Address of the Secretary of the Treasury, to be Delivered before the Academy of Political Science, at the Hotel Astor, New York City, Wednesday Evening, November 10, 1937

I am glad to accept the invitation of the Academy of Political Science to discuss before its members assembled here tonight the subject of Federal spending and its relation to the balancing of the Federal budget.

Nineteen years ago tomorrow, we signed the Armistice ending the World War. That war was unbelievably costly in human values, and it was enormously costly in material values. In the two years between the middle of 1917 and the middle of 1919, the Federal Government spent thirty-one billion dollars and sustained a net deficit of twenty-two billion dollars.

During the past four years, this country has been engaged in another war. This time our enemy was a great economic disaster. In this war we bombed no cities; we machine-gunned no trenches; we killed no human beings. In this war, we fought with jobs and with dollars to save farmers from losing their farms; to save home owners from losing their homes; to give not only bread but work to the unemployed; to increase the security of jobs, property values, and business profits; to bring order out of chaos in our economic system.

This war, like that other war, required a many-sided campaign under intelligent and courageous leadership -- a leadership that was superbly supplied by President Roosevelt.

Finally, this war, like that other war, required a large spending program. This program, plus the special needs arising out of the great drought and the prepayment of the soldiers' bonus, necessitated outlays during the four years ended June 30, 1937, of some fourteen billion dollars in excess of our receipts.

We deliberately used an unbalanced Federal budget during the past four years to meet a great emergency. That policy has succeeded. The emergency that we faced in 1933 no longer exists.

I am fully aware that many of our problems remain unsolved. I am aware that there still remains a considerable volume of unemployment; that the speculative markets have recently been under severe pressure; and that certain of our business indexes have recently shown a declining tendency. I am further aware that some persons contend that another great spending program is desirable to ward off the risk of a serious business depression.

I claim no prophetic insight into the future. But, after giving serious and careful consideration to all these and other factors, I have reached the firm conviction that the domestic problems which face us today are essentially different from those which faced us four years ago. Many measures are required for their solution. One of these measures in the present juncture is a balanced budget.

Early in 1933, after three years of progressive deterioration, our whole economic mechanism was demoralized. Under these conditions, there was no agency outside of the Federal Government with the resources and the courage to bring about a business revival.

Today the situation is greatly changed. We are now nearing the end of one of the most active years in the business history of this country. On the whole, this high level of activity has been of a healthy character -- not of the character that usually marks an unhealthy boom and precedes a serious depression. The present situation is not characterized by the existence of huge inventories, high interest rates, over-extended credit positions, or great surpluses of housing accommodations,capital equipment, et cetera. We have not reached the stage of full employment of our productive resources. On the contrary, from all these standpoints, conditions are favorable for a continued increase in the level of business activity.

This situation stands in sharp contrast to the banking collapse, the bread lines, the bankruptcies, and the general demoralization of 1933. It also stands in contrast to the unhealthy excesses of 1929.

The basic need today is to foster the application of the driving force of private capital to the existing favorable circumstances. We want to see capital go into the productive channels of private industry. We want to see private business expand. We believe that the bulk of the remaining unemployment will disappear as private capital funds are increasingly employed in productive enterprises. We believe that one of the most important ways of achieving these ends at this time is to balance the Federal budget.

In this connection, I should like to point out that the underlying technical conditions that made deficit spending the wisest kind of economic policy during the depression no longer exist. Thus, when we borrowed during the depression to finance our deficit spending, a large part of the funds was obtained through an expansion of bank credit. To this extent, our spending did not absorb capital funds that might otherwise have gone into private industry, nor did it absorb taxpayers' funds that might otherwise have gone into private consumption. Even to the extent that our bonds and notes were purchased by non-banking investors, the effect was largely to put to work capital funds that would otherwise have remained idle.

A different situation prevails today. Our industrial recovery has created large new demands for private capital. Our commercial banks are again utilizing their credit resources for the financing of private industry. During the first six months of the present calendar year, the insured commercial banks of the country reduced their holdings of Government securities by six hundred eighty-five million dollars in order to meet actual and prospective demands for commercial credit. The obligations that they sold, plus an amount equal to the securities newly marketed by the Treasury, were purchased by investors. Any deficit spending that takes place under these conditions must be financed in large part by capital funds that would otherwise be available for business purposes.

