REMARKS BY
HONORABLE G. WILLIAM MILLER,
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BEFORE THE
NATIONAL GOVERNORS' ASSOCIATION EXECUTIVE COMMITTEE
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I am delighted to be here. I do feel I am among some friends, Governor Garrahy being the Governor of my state, the Coalition of Northeast Governors was a bit of a fortuitous event in my life.

Ever since I got associated with that particular organization I have been involved in government. And I don't know whether you fellows pushed me into Washington or what, but I'm delighted to be back sharing some of these problems with you.

We do have an atmosphere in the economy which is difficult. It's been opened up over a long period of time. The inflation that we are now experiencing is the aftermath of some 15 years of both policies and external events that have led us into a path from which there is no easy or simple solution.

The inflation is deeply embedded. It's going tc take quite awhile to wring it out, and it's going to take, I think, a cooperative effort from all levels of government and the private sector.

I think rather than taking your time with a speech, perhaps I will just turn to the subject you'd like to discuss, and that way we will make better use of your time.

QUESTION: Mr. Secretary, perhaps I could start off by asking you to consider how deeply the governors feel, and as a matter of fact, we have found that our concerns are shared equally by county officials and mayors as regards the renewal of general revenue sharing.

We did have a chance to meet with the President this morning and we expressed our concern directly to him, and Mr. McIntyre knows fully how strongly the general revenue sharing is important to the states and the local communities in our efforts to make sure that there is an opportunity for us to use some relatively small share of the total funds made available to a local government to meet those needs.

And, frequently, those mandates of the federal government for which there are no specific funds. And we have today readopted a statement of policy on that matter, which I certainly would like to have you have.

And if you have a specific point of view on the revenue sharing maybe you would be kind enough to share it with us. We have asked the President to please make a statement on this issue as soon as possible, as very shortly now the 1981 budgets for most of the states, many of the communities, counties and municipalities are going to be shaped.

And if there is going to be an erosion of this very important revenue sharing funds, we need to know it as soon as possible.

And, frankly, we think we would be finding it much more difficult to deal with the contraction of the federal government unless we can be assured of the continuation of revenue sharing.

SECRETARY MILLER: I am very conscious of the importance of this subject, and very aware that you do need to know where you stand. I think the President will be making some determinations, and I am sure he indicated that to you.

The program expires at the end of 1980 fiscal year, and so, as you point out, time is short. I hope that we can consider that in the Administration, in the context of all the programs that are going to be competing for limited resources. We have, as you know, pending before the Congress the targeted fiscal assistance, which we think is also important, because of the nature of this recession and the way that it falls unequally on various parts of the country.

And we hope we can have your support in that effort. I am not sure that I can yet express an Administration position on the general revenue sharing future, because that is something that the President will have to decide shortly.

GOV. GARRAHY: I, of course, would like to welcome Secretary Miller, a fellow Rhode Islander, and to also make the same comments that Governor Snelling made about his outstanding participation with the Northeast Governors.

And, more particularly, his outstanding community spirit in Rhode Island. And, Bill, we miss you very much and we miss a lot of the leadership that you provided for many of the civic involvements in our state.

I know I briefly at one point had mentioned to you about the use of tax-exempt revenue bonds, which I know affects the Treasury very much. But in our state we've, very wisely, I think, used tax-exempt housing bonds to provide much-needed housing for many people on limited incomes and at affordable rates.

The National Governors, I think in our conference last year, endorsed the use of those, of course with restraint and the wise use of those bonds. And I suppose what we are saying is that we hope the Treasury will continue to look at those and in a way in which they can be widely used to meet the needs of housing in this country.

SECRETARY MILLER: Well, Governor Garrahy, let me just give you a little background on this, because this was something that I faced not only at the Treasury but at the Federal Reserve.

There is a very interesting development in private housing in this country in the way it's financed, and I would like to try to distinguish between the kind of housing which is subject to the market system and that kind of housing which you may have to be concerned about, which requires some public assistance.

The general housing market, since 1966, has been somewhat at hostage to the business cycle, and through every business cycle since that time, as periods of boom or high economic expansion and a corresponding unleashing of inflation developed, we had the increasing of interest rates that goes with higher inflation and there was a closing down of the normal deposit credit sources for housing.

The deposits were disintermediated from the savings and loans and the savings banks, even from commercial banks, and moved into market instruments, where rates were higher.

And this shutting the window, almost, on credit for housing had disastrous consequences. You can see this perhaps most dramatically in the last recession, where at the end of '72 housing starts in this country were running at two and a half million annual rate.

