

THE ECONOMIC ENVIRONMENT OF THE SEVENTIES

Remarks of Mr. Robert P. Mayo  
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at the Thirty-ninth Midcontinent Trust Conference  
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It is a pleasure for me to be here today to participate in the thirty-ninth Midcontinent Trust Conference. I have attended many of these conferences. I've even talked at some. And it has always been obvious to me that your experience in the careful shepherding of trust accounts has been carried over by your program committees to the careful shepherding of participants' time at these meetings. This program is no exception. So I suppose I should consider myself appointed as trustee of your time for the next 30 to 45 minutes. I'll leave it to your judgment at the close of the meeting as to whether I've unduly stretched the prudent man rule or not.

Having just come through a rather hectic election campaign, we are again aware that not all speakers invoke the prudent man rule--prudence and impartiality are not a universal element in speech-making. But I am not running for anything, so let me try to reinvest the proceeds of your delegation of this time to me in what hopefully will be a realization of modest gains or appreciation in value--long-term, that is.

Because of both my previous and current involvement with economic policy it is tempting to spend my time today talking about current economic developments. But you are all aware that it is virtually impossible in this day and age for any speaker--much less an official

of the Federal Reserve System--to offer a treasure chest of new and exciting ideas on the current economic situation. The interest of the press and the public makes it difficult even to offer something refreshing. Furthermore, I don't think you would want me to plough through too much of the same ground to be covered by your investment panel this afternoon.

Because of this and because of the thrust of your program toward longer term developments, I felt that I would be prudent and talk in fairly broad terms about the economic environment of the Seventies. Not that this isn't tempting too. Standing on the threshold of a new decade, it is difficult not to attempt to pick out the outline of the future. Indeed, the temptation to do so is one to which we all inevitably succumb. We know that the world of tomorrow is influenced, often imperceptibly and unexpectedly, by the actions we take today. Gazing into an unclear crystal ball is, consequently, a necessary preliminary to rational human activity.

One of the most formidable obstacles to prediction is the immediate past. It colors our views of the world to an extent few of us realize. It often causes us to mistakenly label the most transient disturbances as permanent features of the landscape. Classic examples of this myopia were the widespread agreement in the immediate post-World War II era that interest rates would never again be high, the general acceptance in the 1950s that the free world faced a permanent dollar shortage, and the predictions of only a few years ago that our affluence would soon allow us to meet all our social needs and that the only remaining problem was to sever the obsolete link between income and productive effort.

At the same time, the superficiality of the great majority of recent events often blinds us to the fundamental and irreversible character of other changes that are taking place. Some of these changes we may welcome; others we may resist. In either case, we misconstrue or ignore them only at our peril.

Despite all these pitfalls, forecasts of the future are necessarily based on projections of the immediate and not-so-immediate past. This is as true of the forecasts generated by the most sophisticated econometric models as it is of the homely predictions of your local barber or taxi driver. Both assume connections between the past, the present, and the future. Ideally, one should bring to the task of identifying these connections the skills of the professional historian. As the philosopher George Santayana once wrote, "Those who cannot remember the past are condemned to repeat it." A more recent observer, obviously more impressed by the hazards of historical generalization, has amended this bit of wisdom by appending: "And he who does remember the past is also doomed to repeat it." Armed with these disclaimers, cautions, and an abundance of trepidation, let us now venture to look ahead into the Seventies.

Perhaps the fundamental question to be answered regarding the 1970s is whether it is worthwhile to make any forecasts--i.e., whether this globe will still be inhabited in the year 1980. It seems fair to say that all forecasts assume an affirmative response to this question. Indeed, we have little choice but to be optimistic regarding the prospects that the superpowers will prevent the cold war from erupting into a hot one. On the basic assumption, therefore, that we will be around to enjoy

the passage of another mere tenth of a century--or a mere 1 percent of a millenium, if you please--what can we say about the prospects for survival of the existing political and economic systems? Will they be recognizable in 1980 or will they have been succeeded by an Orwellian world of centralized authority, thought control, and diminution of the role of the individual? Or, alternatively, will we have reached an age in which civil liberties coexist with an informed use of the state to bring about social and economic equality, and in which competition, struggle, and hard work have been superseded by cooperation, gentility, and the leisurely consumption of goods and services produced almost without human toil?

