TREASURY DEPARTMENT
Washington

STATEMENT BY TREASURY SECRETARY ROBERT B. ANDERSON
BEFORE THE JOINT ECONOMIC COMMITTEE, TUESDAY,
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Experience in the 1950's demonstrated the immense resiliency, strength, and adaptability of our free enterprise economy. As we enter the decade of the 1960's, the economic outlook is indeed encouraging. But we should not permit a favorable outlook to lull us into unwarranted complacency. The challenge that confronts us -- not solely in Government, but every individual, group, and institution in this country as well -- is to conduct our affairs in such manner as to prolong the prosperity that we are now enjoying.

Our budget projection of the economy for 1960 reflects this favorable outlook. It is always difficult, of course, to make specific assumptions covering a budget which extends over the next 18 months. Our best judgment is, however, that a gross national product of $510 billion can be reasonably projected for the calendar year 1960, compared with a $479 billion total for the calendar year 1959. Our projection of personal income for this calendar year is $402 billion, as compared with $380 billion in 1959. Our projection of corporate profits of $51 billion in this year compares with a $48 billion figure for the calendar year which has just been completed. All of these estimates are stated in terms of present price levels. We believe these estimates represent a realistic appraisal of the current outlook and fully support our projection of $84 billion of Federal Government revenue for the fiscal year 1961.

We must make certain that the growth we experience this year -- and in the decade as a whole -- is growth at a sustainable pace, unwarped by the distortions, imbalances, and excesses that, if allowed to emerge, inevitably sow the seeds of reaction and recession. This need for balanced growth emphasizes the necessity for combatting any incipient build-up of inflationary pressures.

Inflation -- either in the form of a gradual, insidious rise in the price level, or as a rapid increase of costs and prices -- is in fact the enemy of sustainable growth. Inflation breeds the very recessions and unemployment that stand as a barrier to sustained growth. And either the fear or the fact of inflation, by impairing the will to save in traditional, fixed-dollar forms, will in the long run lead to a shortage of savings to finance the real investment in plant and equipment that is so essential to the growth process.

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The fact that inflation, if allowed to occur, can be expected to stunt our rate of growth in the future provides sufficient reason for determined efforts to prevent further erosion in the purchasing power of the dollar. We must also be continuously mindful of the impact of inflation on various groups in the economy, particularly those people whose incomes are relatively fixed, who live on the proceeds of pensions, annuities, social security, and similar types of savings.

Beyond these considerations is the important fact that further inflation can only impede our efforts to reduce the deficit in our international balance of payments -- a deficit which threatens to hamper our efforts to contribute as we should to the military security and economic strength of the free world. Our attack on this problem will continue to be consistent with our vital goal of promoting multilateral world trade. It will, in short, be directed -- not toward protectionism and restriction -- but toward liberalization and expansion of world commerce. We shall continue to search out appropriate ways of encouraging American exports of goods and services; to press for removal of discriminatory restrictions on dollar imports abroad; and to encourage other industrial countries to participate more adequately in the provision of capital to under-developed countries.

It would be an empty achievement, indeed, if we were apparently successful in these efforts, only to find that internal inflation in this country had impaired our competitiveness in foreign markets. Thus, international developments provide still another important reason for maintaining stability in the price level as we pursue our goals relating to growth and employment.

Inflation was held largely in check in 1959. Although consumer prices -- reflecting a continued uptrend in prices of all major groups except food -- rose by a small amount during the year, the wholesale price index actually declined slightly. While this performance was good, and is a cause for satisfaction, it is no cause for relaxation of our efforts to protect the purchasing power of the dollar.

In an economy so large and highly diversified, the causes of inflation are bound to be complex, and it follows that there is no single, simple cure. We know, for example, that inflationary pressures are fostered by waste and inefficiency, whether these occur with respect to business management, labor practices, individual actions, or the activities of government. A rise in certain types of costs of production faster than increases in productivity can also contribute to inflationary pressures. In addition, undue concentration of market power may permit certain industries to raise prices in the face of declining demands, and shifts of demand from one type of goods and services to another may also exert a net inflationary impact. The nature of some of these forces is not yet fully understood; further study and evaluation are necessary before policies to deal with them can be formulated.