And within two years they were running at a 900,000 annual rate -- 60 percent decline. But when you dismantle a whole industry and lay off all the people and create no conditions where continuing supply is appropriate, you just completely wreck the industry. It's a very expensive process.

The next time it recovers everyone wants a higher price for their wages, because they may be laid off, and every supplier wants to get the maximum profit, because he doesn't know when he will have an opportunity thereafter.

That problem was so serious that we began recently to look at several changes, the most dramatic of which was the action of June 1, 1978, which we took at the Federal Reserve, to authorize money market certificates to allow the housing industry to compete for funds.

The result is that housing has continued remarkably well through this recession. Even though the cost of mortgages is higher, at least individuals have a choice between buying a car or something else and buying a home, while, before, they had no choice because they couldn't get mortgage credit.

There has also been a development of non-deposit sources of funds in the mortgage pools. All of these things have made housing more subject to the general economy.

Now, if we begin to have, as a result of this, a further innovation where housing, for people who have the means to afford it, is financed on a subsidized basis, then we interfere with a policy direction that was intended to create a market system.

We begin to create a subsidized system which will raise the cry that every other component of society needs subsidy, for automobiles or something else.

So I think what we are trying to do is to take that part of the market which belongs in the market system, where there will be ups and downs in terms of its costs and what not, and let it be free, and let it operate. It will be healthier and it will be better.

And that part which could be subsidized through mortgage bonds should be limited to situations where there is a really predominant need for public assistance.

And that's, I think, the philosophical approach we have. Now that can be accomplished in a number of ways, and I know there have been many, many specific inputs on how that can be done.

But I hope that I can leave you with the impression that there is no intention on my part of supporting a curtailment of the kind of state and local financing for public assistance housing that you are talking about that have done so well in Rhode Island.

But it does not make sense, quite frankly, for subsidized bonds to be issued to finance my house. And I don't think that's a good use of public funds or a good social choice.

And that's what we've got to avoid.

QUESTION: (inaudible) and find something -- percent interest rate, and is it a good idea? And if it isn't, is there anything you can do about it?

SECRETARY MILLER: Well, first, I am enthusiastic about the President's appointment of Paul Volcker, because the action since he has been Chairman of the Federal Reserve makes me look good.

SECRETARY MILLER: Everybody who was complaining about my actions are now saying --however, in all due respect, I think Paul has pursued an inevitable policy -- good, bad, I don't know.

But let me tell you why it's inevitable and why it is part of a process that we cannot avoid, nor can we avoid it when we look around the world. And that is the oil price increase in the second quarter of this year, increasing our energy prices, our oil prices about 60 percent.

That has had the effect, as it works into our economy, of increasing our inflation about two percent. Now if interest rates stayed stable, that means that interest rates in real terms would go down two percent.

You know, lenders of money would be paying people, in real terms, for them to take the money. And any time you have higher inflation anyplace in the world, those who have capital to lend will try to shelter themselves from losing real capital.

And they will try to get enough interest to make up for inflation. As long as that's true, we are going to have that phenomenon of interest rates that are unprecedented in our experience, because we've never experienced in the peacetime history of the United States the rates of inflation we have in this decade for such an extended period of time.

This is a unique decade. Every number, 19 with a seven in it, has been an unprecedented period of high inflation in peacetime. And that is what brings on these new phenomenas.

Now interest rates need to be analyzed a little. If one looks at the interest rates charged for consumer installment loans, they have changed very little, because the whole reason has been a market premium for the risk of smaller loans, of automobile finance and that sort of thing.

For credit cards revolving finance, the rate hasn't changed. It is only in two areas -- and I'm oversimplifying -- that general interest rates that affect business finance have gone up in sympathy with the increase of inflation and mortgages have gone up because we have allowed the housing market to compete for funds and pay a market rate to stay in business. And that's a trade-off that I think is worth making.

But the only way we are going to get interest rates down to the level that we'll all like, is to get inflation down. And just as soon as we make progress there we can count on interest rates going down.

QUESTION: Mr. Secretary, the economists say that we are now in a recession. I think I heard you essentially say that, too. How serious do you think it will be, and what is the Administration's anti-recession, anti-inflation strategy?

SECRETARY MILLER: The inflation that we are now suffering has built up over 15 years. It started I think, and I don't mean this in terms of a criticism of any one or any decision, but it did begin when we decided as a nation not to pay for the Vietnamese war.

And after that, we made a series of other decisions which contributed toward the build-up of inflation. So over some 15 years this has built up, starting with fiscal deficits repeating each and every year, and building up an excess stimulus from federal financing.

