

## FEDERAL EXPENDITURES AND ECONOMIC GROWTH

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Serious discussion in the public arena of the economic policy implications of Federal expenditures has been increasingly hampered by the barrage of emotional sloganeering of the two major business organizations and lack of leadership by the administration.

If these hearings help to clear away only a small part of the emotional impediments to a calm appraisal of this issue, it will serve a most worthwhile purpose.

Unfortunately, however, academic discussions of this topic can be only partially helpful, at best. As long as the administration and the Congress deal with this issue in the 19th century cut-expenditures-enlarge-the-pork-barrel manner, little significant progress can be made in the necessary public understanding of the role of Federal expenditures in our national economic development. There is a huge reservoir of nonsense on this issue that has been spread widely by people in responsible positions.

Federal expenditures are neither good nor bad in themselves. They must be viewed in terms of their purpose, in relation to the gross national product, in relation to the level and trend of private activities, and in relation to fiscal and monetary policies.

It is sheer nonsense to say—as some have said or have implied—that any rise in Federal spending is a threat to our national well-being. To meet the needs of national security and some of the needs of our growing population may well require a rising level of Federal expenditures. Under such conditions—that characterize the current period of our history—it is the duty of Federal Government leadership to seek the adoption of adequate and fair tax and monetary policies to meet our national needs, rather than to ignore defense and social necessities.

It is ridiculous to proclaim—as some have declared—that a dollar spent by a private person is always somehow preferable to a dollar spent by government. There is a positive economic role for government—defense, education, postal services, roads, and conservation of natural resources are but a few functions that require some activities and outlays by one or another level of government.

It serves no purpose other than confusion to wield the broadax blindly at suggested Federal expenditures and, at the same time, to thank God that Federal expenditures have been helping to hold up the level of economic activities—as did many responsible people in the first half of 1957.

Neither does it serve any purpose of achievement or understanding to propose Federal programs on the one hand, to threaten the Nation with disaster if they are adopted, on the other hand, and to acquiesce

quietly to their defeat—as the administration did on so many public welfare program issues in the past session of Congress.

It is disgraceful that the Russians should have been first in firing successfully an ICBM. The budget and the legislated debt limit seem to be the major criteria for meeting defense needs, as well as public service needs.

I stress these factors because I am convinced that the subject of Federal expenditures and economic growth, in its economic policy implications, is more of a social and political problem than one of economic theory. Arrival at some general conclusions on this subject by this or any similar panel is not going to provide us with a bold national leadership. Economic theory alone is not going to produce serious concern among private and public policymakers with the social objectives of a rich and productive economic system such as ours.

To discuss properly this subject of Federal expenditures and economic growth, there are a number of questions that first must be posed and answered.

#### QUESTIONS ON FEDERAL EXPENDITURES POLICIES

Can we conceivably expect, within the near future, any substantial reduction of defense expenditures, by about \$10 billion to \$20 billion—and thereby obtain some significant cuts in Federal spending? I do not believe so, in the absence of some settlement of world tensions, because I do not believe that the world we live in will permit such cuts in Federal spending, unless we are prepared to face the alternative of a loss of national sovereignty and a collapse of the free world. I therefore expect Federal expenditures to be high and to remain high in the foreseeable future, by comparison with pre-World War II peacetime years.

Can we expect to meet the growing needs of a growing population with real or dollar outlays for public services that are no greater than in 1940? I think not, and I don't see how any thinking person can advocate chopping away at public service expenditures and expect the Nation to maintain adequate educational, health, road, and similar facilities. Furthermore, there have been 15 years of postponed and neglected public service efforts. Our population has grown almost 30 percent since 1940—and the proportion of the population below working-age at one end and above 65 at the other end has been rising. Not only have public service needs as a whole grown, but the public service needs of the young and the elderly have grown most rapidly. In addition to the expansion and the changing characteristics of the population, our standard of living, as well, has improved. There are greater demands and greater needs for education beyond the elementary school; technological changes in civilian pursuits and in the Armed Forces require an increasing degree of advanced scientific education and technical training; increasing leisure has increased the demand and need for adult education; paid holidays and vacations have resulted in pressing demands on our existing recreational facilities.

