For use in afternoon papers
August 21, 1975

ECONOMIC POLICY -- SOME THOUGHTS ON THE LONG AND SHORT OF IT

Remarks of

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Gulf Shores, Alabama

August 21, 1975

ECONOMIC POLICY -- SOME THOUGHTS ON THE LONG AND SHORT OF IT

Very often, the conventional phrases we use in everyday language are shorthand for a substantial body of wisdom. An example, which we have borrowed from the French, is: "The more things change, the more they are the same." Another, borrowed from Italian, is: "Don't give me advice, I already know how to make mistakes." An example of our own devising is: "You can't take it with you." Borrowed or home grown, such examples could go on almost endlessly. They are expressions that bridge depths profound enough for philosophical enquiry. They represent long slow accretions of wisdom learned directly from everyday living where, over the generations, experience averages out to truth.

I have not undertaken this little excursion into linguistics without design, for there is another everyday saying that I want to take as my theme today. It is: "That's the long and short of it."

We end many of our discussions with that little phrase. Or we begin many discussions with it, in slightly different form. It is a conventional prologue or coda to our views that we use without much thought. Nevertheless there is behind it a simple truth learned through ages of experience. That truth is: In nearly every experience, or problem, or circumstance -- however you prefer to characterize it -- there is a short term situation, and a long-term unfolding of consequences to our handling of that situation.

I have chosen this as my theme in talking to you today because you, as investors for retirement, have a strong community of interest with the Federal Reserve. You -- as we at the Fed -- must keep your eye fixed on the long term consequences of your actions. And yet you -- like the Fed -- are required to take constant action in the present, in the light of and partly in response to short term situations or problems. Neither of us can ever forget that what we do currently, to some extent transforms the future, makes the path to our long term goals harder, or, even impossible.

Before proceding further let me illustrate with my own short-term and long-term circumstances. The short of it is, that I am a very new member of the Federal Reserve Board. The long of it is that I have been inducted into a term of service that has $6\frac{1}{2}$ years to run. (By the way, I regard the fact that the President did me, and the Board, the honor of paying us a visit and saying some good words about the need for continued independence of the Federal Reserve as more than offsetting any untoward vibrations that might arise from the fact that I was inducted on Bastille Day.)

The short term of my present service on the Board would make any attempt by me to plunge now into the swift waters of monetary policy and related economic analysis and forecasting, or the intricacies of the regulation of banks and bank holding companies a demonstration of the fact that there is no such thing as an instant Federal Reserve expert. The long-term consequences could be obstacles to my future ability to communicate on those subjects. Thus, I have felt it to be the better part of wisdom today not to enter into the specifics of Federal Reserve policy concerns. I think there are substantial long-term benefits, at this juncture, in keeping my mind and attitudes open to new facts and conclusions.

Instead, I would urge you to read the testimony given to the House Banking, Currency and Housing Committee on July 24 by Chairman Burns. This testimony looks a year ahead, in terms of the desirable monetary goals as the Federal Open Market Committee currently sees them. More important -- to me, much more interesting, since so much can happen to upset current views of the future -- is the discussion, in this testimony, of the origins of the inflation we are suffering, how far back those origins reach, how widely they spread, and how necessary it is to break the spell in which inflation has transfixed us. I have arranged for Dr. Burns' text to be available to you, together with my remarks.

Let me add just one word to this personal aside. Even if I held very strong views on monetary policy at this point, I would hestitate to express them, or to express views about current Board policy I did not help make, without the benefit of my own experience on the Board sufficient to validate -- or alter -- my present thinking. Nevertheless there are some underlying views of the economy -- such as my thinking about inflation -- that I believe to be fundamental and that I will be expressing today.

The Short
Of It

One short-term change we are facing is the opportunity for dramatic alteration of financial technology. For centuries financial transactions were done by means of transferring funds using instructions on paper called a check or a draft. Today, we have the opportunity to change the means by which we transfer funds from an exchange of paper instruments to an exchange of electronically transmitted and recorded instructions. How you as investors, the Federal Reserve and other state and national regulators -- and the public -- react to this opportunity today will determine to a substantial degree the efficiency and the cost of future distribution and use of goods and services. It will likewise affect the way many of our people earn their livings, and it will open investment opportunities presently unknown. While you and I may have opinions about what decisions should be made currently in this area, the acceptance or not of electronic payment by the average family will in the long run make the decision for us.