And then we had the events that we couldn't control, such as crop failures around the world, which drove up food prices. The anchovy crop that one year left us short of protein had much to do with inflation in the early seventies.

Then we had the oil boycott and the whole phenomenon of energy. And the process started and got trapped into the ratcheting up of everyone protecting themselves, and has continued until it has been excruciatingly difficult for us to begin to address the underlying fundamentals that we need to address if we are to correct this.

In the last year and a half that I have been in Washington we have been in the process -- and I think that I was a part of this process at the Federal Reserve -- of putting in place an integrated strategy to wage a war against inflation.

And to wage that war we need to marshall every policy weapon at our command, and we need to deploy those policy weapons and to continue to apply them.

Congress and the President recognized that inflation was getting out of control, more than they had expected, and they redirected fiscal policy and are bringing in a deficit for the current fiscal year of less than $30 billion, compared to earlier plans for a $60 billion deficit. It took a very courageous decision to do that.

That's a good direction. We recognize that business cycles make this difficult, but we must continue on a track that will bring us to a balanced budget in times of optimum use of our economy, and not run deficits in 19 out of 20 years.

We can't continue that. And so the President and the Administration are committed to a policy of not shocking the world by suddenly trying to balance the budget overnight -- which would mean a disruption of many of your programs and other people's programs -- but of bending down, holding down government spending so that as the economy grows we can make the budget balance.

The second part of a disciplined fiscal policy is to reduce the relative role of the federal government in our economy. In the last decade our federal government took 17 to 19 percent of our GNP. Recently it was 23 percent. Now we are moving down as fast as we can to 21 percent, and we'd like to move it lower.

And as we do that, resources are transferred back to the private economy, where the spending and investment decisions are far more effective in creating a vital and productive economy. And so the process of fiscal discipline and its direction over a number of years is critical.

Second, because monetary and fiscal policies take a long time to have impact, because of their lag effect, we have an interim period where we need everyone's help to moderate the inflationary forces.

It is for that reason that the President inaugurated a voluntary wage-price program. Because its voluntary, it has enough flexibility to take account of differences in industries and regions and individual firms, so that it isn't rigid and overly specific.

But it does seek an overall moderation of the rate of wage and price increases to contribute, on a fairly shared basis, to moderating the wage/price cycle until we can get the other fundamental policies biting.

And I would say to you that in my opinion there has been a very responsible reaction to this program from both the business community and the labor leadership. And wages have been held below what they otherwise would have been by this program.

We are now deeply involved in extensive consultations on how to extend this program for one more year, and to do so on a basis that involves more participation, more assurance of the commonly perceived need and a process by which there can be equitable and fair treatment, but through which there can be a deceleration and moderation.

Third, international accounts. It is critical in this strategy to defeat inflation that we have a sound dollar. A weak dollar introduces inflation.

The decline of the dollar from September, 1977, to October, 1978 added one percent to inflation last year because the essential goods we bought cost more in dollars. We had to pay more dollars, because of a weaker dollar, to buy the same thing. And because contracts roll in slowly, and because prices get ratcheted up only slowly, that dollar decline has rolled into 1979 and we have one percent more inflation this year because of that long ago decline of the dollar.

And so over two years the costs to the American consumer for a weak dollar is $30 billion of inflation -- a $30 billion price tag. That's why we moved so forcefully last November 1 to establish a powerful program to see that we have a sound dollar.

And today, one year later, the dollar is about four, five percent higher on a trade-weighted basis than it was then. So we've stopped that source of inflation.

But we not only must be sure of a sound dollar, but we must make the fundamental corrections. In 1973 this nation imported $8½ billion worth of oil; this year we will import almost $60 billion worth.

We have to pay for that by more exports. So we've got to bring our international accounts into balance. Fortunately, we are getting help in that. Our agricultural program has been successful in expanding our agricultural exports. And there has been a tremendous growth of exports of manufactured goods. I think, Dick, in your state there is a lot more export of your product, and that is the kind of thing we need to do with every state. And we are seeing more of this, Joe, in Rhode Island also.

Last year we had a deficit in our current account of $14 billion. Through the progress that we have made this year it will be less than half, and next year we'll be in surplus. So we have moved that fast in trade and other current account items to bring ourselves into balance.

Okay, that's three major policy directions: fiscal, wage/price and international. The fourth is energy. This nation was built up for its first 100 years of existence by renewable energy sources: water, wind and wood.