If we compare nondefense budget expenditures in 1940 and 1956, we find the following: in 1940, Federal budget expenditures for non-defense were \$6.9 billion in an economy whose gross national product

was \$100.6 billion—these outlays were 6.9 percent of total national output. Between 1940 and 1956, our gross national product rose more than four times and our population increased almost 30 percent. But in 1956, Federal budget outlays for nondefense purposes were \$25.8 billion—6.2 percent of \$414.7 billion gross national product.

Organized business and conservative politicians screamed to high heaven about these 1956 expenditures, predicting gloom and doom, despite the vast subsidies that go to business, largely in the indirect form of tax concessions. It seems to me, however, that the growth of the population and expansion of public needs justify some significant improvement of public and social services. Merely to have lifted nondefense budget expenditures to 7 to 7½ percent of gross national product would have meant Federal outlays for these purposes of \$29 billion to \$31 billion—it would have made possible an increase of some \$3 billion to \$5 billion over what was actually spent for public services and social programs.

As I look at these figures, I am utterly convinced that the problem is not whether we can afford some improvement of public and social services. The problem is a political one—with the administration and the Congress. The question is whether our national leadership desires a significant improvement of public and social services.

Should an expanding high-employment economy have social objectives that are somewhat more meaningful than rising lines on charts and a continuing outpouring of automobiles and other consumer durables? My answer is definitely in the affirmative. During the depression of the 1930's, we concentrated our attention on achieving full employment, more effective use of our productive capacity and a more equitable distribution of income. Since 1940, we have made vast strides in those directions. We now have the job of sustaining economic growth and high levels of employment and of achieving some further improvements in income distribution. But more than 15 years of generally high levels of employment and production have posed new questions that deserve the attention of national leadership.

What is the purpose of sustaining continuing economic growth and high levels of employment and output—is it merely to turn out more and more automobiles and electrical appliances? Should a rich and growing economy seek to wipe out remaining pockets of poverty? Should the benefits of economic growth be used to improve the Nation's health and educational facilities, to eliminate slums and provide improved housing, to revive decaying urban centers, to encourage cultural activities? Should an economy, such as ours, shift an increasing degree of attention to leisure and to leisure-related activities?

I would suggest that the Nation's productive ability, after more than a decade of generally high employment, makes it possible for us to turn at least part of our attention, to these social objectives. An expanding and productive economy, such as ours, can afford to devote a share of the gross national product—as well as imagination and leadership—to eliminate poverty, to improve health and educational facilities, as well as housing, to redevelop our urban centers, to conserve and develop natural resources, to expand recreational and cultural facilities.

Economic growth makes it possible for the Nation to devote increasing dollar outlays for public services and social advances. Seven

percent of a \$100 billion output in 1940 was \$7 billion—7 percent for public services, social programs and other nondefense purposes of a \$415 billion output in 1956 would have been \$29 billion. Furthermore, economic growth expands the tax base and revenues rise as output and sales grow. There is no doubt that the national economy can afford to improve and expand its public services and devote some portion of its total output to enrich our social order. In some of these areas the question, I believe, is whether we can afford not to make improvements—in education, for example, or resource development or urban redevelopment.

Can we expect the business community to finance such developments? I think not and it would be unreasonable to expect profit-seeking enterprises to do very much along these lines. It is a tragedy, however, that the business community traditionally blocks such advances by government, as revealed again, in the past few months, by the organized business attack on Federal aid for education. The record of the business community on these issues is overwhelmingly negative, except where it touches the pocketbook nerve of specific business interests, as indicated by the widespread built-in business support for Federal outlays for road building.

#### NATIONAL LEADERSHIP IS REQUIRED

Almost all of the efforts in improving public services and in enriching our social order, therefore, inevitably fall upon the government, upon both Federal Government leadership and expenditures.

