9,233,000	69	Skagit
Olympic	3,076,000	35	Grays Harbor, Clallam, & Jefferson
Snoqualmie	9,378,000	68	Yakima, Pierce
Colville	2,043,000	49	Stevens, Pend Oreille
G. Pinchot	2,487,000	21	Lewis
Okanogan	1,368,000	22	Chelan
Wenatchee	4,593,000	39	Chelan
Total	\$ 32,178,000	303	
			Annual apportionment \$ 2,293,608
West Virginia			
Monongahela	\$ 46,705,000	931	Greenbrier, Randolph
George Washington	1,331,000	13	Greenbrier
Total	\$ 48,036,000	944	
			Annual apportionment \$ 130,226

<u>State and Forest</u>	<u>Estimated Cost</u>	<u>Mileage</u>	<u>County</u>
Wisconsin			
Chequamegon	\$ 474,000	37	Price
Nicolet	<u>446,000</u>	<u>28</u>	Florence, Oneida
Total	\$ 920,000	65	
		Annual apportionment	\$ 184,545
Puerto Rico			
Caribbean	<u>\$ 1,037,000</u>	<u>6</u>	Puerto Rico
Total	\$ 1,037,000	6	
		Annual apportionment	\$ 9,307
Grand Total	\$986,238,000		

DEPARTMENT OF THE INTERIOR
BUREAU OF INDIAN AFFAIRS

Road Construction Program

Thousands of Dollars

<u>STATE</u>	<u>RESERVATION</u>	<u>PRESENT ANNUAL PROGRAM</u>	<u>TOTAL ROAD COST NEEDS</u>
Arizona	Colorado River Agency	220	3,212
	Fort Apache Agency	200	2,671
	Hopi Agency	455	6,774
	Papago Agency	100	4,111
	Pima Agency	195	4,595
	San Carlos Agency	450	5,992
	Navajo Agency	2,368	27,036
	Phoenix Area Office	70	1,224
TOTAL ARIZONA		4,058	55,615
California	California Agency	170	3,256
	Fort Yuma Reservation	0	661
	Hoopla Area Field Office	281	3,500
	Riverside Area Field Office	0	1,182
	Sacramento Area Office	39	629
TOTAL CALIFORNIA		490	9,228
Colorado	Consolidated Ute Agency	51	3,146
Florida	Seminole Agency	80	1,034
Idaho	Fort Hall Agency	185	3,144
	Northern Idaho Agency	0	1,438
TOTAL IDAHO		185	4,582
Kansas	Haskell Institute	80	200
Minnesota	Minnesota Agency	300	3,357
	Minneapolis Area Office	12	179
TOTAL MINNESOTA		312	3,536
Mississippi	Choctaw Agency	53	613

<u>STATE</u>	<u>RESERVATION</u>	<u>PRESENT ANNUAL PROGRAM</u>	<u>TOTAL ROAD COST NEEDS</u>
Montana	Blackfeet Agency	165	2,436
	Crow Agency	120	1,426
	Flathead Agency	40	1,221
	Fort Belknap Consolidated Agency	195	2,132
	Fort Peck Agency	49	1,739
	Northern Cheyenne Agency	74	936
	Billings Area Office	65	748
TOTAL MONTANA		708	10,638
Nebraska	Winnebago Agency	62	698
Nevada	Nevada Agency	300	5,283
New Mexico	Consolidated Ute Agency	0	448
	Jicarilla Agency	595	5,190
	Mescalero Agency	0	3,868
	United Pueblos Agency	410	13,180
	Zuni Agency	0	3,273
	Navajo Agency	0	8,461
	Gallup Area Office	476	3,179
TOTAL NEW MEXICO		1,481	37,599
North Carolina	Cherokee Agency	80	1,282
North Dakota	Fort Berthold Agency	5	2,169
	Standing Rock Agency (Sioux County)	0	1,169
	Turtle Mountain Con- solidated Agency	260	2,303
	Wahpeton School	0	50
TOTAL NORTH DAKOTA		265	5,691
Oklahoma	Five Civilized Tribes Agency	337	5,421
	Chilocco School	0	60
	Cheyenne & Arapaho Area Field Office	90	1,841
	Kiowa Area Field Office	85	5,151
	Pawnee Area Field Office	0	1,418
	Shawnee Area Field Office	85	1,418
	Anadarko Area Office	50	578
	Muskogee Area Office	20	308
TOTAL OKLAHOMA		667	16,195

