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of the

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Progress and Economic Stability

Last Sunday my young son and I were walking along the old Chesapeake and Ohio Canal near Washington and happened on a very talkative woman who had buttonholed a fisherman who was sitting on the bank minding his business. She said: "Aren't you ashamed of yourself? A big fellow like you might be better occupied than in catching poor little fish." The fisherman replied: "Maybe you are right, lady, but if this fish had had the sense to keep his mouth shut, he wouldn't be here." If I had had the sense to keep my mouth shut when your President buttonholed me, this banquet would have been much more enjoyable for all of us. But it is now too late for me and too early for you to be remorseful.

Washington is an exciting place these days to anyone concerned, as most of us are, with economic conditions and economic philosophies. Congressional committee hearings, held almost daily, are focusing the light of reason and fact on some of the most fundamental issues of our economic life. Along with the testimony of eminent economists and representatives of various private groups, have been statements by government officials setting forth their views on crucial issues. In addition, special investigations by high level committees and commissions are being launched.

You are familiar with many of the questions being raised: How can we insure ourselves against the losses and deprivations of unemployment? How can we grow faster? Could we grow faster if we broke up big business and big unions? Are they the cause of rising prices? Will acceptance of creeping inflation solve or complicate our problems? Is there excessive concern about the threat of inflation? Must the budget be balanced? Would the operation of the economy be improved if monetary policy were more subject to direction by the Executive and if the Federal Reserve were made less independent? Would the national interest be served better if the law required labor, consumer, and small business interests to be specially represented on the Board of Governors?

I do not propose to bore you with my answers to all these questions, but each of us must wonder at times what this ferment of economic ideas is all about. Is it the usual situation in Washington at this season or is this something different? It is hard to give a categorical answer. As I view it, the discussion this year is different and goes beyond preoccupation with the immediate economic situation. Even though there is obviously some special interest pleading and some "headline-thinking", there seems to be more provocative questioning of generally accepted doctrine, and more intense and imaginative effort to extend the horizons of economic understanding. In part this ferment may reflect a wider recognition of the Russian challenge to our economic way of life as well as to our leadership in other fields. In this sense the current probing and debate may reflect some hopes, not fully expressed, that we may, by persistent searching, make the kind of break-through and progress in the economic field which has become commonplace in the fields of rockets and atoms.

More importantly and more directly, however, these testimonies reflect the age-old conflict of unlimited human wants and aspirations confronted by limited means of satisfying them. These wants and aspirations take many forms, some material, some intangible, and some are inconsistent with others. We want more leisure and we also want the products of more work. We want rapid economic and technological growth but we do not want to postpone the satisfaction of our desires for current consumption. We want more freedom for ourselves but we do not always recognize that this may mean less freedom for the other fellow. We want more defense, more schools, better roads, cleaner rivers, more hospitals and more protection against the risks of unemployment in industry and of weather and markets in farming. Unfortunately, along with these things, which are usually provided by government, we want lower taxes and balanced budgets. We also want prices and living costs to hold still while wages and profits rise. And, of course, we want easy access to credit at low interest rates, and, at the same time, high returns on our savings, as well as safeguards against depreciation in their buying power.

All of these desires - and many more - are not only proper but laudable; in fact, they are the mainsprings of our type of economy. In a country as rich and dynamic as ours, a surprisingly large number of them can be realized if we take them a step at a time and with due recognition (1) that progress has never followed a smooth upward path in our society or in any form of society, and (2) that at each step we are confronted with the opportunity and necessity for making choices. These choices must be made not only among competing goals but also among the means by which common goals can be reached.

Unfortunately, or maybe fortunately, the testimony of the experts on the right choices to be made often points in opposite directions. For example, one well-known economist asserts that creeping inflation, while not desirable, is necessary, and a small price to pay for rapid progress in an economy in which labor unions are able to press their demands beyond the limits of productivity growth. Other equally eminent economists beseech us not to accept this prescription because creeping inflation must result in slower economic progress over the long run, and because the intangible cost of such inflation - its inequitable consequences - is unbearably high.

One witness contends that creeping inflation cannot be the answer to our problems because it tends to undermine the very cornerstone of our capitalistic democracy - the savings of the public. He thinks the real danger is that our people are beginning to expect creeping inflation and, in view of this, further inflation is inevitable unless the monopolistic powers of organized labor are controlled.

Another alleges that "administered prices" are the prime cause of inflation. But his opponents emphasize the importance of the numerous other forces contributing to inflationary pressures, including the strength of demand in the areas in which prices have tended to rise most.

Some of these experts in their certainty that their solution is the only correct one remind me of what my late father-in-law, a Baptist preacher, once said to my own Presbyterian minister: "There is no reason for bad blood between us. We are both doing the Lord's work - you in your way and I in His."

