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Statement by

Arthur F. Burns

Chairman, Board of Governors of the Federal Reserve System

before the

Senate Budget Committee

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It is a pleasure to meet with this Committee as it undertakes its momentous responsibilities under the Congressional Budget Act of 1974. In recent years, Federal spending has risen swiftly, deficits have become chronic, and the public debt has mounted. Our present grave problem of inflation stems from many causes, and inadequate fiscal discipline is prominent among them. You and your congeners in the House of Representatives therefore face a great challenge, but you also have a unique opportunity to reestablish order in our nation's finances.

The budget that the President recommends to Congress at the beginning of each session is the product of a systematic process aiming to establish an overall limit on outlays in relation to expected revenues, and to determine priorities within the totality of outlays. This process, as you know, has hitherto had no counterpart in the Congress. Instead, Congressional decisions that determine the ultimate shape of the budget have been taken by acting separately -- or at times by taking no action -- on a hundred or more entirely independent measures. It is only after separate votes are cast on housing, education, defense, welfare, and whatnot that we put the pieces together and discover what kind of a budget has emerged.

Thus, year after year, members of Congress have been voting for or against larger benefits to veterans, for or against better schools, for or against cleaner air, and for or against a host of other good things that government can help to provide. But the Congress has not had the opportunity to vote on what total outlays should be, or whether an appropriation for a particular purpose is needed badly enough to raise taxes or to make offsetting reductions in other appropriations.

This fragmented Congressional consideration of the elements that make up the budget has contributed materially to the almost uninterrupted succession of budget deficits. Since 1960, we have had a deficit in every fiscal year except 1969. True, some of these deficits occurred because of efforts to use the Federal budget as a means of stimulating a lagging economy, but for the most part we have allowed deficits to happen without plan or purpose. Machinery for putting effective ceilings on expenditures, and for establishing priorities among alternative uses of Federal revenues, has simply not been available.

By passing the Budget Act of 1974, the Congress has established a framework for exercising this much needed control,

and has also indicated its firm resolve to do so. The Budget Act is a milestone in the reassertion of Congressional authority and self-discipline. There is now real hope that we can avoid the massive increases of Federal expenditure and the persistent deficits that have plagued us in the past.

The immense importance of your Committee's new responsibilities may perhaps be more fully appreciated by reflecting on what has happened to the Federal budget over the long sweep of our nation's history. Total expenditures did not reach the \$100 billion level until fiscal 1962, or nearly 200 years after the founding of the republic. By fiscal 1971, nine years later, Federal spending had risen another \$100 billion and thus passed the \$200 billion mark. In the budget as now projected, the \$300 billion mark will be passed this fiscal year. Clearly, the pace of Federal spending has been accelerating rapidly, and a pause for taking stock of where we are is overdue.

One result of the sharply rising curve of expenditures is that government has been assuming an ever larger role in the economic life of our people. In 1929, Federal expenditures accounted for less than 3 per cent of the dollar value of our total national output, and expenditures at all levels of government --

Federal, state, and local -- amounted to about 10 per cent of the national product. By 1950, the share of national output absorbed by government had risen to 23 per cent. Since that time, governmental involvement in the economy has increased further; last year, Federal expenditures alone accounted for 22 per cent of our national output, and the combined expenditures of all governmental units for 35 per cent.

A significant increase over the past four decades in the role of government in economic life was inevitable. A growing population, and the increasing complexity of modern urban life, gave rise to new and expanded governmental activities. This was also a period in which the United States came to occupy a position of leadership in international political affairs and in world economic development.

Some part of the rapid upward trend of Federal spending, however, is attributable to widespread acceptance of the theory that social and economic problems can generally be solved by quick and large expenditure of governmental monies. We have tried to meet the need for better schooling of the young, for upgrading the skills of the labor force, for expanding the production of low-income housing, for improving the nation's health, for

ending urban blight, for purifying our water and air, and for other national objectives, by constantly excogitating new programs and getting the Treasury to finance them on a liberal scale before they have been tested.

The result has been a piling up of one social program on another, so that they now literally number in the hundreds and practically defy understanding. Not a little of our taxpayers' money is being spent on activities of slight value, or on laudable activities that are conducted ineffectively.

Another result of the rapid growth of Federal spending has been a larger tax burden borne by our citizens, and a blunting of economic incentives. Business capital investment in recent years has certainly been inadequate for a nation that is eager for rapid improvement in the general welfare. There is thus reason to believe that governmental spending and taxing may have gone beyond prudent limits.

Where the line should be drawn between governmental and private use of resources is, in the final analysis, a matter of judgment and of social values. However this question is resolved, it should be clear to everyone that Federal spending, whatever its level, needs to be financed on a sound basis.