<u>STATE</u>	<u>RESERVATION</u>	<u>PRESENT ANNUAL PROGRAM</u>	<u>TOTAL ROAD COST NEEDS</u>
Oregon	Umatilla Agency	102	1,117
	Warm Springs Agency	186	3,845
	Portland Area Office	72	1,223
TOTAL OREGON		360	6,185
South Dakota	Cheyenne River Agency	265	3,698
	Pierre Agency	95	2,238
	Pine Ridge Agency	255	7,378
	Rosebud Agency	335	2,981
	Sisseton Agency	38	1,187
	Standing Rock Agency (Carson County)	270	1,897
	Aberdeen Area Office	125	1,700
TOTAL SOUTH DAKOTA		1,383	21,079
	Intermountain School	0	81
	Navajo Agency	0	700
	Uintah and Ouray Agency	220	3,708
TOTAL UTAH		220	4,489
Washington	Colville Agency	425	6,979
	Western Washington Agency	168	2,815
	Yakima Agency	262	4,623
TOTAL WASHINGTON		855	14,417
Wisconsin	Great Lakes Agency	178	2,113
Wyoming	Wind River Agency	92	2,492
Washington, D. C.	Central Office	440	1,168
TOTAL ROAD CONSTRUCTION		12,000	207,283

Excerpts from Bureau of Land Management Letter 1/

"As a result of the March 20 meeting, we are submitting the enclosed program for road construction in the Bureau of Land Management (Attachment A). It should be recognized that our road program covers work to be accomplished in only 10 western states and Alaska. Based upon road requirements to permit proper resource management, the recent compilation indicates that the long range road construction program will amount to approximately one billion one hundred million dollars. Current planning proposes to accomplish approximately 14 percent of the overall total during the next ten years, which amounts to \$164 million, the remaining portion of the program to be completed during the next thirty years. It will be noted that we have not been able to break down the amounts on a county basis since that information is not now available to us. Most of the work would, however, draw labor from and thereby assist those counties which are now in surplus labor areas, or prevent additional surplus labor areas. It should be borne in mind that the above costs include all forms of road construction such as design, grading, drainage, surfacing, culverts, and bridges."

"All of the contemplated construction could not be accomplished in a short period of time. The current proposal for authorization for road construction, using Federal-Aid Highway funds for FY 1964, is only \$2 million. Funds for road construction are currently in our normal activity construction appropriations and run well under a million dollars each year. We propose a gradual increase in future years which will permit this Bureau to fulfill our roadway building program for the purpose of enhancing our resource management responsibilities in accord with our plan to spend \$164 million in the first 10-year period."

1/ Letter to Mr. Kraft, ARA, from C. E. Remington, Acting Assistant Director, Operating Services, Bureau of Land Management, dated May 2, 1962.

Road Construction in the Bureau of Land Management

	<u>Total</u> <u>in first 10 years</u>	<u>Total</u> <u>in 40 years</u>
Alaska	\$ 26,600,000	\$ 200,000,000
Arizona	6,412,000	43,930,000
California	11,541,000	79,142,000
Colorado	14,572,000	99,910,000
Idaho	11,674,000	80,065,000
Montana	13,691,000	93,935,000
Nevada	22,367,000	153,448,000
New Mexico	7,713,000	52,860,000
Oregon	13,158,000	90,238,000
Utah	21,049,000	144,400,000
Wyoming	<u>15,223,000</u>	<u>104,455,000</u>
	\$164,000,000	\$1,142,383,000

USCOMM:DC



Minnesota Historical Society

Copyright in this digital version belongs to the Minnesota Historical Society and its content may not be copied without the copyright holder's express written permission. Users may print, download, link to, or email content, however, for individual use.

To request permission for commercial or educational use, please contact the Minnesota Historical Society.



www.mnhs.org