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Despite the substantial increase in the public debt during the past four years, the credit of the Federal Government has remained absolutely unimpaired. Not once during even the darkest days of the depression did the Treasury experience the slightest difficulty in borrowing all the funds that were required. Moreover, the rates of interest on our borrowings have been lower, for comparable securities, than at any other time in the history of the country.

We wish to preserve the financial power of the Federal Government to aid in restoring economic order in the future, if the need again arises. To preserve this power, we must liquidate during prosperity the debts incurred during periods of depression.

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I turn now to the immediate practical aspects of budget balancing for the coming fiscal year. What are the controlling figures?

Our total receipts for this year are estimated at about six billion six hundred millions, and our total net expenditures at about seven billion three hundred millions, leaving a net deficit of roughly seven hundred millions.

To seek an ordinary balancing of the budget next year -- that is, a balance after full provision for accruing liabilities for old-age benefit payments, but exclusive of debt retirement --, we must therefore accomplish a net improvement of seven hundred million dollars in our budgetary position. In estimating revenues, it is better to underestimate than to overestimate. We should not <u>count</u> on an increase in revenues next year from the existing tax structure, nor should we impose additional taxation. Instead, we should plan to bring next year's expenditures within this year's income; and then, if the tax receipts rise above those of this year, the excess should be used to reduce the national debt.

Let us stop at this point to consider the revenue side of the picture.

The Federal tax system affects every one in the country. We in the Treasury are constantly studying the tax problem with two objectives always before us: First, that the tax burden shall be distributed as fairly as possible and, second, that the collection of taxes shall be as little burdensome to the taxpayer as possible.

It is with these aims that, by direction of the President, we have been reviewing the whole tax structure in the last few months and are just now in the process of presenting to a committee of Congress the information we have collected. The study has not been directed toward raising new revenue. Rather we have sought to determine whether there are inequalities and injustices in the distribution of the tax burden and whether there are some taxes whose cost of collection and whose burdensome effect outweigh the revenue gain. In addition, we want to simplify collection and make the taxpayer's record-keeping less difficult.

In making this study, we have invited the assistance and the advice of groups of taxpayers and of individuals. We want to hear the taxpayer's side of the story. We want all the facts we can get and we have obtained both facts and opinions.

Our tax revenues come largely from individual earnings and business profits. We do not wish to impose levies which tend to dry up the sources of tax revenue. The laws should be so written and administered that the taxpayer can continue to make a reasonable profit with a minimum of interference from his own Federal Government. Of course, tax policy cannot be determined from one individual case alone. We must look at the whole picture. We must take testimony and we must examine actual tax records and returns.

We realize that our tax laws are too complicated; we want to make them less so. We realize that there are inequities; we want to eliminate as many of them as we can.

The amount of our income-tax revenue is only about half our total internal revenue. Less than three million people out of our total population pay income taxes. We would be applying the principle of capacity to pay more justly if we were to reduce the number of consumer taxes and at the same time to increase the number of income tax payers. Taxpayers who are squarely confronted with their own tax burdens are bound to be keenly alive to the way the money is being spent by their Government.

The budget now nearing completion is predicated on a definite estimate of receipts, based on the existing tax structure. It is a cardinal point that the tax system, as revised, must not yield a smaller return for 1939 than the present system would yield.

We want to adjust inequalities and remedy defects in the tax laws. In doing this, we have sought the help of the taxpayer and have given him a sympathetic hearing. If we find that the operation of any particular tax is unfair, we stand ready to say so publicly.

Our immediate goal, then, should be to reduce expenditures by seven hundred million dollars. In addition, every dollar that the Treasury realizes from the liquidation of revolving funds, and from other repayments of loans and capital advances, should be set aside for debt retirement. In no event, in my opinion, should we contemplate total net expenditures in excess of the level of this year's estimated receipts. That means that our expenditures must not exceed six billion six hundred fifty million dollars for the coming year.