But of one thing we can be certain: the over-all relationship between the demand for and supply of total output is still basic to any meaningful attempt at inflation control. Consequently, unless we are especially diligent in our efforts to prevent an unsustainable upsurge in economic activity during a period of expansion, we almost surely must resign ourselves to the price increases that result from such excesses. Moreover, as pointed out earlier, unsustainable upsurges tend to be followed by corrective recessions and consequent unemployment of labor and other resources.

Federal financial policies -- including Government actions with respect to the budget, monetary management, and public debt operations -- are generally recognized as having a significant impact on total demand for goods and services in the economy. As a result, the constructive use of these policies must stand in the forefront of our efforts to fight inflation, as well as our efforts to combat recessionary tendencies. We must recognize that, while such policies alone cannot assure success in our efforts to attain sustainable economic growth, their utilization in a prudent and responsible manner is essential.

Opinions differ as to how these three policies should be used, and this is especially true with respect to budget policy. According to one view, a period of actual or threatening inflation, reflecting at least in part the pressures of demand, would call for a large surplus in the Federal budget. This would be achieved by an increase in tax rates, a cut in expenditures, or some combination of the two. Such a surplus, it is argued, would help dampen total demand inasmuch as Government spending would fall short of revenues.

This program would, according to this view, be consciously and actively reversed during a recession. Reductions in tax rates and increases in expenditures would contribute to a large deficit in the budget; such a deficit would stimulate total demand, inasmuch as Government spending would exceed revenues.

This approach has some serious shortcomings in practice. For one thing, decisions as to taxes and spending programs often reflect many factors other than broad economic considerations. Moreover, the timely use of budget policy as a conscious countercyclical weapon is hampered by the fact that authority over taxation and spending is the joint responsibility of the Executive and the Congress and is not centered in one branch of the Government.

In addition, experience since the end of the Second World War indicates that it is much easier to achieve a budget deficit in a recession than a surplus in a period of economic expansion. Sizable deficits in recessions -- only partially offset by modest surpluses in periods of expansion -- tend to complicate the task of achieving sustainable growth in at least two ways. The net deficit over a period of years probably adds to inflationary pressures and secondly, the growth in the public debt that is implied by such deficits, along with the difficulties encountered in managing a growing debt, is likely to complicate the flexible and timely administration of monetary policy.

Moreover, recent experience supports the view that conscious and active attempts to vary tax rates and spending to help avoid inflation and combat recession may well have perverse effects. Changes in tax rates and spending may sometimes take so long to plan, legislate, and put into effect that many months may pass from the time the need for a change in budget position becomes clear until the change actually affects total spending in the economy. By the time the actions become effective, the economy may have changed radically. As a consequence, large deficits may have their major impact during periods of rising business activity; surpluses may in fact be encountered during a business slump. Any proposals for an arrangement that would permit some sort of administrative variation in tax rates to counter cyclical trends, such as vesting additional authority in the Executive Branch, do not seem to be consistent with the system of checks and balances that is so important in our form of government.

Are we thus left only with the alternative of striving for a rigorous balance in the budget, year in and year out? I do not think that we are. The goal of a net surplus in the budget -- not only in prosperous periods but, on the average, over a longer period of time also -- is highly desirable. Furthermore, budget deficits of moderate size are probably unavoidable -- and indeed, desirable -- during periods of economic recession.

We should, in my opinion, follow some variation of the stabilizing budget proposal, in which budget policy, year in and year out, would be geared to the attainment of a surplus under conditions of strong economic activity and relatively complete use of labor and other resources. On this basis, the automatic decline in revenues and increase in expenditures during a recession -- reflecting in part the operation of the so-called "built-in stabilizers" -- would generate a moderate budget deficit. In prosperous periods, tax receipts would automatically rise and certain types of spending would contract, producing a budget surplus.