That's how we fueled our nation. The second 100 years have been using depletable energy sources, principally: oil, gas and coal.

Now events of the world and our geometric progression of building a great standard of living has left us where, with finite resources, the cost of recovery of those resources just has come to the end of the cycle.

And we've got to make the transition to a new kind of energy source that will carry us into our third century. And in the process we've got to reduce our dependence upon oil as a source of energy.

And we must reduce our dependence upon imported oil, because we just cannot be subject, either in terms of cost or availability, to decisions made outside our country that affect our vital welfare.

So we must make that shift, and in that regard we need to support the comprehensive energy programs that are being worked on and have been worked on to bring us back into alternate sources of energy and more independence.

Now some things have already been put in place. The natural gas bill passed last fall shifted us from spot shortages of natural gas to abundant supplies now.

And we are putting people back on gas again, putting industry back on gas where we were denying it. So the market system of going to the deregulation -- I remember CONEG, the Coalition of Northeast Governors, against all historic odds, with no dissenting vote, voted for phased deregulation of natural gas, as consumers.

And the result is they have a supply of fuel now that turns out to be cheap, when every reason told them before that to try to control the price and hold it down. And they are better off in New England now, to have gone with that decision, which was courageous at the time.

And that kind of leadership from governors I think shows that we can do the job when we realize what the real world is about.

Now we have a question of using the market system to deal with oil. So the President has made this decision to deregulate domestic crude. That will generate a very substantial amount of new, unearned revenue.

So we have an important decision to make. How much of that unearned revenue to allocate to the oil producers, so that they will have funds to develop more abundance of conventional fuels.

And how much of that revenue should be allocated to public purposes to finance, through the public sector, the development of unconventional sources of energy which cannot be financed by private companies, because they are too uncertain, not profitable, not known, but yet we need to take the risk and do it?

And how much needs to be allocated to such energy conservation efforts as mass transit, which you were just talking about, to reduce our transportation system's requirement of energy while delivering the service to the public?

And how much should be used to shelter the poor and the aged and the ill who can't afford to pay the higher price? So that allocation decision is in debate, and I think we can make it wisely and fairly.

When we do that we need to mechanism like the Energy Security Corporation to get outside of federal bureaucracy, to set up a financing mechanism, not to operate energy projects, but to pass the funds around judiciously to private companies, so that we have smorgasbord of options of how to do it, whether it's loan guarantee or grant or a purchase agreement or a price guarantee, to get this job done.

And we need a Mobilization Board to cut through some of the red tape that otherwise will delay needed projects and we need a stand-by system to take care of emergencies, in case we get caught short.

So the energy program is another powerful weapon to defeat inflation, by getting us independent of this great drain on our resources.

And then there is monetary policy. And monetary policy, which Governor Brown was just speaking of, must continue to be disciplined. If we merely pump out money to finance the 60 percent oil increase that means we will just have permanent inflation.

We won't have two percent that we get rid of next year; we'll have two and four and six percent on top of what we have, just going on and on. There's a painful price we must pay, but monetary policy needs to be exercised in a way that makes the economic adjustment as orderly as possible and avoids dislocation and avoids harm.

The next policy weapon that is terribly important is to work on the supply side of the economy, to create the conditions for saving, investment and productivity that we must have.

Our nation has been under-investing, compared with other nations. Japan invests over 20 percent of gross national product each year in capital projects, Germany, over 15 percent.

If you take private and public investments in the United States you are talking about 12 percent. We need to step that up, if we are to be competitive in the world, if we are to have the modernization of technology, if we are to have the best practice, the reduction of unit costs of output, new systems to reduce the energy use per unit of output and all of the things we need for productivity.

And, of course, another major policy area is to reduce the burden of government, which falls so heavily on our system and comes out in price increases and burdens and dislocation.

So these policy weapons which I've summarized are being mobilized, and with your support and understanding I think we can apply them forcefully. It will test our determination and our will.

We will be sorely tempted to go the easy path, but it's going to take a period of austerity, fairly shared by everyone so that no one is taken advantage of. But from that, from that austerity, by taking a little less now, we will share a greater bounty of this nation later on.

And that's what I think we need to do. In the process, we will re-establish America's preeminence, both at home and abroad, and we will improve our leadership and we will contribute to the solution of other problems that are so critical in our nation.

VOICE: Governor Brown has a question, followed by Governor Garrahy.

GOVERNOR BROWN: Mr. Secretary, in the course of preparing our budgets we have a factor on the rate of inflation. What figure should we realistically factor in for the next calendar year?