As one who is far less certain about the true economic gospel, I regard as highly desirable the ferment of ideas and the debates and inquiries going on about economic developments and policies, growth and stability, levels of unemployment, and the role of monetary policy. The conflicting testimony of the experts, while at times confusing, is also heartening. Differences need to be brought into the open and freely discussed. It is really only in this way that the public will become increasingly able to differentiate for itself the technical issues from the personal judgments and biases of individuals - whether they hail from Cleveland, New York City, Washington, or - like me - from our country's focal point, Broken Bow, Nebraska.

One might wish at times that the presentations of basic issues were more qualified or less blatant, that more precise information could be obtained, and that those wearing the mantle of objectivity were always truly objective. Also it might help if the issues were not so often overdrawn. But then issues do have to be stated clearly, and stands do have to be taken; when a firm stand is taken there is always the fear, I suppose, that qualifications may lead to other qualifications with the result that the issue will become confused or obscured.

It is well to bear in mind, too, that it is not only possible, but perhaps desirable, for "outside" experts and others not charged with policy responsibilities, to stimulate thinking by taking stronger positions than they might take if they were in the decision seat. The consequences would likely be quite different if such positions were taken - and acted upon - by persons charged with responsibility. In that case, the results might not be stimulative but disruptive.

This does not mean that those carrying policy responsibilities should remain silent. On the contrary, it is important that policy officials speak up clearly and let people know where they stand. I would like to do just that with respect to two points, but before doing so let me say, needlessly I am sure, that we in the System have no secret source of wisdom; we, too, must weave our way, taking account as best we can and as objectively as we can, of all the facts and informed judgments we can marshal.

First, let me deal with the complaint that the independent status of the Federal Reserve enables it to follow policies that are contrary to over-all government policy and with the result that economic growth is being impeded. A part of this complaint is that the System's independence is not truly democratic. This reflects some misunderstanding of the System's status.

As everyone knows, the Federal Reserve System is the creature of the Congress and can be changed by it at any time; indeed, changes are made from time to time. Consequently, the System is not independent _of_ government, but merely independent _within_ government. It does not function in isolation from the legislative or executive branches of government. Representatives of the Board testify frequently before Congressional committees, and at all levels and with great frequency we are consulting, working, advising, and cooperating with other agencies of government.

Congress created the System because it had been learned by hard experience in this country that money will not manage itself and must be regulated in the public interest. As an agent of the Congress, and with the members of the Board of Governors appointed for long and overlapping terms by the President with the advice and consent of the Senate, the Federal Reserve is the management mechanism that was designed to safeguard and promote the longer-run economic interests of the nation. As such it has functioned effectively, although by no means perfectly, over a very long period. Far from being undemocratic, the Federal Reserve represents a high degree of democratic maturity. It reflects recognition of the fact that in a twentieth century industrial democracy, all issues cannot be settled best at town meeting. Appropriately safeguarded delegation is essential to effective government.

Effective regulation of money and credit, as you know, is a complex and technical matter. It requires both continuity and flexibility. Often timing of actions is of the essence; frequently action must be taken before fiscal measures and other tools of economic policy can be brought to bear. In taking action, the System must be above suspicion of political influence or private pressure, and at the same time knowledgeable about both current and long-run economic and financial developments, here and abroad. It needs to be able to be heard above the clamor of day-to-day pressures. It will not be heard unless the country and the world have confidence in its technical competence and its economic statesmanship. Courage to face difficult and unpleasant issues and willingness to act promptly and decisively are important if such confidence is to be earned.

I seriously doubt a System headed up by a Board composed of members deliberately appointed to represent special interests - whether labor, consumers, small business or big business - would square with the requirements of an acceptable money-managing central bank. Each Federal Reserve official must represent the whole public interest - there must not be pulling and hauling between special interests. Benjamin Strong must have had this in mind when, as President of the Federal Reserve Bank of New York, he wrote to himself this reminder:

> "Never forget that...(the Federal Reserve System) was created to serve the employer and the working man, the producer and the consumer, the importer and the exporter, the creditor and the debtor; all in the interest of the country as a whole."

Now let me turn to a bird's-eye appraisal of the growth performance in this country, for a significant part of the ferment of the day bubbles around this point. It seems to me we hear a great deal about growth but not enough about progress. After all, it is not just rising indexes of economic activity that we are seeking. Progress is more than growth in total output; it relates to issues of quality of living, health, and equity. It must encompass freedom of inquiry, safeguarding of individual rights, freedom of choice of occupation and of decision to spend or save. It should include increasing scope for individual initiative and for innovation. These things, too, are measures of progress even though they are not readily encompassed in percentage rates of economic growth.

In my judgment a society organized, as ours is, on these principles will be able to <u>sustain</u> a more rapid rate of growth and progress than a society in which all economic decisions are subject to centralized direction and control, and in which the compulsive power of the state rather than the operation of free markets is the prime source of economic discipline.

