TIGHT MONEY, ITS CAUSE, AND ITS CURE

At The Moment

Major Areas of Weakness Being Pointed to by Some Official and Non-official Spokesmen:

- Unemployment - about 4%
- Wholesale price index - unchanged in Sept., down in Oct.
- Housing construction - down 22% rate since Dec.
- Industrial production index - off slightly in Sept.
- Retail sales - little change since March

Counter Areas of Strength

- GNP - up 8% rate since end of 1965
- Disposable income - up 6% rate since end of 1965
- Federal budget

Prices - Inflation

- Wholesale - steady 1958 - 1964
  - Starting rise from mid-1964 (1964 to 1965 at 2%)
Rises have accelerated (so far 1966 about 3.5% rate to Sept.)

Industrial component since last year 2.3% - 1965 year 1.5%. (No change since July)

Cost of Living

1958 to 1964 - 1.2% annual rate
Feb. to Aug. 1965 - 2%
Aug. 1965 to Feb. 1966 - 3%
Feb. to Sept. 1966 - 4%

The Build-up to Excessive Demand

Over-taxation of our ability to produce
Plant capacity - 93% (over optimum level)

Labor capacity - 1966 Emp. up 1.5% Half of 1965

Unemployment of 4%

Why excessive demand

Government's Concern with Optimum Utilization of Resources

Production
Plant – labor
A necessary influence to long-run stability
Accepted doctrine among economic thinkers
The doctrine in action – from 1961
Public programs
The tax cut – a series over the period
The Vietnam War
The resulting fiscal pressure
The high employment budget
Reinforcement by monetary policy
Normal counteraction absent
Rates of growth of money, 6% from Apr. to Apr.
Supply fell since Apr. – 1.5% rate
The Fiscal-Monetary Mix
Dual expansionary forces (until recently)
Money Market Reactions – Supply and Demand
Tremendous demand for credit
Government
Business to meet demand
Past 12 months - 17%
Jan. to July - 22%
Some tapering off recently - 7% since July
Others
The resulting tightness in money markets
Despite record growth of money supply
Demand forces rates upward
Policy tight only in sense - didn't provide all
What do we do?
State of economic intoxication may lead to
National economic frustration
Everybody has it so good
Close our eyes to threatening clouds of further inflation
We are slow to take chances with our present comfort to do what's needed to assure long-run well-being.

How It Can be Solved - With a Lag

- Fiscal adjustment
- Reduce spending
- Increase taxes - while holding spending
- Restore the Fiscal-Monetary Mix

Likely continued upward pressure on prices:

- Total demand continues 8% growth rate
- Productive capacity only 4% rate
- Price lags

Can Monetary Policy Do the Trick?

Perhaps - If -- But

If - economic forces only concern

But - social and political issues involved
Restrictive monetary - expansive fiscal
Non-selective in impact
Somebody gets hurt - housing
Social to political issues
Then comes talk of legal control - and the great debate goes on
Prices continue to move - they don't roll back
Inflation continues to take its toll

The Solution

Restoration of Fiscal-Monetary Mix
Impact of Higher Rates on Agriculture

Will push current expenses higher

Little effect on current production

Will tend to reduce purchases of operating capital items

Slow down the rate of increase in farm land values.