Over a period of a complete business cycle, a surplus for debt retirement would be achieved, but without the disrupting effects of necessarily attempting to balance the budget in recession. While intentional variations in tax rates and spending for cyclical purposes would thus be kept to a minimum, conditions might well arise in which such variations would be desirable.

The budget submitted by the President for fiscal year 1961 is fully consistent with this approach; about 5 percent of Federal revenues are earmarked as a surplus for debt retirement. If economic conditions were to change drastically and recession were to set in -- a contingency which does not seem likely but is of course possible -- the surplus would automatically be converted into a moderate deficit as tax revenues decreased and certain types of expenditures rose.

With the economy operating at high and rising levels of activity, the achievement of a $4.2 billion surplus in the Federal budget will help reduce the burden on monetary policy and will also facilitate debt management. In my judgment, the lack of adequate surpluses in the prosperous years following the Second World War -- which has resulted in a more than $30 billion increase in the public debt since the end of 1946 -- has meant that monetary policy has been called upon to bear more than its proper share of the burden in promoting sustainable economic growth. This unavoidably heavy reliance on monetary policy may have contributed to wider swings in interest rates and capital values than would have been necessary if budgetary surpluses had been adequate. But it seems incorrect to argue that monetary policy has tried to assume too large a role; the conclusion is rather that the degree of monetary restraint has had to be greater than would have been the case if budgetary surpluses had been adequate.

To some observers, Treasury debt management -- the third Federal financial policy -- affords a highly useful technique for promoting sustainable economic growth. Although the Treasury attempts to manage the public debt in a manner consistent with the attainment of our basic economic goals and, insofar as possible, tries actively to promote these objectives, the vigorous use of debt management in this fashion is sometimes impeded by important practical considerations. Inasmuch as these difficulties have been described in detail in the material supplied by the Treasury to this Committee in connection with its recently completed study of employment, growth, and price levels, I shall not discuss them at this time.

During a period of strong business activity, however, the Treasury should at least possess sufficient flexibility in debt management to be able to avoid debt operations that actively promote inflationary pressures. Otherwise, the beneficial effects of prudent budget and monetary policies may in part be offset. In particular, reliance on inflationary short-term financing should be minimized, and a reasonable amount of long-term securities should be marketed, either through cash issues or in advance refunding of outstanding securities.

Under today's market conditions, however, the 4-1/4 percent interest rate ceiling on new issues of Treasury bonds effectively prevents the Treasury from issuing any significant amount of new marketable securities of more than five years' maturity, either for cash or in exchange for securities at maturity or in advance of maturity. The Treasury is thus prevented from achieving any meaningful amount of debt lengthening -- or even of holding the average maturity of the debt close to its present length of only 4 years and 3 months. The interest rate ceiling is therefore forcing the Treasury to pursue inflationary debt management policies.

To the extent the Treasury concentrates its new issues in the four to five year maturity range, the decrease in the average maturity of the debt can be slowed, but there is a limit to the amount of securities of this maturity that can be sold without driving interest rates in this sector of the market to very high levels. Moreover, experience has indicated that undue concentration of new cash issues in the four to five year range, at the rates the Treasury would have to pay, might have a strong impact on the capital market -- and particularly the mortgage market -- as individuals withdraw funds from savings institutions to purchase the Treasury issues.

The restriction on interest rates that the Treasury can pay on new marketable bonds is in effect preventing the effective and proper use of Federal financial policies to promote sustainable economic growth. It would be regrettable indeed, if the salutary effects of prudent budget and monetary policies were permitted to be offset in part by so artificial a restriction. The President has once again urged removal of this harmful restriction, and it is to be hoped that early action in this respect will be taken, so that debt management can also bear its proper share of the burden in our efforts to achieve our vital economic goals.

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