

NOMINATIONS OF PHILIP A. LOOMIS, JR., AND ALAN GREENSPAN

HEARINGS BEFORE THE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS UNITED STATES SENATE NINETY-THIRD CONGRESS

SECOND SESSION

ON

THE NOMINATIONS OF
PHILIP A. LOOMIS, JR., TO BE A MEMBER OF THE SECURITIES AND EXCHANGE COMMISSION; AND ALAN GREENSPAN TO BE A MEMBER OF THE COUNCIL OF ECONOMIC ADVISERS

AUGUST 8, 1974

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NOMINATIONS OF PHILIP A. LOOMIS, JR., AND ALAN GREENSPAN

THURSDAY, AUGUST 8, 1974

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS,
Washington, D.C.

The committee met at 10 a.m. in room 5302 of the Dirksen Senate Office Building; Senator John Sparkman, chairman of the committee, presiding.

Present: Senators Sparkman, Proxmire, McIntyre, Cranston, Stevenson III, Hathaway, Biden, Tower, Brooke, Brock, and Weicker.

The CHAIRMAN. Let the committee come to order, please.

Today the Committee on Banking, Housing and Urban Affairs will be holding hearings on two nominations submitted to the Senate by the President for its approval.

First is the Honorable Philip Loomis, a reappointment to the Securities and Exchange Commission. The second nomination is Mr. Alan Greenspan to be a member of the Council of Economic Advisers.

After these hearings are completed, the committee will go into executive session and I will ask the audience to leave the room at that time.

However, I expect that executive session to be quite brief and then the committee will go back into open session for the consideration of some pending bills.

First, I would ask Mr. Loomis to come around.

Mr. LOOMIS. Mr. Chairman.

The CHAIRMAN. Mr. Loomis, I am glad to see you again. You have been before this committee a good many times.

Mr. LOOMIS. Yes, sir.

The CHAIRMAN. I am glad to have you back.

Mr. Loomis is nominated to be a member of the Securities and Exchange Commission for the term expiring June 5, 1979, and as I said, it is a reappointment. Mr. Loomis is recommended by the two Senators from his state, Senator Cranston and Senator Tunney.

Mr. Loomis, we have your financial statement?

Mr. LOOMIS. Yes, Mr. Chairman.

The CHAIRMAN. That will be, as you know, open for the inspection of the members of this committee in this room. Then it will be locked up in the safe and kept there during the time you hold the office and for 1 year thereafter.

You tell us, Mr. Loomis, that you have no holdings or interests

that would constitute a conflict of interest in your holding this office.

Mr. LOOMIS. I believe not. They are exactly the same with very minor changes as were submitted to this Committee on prior occasions. They conform fully to the rules of the commission in respect to such matters.

The CHAIRMAN. Very well, sir.

In the event you are confirmed for the reappointment, will you hold yourself out for invitations from this committee or any other appropriate committee of the Congress to appear and testify without reservation?

Mr. LOOMIS. Yes, sir, I have always done that.

The CHAIRMAN. Very well, sir.

Mr. Loomis, you have had a long and distinguished career with the Securities and Exchange Commission. How long have you been with them?

Mr. LOOMIS. Next month it will be twenty years.

The CHAIRMAN. That is a long time. You have had, as I say a distinguished career we might say working up through the ranks. You served as General Counsel.

Mr. LOOMIS. Yes, from 1963 until I was appointed to the Commission in 1971.

The CHAIRMAN. Yes, we are very glad to have you here. I think it is a fine reappointment and I commend the President and congratulate you.

Senator PROXMIRE?

Senator PROXMIRE. Mr. Loomis, at the time you were appointed, I said it was an excellent appointment and I agree. I think the President has made some of the best appointments to the Securities and Exchange Commission since the Commission came into existence many years ago. This is, perhaps, the strongest SEC we have ever had. The Chairman is a very fine appointment. One of the greatest distinctions of these appointments is that they are staff people who understand the agencies. They know what they are doing. And they have a fine and distinguished record of very high competence.

Having said that, let me ask about a couple of questions with respect to the SEC that have been bothering me lately. I asked the Chairman to have you come before us even though we all highly approve of you, I believe, because I think this is one of the occasions we have for an effective reconsideration of this most important agency. One of the problems we have on our financial markets is the responsibility of our accounting professions. The equity funding scandal is a conspicuous example of a failure in this respect and there have been other failures.

Now, what progress has the Securities and Exchange Commission made to improve financial accounting projects in the wake of the scandal?

Mr. LOOMIS. We have been working on that in increasing intensity in previous years to the extent the accounting profession is rather annoyed with us.

We have been taking the initiative more than we have in the past

to issue accounting series releases, directed, in effect, to state insofar as our jurisdiction lies, how accounting should be done. We have been meeting with the accountants frequently. We have been making speeches—even I have done that—through I have some trepidation about making speeches about accounting. We have been trying as hard as we can to improve the standards of accounting and auditing.

Now, we continue to adhere to the historic policy of the Commission and of the Congress to rely heavily upon the accounting profession today to do the job. We recognize that this requires, as I told an accounting group recently, that we should be much more active in making sure, insofar as possible, that their procedures are such that they are able to discharge their responsibilities. We have named accountants in enforcement actions with greater frequency than has occurred in the past. This is a controversial policy. The accounting profession does not like it but we feel that it is a way of elevating and maintaining standards in this field.

Senator PROXMIRE. One of the problems as I understand it is that the accounting profession of Great Britain, for example, is regarded as highly professional and truly independent and that the people who work in the accounting profession do not regard themselves so much as sort of employees or subject to the decisions of the people whose accounts they audit and that degree of independence, it is said by some critics, is not enjoyed by our accounting profession.

Do you think this is true and if there is any truth in it, is there any kind of legislation that we could consider adopting that would provide for a greater degree of independence and effectiveness on the part of so-called independent public accountants?

Mr. LOOMIS. As far as independence is concerned, the statute requires that the accountant be independent when he audits financial statements filed with the Commission. The Commission, over the years, has attempted to define "independence" primarily in terms of conflicts of interest if I may put it that way.

I do not think that this is a serious problem. I would be surprised to learn, although you probably know more than I, that the accounting profession in Great Britain is more independent than it is in the United States.

The accountants do not regard themselves as employees. That is contrary to all the standards of ethics in the profession. They have no interest in the affairs of their clients. The economic situation of course is troublesome in that accountants like other people have to get jobs and get work. And that, sometimes creates a problem but I really am not greatly concerned about the formal independence of the accountants. I think that is well established, we do have this problem occasionally of an auditor who does not want to lose the engagement just as you have perhaps with other professional people. I really do not regard that as a great problem we have to contend with.

Senator PROXMIRE. Do you feel you have enough authority under the law to provide effective regulation in this area? Would additional legislation be helpful?

Mr. LOOMIS. I think, as far as the independence of the accountant

is concerned, we have adequate authority. The statute requires that they be independent and we have considerable applied authority exercised over a number of years.

Senator PROXMIRE. You have the kind of authority to handle something like the Equity Funding scandal.

Mr. LOOMIS. That was quite another thing. There was a computer fraud going on. Since the case is pending in the courts, I would not wish to comment on the possible derelictions of any person.

Senator PROXMIRE. No, I am asking whether, with that experience behind us, legislation would be helpful to the SEC in preventing an occurrence of that sort of scandal.

Mr. LOOMIS. Frankly, Senator Proxmire, I do not think that is the kind of thing that can be corrected by legislation. You can say, people should not perpetrate fraud, that they should do their best to detect it, but it is more a matter of vigilance and integrity on the part of individuals.

Senator PROXMIRE. Why has the small investor lost confidence in the stock market and what is the SEC doing about it?

Mr. LOOMIS. I have not done any polls. I have only talked to a few investors. I do not know exactly. I think that the basic reason is economics. That is, historically when interest rates rise investors tend to shift out of stocks into fixed income securities because they get a better return. In addition, there is considerable concern over the state of the economy and that obviously dampens investor feeling.

I don't think that it is the fault of the securities markets that this lack of confidence exists.

Senator PROXMIRE. Do you think that the present disclosure requirements in the law are adequate?

Mr. LOOMIS. Generally speaking, yes, sir.

Senator PROXMIRE. You say "generally," they are. Where are they not?

Mr. LOOMIS. Well, the disclosure requirements in the law are I think adequate. There are of course, problems in making sure that full disclosure is made because people fail to do so and that is one of the major parts of our enforcement program. There are some areas, for example, where disclosure may not be obtained to the extent we wish because of exemptions such as the exemption of railroads from our full disclosure requirements and certain other matters of that kind, which the Congress has under consideration. But the legal authority, subject to exceptions of that kind, is I think adequate.

Senator PROXMIRE. You say that it is under consideration now?

Mr. LOOMIS. Yes, legislation is pending in Congress on that.

Senator PROXMIRE. One other area, this refers to the SEC and defense contractors.

I have been most disappointed by the lack of progress of the SEC in getting full disclosure in financial reports with the aerospace firms. I have discussed this before but received only promises and assurances. What other promises have been made and how can you assure me that steps will be forthcoming in the next weeks and months to correct this?

Mr. LOOMIS. Well, I made a speech that concerned itself with

that and I will be happy to send it to you. It is an exceedingly difficult problem because of the inherent nature of accounting and the operations of these defense contractors. They are engaged in many instances in manufacturing highly complex products on the very frontiers of technology. No one can know with certainty how much it is going to cost to develop one of these things and build it and make it work, and no one knows usually how successful it will be and how many will—

Senator PROXMIRE. We recognize that.

Mr. LOOMIS. That is, to my mind, the basic problem.

Senator PROXMIRE. I am not talking about that but situations have occurred in Lockheed where you have insiders with information on developing problems and trading in their stock because of that.

Mr. LOOMIS. Wherever that occurs, it is illegal and we will bring an enforcement action if the information is material.

Senator PROXMIRE. We are talking about full disclosure of problems like cost overruns and matters of that kind.

Mr. LOOMIS. Yes, we have been taking various steps through a special group we have to get full disclosure on those matters and of course it is difficult to get full disclosure of a cost overrun.

Senator PROXMIRE. How many people are working on that?

Mr. LOOMIS. It is not a large group. I do not have the exact number in mind.

Senator PROXMIRE. Two, three?

Mr. LOOMIS. In that general neighborhood. I think maybe more.

Senator PROXMIRE. The SEC relies totally on certifications by independent auditors who are hired and paid for by firms. I have asked for spot checks of auditors. Has this been done yet and if not, why not?

Mr. LOOMIS. Our staff has been certainly making spot checks in the sense of examining the material in our hands. We do not go and audit defense contractors.

Senator PROXMIRE. I understand. You cannot do that. I am talking about spot checks.

Mr. LOOMIS. We have been making spot checks although not generally going out to the plant but rather, relying on the information that we have or can obtain.

Senator PROXMIRE. Why can't you go out to the plant on a spot check?

Mr. LOOMIS. We can visit but that kind of a visit does not do much good. It is a matter of digging into the available papers and information much of which can be furnished to us or is in the Defense Department.

Senator PROXMIRE. You need to go out to the plant to get the records and so forth. Way back since McKesson-Robbins, you have had accountants who have failed to check a plant and found there was no plant.

Mr. LOOMIS. Well, that has not happened. The plants are there.

