YEAR-END STATEMENT

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The policy innovations of 1971 will not work in 1972 unless they are tempered by sound, established economic principles. Finding this blend of the new and the old will be the main challenge facing policymakers in the coming year.

Initial success of the New Economic Policy appears unquestionable. Inflation has been reduced, the business recovery is picking up steam, and the United States, through currency realignment, has become more competitive in world markets. Yet, the continued success of NEP in 1972 does not depend so much on bold new policy announcements as it does on blending the innovations that have been made with some long-established economic principles.

Perhaps the most important of these is that the market system, in which everyone is more or less free to buy and sell without excessive interference from Government regulation, is the best guarantee of a dynamic economy. If the domestic economy is to be strong in the long run, ways must be sought in 1972 to make the transition from controls to a freer economy.

Another principle is that the twin problems of unemployment and inflation cannot be solved without a flexible monetary policy, and a flexible monetary policy requires flexible interest rates. Strong pressures may come from influential quarters to keep interest rates from rising in 1972. But if business picks up, as everyone hopes it will, some interest rates may tend to rise. To try to keep the overall level of rates down would mean that the Federal Reserve would be undermining efforts to contain inflation. This old lesson from World War II and afterward should be constantly before policymakers as they grapple with the problems of the coming year.

In a third area--the international economy--striking innovations have been moving us away from long-established practice. Currency values have been realigned; there is hope that the new order will be less rigid and more flexible than the old one; there is a groping for ways to deemphasize gold and the dollar and give credibility to an acceptable international reserve unit. Yet, despite these innovations, the basis for international trade remains the same: each nation should sell abroad those goods and services which it produces most efficiently and buy those it produces less efficiently. Trade barriers which interfere with this free flow of goods work in the end to the economic disadvantage of all nations. So, for the United States to reap the benefits of a new monetary order, it must continue to pursue vigorously the established principles which underlie a liberal trade policy.

There is, then, more to a New Economic Policy than the glitter of innovation. Domestically, the old principles of a market economy are still sound and should be returned to as soon as possible. A prudent monetary policy, implemented through flexible interest rates, will still be essential if high employment and low inflation are to be achieved. Internationally, trade barriers must be reduced further if the fruits of world monetary reform are to be harvested.

We are not likely to be as dazzled in 1972 as we were in 1971 with economic innovations. But making the innovations work by blending them with established economic principles will be equally challenging--and rewarding.