Our problem is clear. Our expenditures must be cut seven hundred million dollars.

But where can cuts totaling this amount be made? After careful study of the whole problem, I have come to the following conclusions: On the one hand, little or no money can be saved in the regular operating expenses of the

Federal Government, including the national defense and interest on the public debt. Further, our expenditures under the Social Security Act will probably increase by a hundred million dollars or more in the next fiscal year.

On the other hand, by focusing attention on the several classes of expenditures that have been mainly responsible for our past deficits -- public highways, public works, unemployment relief, and agriculture -- I am convinced that the necessary savings can be made.

Let me give you a rough idea of the possible savings in these fields.

First, take the item of highway expenditures. Prior to the depression, the Federal grants to the States for public highway construction regularly ran under one hundred million dollars annually. This year the total Federal outlays for highways, inclusive of emergency expenditures, are estimated at two hundred fifty-three millions; and, in addition, the existing highway programs call for new appropriations totaling more than four hundred million dollars for the next two years. I believe it is now time to return to the average annual level of highway expenditures that existed prior to the depression.

Second, there is the field of public works, other than highways, on which we are spending five hundred seventy-three millions this year. This is a greater sum than was spent for this purpose during the entire five-year period between 1926 and 1930, inclusive. Next year, despite the fact that available unspent appropriations for this purpose already exceed six hundred millions, I believe that we can and should move definitely toward a lower level of public works outlays.

Third, it should be possible to make a further substantial reduction in our outlays for unemployment relief and the C.C.C. camps. During the present fiscal year, by reason of business recovery, these expenditures are already being reduced by some seven hundred eighty millions below last year's.

I turn next to our expenditures on behalf of agriculture. The plight of agriculture in the depression called for emergency aid, not only in the farmers' interest, but in the interest of all of us. As many of you know, I have been deeply concerned for more than twenty years with the problems of agriculture, and I am most keenly interested in doing all that can be done to remove the economic disadvantages that the farmers have suffered. That very interest impels me to believe and to state with all the force at my command that agriculture cannot continue to rely on merely temporary expedients.

Besides the one hundred sixteen millions included in this year's budget for the general work of the Department of Agriculture, there are, among other items, estimated expenditures of four hundred seventy-five millions for the soil conservation program, thirty-three millions for rural electrification, fifty-five millions for the Federal land banks to provide lower interest rates, one hundred millions for commodity loans, and one hundred twenty-five millions for resettlement. These items total nine hundred three millions for this fiscal year.

Despite the magnitude of the sums we are now expending for agricultural purposes, you are all aware that discussion is taking place in Congressional committees of further measures in aid of agriculture that may involve large additional expenditures.

I am strongly in favor of a long-range program to maintain the independence and the purchasing power of the farmer. That program cannot endure and cannot render lasting aid to the farmer unless it be soundly based. The farmer himself does not want subsidies, but rather such fair prices and such balanced production of crops as will make subsidies unnecessary for his decent economic status.

A sound program must take into consideration the farmer's opportunities in the foreign markets, as well as in those at home; and the character and cost of that program must be determined with full recognition of its effects upon our whole national economy and of the limitations imposed by the Federal finances.

Balancing the budget is in the interest of our agricultural as well as of other parts of our population; and it requires the cooperation of the farmer as well as other sections of the public.

With the solid support of the public, I believe that economies totaling seven hundred millions or more can be achieved in the four fields that I have cited. Since the estimated increased costs of our social security program are more than offset by estimated reductions in miscellaneous and supplemental items, it should be possible to achieve an ordinary balancing of the budget next year.

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There may be some persons who would counsel a more drastic reduction of expenditures or a program of far heavier taxation in order to make certain a substantial reduction in the public debt in the next fiscal year. There are serious objections to such a course.

We are definitely in a transition period between unbalanced and balanced Federal budgets. We are making great progress toward a balanced budget.

Relatively few persons realize the remarkable fact that the net improvement this year in the budgetary position of the Federal Government will amount to more than two billion dollars. In other words, the net deficit this year is estimated at less than seven hundred millions as compared with more than twenty-seven hundred millions last year.