Senator PROXMIRE. Thousands of auditors regularly examine defense contractors. Some are permanently located there. Why can't SEC take advantage of these Government auditors and get them to verify financial statements?

Mr. LOOMIS. We endeavor to do that. We are in touch with the Defense Department. We endeavor to get from them all the information they have. One reason we do not go out there is the extent that will be a duplication of the efforts of the Defense Department.

Senator PROXMIRE. Have you done that in specific cases?

Mr. LOOMIS. You mean check with them? Sure we have.

Senator PROXMIRE. Will you tell the specific cases? Please do that for the record.

Mr. LOOMIS. Yes.

The CHAIRMAN. Senator Bennett.

Senator BENNETT. Thank you, Mr. Chairman. I might say, Mr. Loomis is a regular customer. We have had him before us a number of times. I think he is doing an excellent job. I do not want to delay the proceedings today and I certainly will be prepared to vote for his confirmation.

The CHAIRMAN. Is that all?

Senator BENNETT. Yes.

The CHAIRMAN. Senator McIntyre.

Senator MCINTYRE. No questions.

The CHAIRMAN. Senator Brock.

Senator BROCK. No questions.

The CHAIRMAN. Oh, Senator Tower, I missed you.

Senator TOWER. I am capable of a low profile these days. I, of course, know Mr. Loomis well and I am satisfied with his work and know the job he is capable of doing and the job he is doing and I will vote for his confirmation.

The CHAIRMAN. Thank you, Mr. Loomis.

Mr. LOOMIS. I will look forward to continuing to cooperate with this committee. I have always enjoyed it.

The CHAIRMAN. We have a biographical sketch of Mr. Loomis which we will incorporate in the record.

PHILIP A. LOOMIS, JR.

Born in Colorado Springs, Colorado, June 11, 1915. A.B., Princeton, 1938 (Highest Honors); LL.B., Yale Law School, 1941 (cum laude). Editorial Board of the Yale Law Journal. Married to the late Maryanna Hunter Oliver in 1949 and has three children. Admitted to the California bar, 1941; Supreme Court bar, 1955. Practiced law with the firm of O'Melveny & Meyers, Los Angeles, 1941 and 1946-1954. Attorney, O.P.A., 1942-1944; Associate Counsel, Northrop Aircraft, Inc., (now Northrop Corporation), 1944-1946.

Joined SEC staff as a consultant in 1954; appointed Associate Director, Division of Trading and Exchanges in 1955 and Director later that year. Drafted the 1960 amendments to the Investment Advisers Act of 1940. Had primary staff responsibility for the legislation which became the Securities Act Amendments of 1964. Became General Counsel in 1963. Had primary SEC staff responsibility for the legislation which became the Securities Investor Protection of 1970. Took oath of office as Commissioner on August 13, 1971.

Received the Career Service Award of the National Civil Service League in 1964; the SEC Distinguished Service Award in 1966; and the Justice Tom C. Clark Award of the Federal Bar Association in 1971. Member of the American Bar Association, American Law Institute, Federal Bar Association, State Bar of California, Los Angeles Bar Association.

The CHAIRMAN. Very well, sir. Now, we have Mr. Alan Greenspan of New York to be a member of the Council of Economic Advisers in the place of Herbert Stein.

Senator Javits and Senator Buckley have both approved of the nomination.

Mr. Greenspan, will you come around?

We have Congressman Clarence J. Brown here. Congressman, would you come around now. Take your seat at the table and Mr. Kenneth Rush, will you come around, please, sir.

Mr. Greenspan, that is quite a battery you have to introduce you.

Mr. GREENSPAN. Senator, I have rarely been in the middle of anything.

The CHAIRMAN. All right, Mr. Rush, are you making a statement of endorsement?

STATEMENTS OF CLARENCE J. BROWN, REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO AND KENNETH RUSH, COUNSELLOR TO THE PRESIDENT FOR ECONOMIC POLICY

Mr. RUSH. I very heartily endorse Mr. Greenspan's nomination, Mr. Chairman. I think the Nation is very fortunate that he has accepted.

The CHAIRMAN. Very well. Thank you.

Congressman Brown.

Mr. BROWN. Mr. Chairman, I find myself just slightly embarrassed by the array with which I am sitting since my testimony is, perhaps, somewhat different than you might have anticipated.

I appreciate this opportunity to appear before you to express myself on the occasion of the nomination of Alan Greenspan to be the Chairman of the Council of Economic Advisers. I support his nomination because I feel he is probably qualified for the job.

So, rather than take my time and yours to discuss Mr. Greenspan, I should prefer to discuss with you briefly what I feel the Chairman of the Council should be.

After 9 years in Congress, 5 of them on the Joint Economic Committee and many of them observing politics as a newspaperman before becoming involved myself, I feel strongly that an economic adviser on this Council should be a real adviser and not a mouth-piece for the economics collateral to a political policy. And he should not only advise the President but he should advise the Congress and the people of the Nation with the same determination.

Americans are living with the worst inflation of modern times, a domestic economy which is stagnating and a financial system under severe international strain. And American productivity has fallen to new lows in world competition. To get out of the mess we are in, will require the restoration of the American work ethic, the Yankee thrift ethic and some new economic ethics which must also be translated into political ethics.

For example, if America is to maintain her standard of living in the years ahead—let alone sustain our position in an increasingly competitive world economy—it will be necessary to raise staggering amounts of long-term capital to expand the productive capacity in our basic industries which make possible the jobs which fuel American buying power and pay the taxes to finance social progress. With

depressed financial markets, low real levels of profit in American industry and record dollar outflows to pay for energy, where will that capital come from?

I am not asking that the chairman of the economic advisers be a Jeremiah. But I do want him to have the vision for the long range good of our Nation and the courage to call the shots as he sees them. And to be listened to, he must have the reputation to be able to impress other professionally trained economists and the ability to articulate his views in this often esoteric field so that his ideas will be understood and supported by the average citizen for whom our system is supposed to operate. This is particularly important because, if our system is operating properly, most of that motivation which operates it will be coming from the average citizen rather than from the councils of the supposedly omniscient and omnipotent here in the biggest county seat in the world.

The intertwining of politics and economics cannot be unraveled. But the viewpoints of economists and politicians need not be the same. Our economic advisers should address the problems of investors and jobholders, of producers and consumers, of savers and spenders, and leave to politicians the consideration of them as voters. They should not be reluctant to tell it like it is and prescribe the medicine our economy may need from time to time. Politicians are frequently accused of sugarcoating the pill. But if the economists give us sugar pills to start with, the patient may get into serious trouble before anything effective is done.

The Chairman of the Council of Economic Advisers needs to be more than a statistician. He must be a diagnostician. He is not a tout to be supported or rejected for his accuracy at prediction. Rather, he is to preside over the best economic advice our Nation can get at any particular time.

And, Mr. Chairman, we are at a particular time when we need it now. I think we have such a man in Mr. Greenspan—at least I hope so. And if we do, I hope he will resist the powerful temptation to which other economists seem to succumb in Washington and not give up being a professional economist to become an amateur politician.

The CHAIRMAN. Well, thank you very much, Congressman Brown. It's good to have you here. I had the pleasure of serving in the House with your father-in-law for a good long time.

Mr. BROWN. Thank you, Mr. Chairman, I appreciate that comment.

The CHAIRMAN. All right.

Mr. Greenspan, let me ask you a few questions.

We have your financial statement that you have supplied for the committee, and it's certified by the President, who is your employer, that he has examined it, has checked it; and that he is in agreement that it's all right.

Now, let me ask you this question: While we do have your statement, and we'll keep it as part of our files, do you tell this committee that you have no holdings, no interests, that would constitute a conflict of interest in your holding this job.

I might qualify that question just a little bit because you are asking for a waiver under section under 18 U.S. Code, section 208

(b) (1), with respect to any possible conflict that might be inferred from your retention of an interest in the stock of Townsend-Greenspan Co., Inc.

We will talk about that a little later, but I mention that because it does seem to be a qualification of your statement that you have no interest or holding that would constitute a conflict of interest; is that right?

Is there anything other than that?

Mr. GREENSPAN. Mr. Chairman, at the point of confirmation, I will be selling all holdings which, in any conceivable way, aside from the issue which you have just discussed, can be considered even a potential conflict of interest.

The CHAIRMAN. I think your statement is quite full on just what you plan.

Now, Mr. Greenspan, if confirmed to this office, will you be ready to respond to invitations from this committee to appear and testify without reservation?

Mr. GREENSPAN. Yes, sir.

The CHAIRMAN. I may say we ask that question of all appointees and not just you, but we have to have a record that we did ask you and that you would say you would be willing to appear.

Mr. GREENSPAN. I would consider it a privilege, Senator.

The CHAIRMAN. Fine.

And we'll probably be having you up here and before the Joint Economic Committee, of which some of us on this committee are members.

I have followed with a great deal of interest some of the things that have been written about you since the announcement was made of your nomination and I have been particularly interested in some of the things that you said regarding inflation. I suppose that will be your No. 1 task, in the position you would be holding, to get us out of this ruinous inflation. You and Mr. Rush. I presume that will be the number one task for both of you.

Can you give us some ideas as to how we are going to stop this runaway inflation?

Mr. GREENSPAN. Mr. Chairman, I certainly concur that the Nation's No. 1 problem is inflation. We can scarcely underestimate its severe impact upon our economy. But I'm also terribly concerned that the United States cannot hold its existing economic structure or, perhaps, even its social structure during a prolonged period of double digit inflation.

Our system basically will not hold together in the present form.

Since this is such a critical issue, we have to put every effort into finding solutions, but finding real solutions, not false ones. Not those which treat the symptoms of the problem, which give us some aura of temporary success, only to find at a later date that it was really a small little dent in the problem which merely displaced it into the future.

We have run out of short-term expedients. I fear that the problems that we now confront are going to require some fairly rigorous attempts to suppress what I consider to be the causes of inflation.

I think it's truly tragic that we have gotten ourselves to the point that the remedies for inflation now do not in any respect look either easy, or palatable.

I don't think we have, so far as options with respect to economic policy, easy choices. Our choices, unfortunately, are choices amongst policies, none of which we would choose to follow except in distinction to policies we'd like to follow less.

The CHAIRMAN. Dr. Burns and the Federal Reserve Board, I think, have been very much concerned with this problem of inflation.

I think they had hoped that through the control of the money supply they might be able to do something about it. But I notice Dr. Burns was quoted yesterday, I believe, saying that it would probably take 2 years to get control of inflation.

Do you agree with that?

Mr. GREENSPAN. Let's say, Mr. Chairman, that I can't disagree with it.

I don't know how we can get a specific time frame. I'm fairly sure it's not less than 1 year, and I'm reasonably certain it does not have to take several years. You also have to determine the time frame in the context of the set policies which are taken.

Two years may be a good guess. If I had to put a number on it, I'd put it slightly less; but we really don't know enough to make that fine a distinction. It's a long time, and there's no alternative.

The CHAIRMAN. Do you have any comment on the action of the Federal Reserve regarding the money supply.

Mr. GREENSPAN. Mr. Chairman, I subscribe to the general policy which the Federal Reserve has embarked upon.

I see it as an attempt to suppress the expansion of the monetary aggregates, to suppress the underlying expansion of credit, which essentially feeds inflationary forces.