A frequent answer to questions, such as those posed above, is to talk about States' rights and to declare that these tasks belong with the States. That reply is often a subterfuge and, more often, it is meaningless. Many of these tasks are national in scope and require national direction or coordination. Many of them are too costly for conventional financing by States and local governments—they require Federal outlays, grants-in-aid or long-term loans.

Few States have responded, with positive action, to these issues in recent years. With their current financial burdens and constitutional limitations on expenditures and new bond issues, it is unrealistic to expect much significant action on public welfare programs in most States without long time-consuming delays, at best—especially in the absence of courageous State leadership and national prodding to obtain necessary constitutional changes and improvements of State tax structures. It is no wonder that the States have done so little in these areas in recent years. Not only are they burdened with committed outlays, frequently inadequate revenues, and constitutional limitations, but most State legislatures are so constituted as to be far less than receptive to public service and social programs and improvements of regressive tax structures. Most State legislatures are poor examples of representative democratic government—with their "rotten borough" representation and substantial underrepresentation of the urban population.

To talk about shifting current social welfare programs, and future programs to the States, is to undermine the possibility that much action on such programs will be taken in the near and foreseeable future. It is hypocrisy on the part of the State-righters to say that the Federal Government should not engage in civilian public

services such as aid to localities with chronic unemployment and financial assistance for schools and hospitals. If the State-righters were sincerely interested in strengthening State governments, they would be in the forefront of efforts to make State legislatures more representative of the population, to modernize State constitutions, and to rebuild their State and local tax structures on the basis of ability to pay.

Federal expenditures, as I see it, have to be viewed in the light of these and similar considerations—high dollar outlays by comparison with pre-World War II peacetime years due to national security requirements, the growing public service needs of a growing population with changing characteristics, the need for social objectives of an expanding high-employment economy and the ability of such an economy to turn more of its output and attention to fulfilling these social objectives, and the reality that the States cannot be expected, without long delays, to take leadership on these issues. Federal expenditures have to be viewed, too, in terms of economic growth that expands the tax base and raises the revenue potential from a given tax rate.

This Nation is capable of meeting its currently "normal" defense requirements, as well as improving and expanding public services and social programs, if we are fortunate enough to avoid all-out war or a sudden sharp rise in defense outlays. The problem is essentially not an economic problem—it is a political one.

#### MEETING THE CHALLENGE OF ECONOMIC GROWTH

Foremost, as I see it, is the issue of meeting the public service needs and social advances of a growing population in a rich and highly productive economy. I think it is wrong to base Federal expenditure policies on compensatory financing alone. If we continue to concentrate all of our policies on the basis of compensatory government operations and to delay needed programs, as we have done since the start of World War II, we will be sadly neglecting important underpinnings of our economic system and society.

To think of economic growth as most economic-model theorists do, is to omit the important human and social aspects of economic development. Basically, economics is not numbers, graphs, or charts—it is human beings and society. The school system is a major factor in economic growth. So are the conditions of the people's health, housing and urban areas, roads, resource conservation and development.

In working on economic development plans for underdeveloped countries, economists have all too often planned complicated hydro-electric and irrigation projects, without thought for the need of engineers; steel mills before considering the need for technically trained workers; industrial activities while neglecting the requirement for continuing maintenance of the equipment. In thinking about future economic growth in the United States, we should not and cannot ignore the human and social requirements of continuing economic expansion.

This country's educational system has contributed much to improving productive efficiency and economic growth. The cultural heritage

of the Western World—and of the American people—must be adequately passed down to the new generation. To neglect our educational system at this time of rapid technological change will undermine the potential for economic growth and improving productive efficiency in the future.

Not only is there obvious need for adequate educational facilities—structures and equipment. There is also the need for teachers. Society must be willing to provide these necessities, if it is to continue its advances. Our educational system should be considered at least as important to the Nation as automobiles and washing machines which receive so much of the public's attention. National and State leadership is required to speak up clearly and forthrightly on the needs of our educational system. Federal aid for education is essential for the economic, as well as general, well-being of the Nation.

