

THE QUALITY OF DECISION-MAKING

(Remarks of C. Canby Balderston, Vice Chairman,
Board of Governors of the Federal Reserve System,
Before the Academy of Management Annual Meeting,
on Tuesday, December 29, 1959 at 2:00 p.m.)

Lest the subject of decision-making frighten you that you are going to hear a complete treatment of organization from Fred Taylor and Russell Robb through Lynn Urwick, Luther Gulick, Ordway Tead, to Herbert Simon, I hasten to delimit the scope of my discussion. It will focus upon the role of decision-making as a stabilizer or de-stabilizer of the economy. My excuse for imposing this thesis upon you is that no domestic problem of the moment seems as important as the discovery of how to achieve economic growth without inflation.

The problem is how to keep economic growth so orderly that industry and commerce can provide an increased number of jobs, as well as a greater volume and variety of goods and services, without violent disruptions. Steady, consistent progress calls for decisions of the best quality that business executives and union officers can make. Their decisions, if sound, will do much to lengthen the period of prosperity that the country is now enjoying. Dr. Riefler has remarked: "A business situation is no better than the quality of the decisions that businessmen make," and Chairman Martin has testified: "The state of the Nation tomorrow--its progress and prosperity--rests with the decisions of today."

To avoid traversing too much familiar ground, may I resort to a few dicta:

(1) Policy decisions reflect the main purposes it is hoped to achieve.

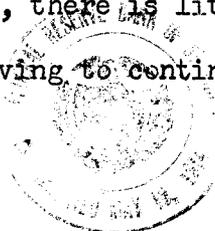
(2) A policy decision is not an island; each one is influenced by a stream of decisions that have preceded it; in turn, each will influence decisions of the future.

(3) Decision-making of high quality involves coordination, timing, balance and proportion.

(4) Decision-making is a crucial point in operating through an organization because it is the point at which action starts, and planning, if any, is converted into execution.

Naturally an executive does much besides make decisions. If he is a great executive, he will also sit and think, and perhaps wear a worried look on the faces of his assistants. But nothing done by him compares in importance with the process of deciding. The higher he is in the executive pyramid, the harder are the questions brought to him to be settled. In that moment of time when he signifies his decision by saying "yes" or "no," or by signing his name, he commits both himself and the forces at his disposal. If his decision is proven correct by subsequent events, his reputation gains luster; if incorrect, he will have pulled a "bloopers".

The art of decision-making is subject to influences within the business and without. They include psychological ones that have to do with people's attitudes and feelings as well as with their thinking. In addition, a modern executive needs an ever-increasing understanding of the complex world about him. International forces and national economic objectives permeate the decision-making process. As long as our citizens deal with general objectives, there is little dispute. Everyone wants the country's standard of living to continue to rise. Strong economic



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activity and adequate job opportunities are goals that all agree upon, and so sustainable growth without inflation is high among our accepted objectives. Freedom--political and economic--is an American hallmark. Peace is a world need, and for this, above all, we pray.

From these generally accepted goals, one may distill three significant economic ones:

- (1) To foster orderly economic growth and to sustain employment at the highest feasible level.
- (2) To protect the purchasing power of the monetary unit.
- (3) To keep international payments in balance.

Healthy growth of the economy will determine whether our nation can provide new jobs in the 1960's equal to twice those needed in the 1950's.

Protection of the purchasing power of the dollar is vital both to those who live on fixed incomes, and to an adequate rate of saving.

The remaining goal, external equilibrium, is one that American citizens are just coming to appreciate. It is related to the ability of our firms to remain competitive with those in other countries that have now obtained equipment and "know how" equal to our own. This objective affects the job opportunities in industries that must compete with foreign firms for business abroad or at home. It is also related to the confidence of the investing community in the dollar.

These three objectives are approached differently by different nations depending upon their recent experience. Britain had years of distressing unemployment and reliance on the dole. She has come to understand that her firms must remain competitive if they are to export, and

that unless they do export, Britishers will not live well. In Germany the guarding of the monetary unit is now a cardinal principle because the suffering during the inflations in the 1920's and 1940's, with the destruction of savings and of individual liberties, was so deeply impressed upon the German consciousness. In our own country, however, it is a long time since its citizens suffered from wild inflation. Their subconscious thinking does not react to the concept in terms of human suffering; rather they remember, even to this day, the 1930's and the sufferings of unemployment. One would hope that they would learn from the experience of other peoples that inflation and unemployment are both threats, and that flirtation with the first does not avoid the second.

It is illuminating to ponder recent history in our own country in order to distill from it whatever lessons it may teach us. In the year 1955 we had extraordinarily high consumer expenditures for automobiles, for housing, and for many durable goods. Businessmen, encouraged by these strong demands, stepped up their capital expenditures, partly because they were projecting these demands into the future. The record level of outlays for plant and equipment helped sustain economic activity in 1956 and much of 1957, even though consumer spending for durables and housing had receded sharply. Then businessmen in many industries decided their capacity was great enough to match foreseeable demand--sometimes even greater. They cut back their expansion programs. The consequent falling off of business capital expenditures in 1957 was clearly a major factor in the recession.

By the same token, the inventory policies that had seemed appropriate in the light of peak business activity were found by the fall of

1957 to be out of keeping with existing needs. And so there began a period of rapid inventory liquidation, but without significant lowering of prices. Current price advances are therefore rising from the price plateau previously reached, instead of a price valley.

Now what are the lessons of history here and abroad? You will, I hope, pardon their statement in cryptic form to conserve time.