I hasten to add, however, that it's a mistake to believe that somehow that's what inflation policy is all about, and that the Federal Reserve is capable, wholly independent of what's happening in the capital areas, to sustain a limited noninflationary money supply growth.

The CHAIRMAN. I believe it's been suggested from time to time that there ought to be some system devised on allocation of credits.

Do you have anything to say about that?

Mr. GREENSPAN. I think it's very difficult to get results in that direction—

The CHAIRMAN. It's pretty hard to do in a private enterprise system; isn't it?

Mr. GREENSPAN. Yes, Mr. Chairman. We have such an efficient flexible financial structure, granted all its imperfections, that it's exceptionally difficult to compartmentalize various parts of the credit markets; that is, if you attempt to segregate out certain elements in the capital market to be given higher priorities than others, what occurs is market readjustments which tend largely to eviscerate the effects that you seek to achieve.

I don't deny that it has some effect, but I think that, in the broad context, it's not an efficient instrument to allocate resources which, of course, it is ultimately attempting to do.

The CHAIRMAN. Mr. Greenspan, the Council of Economic Advisors was created under the Full Employment Act of 1946, the Joint Economic Committee of which both Senator Proxmire and I are members was also created under that Act.

And Congressman Brown, who just testified, is a member of that committee. Senator Brock was at one time, but he left.

Senator BROCK. I left the House.

The CHAIRMAN. Oh, it was while you were in the House.

I was one of the original members. Wright Patman and I are the only two original members of the Joint Economic Committee, and we were appointed in January, 1947 when it was established.

By the way, the chairman at that time, I know the Republicans will be interested, was a man who served for many years on this committee, Bob Taft, a very able man.

Oh, and this might be of interest, too. When we tried to get the Chairman of the Council of Economic Advisors to come up and testify, they declined. It took us, I believe, 3 or 4 years to get that worked out to the point where they would testify.

Maybe that helped originate the question I asked a while ago if you would appear and testify.

But do you feel that that act has worked well?

Mr. GREENSPAN. It's difficult to say, Mr. Chairman, because as you recall, the act specifies the policies which would maximize employment consistent with stable price levels.

Now, I would certainly say that the levels of unemployment on average since the act was initiated, are reasonably good; but I would say that our success in achieving a noninflationary environment, in the context of that original legislation, has been poor.

The CHAIRMAN. Let me say this: Even though it was called the "Full Employment Act, it was never thought it meant really full.

In fact, as I recall back in those days, the economists used to say if we had unemployment, not more than 3 and 3½ percent, I think it was; that that would be satisfying the requirements of the law.

I remember, too, back in those days we used to have some very fine economists testify and one of them, Seymour Harris, was it, of Harvard, I think created a great flurry throughout the country by suggesting, I think they called it, "creeping inflation."

I think his testimony was to the effect that we were bound to have some inflation, and that we could expect it more or less to climb.

Again, I never did think it would climb to such levels as it has attained now.

And I earnestly hope that we can get those levels down. I'm interested very much in your testimony, and I look forward to your being a very capable, able member of that Council.

Mr. GREENSPAN. Thank you very much.

The CHAIRMAN. Senator Proxmire?

Senator PROXMIRE. Thank you, Mr. Chairman.

Mr. Chairman, I want to alert the committee that I expect to take some time in questioning Mr. Greenspan. I apologize if my questions will seem in detail; but, as you said, he will be chairman of the Council of Economic Advisers; he will come before our Joint Economic

Committee; and it's of great importance that we understand him and his views be as much as possible on the record.

Senator BENNETT. Can you give us some estimate of the amount of time?

Senator PROXMIRE. I think 40 minutes and, perhaps, longer.

Mr. Greenspan, in the first place the big problem that was referred to in the press this morning, should the Senate hold up confirmation to give the new President, if we do have a new President, and there's some indication that we will, an opportunity to have his own chairman of the Council of Economic Advisers.

The talk which we never know if it's correct or not indicates that the President may be replaced within a day, 2 days, a week.

Under these circumstances, I just wonder if we should go ahead with the confirmation of a man who is intimately attached to the President and who is his principal economic advisor?

What's your view?

Mr. GREENSPAN. Senator, that's clearly outside my province.

I certainly understand the dilemma that's involved here because it's obviously fairly clear; but I don't know any way I can answer that question.

Senator PROXMIRE. Will you withdraw if President Nixon leaves office?

Mr. GREENSPAN. Obviously, depending on when or if that happens, I will tender my resignation to the President.

Senator PROXMIRE. Have you discussed your tenure with Mr. Ford? Is he aware at all of your position?

Mr. GREENSPAN. No, sir, I have not.

Senator PROXMIRE. Have you ever been associated with Mr. Ford in any way?

Mr. GREENSPAN. I have not been associated with him, but I have discussed economics with him, yes, sir.

Senator PROXMIRE. You have discussed economics with him.

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. Can you give us some rough idea of the extent to which you have discussed economic policy with Mr. Ford?

Mr. GREENSPAN. It really represents one discussion over maybe an hour and a half, of my views on what I thought the nature of inflation was and what remedies I thought were required in order to bring it under control.

That was largely the nature of our discussion.

Senator PROXMIRE. On the other hand, you have been advising President Nixon or been discussing economic policy with President Nixon for many years; is that correct?

Mr. GREENSPAN. With the President, but much more extensively with other members of the Administration in an economic capacity.

Senator PROXMIRE. Now, first, I want to commend Mr. Rush for his appearance here this morning, and I realize that he and the President had a view about executive privilege and about whether or not Mr. Rush should testify at all before the Congress.

I think you have made the right decision, and I deeply appreciate your presence here and the fact that you have testified before the Joint Economic Committee.

I consider that most cooperative and helpful. I would like to ask you, Mr. Rush, because, as I understand it, the assignment which you had was one of being the principal direct advisor to the President on overall economic matters, what will be the working relationship between you and Mr. Greenspan?

Mr. RUSH. I would expect to work with Mr. Greenspan daily. I would expect to see him at least once daily if we're both in town. I would expect also that Mr. Greenspan would be in direct touch with the President, would advise the President directly and, obviously, in my own advice, I would take into full account Mr. Greenspan's views; and I would assume that he might take mine into account when he talks to the President.

I feel, frankly, that it's far better to have a full expression of views than a seemingly false appearance of unanimity; and I would expect Mr. Greenspan's views to be fully available to the President and—

Senator PROXMIRE. Mr. Greenspan, is it your understanding that you would have frequent direct access to the President?

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. Do you feel you will primarily advise with Mr. Rush and see that the President consults you less often than he would in view of the present organization of economic policy?

Mr. GREENSPAN. Senator, the means by which I convey what I think are the important economic issues will probably vary depending on the particular circumstance.

In many instances, the function I conceive for myself will be the development of technical questions and technical options more in an analytical framework, at a level of complexity, which, I think, will be far better presented to the other economic advisors rather than directly to the President. So I hesitate to generalize because it really depends on the circumstances; and I would endeavor to find the best means by which I think policy options could be most effectively implemented.

Senator PROXMIRE. Perhaps you could help us with something that I think is troubling many, many people in our economy and throughout the world.

Recently there's been all kinds of very unfortunate disclosures, but one disclosure that troubles many is the President's reported indifference to economic policy recorded in the tape report of his remarks about the Italian lira.

On the basis of your discussion with President Nixon and your view of your job, would you feel that it would be desirable for that reason to work primarily with the other advisors and then have Mr. Rush carry some kind of consensus view to the President that's been simplified or do you think that your discussion with Mr. Nixon should be direct and, say, weekly?

Mr. GREENSPAN. Well, I must say in my conversations with him, either at meetings or other times, I found his grasp of the subject matter a good deal greater than I think the public press implies.

I can't say I know the President that well and certainly not as well as Mr. Rush; but my experience has not been the type which you have just suggested.

Senator PROXMIRE. Mr. Rush, would you be willing to appear before this committee and testify in view of the fact that you do have such a vital top position on economic policy in the Administration.

Mr. RUSH. Yes, I'll be pleased to, Senator Proxmire.

I would consider it a privilege to appear.

Senator PROXMIRE. Now, Mr. Greenspan, you furnished at my request a client list for Townsend-Greenspan and Co. It's a very impressive list. Do you have any objection to that list being made public?

Mr. GREENSPAN. I would prefer that it not be.

Senator PROXMIRE. Would you mind if I generalize without referring to specific firms then and certainly to the area of representation?

Mr. GREENSPAN. No problem whatever.

Senator PROXMIRE. This includes the biggest banks in the country. It includes a number of very large manufacturing firms, including some that are in a very concentrated position in their industry; isn't that correct?

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. I wish you would spell out for us because, as I understand it, you own 99 percent of Townsend-Greenspan, and you would go back to them after your term of service on the Council of Economic Advisers.

Is that correct?

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. Under those circumstances, I think it would be helpful if you would indicate what your service to these firms represent.

You just simply make economic analyses for them. What kind of economic analyses do you make? Do you ever represent them in any way on economic policy before any kind of government agency.

What do you do?

Mr. GREENSPAN. No, I made it a general practice, Senator, not to represent them in any way with respect to a particular issue before a governmental agency.

As a consequence of that, I deal largely in economic consulting, both on a macro and on a micro basis. It varies from company to company; but, specifically what it would be, for example, in a major industrial corporation, would be to develop fairly elaborate econometric models of the markets into which these companies sell, endeavoring to try to determine layer upon layer the way the particular industry functions, largely attempting to ferret out where various changes occur, where they are significant and, in a general way, try to determine what type of market forces create the physical volume of sales that these companies can sell.

The major purposes for these types of services include facilities planning, long-term financial planning and elements such as that.

Senator PROXMIRE. You're the first business economist ever to serve as Chairman of the Council; is that correct?

Mr. GREENSPAN. That's my understanding, Senator.

Senator PROXMIRE. You have asked the President for a waiver pur-

suant to 18 U.S.C. 208(B) (1), with respect to any conflict of interest that might occur during the period of your service.

Can you be more explicit as to what type of conflict might occur that necessitates a Presidential waiver?

Mr. GREENSPAN. Yes, I think that I have been a consultant to a large number of companies, the list of which you have. I have specifically requested that the company which I created 20 years ago not be liquidated during my term of service because there are a great number of careers involved in that other than my own.

Now, because that firm will continue in existence during my tenure of office, there is a clear potential conflict of interest in my serving in this particular position and what I had attempted to do is to completely sever all connections with the firm; that is, leaving aside the specific legalities because that's basically framed in certain forms.

But my basic purpose has been to resign from the company, put all potential gains, if any, completely out of my reach; not only during my government service but through perpetuity; and request that only in the event that something severe occurs with respect to the company that there be some mechanism through which that can be communicated to me.

Senator PROXMIRE. Why is a waiver required?

Mr. GREENSPAN. I'm not certain, Senator.

I'm not familiar with the legal requirements pursuant to my request.

Senator PROXMIRE. Isn't it true that many economic forecasts require assumptions about the direction of Federal economic policy and isn't it, therefore, possible that the business of Townsend-Greenspan could increase because you had access to inside information.

And, while you wouldn't have any sharing under what profits accrued under those circumstances, isn't there a momentum involved here? Wouldn't it obviously carry over when you go back and resume your virtual full ownership?