It is obviously the mark of an unimaginative and hopelessly conservative member of the Establishment for me to reject both of these extreme visions of the future in favor of one much less heroic. Nevertheless, it is my conviction that the year 1980 will dawn on an America that, if unfamiliar in some respects and uncomfortable in still others, will be both recognizable to those of us here today and with fundamental institutions of both democracy and free enterprise generally intact. This is not to say that they will be unchanged. Survival will require that remarkable resiliency that the Republic has demonstrated throughout two centuries of strife, turmoil, and crises. In particular, the realization of my essentially optimistic vision presupposes that certain of the seeds of social change planted in the 1960s grow to fruition in the 1970s. In some cases this is wholly to the good.

Commonsense and decency dictate that the struggle of black Americans for simple justice and true equality be successful. It is heartening to see the hopeful beginnings in the areas of equal

employment opportunity, open housing, and economic assistance for the inner city. We are finally losing our fears that somehow black progress is inconsistent with our own welfare. It is not.

At the same time, it would be advisable to avoid the self-congratulatory stance taken in some recent advertising copy. We must admit that businessmen as a group have been insensitive over the years toward the legitimate aspirations of racial minorities and that there has been more than a little tokenism in some of the programs undertaken. However, continued and rapid substantive advancement of the minorities is one of the key assumptions underlying the prognosis of a domestic tranquility by 1980.

Certainly there will be other fundamental changes in the political and social landscape. The growing demand of affected groups for a larger voice in private and public decisions affecting their destinies will undoubtedly continue. Consumerism may take its place beside the labor movement as a constraint on the profit-maximizing activities of private business. It may be joined in that role by a disjointed but determined alliance of groups devoted to the protection and restoration of our physical environment.

Some have expressed doubts regarding the staying power of these movements; in their cynical view apathy is the natural state of man. Indeed, to the extent that the consumer movement succeeds in lifting business ethics to a permanently higher plane, it is probably desirable that it then retire to the position of a monitor, rather than trying to assume any role as co-manager of the economy. To put it another way, it would be a happy state of affairs to see simple honesty on the part of all lenders supersede the need for a legal requirement that

the effective annual rate of interest be stated in the instalment loan contract in letters no smaller than three-eighths of an inch in height. After all, the greater part of the proposals originated under the banner of consumerism have been little more than demands that business adhere to a strict standard of honesty and forthrightness in its dealings with the public, including the provision of information necessary to rational consumer choice. Widespread support for legislative proposals to coerce ethical behavior is simply evidence that there have been abuses in the past. The old law of caveat emptor is slowly, but unmistakably, giving way to a higher order of business morality. This, I believe, is one of those changes that will endure beyond their unheralded beginnings in the 1960s--even if consumerism as an organized force eventually retires to the sidelines.

Skepticism regarding the staying power of the ecology movement has been based on one or both of two considerations. First, it has been suggested that such a rapid emergence of the movement brands it as a fad. Like swallowing goldfish and climbing flagpoles, it has been argued that anti-pollution is a phenomenon that will soon run its course. Second, it has been suggested that the current wave of enthusiasm for improving the environment is based on ignorance of the costs which such improvement would entail. Once the bill is tallied up--and particularly when it is made clear that the elimination of noise and air pollution may require curtailment of the prerogatives of what John Keats has so aptly labeled the "Insolent Chariot," otherwise known as the automobile--the movement can be expected to fall to pieces.

I am unable to agree entirely with either of these predictions. Regarding the first, there is an undeniable element of faddishness

and inconsistency among some recent converts to the ecology movement. Many of the people picketing Commonwealth Edison for burning high-sulphur coal undoubtedly use laundry detergents with high phosphorous content, drive automobiles lacking antipollution devices, and vote against bond issues for the construction of sewage plants. We must consider too that protest against pollution is in some ways a healthy replacement for protest against a Viet Nam experience everyone wants to forget. And as for the high costs of preventing or offsetting the effects of pollution, they probably will be even higher than we suppose. They may even turn out to be so high as to retire some of today's environmental crusaders to the sidelines. This much may readily be conceded.