Some experts have testified that our problem is chiefly a matter of a faster rate of productivity growth. They say that we must grow at an annual rate of 5 per cent, or some other per cent higher than we have been experiencing. They often go on to demonstrate, vividly, that if we grew at the higher rate Utopia would be just around the corner.

Except as indicating a widespread desire for rapid improvement in industrial capacity and levels of living standards, controversy about "target" rates of growth is not very helpful to those charged with policy determination. From where I sit it would appear that our goal should be to grow at the fastest rate that can be sustained, with full recognition of our other goals, including maximum freedom of choice for individuals, reasonably free markets for goods and services, stability of prices, and national security.

However, in a dynamic economy, growth will not always be at a uniform pace. Sometimes it will be slow, at other times very rapid. Variations in rates may reflect changing rates of growth in the population, or population of working age, needs for the economy to digest temporarily overexpanded plant or inventory, adjustments to crop failures, the tendency for innovations to come in bunches, adjustment to the changing intensity of foreign competition, and so on. It will never be possible in a free society to force and maintain a predetermined annual rate of economic growth.

Some critics have pointed to the annual growth rate from 1952 to 1958 to indicate a slackening pace of growth. The selection of this period gives a misleading idea of the postwar rate of growth because it takes us from near the peak of a cycle to a recession low. To get a proper perspective of "growth", one must not look only at changes from year to year or even from one cyclical peak to another, but rather at changes over longer periods.

In the six decades from the beginning of this century, a broad sweep of sixty years encompassing intervals of rapid growth and intervals of decline, real product in this country has increased at an average annual rate of about 3 per cent. During the entire postwar period, growth has been well above the long-term average, amounting to approximately 3-1/2 per cent.

This performance of the economy in the postwar period not only compares well with other expansion periods in this country, such as 1900-1913 or 1922-1929, but in fact has been amazingly good. We have had three recessions, but each has been moderate and fairly short lived. Recovery from the 1957-1958 decline has been rapid and has already brought total real product above pre-recession levels and into new high ground. There are many reasons to expect expansion in activity and employment to continue. Ours is still a growth economy and, typically, the high of each succeeding cyclical peak is well above the peak of the preceding cycle. Furthermore, the recovery has been firmly based on rapid growth in productivity. Rising productivity is, of course, the prime source of higher standards of living and a basis for hope that pressures on prices from the cost side can be avoided.

At the same time, we must not close our eyes to the fact that economic recovery and expansion to date have not solved some important problems. Unemployment, for example, although down more than seasonally, is still with us, and too much of it is concentrated among those who have been out of work a considerable period. Much of the recession increase in unemployment was centered, as you in Ohio know so well, in areas producing hard goods. An increase in spending for plant and equipment is now under way, consumer expenditures are expanding, and businesses are adding to inventory. This must result not only in increased orders and output, but also in increased employment, in these areas as well as others. Still the problem may not be fully solved and may call for further - perhaps different - public action.

However, serious as unemployment is to the nation and to those directly concerned, and it is a gravely serious problem for them, the longer-term problem of sustainable economic growth without inflation is also serious. The spreading inflationary psychology and the consequent speculative climate - as manifested, for example, in the stock market - are potentially very real threats to sustained growth in general economic activity as well as employment. Rapid short-run increases are of little help if they are followed by substantial declines resulting from over-enthusiastic appraisals of market demands, or too heavy reliance on population growth not yet here, or on assumptions that prices can only go up and never down. Moreover, sustainable growth, with expanding employment, cannot be based on reliance that government action or easy credit will validate imprudent commitments or unwise price or wage decisions.

Economic growth in real terms means increases in output and efficiency. These depend mainly on skillful management, imaginative leadership, responsibility, hard work, open-minded welcoming of innovation and change, ambition combined with ample natural resources, and constantly greater utilization of machinery and equipment. More money can be helpful and at times necessary to facilitate the functioning of these factors, but money alone cannot accomplish the job. Indeed, too much money, artificially induced, will disrupt, rather than facilitate, the efficient functioning of the economy, just as disastrously as will too little money.

Economic history, here and abroad, amply demonstrates that the pace of growth is closely dependent on the amount of investment the economy is willing and able to support. Savings are the primary source of investment funds. It is essential, therefore, that the economic climate be conducive to saving and wise investment. The erosion of accumulated savings through inflation and the widening temptation to seek inflation protection through speculative commitments in common stocks, real estate, and the like, endanger the very foundations of growth. There can be no conflict between stability and growth in this sense. We must have one to have the other.

It is on this premise that the present policy of the Federal Reserve is based. That policy is to so formulate and administer our decisions as to help create an environment that is conducive to stability of prices (and hence the soundness of the dollar), in order to maximize sustainable growth and genuine economic progress. We are not disposed to chart our course with the shortsighted view of disarming current criticism and possibly gaining a bit of popularity. Popularity should never be a goal of central bankers. Their only goal must be enhancement of the long-run economic welfare of the nation and all its people - including the generations to come.