Mr. GREENSPAN. Senator, you have to distinguish between what would happen after I left government service in either condition.

If, for example, I am successful in government service, as I certainly hope I shall be, I would inevitably expect that, as has frequently happened in the past, that success to be reflected subsequently in my success outside of government. I don't deny that, and I think one probably must assume that.

The basic question, however, is whether or not the particular level of business which might occur when I leave government service would be effected by the business level of the firm during my period of government service; and I might also say that it presupposes that I'm successful in what I'm doing.

There are clearly risks involved, and it's hard for me to frankly envisage how, under any circumstances, I can conceivably come out of this particular service in an improved financial state. What I am attempting to do is to limit the losses, not in any way enhance my financial capability.

But in direct answer to your question, Senator, I don't see what I

can do other than communicate, as I certainly intend to communicate, that all contact with my firm will be completely severed. I will have no discussion with them. I will have no contact whatever.

Any inference which somebody might make that the firm has some inside knowledge, I hope they will soon learn is false, as I suspect they shall.

Senator PROXMIRE. Now, in doing this service for your clients, as I understand it, you, of course, have to take into consideration, because they're profoundly affected by Government tax policy, by regulatory policy, by antitrust policy, by consumer protection laws, monetary policy, trade policy, environmental policy regulations, major foreign exchange, business subsidy, labor management, wage-price controls, Taft-Hartley, policies with respect to energy, atomic energy, all of these elements are elements in which you would have a very strong voice as chairman of the Council of Economic Advisers; and all of these elements would effect these businesses rather profoundly; isn't that correct?

Mr. GREENSPAN. I think that they will undoubtedly affect almost everybody, not only the businesses who are currently my clients, but almost everybody else.

Senator PROXMIRE. My point is you have no clients who are labor unions, State or local governments, small business groups, small business associations, consumer groups or environmental groups; is that correct?

Mr. GREENSPAN. That is correct, sir.

Senator PROXMIRE. Your clients all tend to have similar views with respect to tax, antitrust, consumer protection and so forth. That is, roughly, with a few conspicuous exceptions, they are similar?

Mr. GREENSPAN. I would say that is so.

Senator PROXMIRE. In general, their interests would be lower taxes on business, less vigorous antitrust laws, no consumer protection agency or other consumer protection policies, ease up on environmental protection pressures, no price controls, little or no jawboning, continued export import subsidies; isn't that generally your position?

Mr. GREENSPAN. I think it would be a mistake to generalize that everybody's opinions are the same on those. In fact, it's quite likely that mine are quite different and have been quite different from theirs on many or most of these issues.

In fact, you may recall, Senator, that most businesses were in favor of wage and price controls in 1971. I would say in that respect I disagreed with most of my clients.

Senator PROXMIRE. Well, of course, an awful lot of them were against it.

Mr. GREENSPAN. No, they are certainly against it now however.

Senator PROXMIRE. NAM took a position in favor; is that correct? And there were other business groups that did favor it at that time, you're right.

But, generally, now and with exceptions like that——

Mr. GREENSPAN. I certainly agree with the thrust of the remarks you're making.

Senator PROXMIRE. What I'm saying is that the position that these firms take is often contradicted by labor unions, consumer groups, environmental groups and so forth.

Senator BENNETT. Will the Senator yield?

Senator PROXMIRE. Yes.

Senator BENNETT. It's my observation that labor unions have their own economists; environmental groups and consumer groups do not employ economic counselors.

So you can't scold him—

Senator PROXMIRE. No, no, I'm not scolding Mr. Greenspan at all. Not one bit. I'm trying to get as clear a picture—

Senator BENNETT. The inference in your question is—

Senator PROXMIRE. If that's the inference, I'm delighted that the Senator from Utah has given me a chance to clarify.

Obviously there's no criticism of you for making a living, and a very good living at that, and being highly competent in making that living.

I envy you—no, I don't envy you—I admire the great success you have had.

Mr. GREENSPAN. Thank you, Senator.

Senator PROXMIRE. Now, let me go on to say in light of this, on the basis of your writings and your speeches and so forth, I get the impression that you too have a very clear and consistent economic philosophy, the consequences of which I often applaud.

I think you cutting down on Government spending now was wise, trying to reduce the role of the Federal Government was good and necessary and desirable. But many of these views may seem rather harsh and, especially, in the context in which we find ourselves now.

Men in public office find that they are best served when they hear a variety of informed opinion. The worst thing that can happen to them is to become isolated or to hear only the views of their allies and supporters.

I have always believed that a President is best served when he is told the truth and when he gets opinions from competing interests in the economy.

Now, the thing that troubles me most about your appointment—and you're an able man, competent man—is just this point. The people who disagree with your economic philosophy applaud your ability and honesty and competence. The President has surrounded himself by a group of economic advisors who essentially come from the same background of big business.

There is Mr. Ash of Litton, Mr. Rush of Union Carbide, Mr. Simon from Wall Street, and now Mr. Greenspan, a business economist whose clients are among the biggest businesses in the country. You're the four principal men.

One or even two men with such a background ought to be in the Cabinet even of the most liberal and progressive President. But if all of them are from the same background, is the President really getting the best possible advice, a conflict of views and opinions, and a basis on which to make good policy that would serve the whole country? How about that?

Mr. GREENSPAN. I understand your concern, Senator, It's important to have a broad spectrum of views and, while it's certainly true that I have a consistent economic philosophy, much in line, I would suspect in most instances, with the existing advisory group to the President, I, nonetheless, think that perhaps just because of that it's incumbent upon me as Chairman of Council of Economic Advisers, to search around for an appropriate spectrum of views.

It's quite sterile for people who fundamentally agree with one another to discuss what they think about the world at large, because there is a tendency for one to learn very little from people with whom you agree.

As a consequence of this, I have sought and will continue to seek views which clash—in fact, the more, the better—with my own views. Because the way one learns the truth is by confronting it with opposing views.

Senator PROXMIRE. What you're telling me is in the present context you wouldn't nominate Alan Greenspan. Not because you're not a very competent man, but because all of the people around the President have the same views.

Mr. GREENSPAN. Well, Senator, one of the reasons that I was very reluctant to accept, was that my views tend to be quite similar to everybody else's.

I didn't appoint myself, obviously. Having accepted, I accepted only in the context that, while my views are well known, I do and shall attempt to bring the full spectrum of the economics profession's views, which I know quite well to the President.

In most instances, I do agree with them; but there are differences.

Senator PROXMIRE. All right, let me be specific.

This was a year ago, July 13, 1973, you said, "What the economy badly needs is a strong dose of do-nothingism."

Mr. GREENSPAN. That is correct, Senator.

Senator PROXMIRE. Is that still your view?

Mr. GREENSPAN. Let's be very specific on what that terms means.

You may recall that was the time at which we were coming out of a period of two freezes and several phases and what we had then and, in fact, what we still have as an aftermath, is a shambles.

The shambles essentially resulted from an overzealous attempt to manipulate the economy in a very specific way. What I meant then in the context of that period was to drop the whole elaborate control structure, which I am delighted that we have done.

Now, do-nothingism, in that sense, which is unfortunately not a terribly philosophical term, represented only that particular context. I think a great deal has to be done now, because if we don't, if we continue in the direction in which we are moving at this particular point with no changes in the way we handle our Federal Budget and a number of the other policies which are in place, we are in very severe trouble.

Senator PROXMIRE. Fine. Now, I'd like to take you down the line and see what you would or wouldn't do.

Yesterday morning Mr. Kauper, head of the Justice Department's Antitrust Division, urged a revision of the antitrust laws to remove

some of the serious antitrust violations and shorten the time it takes to file those cases.

Do you support that?

Mr. GREENSPAN. No, especially not as an anti-inflationary device, Senator.

I don't think that makes much difference. If one is interested in the effects of monopoly on the price levels, one should be looking at subsidies in the business area.

Senator PROXMIRE. Do you disagree with the analysis that Mr. Kauper and Mr. Scherer and Mr. Thompson of the Federal Trade Commission and others, who have said that price fixing by business is costing the Federal Government, in Mr. Scherer's estimate, 6 percent of the gross national product? So it's like a sales tax of 6 percent on everything we buy—I should say, costing the economy.

I meant costing the gross national product. We waste 6 percent, in his judgment, based on his analyses.

Mr. GREENSPAN. Senator, I think it's most inappropriate for me to comment on things which I have not seen. All I can indicate to you is that that number seems incredibly large, and I would frankly doubt it.

Senator PROXMIRE. I think you might fault him on the number, but I understood you to say that antitrust policy is irrelevant to inflation and, obviously, these people think it is very relevant to inflation.

Mr. GREENSPAN. Yes, I would think that the effect on the price level has got to be negligible.

Senator PROXMIRE. Negligible?

I see.

Mr. GREENSPAN. This is not an area in which I would consider myself an expert, and I must say that there are a number of different types of policies with which—

Senator PROXMIRE. Let me give you another specific example of this.

Antitrust action—the threat or the reality of it—coupled with jawboning, coupled with procurement policies, were among the ingredients that enabled President Kennedy to roll back steel prices in 1962.

It had some effect on this bell weather element of inflation. Do you think that kind of action by a chief executive would be irrelevant with respect to inflation?

Mr. GREENSPAN. Yes, sir; it is. It's treating the symptoms of the problem; and, while it may appear to adjust a specific price index for a specific period of time, if you take the full context of the period involved, you would ultimately find that its effect on, one, the general price level; or, two, the price of steel is not visible.

Senator PROXMIRE. Then, in view of the fact I think inflation is our number one problem and you regard it is important too, would you agree with Mr. Kauper's announcement that he intends to conduct a major effort aimed at uncovering price fixing and other anticompetitive actions in major national industries? Would you support that?

Mr. GREENSPAN. No, sir; not as an anti-inflationary device.

Senator PROXMIRE. No, I'm saying, would you support it? Let's forget about the anti-inflationary device.

Mr. GREENSPAN. If somebody asked me, which I doubt, I would say no.

Senator PROXMIRE. All right. Why?

Mr. GREENSPAN. Other than having basically no effect on inflation, it has very little effect on creating a type of competitive environment which is essential for the creation of the highest standards of living for the American people.

I have fairly extensive views on the subject, but let me see if I can summarize them in a somewhat truncated way.

In the full context of a free market system, there are extraordinary adjustment procedures, which tend to make monopolies exceptionally difficult to maintain. However, there are differences, and I would distinguish between two types of monopolies. One, I would call a coercive monopoly. A coercive monopoly by my definition is the type of a monopoly which maintains prices higher than the market would allow wholly because of the ability to restrict entry or a number of other practices with which we are familiar.

Senator PROXMIRE. Take the steel industry. It's been charged they are costing \$1.25 billion in higher price because of their price leadership and effective price collusion.

They increased their prices by 30 percent.

Mr. GREENSPAN. Actually, it was more than that.

Senator PROXMIRE. 31.8, but it's in that area.

It's the biggest increase in the history of our country by the steel industry ever in any year.

This is an industry that certainly is not competitive in their pricing practices or would you say they are?

Mr. GREENSPAN. Well, Senator, yes and no. First of all, let's define as best we can at least in a theoretical sense what is the appropriate steel price level.

In other words, when we talk about issues of any individual industry's price being excessive or suppressed or something like that, it's important to specify what the standard is. I would say the the appropriate steel price level for our economy is that price which would generate a sufficient rate of return which would enable new facilities and capacity to come onstream in order to meet the demand that our economy has for steel.