My own conviction is that the environmental revolution will gain, rather than lose, momentum. Population and industrial production will continue to grow--and although the recent Census suggests that the "population bomb" may have been defused, at least in this country, population growth is certainly going to continue for several more decades. Therefore, the costs of not doing something about pollution will increase at an accelerating rate. It is generally acknowledged that a pollution problem arises only when pollution becomes great relative to the environment's capacity to absorb additional waste material, and even then only when a significant proportion of the population is affected. These thresholds for a number of types of pollution have recently been reached. Many people not too far advanced in years can remember when the beaches of Lake Erie were delightful places for bathing on Sunday afternoons; there is a danger today that no child as yet unborn will have similar memories of Lake Michigan.

Nothing is more specious than the argument that, while in some vague sense it would be "nice" to do something about pollution, the costs make uneconomic any serious attempt to deal with it. Indeed, the very existence of a pollution problem reflects the fact that, under the existing inadequate structure of property rights, there are some costs that are not recorded among the expenses of private business. That taking these costs explicitly into account should be designated "uneconomic" strikes me as reflecting an excessively narrow view of economics. Surely, it is a schizophrenic view of human nature that recognizes the validity and rationality of spending thousands of dollars to flee to the relatively clean and green environs of the suburbs, but which condemns as frivolous and uneconomic a collective decision to preserve the same amenities in the city.

Some fear the consequences of the ecology movement for what they believe to be the sacred rights of property. Again, may I suggest the criticism is wide of the mark. Indeed, it is slowly being recognized that any rational plan for dealing with pollution problems will involve not the abolition, but the extension, of property rights. Surely, the reason that our water has been polluted with impunity in the past is that no individual or institution harmed by that pollution possessed any defensible property rights in the stream or lake in question. Had someone possessed such rights, he would have used them to sue to enjoin, or collect damages from, the polluter. If this seems far-fetched, one need only mention that fishing streams in England are kept pure for angling only through the exercise of the private ownership of fishing rights in those streams to obtain injunctions against industrial establishments dumping wastes therein.



The absence of any such rights in the United States may be traced back to decisions in the early 19th century in which American judges rejected the doctrine that the owners of land through which a stream flowed possessed "correlative rights" in the stream in favor of the "rule of capture"--a euphemism for "gettin' yours while the gittin's good." Though quite consistent at a time when our nation favored the removal of all restrictions to development, the unfettered exercise of property rights by some under this rule was bound, sooner or later, to infringe the similar rights of others. It was to be expected that it would eventually be curtailed, either through legislation or by the gradual rearrangement of property relations in the courts. Both processes have now come into play, as illustrated by the recent law requiring pollution control devices on all new cars and the courts' establishment of the principle that groups affected by changes in the environment may sue to protect their interest.

Each of these developments means further restraints on the businessman's right to run his business as he sees fit. All add to the complexity and potential frustrations of doing business in the 20th century. Yet, each of them--and the acknowledgement of this fact may serve to sweeten the bitter bill of additional regulation--is aimed at redressing what we must admit has been an imbalance between freedom and responsibility in the context of a modern industrial society.

What these changes add up to is a much more demanding environment for business during the Seventies. The rules of the game will be a bit more confining. Decisions inconsistent with a broadened public interest will be much more difficult to make stick than in the past. And businessmen will have to learn to live with the fact that their

constituencies include many more than their stockholders. Within these new and narrower boundaries, however, I am convinced that free enterprise will continue to flourish. and let us hope that business itself and local governmental units too, will take on the essential corrective steps and not throw the whole burden on the Federal Government.

Turning now more specifically to economic prospects for the coming decade, my comments must necessarily be based on specific assumptions regarding the resolution of several questions in the international sphere over which we have some degree of influence. First and foremost, of course, is the assumption of an early end to our involvement in Vietnam. As is well known, the extent to which present and pending claims on the national income can be met depends heavily on our ability to extricate ourselves from an active military role in that unhappy part of the world. If the Administration's efforts in this direction succeed--and it is my earnest belief that they will--we shall gain some further flexibility in meeting our most pressing domestic problems. But if anyone is still suffering under the delusions of future substantial peace dividends in excess of income tax cuts already enacted, he should forget about it.

