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Statement of

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Chairman, Board of Governors of the Federal Reserve System

before the

Subcommittee on Fiscal Policy
of the
Joint Economic Committee

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Mr. Chairman:

This Committee and the Board of Governors share a common concern: that the operations of both monetary and fiscal policy be directed--in the words of a report issued by your Committee in January 1956--to "maintaining a steady and sustainable rate of economic progress."

On behalf of the Board of Governors, I should like to outline some measures which we believe would contribute to the achievement of this common objective.

Events have moved swiftly since passage of the Employment Act of 1946. Congressional debate and expert opinion preceding passage of that Act were in close agreement in pointing to unemployment of men and machines as the primary threat to the national economy. The history of the period since the war, both in this country and abroad, however, has demonstrated that the primary danger was not one of idle men but was one of too much money.

Almost everywhere in the world, pressure on resources has been intense. The necessity of preventing competing claims for scarce resources from resulting in general price increases has been a major problem. Deferee needs have been a major claimant. Other demands on resources have been bolstered by pressing individual and community needs, on the one hand, and by large financial assets, strong liquidity positions, and rapidly rising current incomes on the other. Even so, the opportunities for vigorous growth and accelerated technological progress resulting in sharply rising standards of living and increased security, especially for those in the lower and middle income groups, have been very great. Even

greater opportunities lie ahead, ready to be realized if the threat of international conflict can be reduced and the insidious inroads of inflation curbed.

Inflation is never harmless, even in its mild or "creeping" form. Neither is it inevitable. Given appropriate monetary and fiscal policies, reasonable restraint by consumers and businesses in their spending decisions, and continuing keen competition, price stability with a rising standard of living can reasonably be expected. On the other hand, acceptance of the gradually rising price theory carries with it a widening expectation of further rise. This leads in turn to financial overcommitments, speculation, misdirected expansion of capacity, slackened efficiency, erosion of existing savings and discouragement of new savings, and an ultimate reaction of a serious nature.

For about two years we have been experiencing an intensified demand for funds and, although the supply of savings and the volume of bank credit have both increased, expanding demands have outpaced their availability to potential users except at rising interest rates. Consequently, the price of money has risen. If bank credit had been allowed to increase more rapidly under these circumstances, prices of goods and services, including those purchased by Federal, State and local governments, would have risen further under the stimulus of inflationary credit pressures. How much further no one can say, but the strength of inflationary forces has been and is still formidable.

An increase in the volume of savings is the most effective way to deal with a situation whose inflationary potential would only be aggravated by an excessive use of credit. As these savings are made available to meet demands for more housing, schools, and other public improvements,

as well as expansion of new business plant and equipment, they provide the resources for stable economic growth. To the extent that fiscal policy results in a budgetary surplus and the Federal debt is reduced, the supply of savings is increased and the need for monetary restraint lessened. This is because maintenance of a surplus permits funds to be channeled through Government debt retirement into the capital markets where they would be available to meet private demands and demands of State and local governments for funds to carry through their projects for needed community facilities.

A reduction in taxes would bring welcome relief to millions of taxpayers. Such action, however, without a corresponding curtailment in Federal expenditures, would reduce or eliminate the budget surplus, and tend to stimulate increased total spending in the economy. At the same time the supply of funds made available to the capital markets through Federal debt retirement would be reduced.

As a number of witnesses who appeared before this Committee have pointed out, the general economic situation is still one of very active demands, intensive utilization of resources and continuing pressure toward higher prices for goods and services. They have also noted the declines in residential building and some consumer durable goods, the slight falling off in total industrial production and the drop in prices of some sensitive commodities. However, the general economy is still being stretched by record levels of plant and equipment outlays, rising demands for State and local government projects, further increases in consumer buying, and continued need for large-scale defense spending. On balance, the situation

does not seem to us to reflect a basic weakening that would call for relaxation in efforts to curb inflationary pressures.

Your Committee has indicated an interest in the consideration given to current and prospective economic trends in the formation of Federal Reserve policy. Since Federal Reserve System operations reflect to some degree all phases of the nation's economic life and have a pervasive influence on it, they must be adjusted on a day-to-day basis to the ever changing situation. Hence, the System has need for as much current and background economic information as it can assemble.

Efforts are directed toward bringing together, and combining as background for our decision-making the best available statistical information and the best informed impressions and judgments that can be obtained from businessmen, bankers, agricultural experts, labor leaders, and from others both in and out of government. We also depend on information collected and compiled by other agencies of the Federal Government. For this reason it is important to the proper formulation of monetary policy that the statistical facilities of the Federal Government be well manned.

In our appraisal of economic developments maximum use is made of the decentralized structure of the Federal Reserve System. Through the 12 Federal Reserve Banks and their 24 branches, in business and financial centers all over the United States, and especially because of the caliber and experience of men who serve as the directors and officers of these institutions, the Federal Reserve is in close touch with current and prospective developments throughout the country.

In accordance with provisions of the Federal Reserve Act the Board meets frequently with Presidents of the Federal Reserve Banks, who serve as members and alternates, on the Federal Open Market Committee. The Act also provides for quarterly meetings with the Federal Advisory Council, composed of representatives of the member banks in each district. These occasions make it possible to study continuously underlying developments in all parts of the country and all sectors of the economy.

Much of the statistical data and other information we collect for our own policy decisions is also made available to the public in general. We believe this is as important as its internal use, because it helps to provide a basis for better public understanding and more accurate appraisal of credit and monetary problems and of policy actions designed to deal with them.