I don't know where that particular price is for steel at the moment. I was reasonably sure as of maybe a year or so ago, certainly during price control phases, that the actual published, realized price for steel, was below the equilibrium price; and, in fact, that was one of the major reasons why there was a significant diminution or inability to expand capacity.

Now, under those circumstances, I would certainly say that a significant price increase in steel was required if we are to maintain an adequate amount of steel capacity and steel-producing capability in the United States.

Now, I must say I don't know whether the particular price in-

crease that we have had in the last year is too much, inadequate or just right.

Senator PROXMIRE. Let me ask you this one, Mr. Greenspan, and see if you can bat it back over the fence.

The steel industry has increased its prices by 30 percent this year, chemical industry by 30 percent—29 percent. A fantastic increase. Nothing ever like it.

Wages may be increasing 10 or 12 percent. Nonferrous metals increased their prices 48 percent. Oil by 82 percent.

Now, these are all more or less concentrated industries. These are all enormous increases, increases in which no fiscal policy, monetary policy, no practice of restraint from the Government is going to have any impact at all. There's no way in a reasonable period of time that steel price could have been modified no matter what policy the Federal Government had.

Mr. GREENSPAN. I agree with that.

Senator PROXMIRE. It would seem to me that these are prescriptions or decisions on the basis of a completely free market with a supply and demand curve that there's a degree of independent price determination here.

So this is why it seems to me that the concentration problem is so critical with respect to inflation.

The CHAIRMAN. Senator Proxmire, Senator Bennett is going to have to leave.

Would you yield to him?

Senator PROXMIRE. Yes, I indicated I was going to take a long time.

Would the Senator permit Mr. Greenspan to answer that question in fairness to him and then go on?

Mr. GREENSPAN. Let me see if I can distinguish between the general effect of inflation and the specific prices themselves.

The level of inflation, the general price level, which confronts the American public is essentially a function of the amount of money in the system.

It's a fiscal financial phenomenon, not of specific prices.

Now, what I mean by that is that there is a sense in which the total average price index is determined independently of its component parts; and, as a consequence, when you get into the situation in which we have very dramatic increases in prices such as you quote, there are two things that happen. First, if the price increases are not accommodated in the financial system, other prices fall relatively. Secondly, if the financial system does accommodate it, then you can argue that that really is the cause of inflation.

The reasons for specific price increases, come from a different sort of thing.

The sharp increase in nonferrous metal prices are owing to shortages of facilities, and hence an attempt to return to an equilibrium price. Some of the chemical prices reflect huge increases in world oil prices. A number of the others have specific reasons which I will be glad to get into at another time; but, more to the point and to confront the thrust of your initial question: While there is unquestion-

ably some discretion in what major industrial corporations can do with respect to their prices, the concept that there is some arbitrary price setting procedure wholly independent of the market is not the way the system functions as I see it in working with a number of corporations.

Unfortunately, it varies from industry to industry, but one large important constraining influence is a phenomenon, which every large corporation is aware of; namely, that it's very difficult for the major company within an industry to hold its market share.

The history of American business has largely been that the major producers, the sole exception actually is motor vehicles, have been consistently losing their market share; and the reason for that is when smaller companies like smaller steel companies decide that in a slack market they want to improve their business, they cut prices; and it confronts the large companies with a very difficult business decision of whether to match the price cut of the small guy or to lose business.

Now, in part, it works both ways; but what happens is that rather than dominating their industry as is often maintained, we find that the ones who are really capable, really, of functioning are the smaller producers, and medium-sized producers; and, hence, the price making mechanism in these industries while admittedly complex and admittedly partially optional, is nonetheless something which is determined not in a semicollusive way but, rather, by a mechanism in which competition does function.

Senator BENNETT. I have lost my time.

I have to leave. I just want to make two comments. I come from a State that has a steel mill and the largest open pit copper mine in the world. The American price in copper is below the world price.

The Federal government has helped keep it down by selling copper out of a stockpile and that's an artificial price.

The pressure I have at home is why can't the States' copper prices rise to the world copper price. They consider prices that have been terribly depressed under the presence of Japanese competition.

The Japanese have saturated the west coast markets.

While this hasn't affected the whole level since this is the U.S. Steel unit, it has obviously affected the income of its parent corporation so these are factors which, I think, help create the pressures to keep our domestic prices down, which neither you nor Senator Proxmire have mentioned; but in these two specific cases, they have been very real factors.

Mr. GREENSPAN. Senator, I certainly agree with the issue of steel.

That's certainly the problem, as you suggest: imports. The copper price, however, is a different sort of phenomenon. The American copper prices are fixed by producers in an attempt to make them relatively stable rather than fluctuating as violently as they do on the London Metal Exchange. The reason for this is that producers found the unreliability of copper pricing tended to shift business from copper mill products to aluminum.

As a consequence, a number of years ago many copper producers felt they had to find a way to stabilize the price to enhance the growth of copper business in the United States.

What we see today is that sort of phenomenon where the American producer price tends to be a much more stable nonfluctuating type of price, an averaging out against the world price; and, at this point, of course, it is well below or still below the world price.

Senator BENNETT. What you're saying to us then is that this is an instance in which the capacity of the producer to determine the price is used to keep the price down rather than keep the price up.

Mr. GREENSPAN. Yes, sir, and the reason for it is that price determination in the business is not to maximize profits in the short run.

The way in which the system functions best for a company is to try to maximize profits over the long term life of its facilities, and you rarely find that maximum returns occur, by attempts to get short-term profits.

Maximizing short-term profits, almost invariably is a wrong business decision, if profit, in fact, is the standard.

The Chairman. All right. Senator Cranston?

Senator CRANSTON. I am delighted to have this opportunity to hear your viewpoints beyond those we had in a conversation yesterday.

We were discussing the matter of a balanced Federal budget. I have been one of those supporting those efforts and supporting the efforts to cut us back to \$295 billion. You indicate that you believe we should do this but when you take the Federal budget in the context of the GNP, that is not a decisive matter in terms of inflation.

Would you restate those views for the record?

Mr. GREENSPAN. Yes, Senator.

First of all, let me just preface my remarks by saying that I believe the major underlying cause of the inflation which confronts us at the moment has been an excessive acceleration in Government borrowing, both direct and through guaranteed programs.

When governments tend to preempt an ever-increasing part of private savings as they have been private borrowers are forced to move to the commercial banking system to obtain funds to maintain their business activities.

This induces very considerable pressure on the banks who, in turn, attempt to acquire reserves from the Federal Reserve, which pressures the Federal Reserve to expand the so-called monetary base, which, in turn, accommodates an excessive increase in the money supply. As a consequence, it's most urgent at this stage that we suppress the growth in Federal spending and Federal guarantees and, hopefully, and if at all possible, to try to augment private savings by running Government surpluses.

Now, this is not something which can be realistically accomplished overnight.

What we need is a major change in our methods of constructing the Federal budget, and I applaud the Congress for an excellent bill, which, is going to make it far easier to create a sensible level of Federal expenditures in the future.

I think the Budget Control Act, in my view, has the potential of being perhaps the most important legislation passed in many, many years because, within it are the seeds of solving what I consider to be a virtual hemorrhage in Federal expenditure policy.

Now, while I think the emphasis should be clearly on reformulation of procedures which can't be effective for the fiscal 1975 budget. But anything that can be done for the fiscal 1975 budget, whether it be cut by 5, 10 or more billion, should be done; the more, the better.

The reason I would not overly emphasize the fiscal 1975 budget is that it's definitely my second priority. The first priority is to construct a means of Federal budgetary control so that we are never confronted with this problem of always trying to have to chop off 5 billion, 10 billion, 20 billion.

The issue should never come up, and it should be sort of fended off at the pass before the problem arises.

It's been suggested that a cut in the fiscal 1975 budget, if it's only, say, \$5 billion or even \$10 billion is negligible relative to the gross national product: and, hence, to theoretically not have any impact upon the issue of inflation.

However, I think that the GNP is the wrong denominator to compare it with. The appropriate number is far smaller and represents the level of private savings which is a fraction really of the total GNP. Moreover, reducing expenditures by \$5 billion would remove \$5 billion from the financing needs of the government and what I would call the most interest rate insensitive parties of the demand for funds in the capital markets. The resultive impact upon the total capital markets, on the mortgage markets, on the financing structure of our system, really would be quite out of scale with the seeming small amount of money involved.

So it's a mistake to view the type of numbers that we are looking at as being inconsequential. They would be inconsequential and perhaps not worth the effort if nothing else were done with respect to budget; but there is no reason why we cannot proceed simultaneously on the far more fundamental budgetary reform procedures; and, at the same time come to grips clearly with the level of the fiscal 1975 budget.

Senator CRANSTON. Do you think the psychological impact of an act that balances the budget is important in its economic ramifications as much as the direct economic effect?

Mr. GREENSPAN. Senator, yes and no.

There's no question of the desirable psychological effect; but the psychological effect comes from the economic effect. In other words, if the budget were balanced and nobody knew it, the effects would still be there.

Now, they would be delayed. The psychological approach tends to anticipate the real effects, tends to induce the markets to move sooner than they ordinarily would in expectation of the ultimate effects; but the ultimate effects seem to be pretty much the same psychology notwithstanding.

Senator CRANTON. You spoke of Government guaranteed loans as one of the main sources. Which loans are you talking about specifically?

Mr. GREENSPAN. This extends across the entire spectrum of government guaranteed loans, from the Federal Home Loan bank borrowing to the Lockheed loan. Anything that has a Government guar-

antee associated with it comes to the capital market or money market as though it were a Treasury security; and, as a consequence, the impact, whether it's a direct Treasury issue or an agency issue with de facto guarantees, the impact is indistinguishable. These various instruments are indistinguishable in the capital markets.

Senator CRANSTON. You would include FNMA and GINMA and the Export Import Bank.

Mr. GREENSPAN. GNMA would be—the answer to the question is yes. In that sense, all of those types of industries have——

Senator CRANSTON. Were you separating out GNMA?

Mr. GREENSPAN. I was referring to the fact that it has a different legal status but for economic considerations, it is the same.

Senator CRANSTON. In terms of the consequences of the Federal Reserve Board policies which lead to higher interest rates, you indicated yesterday when we were discussing this that you recognize there were certain short-range results that may be inflationary; but you feel the long-range results are the opposite.

Would you expand on that? What are the short-range inflationary results and what are the long-term anti-inflationary results?

Mr. GREENSPAN. Yes, Senator, there has often been confusion on the problem of whether interest rates are inflationary or not and in a certain sense they are both, but the time frame is different.

In the very short run there is no question that to the extent that Federal Reserve policy leads to higher interest rates and to the extent these higher interest rates work their way through the market place and do tend to be marked up in the price levels that prices are increased by more than otherwise would have been the case.

In the longer run and, here I'm suggesting maybe 6 or 9 months, what occurs is that the monetary policy which engendered these higher interest rates is essentially a policy which is restricting the growth money supply and of credit and hence total demand.

As I indicated earlier, it's the expansion in the level of the so-called money supply or more exactly of the unit money supply that is money supply relative to physical production, which, ultimately, determines the price level.