Resource conservation and development may be somewhat more directly related, in the public mind, with economic growth. But even here, practical efforts and achievements in most fields have been far from noteworthy since the start of World War II. It took many years of work by people like Theodore Roosevelt and Gifford Pinchot, before the various levels of government and sections of industry became concerned with conserving our timberlands. We would be hard put at present to find national leadership of similar force in the effort to preserve and extend our forest conservation programs, in efforts to move toward new river valley developments that would curb flood disasters and enrich the economic potential of several areas of the Nation, to conserve and develop water resources in an attempt to forestall serious water shortages for industry and agriculture in the Western States.

Although the administration has talked about the need for some program to assist economically distressed communities—ever since the 1952 campaign—no legislation on this issue has yet been adopted. Improvement of the economic conditions in such communities would obviously be of assistance in sustaining continued economic growth.

These and similar efforts that require Federal Government outlays and leadership are essential for continuing economic expansion. They form part of the social underpinning for economic growth. Such programs should be started as soon as possible and they should move forward at a steady pace—to be curtailed in the case of a sudden sharp rise of defense expenditures and to be stepped up when private economic activities decline.

What we need at present is not a backlog of public service programs and blueprints that can serve as a means for holding many conferences, but going programs to strengthen and enrich our society.

#### MEETING THE CHALLENGE OF THE BUSINESS CYCLE

In recent years, most attention to movements of the business cycle have been on inflation rather than on deflation. High Government outlays, by comparison with the past, we are told, are inherently inflationary and an excess of Government outlays over revenue will inevitably cause demand inflation. This is decidedly not what has happened in recent years, and experience should have taught us long ago that Government expenditures should be viewed in relation to the gross national product and the level and trend of private activities.

In fiscal years 1947 and 1948, Federal outlays were declining and there were substantial Federal cash surpluses—\$6.7 billion in 1947 and \$8.9 billion in 1948. Nevertheless, there were sharp price rises in those years due to the pent-up demand for all types of consumer and capital goods and to the untimely end of OPA. In fiscal 1951, the year of post-Korean sharp price increases, there was a cash surplus of \$7.6 billion, and in fiscal 1956, when wholesale prices moved up rapidly, there was a cash surplus of \$5.1 billion.

Sharply reduced Government expenditures, as in fiscal 1947, are not guaranties that price rises will not occur. Neither will substantial cash surpluses, in themselves, guarantee against a rising price level.

Federal expenditures, surpluses, or deficits are neither inherently inflationary or deflationary in themselves. The level of Federal outlays—as well as of cash surpluses or deficits—are of great importance when examined in relation to the levels and trends of activities in the other sectors of our economic system and in relation to fiscal and monetary policies.

Concentration of Government activity on anti-inflation policies and restrictive measures, rather than on economic growth, is a departure, it seems to me, from the intent of the Employment Act. It is the maintenance of economic growth to which the Federal Government is committed under the terms of that act, although the administration seems to be too little aware of its obligation under the law.

Continuing economic growth is essential for the maintenance of material strength and high levels of employment. It is likewise essential for meeting national security requirements and for improving living conditions. Economic growth in the past made possible the great material achievements of the Nation. It can make further advances possible.

As the economy grows, its tax base expands and increased revenues can be collected from a proportionately smaller burden on individual taxpayers.

Government policies and measures are important in maintaining economic growth. Changes in Federal expenditures have an effect on the direction of national economic activities, depending on trends in the private sectors.

A significant change in the dollar level of Federal expenditures has an obvious effect on the trend of economic developments, depending on fiscal and monetary counteraction, if any. The degree of effect would depend on the magnitude of the change, as well as on the direction of private activities.

A decline of Federal expenditures of \$11 billion between 1953-54 was bound to have a depressing effect, since no significant private activity was moving up sharply. The effect of the cut of Federal expenditures was to reduce orders, and induce business to cut inventories, output and employment in defense-related industrial plants, to reduce income from private activities and to depress expectations generally. The psychological effect of a significant change in direction of Federal expenditures can and does have an economic impact—as in 1953—even before the actual cuts, or increases, in government outlays occur.