Deficit financing by the Federal Government can be justified at a time of substantial unemployment, but it becomes a source of instability when it occurs during a period of high economic activity, such as we have experienced in recent years. The huge Federal deficits of the past decade added enormously to aggregate demand for goods and services, but they added little to our capacity to produce. They have thus been directly responsible for a substantial part of our present inflationary problem.

The current inflation began in the middle 1960's when our government embarked on a highly expansive fiscal policy. Large tax reductions occurred in 1964 and the first half of 1965, and they were immediately followed by an explosion of Federal spending. New and substantial tax reductions followed in 1969 and 1971, and so too have massive increases of expenditures. In the last five fiscal years, that is, from 1970 through 1974, the public debt -- including obligations of the Federal credit agencies -- has risen by more than \$100 billion, a larger increase than in the previous 24 years.

In the fiscal year just concluded, the condition of the Federal budget failed to improve sufficiently. True, the reported budget deficit declined to about \$3-1/2 billion -- a

much smaller deficit than in the three preceding years. But in a year of such powerful inflationary forces, the Federal budget should have been in surplus. Moreover, when off-budget outlays and the expenditures of governmentally-sponsored agencies are taken into account, as I believe they should be, the total Federal deficit reached \$21 billion last year, which is not much lower than the extraordinary deficits of the three previous fiscal years.

The financing of these huge Federal deficits has contributed powerfully to the upward pressure on interest rates and the tension in financial markets, which have been so troublesome of late. The disturbing effect of Federal borrowing on the flow of funds was illustrated dramatically earlier this month, when the Treasury went to the market to refinance some maturing debt obligations. Long lines of people formed at the doors of the Treasury and the Federal Reserve Banks to bid for the new securities offered by the Treasury. Half of the total of \$4.4 billion sought by the government was obtained through non-competitive bids -- that is, from relatively small investors. A large share of these funds undoubtedly came out of deposit accounts, and thus further reduced the ability of our financial

institutions -- particularly savings banks and savings and loan associations -- to support homebuilding activities.

Despite such concrete evidence, it is sometimes contended that the Federal deficits of recent years have been only a minor source of economic or financial instability, since the amounts are small relative to total borrowing by the private sector. This is a faulty argument. To be sure, the rate of private credit expansion has substantially exceeded the rate of Federal borrowing. But we must never confuse the power or responsibility of private citizens with the power or responsibility of government. Business firms and consumers have no way of acting in concert to prevent an inflationary expansion of credit, and their private responsibilities may conflict with national objectives. The basic responsibility for economic stabilization lies with the Federal Government. Unless our government exercises that function better than it has in the past, there will be little hope for restoration of stability in the general price level.

The central purpose of the Congress, besides providing for the nation's security, is to help find the way to a better life for the American people -- among other things, reasonably full

employment, a widely shared prosperity, and a stable purchasing power of their currency. None of these objectives will be achieved over any length of time without far stricter fiscal discipline than we have exercised in recent years. That is why your Committee, together with the Budget Committee of the House, has such a great and unique opportunity to serve the nation's welfare.

I recognize that you have a good deal of preparatory work to do before you can begin exercising fully your responsibilities under the Congressional Budget Act of 1974. The importance of this preparatory effort should not be underestimated. A highly competent and thoroughly objective staff will need to be assembled to carry out the functions of the Congressional Budget Office. Good working relations will need to be established between your Committee and the House Budget Committee and between both committees and the Office of Management and Budget. Procedures will have to be worked out for implementing the intricate steps in the budgetary process set forth in the Budget Act. Some flexibility is needed in Congressional management of our enormously complex Federal budget, and the Budget Act properly provides opportunity for waiver of procedures and deadline requirements. But unless

the Congress undertakes its new responsibility with a firm determination to reserve the waiver privilege for unusual circumstances, the Budget Act may turn out to be a well-meaning but illusory gesture.

Full implementation of the new budgetary procedures, I understand, will begin in fiscal 1977 -- or two years from now. We dare not wait two years, however, for the additional fiscal restraint that is so urgently needed in the present inflationary environment. Strenuous efforts should be made immediately to pare budget expenditures in fiscal 1975 and to balance the budget in fiscal 1976.

I recognize that this Committee is not yet in a good position to recommend to the Congress where expenditure cuts would be most appropriate. Nevertheless, in view of the special responsibility that has been assigned to you by the leadership of the Senate, you can justly use your good offices to press for restraint on Federal spending. This is the most important single step that can now be taken by the Executive and the Congress to curb inflationary pressures and to restore the confidence of our people in their own and the nation's economic future.

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