Any substantial cut in our expenditures for military preparedness depends to a considerable degree on success in the ongoing SALT talks with the Soviet Union. Past experience suggests that it would be imprudent to include such a success among the key assumptions of any economic forecast. Consequently, such an assumption is not made here.

Assuming that these conditions are fulfilled, then, what is the outlook for a return to reasonable price stability at a high

level of employment? To my mind, the prospects are excellent. But we must retain the courage of our convictions and not expect too much too soon. Clearly, the unemployment we are currently experiencing in the effort to turn the tide of inflation--a 5.6 percent unemployment rate in October with the likelihood of a still further rise, perhaps to exceed even 6 percent sometime next year--is much higher than we can tolerate for any extended period of time. It is urgent that it be reduced as quickly as is compatible with a steady decline in the rate of increase in prices. For the present, we must continue to pay for the sins of our Federal spending orgies of 1966, 1967, and 1968.

It is certainly not a foregone conclusion that the severe round of inflation we have experienced since 1965 was inevitable. The great success of the "New Economics" between 1961 and 1964, when virtual price stability coincided with a gradual decline in unemployment, belies that notion. What was lacking was not the economic knowledge and tools to prevent inflation but the political will to use them. If expenditures for the military buildup beginning in 1965 had been financed through a tax increase, instead of through a deficit financed by an unwarranted rate of growth in the money supply, and had we been more prudent in the expansion of our other Government spending programs we might have enjoyed several additional years of noninflationary prosperity. Instead of harboring deep but unconfirmed doubts regarding the efficacy of "fine-tuning to guide the economy between the perils of unemployment and the risks of inflation, we might actually have attempted the passage.

Once the existing inflation is under better control, we may have a second chance to navigate the straits. What we must avoid is the temptation to veer too sharply with the wind to reach the shore of

full employment. If we did this we would surely go aground once more on the shoals of inflation and again be faced with the necessity of patching the ship before setting sail once more. Having successfully circumnavigated the shoals--with luck, in the next year or two--we can then proceed on our journey.

If this difficult course of action is followed there is little reason to doubt the early 1970 projections of the President's Council of Economic Advisers of a Gross National Product of \$1.2 trillion by the middle of the decade and \$1.5 trillion by 1980, both measured in constant 1969 prices. These figures would be attainable with an average rate of unemployment for the decade of 4 percent, an average annual rate of growth in measured output per manhour of 2-3/4 percent, and an average annual rate of growth in the labor force of 1-3/4 percent. With responsible fiscal and monetary policies, these figures should be compatible with an annual rate of increase in the price level in the latter half--or even the last two-thirds--of the decade of about 2 percent--the average rate of inflation in the United States over the last half century.

On the assumption that population growth to 1980 remains on the low side of projections made by the Bureau of the Census in 1967--and which the 1970 Census indicates may be closer to the mark than other, higher estimates--per capita consumption expenditures in constant dollars should increase by about 40 percent by 1980. It is out of this increase that any important rise in federal, state, and local expenditures for pollution control, revamping urban transportation systems, building public housing, welfare reform, and many other wanted programs will have to come. And yet I see no compelling reason why Federal spending should be any greater relative to the total output

if the country in 1980 than it is today.

In recent years, housing needs have loomed large among the nation's priorities. The recent tightness of credit, which has persisted in varying degrees of intensity since 1966, has not been favorable to the achievement of the national housing goals. The outlook for interest rates depends, to a very large extent, on our ability to turn back both inflation and expectations of future inflation. Success as a nation in this effort gives the only hope of somewhat lower interest rates in the face of the tremendous demand for funds in the decade ahead.

In the final analysis, of course, our economic destinies over the next decade rest in our own hands. If we can respond with sufficient promptness and imaginativeness to legitimate demands for change; if we can muster the political courage to keep the economic ship of state on a true course; and if we defend the traditions of civility and decency in public discourse whenever and wherever they are challenged--then, and only then, can we reasonably expect the decade of the Seventies to surpass in solid achievement the unprecedented progress of the decade of the Soaring Sixties. I am confident that the world of 1980 will be a good world in which to live.