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Four Questions by a Student of Economics

Address by

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I am very pleased to join this audience in honoring the graduating class of The University of Akron. Some of you receiving a degree today will continue with your formal education; others will embark on business or professional careers. But whatever your plans for the future, our Nation's economic and political condition will inevitably remain a matter of concern to you.

Recently, I received a letter from a college student named Rebecca who posed several blunt questions concerning our Nation's economy. First, Rebecca asked, "What was the biggest economic setback this year?" Second, "What has been the biggest economic boost this year?" Third, "What plans are being made to get the U.S. out of the red?" Fourth, "What can we as citizens of the U.S. do to help the economic situation?"

These are thoughtful questions, and they are not easy to answer with confidence or precision. But they undoubtedly express the concerns of many of our citizens, and I want to take advantage of this occasion to share with you my attempt to answer Rebecca's earnest inquiry.

Turning to the first question, the list of candidates for the greatest economic disappointment of 1975 is regrettably quite long. During the past year, we experienced a severe recession. The physical output of our national economy declined sharply before recovery got under way. The unemployment rate rose to levels not seen in a long generation. Inflation continued at a disconcerting pace. The deficit in the Federal Government's budget exploded. Interest rates on municipal securities soared. And efforts to move our Nation towards independence in the field of energy made little progress.

While all these developments have been disappointing, the persistence of inflation at a time of such widespread unemployment of labor and of capital harbors the most troublesome implications for our Nation's future. True, the advance of the general price level moderated significantly during the first half of 1975. More recently, however, the upward climb of prices has begun to accelerate again. Since mid-year, wholesale prices have been rising at an annual rate of a little over 10 per cent. Price markups in various depressed industries -- such as aluminum, steel, and autos -- convey a clear warning that our long-range problem of inflation is unsolved.

By now, many Americans are well aware of the profoundly disruptive consequences of inflation for our country. The inflation from which we continue to suffer got under way more than ten years ago and eventually became a dominant feature of our economic life. As wage and price increases quickened, seeds of trouble were sown across the economy. Rapidly rising prices eroded the purchasing power of workers' incomes and savings. Speculative fever mounted. The construction of new homes, condominiums, and office buildings proceeded on a scale that far exceeded the underlying demand. Managerial practices of business enterprises became lax and productivity languished. Corporate profits -- properly reckoned -- kept falling. And as businessmen reacted to fears of shortages and still higher prices, inventories of raw materials and other supplies piled up.

It is these basic maladjustments that led to the recent economic decline -- the deepest since World War II. This slump has entailed enormous human and financial costs, and we have as yet only partly recovered from it. The behavior of prices in recent months is therefore very worrisome. Not only are the incomes and savings of our people still being eroded, but revival of

confidence in the economic future is being hampered by fears of a fresh outburst of double-digit inflation. If such a development occurred, it would ultimately plunge us into an economic recession even more serious than the one we have just experienced.

I therefore believe that control of inflation requires a higher priority in managing our economic policies than it is as yet receiving. We cannot expect inflation to be brought under control if the Federal Government continues to run huge budget deficits or to permit money and credit to expand unduly. We must also face up to the hard truth that competition has become less intense in many of our private markets. If an unemployment rate of 8 or 9 per cent is insufficient to bring inflation to a halt, then our economic system is no longer working as we once supposed. In the future, governmental efforts to achieve economic progress will need to encompass structural reforms as well as responsible monetary and fiscal policies.

Let me turn next to Rebecca's question concerning the most beneficial economic development this year. Once again, there is no shortage of plausible candidates. The recovery in business activity since the spring has been quite vigorous.

Indeed, the rise during the third quarter in the physical volume of our national output was the largest in many a year. Since March the number of people employed has risen by 1-1/2 million. The recovery in stock prices since the beginning of the year has been heartening to investors. The decline in interest rates from the extraordinary heights of 1974 has brought a measure of relief to business borrowers and home buyers. And the turnaround in our foreign trade from a deep deficit to a large surplus has helped to make the dollar once again a highly respected currency around the world.

These recent shifts of economic fortune deserve, and they are in fact receiving, much attention. But another and less widely noticed development -- namely, rediscovery of the need for prudence in the conduct of financial affairs -- is likely to prove of greater and more lasting benefit to the American people.

During the past year, we have seen the consequences of more than a decade of neglect of the principles of sound finance. Some major business corporations and many smaller ones have fallen into bankruptcy. A number of real estate investment trusts and some airlines are in serious trouble. Many individuals have lost their life's savings by making careless investments.

Not a few of our Nation's commercial banks face the possibility of large losses on dubious loans. And various State and local government units are now finding it difficult, if not impossible, to raise new money through our financial markets.

More than any other single event, the agony of New York City has made the consequences of financial mismanagement apparent to the entire nation. A Federal budget deficit in the neighborhood of 90 billion dollars, which is in prospect for this fiscal year, may stagger the imagination; but few of our citizens can grasp its impact on their daily lives. Everyone, however, can relate to what has been happening in New York City -- with thousands of municipal workers being dismissed, the number of policemen and garbage collectors dwindling, the subway fare going up, taxes rising, interest on outstanding municipal securities being scaled down, pension benefits being readjusted, and free tuition in the city's colleges placed in jeopardy.

Our country has been divided on the issue of whether, or under what conditions, Federal financial assistance to New York City is justified. But those who favor Federal assistance, as well as those who are opposed, agree on this much: that what happened to New York must not happen in our community or in our state. New York's dramatic encounter with bankruptcy

may therefore mark a major turning point in the management of fiscal affairs in our country -- certainly at the local and State level, and perhaps at the Federal level as well.