While the short-term result of suppressing the money supply may be an increase in prices the longer term effects far more than offset these and you find that the effects of restrictive monetary and credit growth do indeed suppress the level of prices.

Senator CRANSTON. Mr. Chairman, I think my time is probably about up.

The CHAIRMAN. Senator Stevenson?

Senator STEVENSON. Mr. Greenspan, you blame much of the inflation on government borrowings. The Exim Bank borrows through the Treasury and, of course, it subsidizes the export sector.

Should the subsidies of the Exim Bank in that sector be suspended?

Mr. GREENSPAN. Senator, there's more than economic policy in the Exim Bank, as I understand it. I presume that there are a number of areas of foreign economic policy which are involved, and I must say at this point I don't feel myself competent.

Senator STEVENSON. Let's leave aside the use of the Exim Bank for political and foreign policy purposes.

I grant you that there are legitimate purposes which can be achieved in that regard.

With regard to the remaining activities of the bank, would you suspend them?

Mr. GREENSPAN. I don't approve of that sort of subsidy, Senator.

Senator STEVENSON. Thank you.

Now, getting back to wage and price controls, you have reiterated your opposition.

The question before us is not so much one of wage and price controls as it is to adopt some sort of stand-by authority, authority to impose wage and price controls or simply keep the broom in the closet.

Arthur Burns has suggested that the Cost of Living Council or some agency be activated to monitor and exercise standby authority. I think he suggested some authority which could at least temporarily defer wage and price increases.

In other words, wage and price controls. Do you agree or disagree with Arthur Burns?

Mr. GREENSPAN. Well, I have disagreed with him on the subject, and I must admit that, whenever I disagree with Chairman Burns, I double check my analysis.

Having double checked, I must say I still disagree with him; and the reason is basically this: First of all, wage and price controls per se suppress the symptoms of inflation and ignore the causes. Nor, as is often argued, do they reduce inflation psychology. I know of no evidence which supports the view that wage and price controls do that.

And unless they do that, their value in maintaining a stable non-inflationary price level is nil.

If this is the case, as I believe, then what advantage is there in attempting to suppress prices under their equilibrium level? You are distorting and suppressing potential increases in supply, and aggravating inflationary pressures because ultimately they're going to break out and lift prices to a much higher level than you otherwise would have had.

Now, I cannot see any value in a broom if the broom itself doesn't work. I just don't see any reason why one should keep one in the closet. The mere threat that the broom is there and could be taken out and used to swat actually has the potential effect of making people concerned about being locked into a new wage and price control system.

A number of people are going to try to move to anticipate that event, and they will jack up their prices to levels which would not otherwise be sensible for them to do.

If they fear a reimposition of wage and price controls, they might say that while it is in our short-term disinterest, it is in our long-term interest to raise prices now.

Senator STEVENSON. Are you opposed to the monitoring sup-

ported by Arthur Burns and in the past by the administration, for the activation of the Cost of Living Council or some agency for that limited purpose?

Mr. GREENSPAN. I am not certain what that purpose is. Specifically, if its purpose is merely a prelude to price and wage control, I do not favor it. If it is strictly analytical or something which enhances everyone's knowledge of what the price and wage relationships are and enables them to make more sensible judgments in the marketplace, I am all for it but if it is other than that, I see no advantage.

Senator STEVENSON. Do your views about price controls extend to the oil industry? This industry has argued that high prices are necessary to create the incentives to increase the supply. The facts strongly indicate that to maintain high prices, the industry is now decreasing supply and in fact the production of gasoline has decreased below the levels of last year so far by about 1 billion gallons.

You see no necessity for any price controls on domestic oil prices?

Mr. GREENSPAN. At this stage, the world oil situation is moving into surplus. As I recall the figures, the oil product inventory situation in the United States is exceptionally heavy and I would expect that continued flows of oil at the present levels will probably reduce gasoline prices at the pump in the United States in the period ahead.

Senator STEVENSON. Well, there are many refined products in surplus, but prices have not come down, either international crude prices, (except occasionally on a spot basis), or domestic prices. What is coming down is production. Now, in those circumstances, what do you do—wait?

Mr. GREENSPAN. Yes, and let me say why. In the first instance, one of the reasons why there has been some flattening-out of refinery production is the fact that inventories have been built up and I suspect storage problems are emerging. Actual retail sales at the gasoline pump in the United States today are running slightly under a year ago.

Now, so far as the immediate short-term outlook is concerned, these conditions appear to be returning us to the type of situation which used to induce gasoline price wars or the equivalent—some significant deterioration in the price structure of gasoline at the pumps.

Now there is no question at this particular point that we have passed through a traumatic period of this gasoline crisis. We have had some very dramatic shifts in the structure of gasoline marketing.

I must say that at the moment, I do not know the effects of the various regulatory actions which have been taken, such as the various allocations and the other things which have been carried over from the winter period. As I say, I am not familiar with the full impact of these regulations, but my impression is that this is the type of environment in which prices eventually begin to become shaky so, in answer to your question I would say that as a price forecast,

I would suspect that gasoline prices are close to their peak, if not already there, and may well likely come down.

Senator STEVENSON. I think you will find that upon examination, the oil companies are dealing with the surplus by forcing it on their dealers, impelling them to sell in contravention of a national policy which supports conservation, and are cutting off and cutting back supplies to independent refiners who, in turn, supply independent markets with the loss of competition at both the refining and the marketing level. Do your views with respect to anti-trust policy and antitrust enforcement apply in this industry?

Mr. GREENSPAN. First of all, I would like to comment on something on which I had not given any study to. The jacking up of the world price of oil is not a free market situation and it has caused a terribly complex situation. As a result there are extraordinary things happening to the structure of these markets. I do not feel as though I should make any comments until I have taken a closer look at this. It is really a complex situation which changes from week to week and there is a great deal involved, not only with respect to U.S. inflation policy, but also with what I consider, at this stage, to be the most important financial problem that we face—the extraordinary generation of debt as a consequence of the oil-importing countries having to pay these particular prices. So I would much prefer to delay an answer to that, Senator, and give that whole issue considerably more study before I make any comments on that.

Senator STEVENSON. I will pass, then, the petro-dollar problem and the recycling issue to one final subject.

Again, the issue is not really, it seems to me, whether to cut the Federal budget. I do not think you will find much disagreement in the Congress. We all want to cut the Federal budget. The question is where. Where would you cut the Federal budget?

Mr. GREENSPAN. All I can say is that I don't think there are any areas of the budget which one should just automatically assume cannot be cut and that includes such things as interest on the public debt which is considered literally untouchable. When I say it is not that you cut it, but remember that even that is a function of the so-called term distribution of government debt and the way in which we do things, but this is another question which I would like to hesitate on largely because I have not had a chance to look at it.

Now, I, too, am disturbed as many people are, that everybody is in favor of cutting the budget \$X billion but it is always the other guy's program to be cut in the process.

One thing I think you have to come to grips with and fairly quickly is when you cut the budget, some program is cut. One of the things I like about the new budget control legislation is that it sets up a fairly sensible mechanism by which the Congress can determine priorities in a relatively structured form and in which there is an awareness of a total which has meaning for economic policy purposes. You then get to the issue of what the priorities are, and the Congress is now or soon will be very substantially equipped

to make the type of judgment which will hopefully deal with this point. If you are going to cut the budget, what programs do you cut?

You need something similar to the new budget authority and procedures to deal with this issue. At this stage I can give a long list of recommendations of what I think should be cut but I am not an elected representative of the people, and I think this is basically the job of the President and the Congress.

Senator STEVENSON. Well, let me ask you whether you would at least agree with this proposition: That there is in making these decisions on where to cut, there is a qualitative judgment to be made and a qualitative judgment is what has been lacking.

So, all spending is inflationary. It all attempts to increase demand, but some spending also has deflationary—at least long-term consequences.

In our conversation the other day, you indicated a general agreement with the proposition that to combat inflation at least over the long term, we have to try to increase productivity in the country, our industrial and agricultural capacity.

Some programs are aimed at increasing productivity, spending for energy research and development, for transportation, for agriculture, and so on.

Do you at least accept that proposition that we ought to, in making that decision, whoever makes it, try to take into account the impact of the particular program on inflation, recognizing that some can be deflationary, at least long-term, and that some spending, particularly for military programs and foreign aid programs, is especially inflationary because it does create the demand without any offsetting increase in productivity?

Mr. GREENSPAN. Senator, I would probably, in general, agree with the thrust of your remarks. I don't know if I would specifically—you can't take the military or foreign aid in total as differentiated from various other programs.

There is no question that the composition of the budget is as distinct from the total is not irrelevant and I think that certainly should be taken into consideration in evaluating where, if necessary, cuts should be made and I probably would generally subscribe to your overall point of view.

The CHAIRMAN. Senator Biden.

Senator BIDEN. Thank you, Mr. Chairman. I have a prepared statement I'd like to insert in the record.

[The statement follows:]

OPENING REMARKS OF SENATOR JOSEPH R. BIDEN, JR.

We are meeting this morning to hold hearings on a nomination to what should be one of the most important institutions in our government—the Council of Economic Advisors. In these times of economic distress and turmoil, not only in our country but abroad, we need the best economic advice we can get and we need the leadership to carry it out.

We carry many burdens.

The greatest peacetime inflation in our history—an annual rate of 10 to 12 per cent.

More than 5% of the workers of America are jobless—and some say it may reach 7% before the year is out.

Our growth rate has weakened—during the past week we learned that the leading economic indicators dropped four tenths of one per cent in June, the first drop this year.

The Nation's foreign trade surplus turned to a deficit in June.

Interest rates are breaking all records—hurting home buyers and business men alike.

In the light of these and many other factors, it is indeed a matter of concern that economists seem unable to point to a way out. This is even more distressing because I believe that this is what the American people want and need. They need a program for recovery. I believe that if they were given such a program, and the leadership to carry it out, they would be prepared to endure the difficulties and hardships any solution is going to require.

As a Senator I am being told by my constituents that their primary concern is inflation. They feel it when they buy groceries; they feel it when they buy gasoline; they feel it when they pay their utility bill. It is all around them. My judgment is that they want some measure of price stability—even at the cost of some loss in economic growth.

While we must take care that the present economic downturn does not become a major recession or depression, However, I believe that right now we must shift our emphasis away from fiscal policies which emphasize concern for recession and unemployment. We must shift toward policies that will cut inflation.

To this end I intend to pursue a selective course of voting to reduce government spending in this time of inflation. I recognize that every fiscal program has its own constituency. And before I am through I will be treading on all their toes—the farmers who need help because of losses they have incurred; the workers who, are understandably worried about their jobs; those who seek to bring cultural programs to people who have never had the benefit of them; those who seek public improvements in my State.

I believe that all these people with their special needs or wants also share one need in common. They need to get out from under killing inflation. So I hope to convince them that what seems a vote against their interest, is really very much a vote in their best interest.

I do not want to imply that cutting the budget will solve all the economic problems of the country and the world. I just consider it to be the first priority. We must clearly have a balanced program to deal with international monetary problems as well as other contingencies that may arise here at home.

I hope that we can explore some of these things here today.

Senator BIDEN. Mr. Greenspan, a number of the questions I had, have been answered, or at least spoken to. I have a number of other questions which would take much more than the 10 minutes I have allotted to me and assuming you are confirmed, I would like to ask for the opportunity to pursue some of these questions with you at a later time, the ones I do not get to.