And when we do that, don't we further feed the inflationary spiral? What can we really do? Is there an end?

SECRETARY MILLER: Yes, there is an end. The end is over a long period of time, as I indicated, because once you have climbed this 15-year path of escalating inflation, and once you've put in the policy weapons to fight the war, you begin to turn it down slowly.

And each and every year we need to move inflation down and it will take five, six, seven years to wring it out, to get it to acceptable levels. But when you think of your budgets, you must think of inflation related to things that you spend your money on.

If you look at the Consumer Price Index, it has been my estimate that for this year we are going to see an increase in inflation rate of somewhere between 9½-11. We will see it trailing off toward the end of the year, because we will have gotten over the hump of some of the special factors.

Next year it will be below that. Probably in the range of 8½ to 10 percent. But you don't necessarily buy that market basket, and so I think you have to price it out in terms of your particular items.

And, of course, I am not that expert in your particular state. But in doing this, certainly the federal government is taking the view that we price out all of the programs that we are involved in, and the inflation impact, and in some cases we ask those who are part of the federal process to share with us some of the austerity that's necessary to avoid just ratcheting it up.

The President a year ago imposed a five and a half percent pay cap on federal employee salary increases, which was way below inflation, and federal employees were asked to show leadership by taking less.

This year, recognizing that the oil shock of the second quater has driven inflation to the rates I mentioned, of 9½ to 11 percent, it's just asking more than I think is wise to ask the federal employees to continue to absorb all of that.

And so he has set a 7 percent raise. But that certainly indicates some sharing of austerity, and I think it is that kind of approach that we all need to take.

QUESTION: Secretary Miller, another subject that is quite topical, from your leadership, of course, of one of this country's great corporations, do you see any efforts being made by Chrysler of their own belt-tightening and some of the governmental help to save that company in the long run?

SECRETARY MILLER: Well, I'd appreciate some inputs from all of you on this subject. Some of you probably have operations -- although I don't see any major states here that have Chrysler operations, there must be some.

But as a general proposition, it seems to me that it is not good policy for the federal government to provide financial assistance to industrial corporations. As a general proposition I think that violates the principles of our private enterprise system, which is the strength of our country.

That is, there is the opportunity in our great land to make private investments and reap the rewards. But there is a risk. And if there is an inefficient operation or a misjudgment, that risk means that the process of failure has to be there.

As you know, from our own experience, if we don't take our failures and try to subsidize inefficient industries, we just push the problem off until it gets bigger. And if New England had tried to subsidize the textile industry, even though the process of redistribution of that industry was dreadfully painful, we wouldn't have the diversification in New England and the vitality that we have today that's so critical.

So we cannot just take inefficient operations and subsidize them. However, the RFC was put into being to help finance industry generally from a national emergency, the Great Depression.

In the case of Chrysler we have had in the last six years an enormous shock to the automobile industry, from the change in oil and gasoline prices, and plus, at the same time, the expectation not only to shift the whole industry towards smaller, more fuel-efficient cars, but many environmental considerations.

And not every corporation has had the financial strength to survive that process. Whether Chrysler could have or should have or would have done it in a different way is beside the point.

We now have a case where the company is in financial difficulty, and we do have an industry that has very few producers, and one in which we need to maintain competition.

And if that corporation can come up with a sound plan, that is, a transition from here to there, but is not seeking a permanent subsidy or a permanent federal support, but is seeking a help from Point A to Point B to get over this hurdle, and if that plan is sound enough and has contributions from all of its constituencies in the form of curtailment, and moderation of demands by its employees, foregoance of dividends by its shareholders, with better terms from suppliers and banks who are willing to stretch and recapitalize the debt to take off the load of cash requirements, and infusions of capital from new sources -- if all those things could be done, and if the federal government could, in a limited way for a limited time, provide something in the way of a loan guarantee to bridge over, than I think the public interest in maintaining a viable company and competitor, in maintaining the productive capability of that operation, would be worth looking at.

Whether that plan will be presented by the Administration to the Congress depends on how sound it is and how good it is and, whether the role of the federal government would be well secured and well protected and assured to be repaid.

Or if it is a plan that is inadequate, in that case we would be better off to face the inadequacy now than later. But I'd like inputs.

VOICE: Mr. Secretary, we promised to have you out of here by this time, so we want to thank you very much for joining us and discussing with us some of the economic issues that affect us in the states.

And we look forward to seeing a lot of you in the next year or two.

SECRETARY MILLER: Thank you very much. I am carrying away your position, and I will read it with great care and do my best to be helpful.

Thank you.

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