The quality of business decisions is important at all times, but especially so during prosperity. In short, the duration of the current expansion will be influenced by the quality of decisions now being made by business executives. I am talking about the heads of manufacturing, mining and commercial enterprises, about farm managers and bankers--and about union officials, too. Unless their decisions reflect prudent judgment as well as a reasonably well-founded appraisal of present and future trends, executives, as well as workers and investors, will pay the penalty. The problem, of course, is how to balance insufficient protection against too much; to achieve a proper compromise between caution and enterprise, between conserving and expanding, between the safety of a strong cash position and the growth that borrowing makes possible. Proper balance requires that we not be overly cautious when times are bad, nor overly optimistic, to the point of imprudence, when they are good; executives should risk neither too little nor too much, be willing to venture but still guard against unwarranted optimism.

Diluting the purchasing power of the dollar does not provide permanent employment opportunities. Persistent depreciation in the value of the dollar injures those who must live on fixed incomes but its significance extends beyond equity for such individuals. For one thing,

inflation diverts business energy into speculation and away from the increasing of output and of productivity. Not only is the productive process disrupted by hyperinflation, but even steadily creeping inflation is inconsistent with well-maintained productive activity.

It is a mistake to equate economic growth with governmental spending. We must ask ourselves: What kinds of growth are most beneficial? What kinds of governmental spending are conducive to stable growth and what kinds are detrimental?

What is it we desire to create in greater quantity? Is it more missiles, or more perfume? More plant capacity, or more schools and roads, or more farm crops? More producer goods, or more consumer goods and services? In our economy, of course, the majority of such decisions are made in the market place, even though the role of government has been progressively widened. Government spending, however, will not enhance the savings required to provide the tools and other capital equipment needed. Spending dictated by pressure groups will scarcely achieve the changes needed for real and sustainable growth--in fact, it may impede such changes. I should observe, in passing, that GNP is too limited a measure of a country's progress and of its ability to satisfy human wants to serve as the sole basis for comparing our country with other countries that operate under entirely different rules. Material goals are only one aspect of our way of life; the dollar value of GNP may rise while living standards fall, or while job-creating activity declines.

Most of the day-to-day problems in economic policy-making arise not out of differences as to objectives, but out of the choice of specific policies which will promote them. It is at this point that confusion starts. It is asserted by some that a stable dollar and enough economic

growth to provide an acceptable level of employment are incompatible. It is my own conviction, however, that price stability is necessary for high employment to be long sustained. Perhaps our most urgent domestic necessity is to protect the purchasing power of the dollar while providing widespread employment opportunities. Both for the protection of those who live on fixed incomes, and for the benefit of those who need steady work to support themselves and their families, we must--as indeed we can--achieve high employment without inflation.

Inflation is not an effective long-run means of creating job opportunities. On this point thinking is confused. A recent letter asked "How can industry expand, buy machine tools and provide jobs for us millions of unemployed when you guys create tight money? . . . Haven't any of you men got the guts to stand up for an expanding money supply and abundance of credit to encourage production and help make jobs?" A blunt answer to this heart-felt query is that the tightness of credit is influenced by the demand for it as well as by its supply, and that the mere running of the printing presses, or the ballooning of bank credit, does not foster productivity improvement and higher standards of living. Even when credit is under restraint, it usually is growing, but the proper idea is to keep its growth in line with the possibilities of increasing the "real" output of goods and services. In other countries, and even in our own, inflation fever has diverted trained ability from producing goods to speculating on inflating prices. Speculative activity does create some employment to be sure, but not employment that lasts. Eventually inflation disrupts job stability for it is during inflationary booms that the seeds of deflation are sown.

The rising investment demand stemming from industrial research and management initiative requires an increased flow of savings. If we are to remain competitive at home and abroad, we shall need enough capital to implement technological advance, and also competitive prices. While our products have improved, foreign-made ones seem to have been improving even more rapidly. There is evidence that our cherished advantage in some types of machinery, as well as in autos and certain other mass-produced items, has been diminishing. This is a situation that will not be cured by ignoring it, or by the mere passage of time, or by passing laws. The sole solution lies in seeking continuous increases in technological and marketing efficiency, while preventing costs from rising faster than compatible with such improvement. Only thus will our firms remain competitive.

The problems of monetary policy are the problems of a society organized around the principles of free markets and freedom of choice. In an economy where freedom is exercised by individuals and by business units, effective regulation of the money supply is of prime importance. In fact, the major concern of monetary policy in such an economy is to minimize the unstabilizing effects of changes in the use of money and credit that businesses and individuals generate in the exercise of freedom. But freedom, even though it entails flaws, is the well-spring of social and economic advance. It spurs the creative process; it permits experimentation leading to change. The resultant economic hazards are small prices to pay for the rewards.

The freedom to make private economic decisions is not only consistent with our system of economic and governmental organization; it is one of the basic human values that we prize. But freedom can be preserved only so long as it is accompanied by wisdom and restraint. Moreover, our freedom does not include freedom from the consequences of natural economic law. Each time we elect to spend, we must figure out how the bill will be paid. In homespun language, "There is no such thing as a free lunch." Government cannot give to some citizens what it does not take from others. A nation cannot spend more than it earns through production. The goods we enjoy have to be produced by someone's sweat and the capital we use have come from someone's saving. Intemperate and unwise decisions could squander our resources, magnificent as they are. It would be tragic if inept financial husbandry were to injure a future that appears to be so rich in promise and in hope.