This net improvement of more than two billion dollars that is taking place in a single year provides the best answer to those who have publicly despaired of our willingness or our ability to balance the Federal budget.

I firmly believe that there is just as much danger to our economy as a whole in moving too rapidly in this direction as there would be in not moving at all.

The minimum goal that I propose will by no means be easy to achieve.

I have already indicated my belief that it would be unwise to raise taxes at this time solely to accumulate a surplus for debt retirement. More than two-thirds of this year's budgetary improvement comes from increased revenue, rather than from reductions in expenditures.

There are equally compelling considerations on the expenditure side. I strongly favor a vigorous program for the progressive reduction of Federal expenditures to the minimum demanded by the Government's increased responsibilities. But it would be clearly unwise, and disruptive to many sections of private industry, if we were suddenly to slash Government expenditures by more than the amount I have indicated.

In addition to these considerations, there is a new and important aspect of our budget that must now be considered in analyzing the economic effects of Federal expenditures and receipts. The Social Security Act has introduced new items into our budget. A major one of these, the annual appropriation for the Old-Age Reserve Account, calls for the investment of this appropriation in Government obligations. The same Act also provides for the investment in Government obligations of moneys paid by the States into the Unemployment Trust Fund.

The funds paid into both of these accounts operate just like payments made by an individual to a private insurance company. Such a company invests your premiums in Government obligations, in farm and urban mortgages, in railroad, industrial, and public utility bonds, and in other forms of investment approved by one or more of the forty-eight different State laws. All that the insurance company has when it has invested your premiums in this manner, are bundles of pieces of paper representing all kinds of promises to repay your money with interest to the insurance company.

The Federal Government, in connection with the Old-Age Reserve Account and the Unemployment Trust Fund, also invests your money in pieces of paper. But these pieces of paper are Government bonds and not private promises to pay. It is not overstating the case to say that your money is safer in Government bonds than in a multiplicity of private obligations, though, of course, I am in no way reflecting on the soundness of private insurance companies.

It is very clear that the credit of the Government is the soundest in the Nation. And if anything should happen to your Government, nothing else would have any value at all.

Now, when the Treasury invests your old-age taxes and your unemployment compensation taxes in Government bonds, it reduces the amount of the public debt held by private investors. This is obviously so if the Treasury buys bonds in the market directly for the accounts. However, the rates of interest which the Treasury is required by law to pay on funds invested for these accounts are higher than those which can be obtained by purchasing suitable Government obligations in the open market. Hence, the Treasury is issuing special Government bonds to these accounts, and is using the funds so obtained to reduce the amount of its obligations sold to or held by private investors.

Next year, as a result of the Social Security Act and the related State laws, it is estimated that the Federal Treasury will receive more than one billion dollars net for investment in Government obligations for these two accounts. With a balanced budget, this billion dollars will be used to retire public debt now in the hands of private investors. In other words, the Treasury next year will be adding one billion dollars to the supply of funds in the capital market.

Even during the decade of the Twenties, when the Treasury was receiving large payments of interest and principal on war debts, and from the sale of surplus war materials, the maximum reduction made in any single year in the public debt held by private investors was one billion three hundred millions.

My object this evening has been to present, as clearly and as frankly as I know how, a comprehensive picture of Federal expenditures and the budgetary outlook. I have tried to make plain the underlying economic reasons, as well as the humanitarian ones, for the past deficits; and I have tried to bring out clearly the underlying economic considerations that now demand a balanced Federal budget. I have shown why, in my opinion, this balance should be sought by a reduction of seven hundred million dollars in expenditures, and why a large surplus for debt retirement would be undesirable at this time if it must be achieved by eliminating essential Federal services or by increasing the existing tax burden.

The principal aims of our budgetary policy have been, and I hope will continue to be, to promote a large volume and healthy character of business activity, a maximum volume of employment at good wages in private industry, fair treatment for our agricultural population, adequate revenues to meet the increased services now demanded of the Federal Government, and the preservation of the credit and currency of the United States, on which depends the security of jobs, property values, and orderly business relations.