Mr. GREENSPAN. I would be delighted, Senator [see p. 45].

Senator BIDEN. One of the things that I think is rather encouraging is that everyone I speak to including some of your colleagues tells me you are going to depoliticize the office which is a welcome thing. You went on to point out, accurately, as have many who have testified before in the 1½ years I have been here, that the choices ultimately come down to political choices, ones which the politicians must make and should be made by Congress on the basis of information presented.

We move from that encouraging note, that you are going to depoliticize it, and see yourself as much more—and I have read in your statement as saying, as you said this morning, a number of tough choices are going to have to be made. I assume that means you are going to present the President and/or anyone else around the President, with the various options that are available and the No. 1 thing

we have all talked about here this morning and I suspect we will talk about for sometime, is inflation.

You have indicated again this morning there are some tough choices. Can you enumerate some of these tough choices for me now?

Mr. GREENSPAN. Certainly. I think it is tragic that we have come to the point where essentially we have a relatively turgid, almost stagnant economy and a rate of inflation which, in my view, is barely tolerable.

Let me take two basic instruments that really do work, namely, monetary and fiscal policies, and describe what I think the real alternatives are. I may get scolded by Chairman Burns for moving into his bailiwick but being an ex-student of his, I am used to that, so I will go ahead in any event.

The Federal Reserve, as I see it, is confronted with a very serious problem at this stage. The pressure that is being maintained on the money and capital markets in order to ultimately return to a stable noninflationary environment brings with it very severe pressure on the financial system.

Now, in and of itself, that does not necessarily lead to increasing unemployment and, in fact, I have often heard it said that one uses increasing unemployment as an anti-inflationary device. I think that is wrong. I think it is unfortunate that anti-inflationary policies often as a byproduct, but not as a cause, create increases in unemployment and other distortions in the particular system.

Now, it would be most pleasant if the Federal Reserve had a better alternative at this stage. It would be pleasant if it could say well, there it at a risk of a very turgid, very nonbuoyant economy for the next year or two and we should therefore accommodate the extraordinary pressure in the money markets and allow credit to flow freely. I have no doubt that in the very short run we would perceive an easing in the pressure on the economy.

We might even see some modest decline in the unemployment rate and a certain aura of remission of the overall inflationary pressures and a sense of imbalances that we sense at the moment.

However, what that does is merely create a short-term benefit which would be purchased through some very expensive long-term costs. What would be likely to occur as a consequence of this major increase in the money supply is that 6 months, 12 months, perhaps 18 months down the road, we are confronted with a much higher rate of inflation and we find ourselves a year hence we would find ourselves confronting an unemployment problem which may be 5 or 6 percent, but then with an inflation rate far higher than today.

In other words, our trade off would have deteriorated.

Senator BIDEN. If I could be more specific, it seems to me, were I President, you would have not just presented me with an option, but a dictate. You have said to me my option is higher unemployment, not affecting inflation in the long run, meaning 18 months, and inflation will go higher, unless we continue a high interest rate policy.

But is there any option to the policies of Mr. Burns today and still affecting the problem of inflation? That is, decreasing it?

Mr GREENSPAN. Well, yes. This is where you get into the differences among economists in areas where the State of our knowledge is not such that there is unanimity of view.

In fact, as a practical matter I think it is necessary for me to communicate what these differences of opinion are, what the alternate economic analyses are, where they disagree and the alternative policies they point toward. You gentlemen are certainly aware of this and have heard many views which are different from mine, but if you are talking about the question of the policy options which will be presented to the administration, I think that I would tend to give the full spectrum of what alternate analyses or diagnoses are of the problem; and, therefore, what the corresponding alternative policies should be.

One more thing Senator, is that there are areas in which I am less certain that my answers are right and I think it is important for me to communicate this as well.

Senator BIDEN. That is encouraging.

I always worry about people who are sure they are right. We have had a number of people who were sure they were right and, boy, it turned out they were wrong.

You have indicated in several articles I read that you believe in the Congress that you have fiscal constituencies and they don't always produce the most sound economic policy in the Congress; and I suspect you would not exclude the administration from those same fiscal constituency pressure.

Mr. GREENSPAN. I would not.

Senator BIDEN. Now, you went on to say in one article that I read, and I believe it was a June article, an interview. It seems to me that you said, you were reported as saying this fiscal constituencies account for 80 to 95 percent of the present day inflation. First of all, do you believe that? Is that correct?

Mr. GREENSPAN. Well, let me be more general.

I believe that governmental fiscal policy in the long-term accounts for, I don't know what number, but, yes, 80 percent, 90 percent, I don't know what the number is. I believe that the basic problem which has emerged with respect to the difficulties with the Federal budget is largely the consequence of fiscal constituencies. But that is not the whole story.

Hence I would not then interpret that 80 percent of the present day inflation problem is fiscal constituencies. Fiscal constituencies is only part of the fiscal problem.

Senator BIDEN. Okay, that was my next question.

You also went on to say that there needed to be some politically disadvantageous things needed to be done to curb inflation.

I assume one of those would be to maintain policy which the administration presently has with regard to interest rates. Can you tell me what some of those other politically disadvantageous things are?

Mr. GREENSPAN. Yes, as we go on we are going to find that inevitably many of the programs which are advocated by very substantial fiscal constituencies are going to have rise much less than they have been and some instances these will have to be cut back.

That is likely to cause a great deal of problems because there are a number of people who expect certain ongoing benefits from the Federal Government. Obviously, if they get less than they expect that is going to cause difficulties.

Senator BIDEN. I suspect some of those that you're referring to would include everything from indexing in the social security system to pensions to government employees, pay rates, and so on.

Now, all of those things which we so often speak to address themselves to that segment of our economy which can be determined low, moderate, or middle income persons.

Now, is there anything that any of those politically disadvantageous things that we could do in the upper income bracket and with regard to the corporate structure of this country, which would help us curb inflation?

Mr. GREENSPAN. Well, I think—

Senator BIDEN. I have not heard it mentioned.

That's why I asked.

Mr. GREENSPAN. No, I think that the major—where I think where inflation is generated is largely in the subsidy area. In other words, I hate to get into a position where, after I'm talking about depoliticizing the Council of Economic Advisers, sitting here and discussing the issue of politics—

Senator BIDEN. I'm really not asking you to discuss the political side but if I were President, how would you respond if I said you have given me a range of options that affect this particular area of economy.

Are there any options which affect this sector of the economy?

Mr. GREENSPAN. Senator, the problem I have with the question is I don't view it in those terms. I think essentially inflation is hurting everybody and I grant there are modest differences, but once we get into the question of differentiating who gets hurt or who doesn't get hurt or try to formulate policies, the first point of view is, now what is the distributive effect of these various policies. I think we will find that we don't put the policies in place.

If you're asking me specifically do I think there are certain, what you might call tax loopholes or whatever, should we plug those or make changes, I would be willing to confront those individually; but I wouldn't know how to answer the question directly.

Maybe it's because I don't think exactly in those terms and I don't understand your question.

Senator BIDEN. Let me ask you the question this way: As I understand it, you would not support a tax reduction in any area now; is that correct, first of all.

Mr. GREENSPAN. That is correct, I must say, Senator, that is the first time, I have found myself in that position. The budget problem and fiscal problem is so severe that even though I am always in favor of reducing taxes for everybody this happens to be the one period where I feel bad about not taking the risk.

Senator BIDEN. You think you feel bad about that. You ought to be here.

I assume in conjunction with not wanting to cut taxes and your

emphasis on the need, the effect of balancing the budget, that there is a recognition effect purely from an economic standpoint that increased revenue by eliminating certain preferential treatment, could have the effect of increasing revenues which would have the effect, I assume, I'm not sure, have a diminishing effect on inflation.

Mr. GREENSPAN. To the extent that you increase revenues, other things equal, unquestionably, you improve the fiscal situation.

Let me just say, there must be, may be other consequences depending upon the specific program indicated which may have exactly the opposite effect, so it is important when we talk about tax policies not only to look at the revenue side which is unquestionably important, but to look at the other consequences as well.

Senator BIDEN. I would suspect you would put that in the same general framework which was stated as far as the budget cutting side. A cut in one segment of the budget may have a greater or lesser effect than another, or it may even have a counterproductive effect. Recognizing that, and it is so difficult to ask any kind of penetrating question in the time span we have and the amount of ground that needs to be covered, I'd like to move on to something that Senator Proxmire is dwelling on and that is the conflict of interest question and preface it by saying I have not discussed this with Senator Proxmire or anyone else, but I am concerned.

His concern is would an economic benefit inure to you as a result of your position either now or later. Would clients come to your firm 2 months later or 6 months later or 10 years later. That doesn't concern me very much, quite frankly; but what does concern me is sort of the other side about which I suspect not many people would be concerned and maybe I am off base on it.

We just said you are going to give the President, whomever he or she may be, a range of options that you think are available; and I suspect we made a recommendation on those; but however you have not taken into account the political ramifications of your suggestions.

And then you have gone on to say, we have enumerated a few, that there are tough choices to be made, tough choices implying that some sector of the economy may not like the action taken as well as another; and then we get to the point, although I have not seen a list of clients that you apparently represent a group of clients that could be generally stated to be of the same constituency; and Senator Bennett's point is very well taken that that's certainly not your fault; and there is no question of fault.

Mr. GREENSPAN. I understand what you mean.

Senator BIDEN. You get to the next point, though, that worries me; and that is that the range of options that you present to the President, are you going to really be able to present any option to him? Will you present an option to him that would have a detrimental effect upon your constituency in the short, run even though it may have a beneficial effect upon the economy as a whole and not so much in terms of your profit.

It would seem to me, I'm an attorney, if I sold all my stock in the company that I represented but yet kept my law firm, which I had

at Biden and Walsh with the expectation that depending on how things went I would go back, if I acted adversely to the interests of my clients with the recommendations to the President, I may go back and find out I don't have those clients.

That's the conflict that occurs to me.

The CHAIRMAN. Mr. Greenspan, may I interrupt.

Senator Biden, we are going to have to go for a rollcall, but before I go, Mr. Rush, if you wish to go, you may go whenever you please.

Senator Proxmire told me he had no further questions for you. I want to ask just one question here, Mr. Greenspan: when you say that you would like for us to grant a waiver under section 208, do you propose we take positive action?

Mr. GREENSPAN. No, as I recall, Senator, and unfortunately I'm not a lawyer—

The CHAIRMAN. Oh, that was addressed to the President?

Mr. GREENSPAN. Yes.

The CHAIRMAN. And he would be the one to exercise that. I see Senator Proxmire is coming back, and he will want to continue.

Senator BIDEN. Mr. Greenspan, maybe I could run over and catch that vote and you might think about the question I have because that's the only thing I have.

I don't share your view nor do I have your expertise on some of your economic policy matters, but I don't feel I have any right as a Senator confirming the Presidential appointment to deny that confirmation based on the difference in philosophic approach to the problem, but I am worried about this other aspect and setting a precedent.

Maybe it's already been set by giving an exception of what could be of significant content. That I would like to pursue.

Thank you,

[Recess.]

Senator PROXMIRE. Mr. Greenspan, we are all set any time you are.

The other Senators will be coming back. I apologize for keeping you so long. This is a very important nomination.