Another ongoing stream of change is in the structure of our financial institutions. This will affect your decisions as to where to put your funds, how you can get the most out of your money, and what is best for the retiree who is your ultimate concern. Savings institutions are moving strongly to become more like banks. Many commercial banks, in turn, take the view that our thrift institutions have been given the right to pay somewhat higher ceiling interest rates on their funds, as well as other special operating benefits, as an inducement to the accumulation of savings to service the housing industry. In that way, the laudable ends of helping to upgrade the housing of the American public and to spread home ownership from the privileged to the many have been served. From this viewpoint, if savings institutions are now to gain the right to make all, or some substantial part, of their deposits available upon demand, either by checklike instruments or through electronic transfer, it is only fair to question the special advantages they have been given as a quid pro quo to induce them to specialize in housing finance.

The Federal Reserve stands at the confluence of both these streams of change in the world of finance -- technical and structural. It has pledged its cooperation with the Congress in working out the new rules and structural lines that will mold the future.

One other major element of short-term interest could have a long train of consequence in the future, although this by no means exhausts the subject. This other stream of change -- or proposed stream of change -- is related to the pressures I have already cited that may bring about the evolution, in the near future, of a financial system in which most institutions have more or less the same powers and functions.

With a considerable amount of change in that direction already in being, the Federal Reserve has recommended to the Congress that all depository institutions, member and nonmember, commercial bank and thrift, should be required to keep reserves on deposit with the Federal Reserve consonant with member bank reserves. Such a change in the law would increase equity among financial institutions. And, it would improve the Federal Reserve's ability to control the money supply by improving its ability to keep track of the increase or decrease of deposits of various kinds. I would think that investors would welcome this improvement in the efficiency of monetary policy.

The Long vs.
The Short Of It

These are only a few of the short-term considerations that will influence your long-term outlook and goals -- and ours. Another class of such short-term factors is one over which we have no control, but to which the Federal Reserve must react, whatever the effects of such reaction on achievement of such long-term goals as a prosperous economy, with capital and people at high employment, and with prices reasonably stable.

This class includes disparate events, each calling for a different type of central bank response, such as the Penn Central collapse, major bank failures, and the decisions of the Congress and of the Administration about Government spending. And it includes, finally, such cost increasing factors as the recent great price increase of oil, and of the long, steady rise in wages and prices persisting in both prosperity and recession.

In general, the short-term factors I have just mentioned increase costs that are not recouped in some other way, as, for instance, by increases in productivity, cheaper means for releasing energy, better informed business decisions, and the like.

Together they are a few of the more prominent factors in what I regard as the basic, fundamental and most consequential standoff of all between short and long-term influences on the economy: the short-term tendency toward inflation versus the long-term goal of a prosperous, high employment economy with general price stability.

I believe inflation is a root economic problem -- a problem underlying even such problems as unemployment, living standards, social peace and the productive uses of capital. Inflation, I believe, has the power to shape all these other basic concerns of economic policy.

I do not think we have real choices between inflation and unemployment, inflation and better living standards, inflation and economic justice toward the sick, the old, and the halt, the blind, the widowed or others who cannot produce, or inflation and social stability.

I do not think these are alternatives. I do think that inflation causes recession; that inflation causes unemployment; that inflation causes lowered standards of living, destroying the value of accumulated savings; and that inflation causes the injustice of failed welfare programs. And I believe that inflation causes crime, alienation of us one from the other and divisiveness in society. I say this because, in my view, so long as we have substantial inflation we will continue to have these other problems, even if other causes of them are removed.

I believe further that there is a gathering of public opinion that has been slow in making itself felt, but is a growing undercurrent in our society today. I think we are all learning that the notion that we could choose between recession and inflation is dead wrong; that in fact the only road to a high employment economy is the road of reasonable long-term price stability. This has been demonstrated to the public at large convincingly, I think, by the increasing tendency during recent recessions for inflation to co-exist with rising unemployment.

This, to me, is the critical issue of our economic life. It is a fact that each of us, and all of us together, must face squarely.

Please do not misunderstand. Neither I nor the Board is unaware of the anguishing problem of unemployment. Chairman Burns has suggested to the Congress that there should be a public employment program that would offer everyone a job, while inflation is unwound. I believe that is a wise proposal.

But if, over the long run, we all wish to be gainfully employed, to be at economic peace with one another, to provide opportunity for all to break out of the slough of poverty, to ensure real increases in our incomes, to make our savings a bulwark against the unknown instead of a gambling device, and to have the resources for just welfare programs, then we will all have to make peace with the iron law that, over time, we cannot consume more than we produce, as a nation.

This is to say that it is my view that reliable and lasting prosperity can rest only upon a "real" economy taking its gains out of its *per capita* increases in production.

I urge each of you to take an active role in spreading the word that we must give up the habit of short term expediency with our eyes closed to the long-term consequences. I think you could make no better investment for the future and for the state employees whose future you safeguard.

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