One cannot forecast these effects with mathematical certainty. It is even more difficult to measure the precise effects of one type of pro-

gram, as compared with an alternative program. The direction, however, can more easily be foreseen.

Improvements in the unemployment compensation and social security systems help to bolster consumer income at a time when wages and salaries from private activities are declining. An increase in transfer payments of \$1.9 billion between 1953 and 1954 helped to produce a small rise in total personal income, despite a decline in labor and farm incomes. This maintenance of high levels of personal income during the 1953-54 downturn helped to reduce the impact of the decline in government spending and in industrial output. The reduction in personal income taxes, effective January 1, 1954, had a similarly strengthening effect on consumer buying power, which cushioned the economic decline.

Alternative types of programs have differing effects in specific areas of the country, specific industries and among specific groups of the population. The recent cutbacks of defense outlays, particularly aircraft, for example, have had the most notable effect as yet in California and seem to have dampened expectations generally.

Countercyclical policies, when economic activities are moving down, should require, I think, a stepping up of government expenditure programs, tax cuts or a combination of both. On this, there is little disagreement against most Americans. There is disagreement, however, on the issue of which part of the economy should receive most government attention.

During the downturn of 1953-54, the administration strongly emphasized its views that Federal efforts should be concentrated on stimulating business investment. We, in organized labor, opposed the administration's suggestions—we were convinced that the administration's proposals were based on faulty economics and would further erode the progressivity of the Federal tax structure. We are now convinced that the administration's success produced a lopsided economic development between the spring of 1955 and the end of 1956—sharply rising business investment in new plant and equipment, accompanied by sluggish consumer markets. We are now beginning to see some of the consequences of this lopsided development that was encouraged by administration policies.

With current cuts in defense outlays, at a time of a general lull in economic activities, it is my belief that a cut in the Federal income tax—by increasing the individual exemption from \$600 to \$700—is essential. It was my view before this committee, several months ago, that congressional action on reducing individual income taxes should have been taken immediately by the past session of Congress, accompanied by closing some of the many tax loopholes, if possible. Action on this issue by the forthcoming session of Congress may be too late to halt a downturn from getting underway.

Involved in any countercyclical policies, therefore, is the economic sector or population group to be affected and proper timing. It is my view that under most conceivable conditions of a turning down of economic activities, the major part of the Government effort should be aimed at bolstering consumer buying power. In our kind of economy, the long-run health of the system largely depends on consumer activities. This point, as I see it, should be kept in mind in pursu-

ing economic policies to forestall a decline in economic activities and, also, in pursuing policies to curb the possibility of demand inflation.

Built-in stabilizing forces should be strengthened so that their action may be forceful at the beginning of a downturn. That would mean, among other things, the development of Federal standards for the unemployment compensation system and a general improvement of that system. It would mean, too, a substantial overhaul of the Federal tax structure to restore that structure's progressivity—so that Federal revenues could be raised more on the basis of ability to pay than they are at present.

The built-in stabilizers, inherited from the New Deal and Fair Deal, are strengthening factors in our economy and society. They do not and cannot provide, however, in my opinion, a guaranty against depression.

While the built-in stabilizers would go to work automatically, in case of a downturn, their operations may conceivably only alleviate a downswing and not halt it. Tax cuts should be considered. Government public service and social programs, under those conditions, should be stepped up. Tax cuts and the stepping up of such programs should not and need not await economic disaster—quick Federal action is essential when production is declining and unemployment is rising rapidly.

In order to build confidence, strong countercyclical measures should be the announced policies of the Federal Government. The American people have a right to expect intelligent and courageous action from their Government.

In conclusion, I should like to emphasize my conviction that the subject we are discussing is much more a political issue than an economic one. We need government policies to encourage continuing economic growth—certainly not government measures to restrict the general level of economic activities. We need an expansion of Federal efforts to improve public services and to strengthen our society. We need an equitable and progressive Federal tax structure—and in the States, as well. We need more and better economic data and more information about current movements of the business cycle and the effects of specific types of Federal actions. But above all we need national leadership, worthy of a rich and productive democratic society.