State and local governments are now busy reexamining their financial condition. Many of them are cutting back on postponable or avoidable expenditures, and raising taxes as needed. Proposals for bond issues are being appraised by the citizenry with a more critical eye. And recognition is growing across the country that the New York City crisis is just one manifestation of the lax financial practices that spread through the business, financial, and governmental sectors over the past ten to twelve years.

Fortunately, these unsound practices are now being corrected in our business firms and banks, as well as by State and local governments. This curative process is not without some pain. Capital for risky ventures is harder to obtain nowadays and it is also more costly. But this return to standards of prudent financial management has been an essential step in rebuilding the foundation for a durable prosperity.

I now come to Rebecca's third question: What plans are there for ending the persistent stream of Federal budget

deficits? This concern with the need to restore order in our national fiscal affairs is shared, I believe, by the great majority of our people. To be sure, the swelling of the deficit this year reflects the deep recession of economic activity -- which reduced Federal revenues, besides increasing outlays for unemployment benefits, welfare payments, and related programs. But the Federal deficit was large even before the recession started; it has continued year after year, in both good times and bad; and it has largely resulted from inadequate attention to the consequences of excessive governmental spending.

Of late, there have been some encouraging changes in the Federal budgetary process. A major reform of Congressional procedures was set in motion by the Congressional Budget Act of 1974. In the past, revenue decisions by the Congress were separated from its spending decisions, and the latter were handled in piecemeal fashion. The result was that budgets just happened; they were not planned. Under the new Budget Act, Congress must assign priorities to the various outlays and set an over-all limit on spending in relation to expected revenues. Hence, Congressional decisions on expenditures will in the future be integrated with decisions on revenues. The discipline

imposed by these new procedures offers hope, I believe, of reducing the chronic bias toward deficits in the Federal budget.

So, too, does the initiative of the President in recommending that Federal expenditures be cut next fiscal year by \$28 billion below the level that they would otherwise reach. The basic principle underlying this expenditure proposal is sound, and I hope Congress will support it.

Once we put an end to the rapid upward spiral of Federal spending, budget deficits are likely to run smaller or vanish entirely. When the government no longer pours more money into the economy than it withdraws in tax revenues, it will have removed the single most important cause of inflation in our times. Moreover, when the government no longer absorbs so large a portion of private incomes, private capital investment will tend to increase more rapidly. Improved productivity, lower product prices, and a higher standard of living will therefore be fostered.

Let me now turn to Rebecca's final and most challenging question: What can we as citizens do to help the economic situation? This question is so difficult because our economic situation has numerous dimensions -- the level of production, the extent of

unemployment, the level of prices, the distribution of incomes, the profitability of investment, the state of the environment, and so on. Improvement in any one of these respects need not be accompanied by improvement in others. The question is also difficult because what any one of us can do depends on his personal situation -- whether we work at home or in a business, whether we are farmers or miners, journalists or scientists. Moreover, as you well know, even experienced economists who have similar social objectives frequently disagree on what can or should be done to improve economic conditions.

Nevertheless, there are some principles of life that all of us can observe with the conviction that we will be helping our Nation's economic situation.

First of all, we can curb any latent discontent or cynicism we may feel about the motives of our fellow citizens in business or government. Americans, by and large, are a moral people who have wrought economic miracles by seeking to improve themselves, their families, and their communities. We have demonstrated across the years that hope is perhaps the most powerful of all economic forces, and that a spirit of

purpose can give meaning to human energy and overcome a lack of material resources.

Second, everyone of us can surely improve his understanding of economic phenomena. Education is a never-ending process. The intellectual excitement of the classroom need not be lost, and should not be lost, as we move on in life. The economic problems of today are profoundly challenging, and there will surely be new ones tomorrow. As citizens we need to strive for dependable knowledge of economic realities, so that we can make wiser decisions in the marketplace and in the voting booth.

Third, we can become more actively involved in the political process of our Nation -- by electing officials at all levels of government who demonstrate a serious and informed awareness of our economic problems, by communicating our thoughts on public issues to our representatives with the clarity of conviction, and by holding them responsible for their actions.

Fourth, we can avoid the temptation to implore the Federal Government to solve every economic and social problem through the expenditure of public funds. We are a compassionate people, and I trust we will remain so. It is understandable that

we attempt to muster our collective resources to aid the less fortunate among us. Yet we must take great care not to weaken the spirit of self-reliance that has been instrumental in releasing the creative and productive energies of the American people.

Fifth, we can impose discipline on our business enterprises through our daily decisions in the marketplace. The power of the consumer to force business firms to price competitively and to improve their products must never be underestimated. We as consumers can help to keep the spirit of price competition alive by shopping carefully and avoiding impulse buying.

Finally, every American can experience the satisfaction that comes from honest effort -- by putting in a full day's work for a full day's pay, whether it be work in a factory, a scientific laboratory, a corporate office, a governmental agency, or wherever one may labor. "Sweet is the sleep of a laborer," so sang Ecclesiastes. Centuries later, Carlyle reminded us that "there is a perennial nobleness . . . in work," that indeed "a man perfects himself by working." The rewards of work accrue, of course, to the public at large as well as to the laborer; for the more we produce by the day or by the hour, the more surely will the standard of living of the American people improve.

The needs of the American economy today are large and compelling. Some of you graduates will approach these needs as liberals, others as conservatives. Some of you doubtless believe in free enterprise, others may aspire to a welfare state, still others may seek the nationalization of our industries. But whatever your philosophic or political attitudes may be, I hope you will recognize that your dreams of a good society have no chance of fulfillment unless our government conducts its financial affairs responsibly. This condition is essential to bringing an end to the inflation that has been raising havoc with our economic institutions; it is essential to the restoration of a lasting prosperity; it is essential also to the preservation of our democratic system.

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