There has been apparently some confusion on the part of some people to your response to the very first question with respect to your position in the event the President leaves office, and the Vice President succeeds him.

Under these circumstances, you said you would submit your resignation. Would that be a pro forma resignation or would you resign?

Mr. GREENSPAN. Pro forma.

Senator PROXMIRE. In the event the Vice President asks you to stay on, would you do so?

Mr. GREENSPAN. I would consider it a privilege.

Senator PROXMIRE. You would consider it a privilege.

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. Now, one of the things that most troubles me and the reason I spent so much time, I realize that Senator Biden had asked a question but not gotten the answer with respect to whether you would recommend antiinflationary measures.

Mr. GREENSPAN. Would you like me to answer before he returns.

Senator PROXMIRE. Let's wait until he gets back.

My difficulty with your position in part is you are a strenuously free market economist. That gives you enormous merit, but you don't seem to have much faith in antitrust laws, and I think that suggests a contradiction.

Dr. Burns came out yesterday for vigorous enforcement of the antitrust laws. He said he would like to see stiffer penalties. He thinks the \$50,000 penalties are a slap in the wrist.

How do you feel about that?

Mr. GREENSPAN. First, let me preface my remarks by saying I don't consider myself an expert on the antitrust statutes or antitrust enforcement and I doubt very much whether the Council of Economic Advisers does or should be involved in this thing.

Senator PROXMIRE. Let me just interrupt at that point to say the difficulty is that the President, on the basis of what has been disclosed in the tapes and so forth, obviously doesn't believe in vigorous enforcement of antitrust laws, at least in some circumstances.

He wanted to get rid of McClaren and he told Kleindienst to stop prosecuting these cases, and that was a problem in this case.

Mr. Ash who is part of the Quadriad, I guess, and as you will be, is the founder of one of the biggest conglomerates in the country. Mr. Rush, who accompanied you this morning and also part of this, is a Union Carbide head. Mr. Simon is a man very closely associated with the biggest business in the country, and I think the President, of course, determines everything.

He is the only elected official. He appoints the people who administer the antitrust laws, so your advice to the President would be rather critical in this area. You and your colleagues.

Mr. GREENSPAN. Well, let me indicate to you what my view is. My view is based on my observations of the way the economy functions, and it's based on history, and as I recall it, the means by which our whole philosophy of antitrust and antitrust enforcement emerged in this country.

Essentially there are certain types of monopoly practices and monopoly things that occur which are considered illegal, and I find it difficult to understand the logic underlying some of them.

Let me give you a very specific example. There are a number of instances in which a company is capable of maintaining a significant market share of a particular industry because of continuous improved techniques, technology and capability in keeping its costs low.

The only way to keep a significant share of an industry in the sense of maintaining a large position in it is if by some means you can keep your price down. Now, there are only two ways to do that—

Senator PROXMIRE. Now, that's quite an oversimplification.

There are all kinds of ways. You may have an industry like automobiles in which it takes a colossal investment to get in. Very few people are going to enter an industry of that kind. Steel is another industry in which it does take a very large investment.

You do have a situation with those who have the greatest power

with respect to capital, have on their board of directors, the people from the steel industries and vice versa, I have a list here.

For example, of the Morgan Guaranty Trust Co. which has direct interlocks with respect to oil, for instance, Continental Oil, Cities Service, Atlantic Richfield, Columbia Gas System.

The First National City Bank has representation from Allied Chemical, Monsanto, W. R. Grace Co., Standard Oil of New Jersey, Mobil Oil and Sinclair Oil.

The Chase Manhattan has Standard Oil of New Jersey and Standard Oil of Indiana.

The First National Bank of Chicago has Swift & Co., Shell Oil Co., and Standard Oil of Indiana. Continental Illinois National Bank & Trust Co. has Consolidated Coal, Old Ben Coal Corp., Swift & Co., FMC Corp., Standard Oil of Indiana, Continental Oil, Union Oil of California, and Northern Natural Gas Co.

So they don't function as freely as they do in the textbook. Competitors are not free to move in because there obviously is a very serious powerful interest in preventing competition that could result in reduced profits and reduced prices.

Mr. GREENSPAN. Well, there are certain cases, on which I agree. When I am talking about basic antitrust, I am talking in the context of the free market society essentially one in which you don't have the extraordinary, the very substantial intervention of Government charters, and other restrictive policies and the like, and subsidies, which all tend to create or reinforce some fairly rigid systems.

Now, for example, I don't know whether, in fact, one couldn't get into the steel business at this stage. There are a number of small steel firms that have emerged in recent years.

The capital requirements were not particularly large. If the capital requirements are relatively modest—and \$10 or \$20 million is modest in these markets—that's really quite easy to raise if there is potential profit involved.

Senator PROXMIRE. If you are going to be an integrated steel producer, as U.S. Steel and Bethlehem, it requires a colossal amount of capital. If you are going to be a vertically integrated oil company, it requires an enormous amount of capital. That capital is available from the big banks.

Those banks have a clear and conspicuous interest in assisting the presently established oil and steel companies. They have those directorships, associations, and investments.

Mr. GREENSPAN. Senator, I would be more inclined to believe that the reason that a lot of the major large loans go to a lot of the major companies is because they are the most likely to be paid off.

I don't know how most corporations work, but I must say maybe it's an act of naivete, but I do believe the shareholders still have very significant clout on the boards of directors of the banks and that the credit policies of the banks are not directed toward making loans to the people who happen to be on the boards of directors.

From what I can see that does not generally happen unless those are good loans.

Senator PROXMIRE. Oh, I know they are good loans. What I am talking about is whether a competitor interested in entering and

providing competition and getting in a big way is in a position to do that.

There are a few enormous concentrations of wealth that cannot move without reliance on the banking fraternity.

Mr. GREENSPAN. Well, sir, overnight, of course, no, sir.

There is no way someone can construct the equivalent of United States or Bethlehem Steel Corp. almost immediately.

That may be the case, but that's always been the case, and that's not what curbs the market behavior of the large companies.

In other words, if you are concerned about what determines the price level, let's take the case about what determines the price level in steel—

Senator PROXMIRE. I hate to interrupt so often.

I do want to give you the full context. You have Professor Houthakker, the economist, who I am sure you respect the views by him as a conservative, at least, who argues:

In a competitive market the normal reactions to a fall is a decline in price, but where competition is weak, the usual reaction is to cut the quantity supplied.

You ratchet up your prices. They go up, but they don't go down. Paul McCracken, your predecessor, said:

The process of unwinding some of these monopolies, however, could exert some downward pressure when we are trying to restabilize the price level.

There does seem to be considerable consensus among moderates that the antitrust laws can considerably help.

Mr. GREENSPAN. That is right. I agree. Where we disagree is essentially on what we use as the standard.

In other words, I don't consider that specific price flexibility per se is a value. Where I do consider it as a value is the maintenance of the most efficient productive system, the lowest long-term price levels, the highest quality of goods for the American consuming public.

Now, there are disagreements about whether or not price flexibility per se in the short run actually enhances that.

Senator PROXMIRE. Let me just say do you think steel is an efficient industry compared to European competition.

It seems to me we have stable prices as long as we permitted foreign competition. When we put on the quotas, steel prices have gone through the roof. You are right, the figure is 40 percent increase in 1 year, in 1 year, in steel, fantastic. Twice as big as the biggest increase in any year in our history.

This is as a result in part of insulating this industry with price fixing apparatus from European competition which seems to be a lot more difficult.

Mr. GREENSPAN. Senator, I was opposed to the quotas for precisely the same reason you suggest. I thought it was a mistake. Much of the problems we have had in the industry with respect to pricing, I think, reflects that.

Senator PROXMIRE. I am delighted to hear that.

You do oppose the quotas in the steel industry?

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. Oil import quotas?

Mr. GREENSPAN. Opposed.

Senator PROXMIRE. You have stated your opposition to Government guaranteed loans and indicated opposition to direct subsidy. Would you spell out for us the inflationary effect of Government guaranteed loans on subsidies.

Mr. GREENSPAN. How they work?

Senator PROXMIRE. Just very quickly, yes.

Mr. GREENSPAN. A Government guaranteed loan, largely because it pre-empts private savings, forces the other private borrowers to move into the commercial banking system and directly expand the money supply.

Subsidies do it by building in various distortions of one type or another.

Senator PROXMIRE. You indicated disapproval of the Lockheed loan.

Mr. GREENSPAN. I have testified before this committee against it.

Senator PROXMIRE. That's right.

We missed it by one vote.

The administration beat us. The administration has proposed to approve \$100 million loan to the Grumman Corp.

Mr. GREENSPAN. I oppose that sort of thing.

Senator PROXMIRE. Why make an exception for Grumman?

Mr. GREENSPAN. Largely because the Lockheed loan was for civilian profitmaking purposes. If this loan is for some type of military expenditure, it may not relate to the same type of problem.

If it does not, I would say it is exactly the same.

Senator PROXMIRE. They have asked for it, but they have no line with the banks.

Do you oppose Government bailouts of businesses of defense contractors who are experiencing financial problems?

Mr. GREENSPAN. Yes, I do.

Senator PROXMIRE. What about failing banks? Was the Federal Government correct in supplying Franklin National with a \$1 billion bailout loan?

Mr. GREENSPAN. I don't know the specifics of that, but unless there are other considerations which affect the total financial structure, I would oppose it, as I did before.

Senator PROXMIRE. Would you oppose making that on a subsidized basis? The Federal Reserve Board made a discount loan of 8 percent and the going rate was 4 percent above that.

Mr. GREENSPAN. Yes, I would oppose that, and I feel that is unnecessary.

Senator PROXMIRE. Now, you are on record in the past as opposing consumer protection laws as being not really in the interests of the consumer.

Mr. GREENSPAN. Yes, sir.

Senator PROXMIRE. Let's take truth in lending. Don't you think that can be helpful in keeping down prices? It is primarily a disclosure law. It requires that the lender disclose the true rate so that the borrower can shop around for credit.

Mr. GREENSPAN. I have no objection to that.

If anything, our fraud statutes require considerably more tightening.

Senator PROXMIRE. How about truth in packaging?

Mr. GREENSPAN. I don't know what that is.

Senator PROXMIRE. Well, it requires the seller to indicate what's in the package in simple terms so it can be understood.

Mr. GREENSPAN. I would be in favor of that.

Senator PROXMIRE. The original free market concept is based on a large number of buyers and sellers with full information.

Mr. GREENSPAN. May I just make one statement with respect to these general questions, Senator, most of these things actually are in the benefit of the producers and sellers.

Now, one of the things we have to be careful about, when we look at legislation per se is that there really is a competitive advantage, in somebody's good will or integrity or in marketing and in many instances, the reason why the quality products have emerged in the forefront of the market place is that it really is in their self interest to maintain the absolute highest quality and highest integrity in the retail markets.

Senator PROXMIRE. No question about it. If you have a fully informed consumer, but the power and information is on the side of the seller in many, cases in this society of ours.

Mr. GREENSPAN. No, I have no objection to that sort of information, and I think the more the better, certainly.

Senator PROXMIRE. How about weights and measures? The requirement that the States require periodic checking of the weights and measures so you are sure when the butcher sells you 1 pound of beef, that it is 1 pound of beef and not 10 ounces.

Mr. GREENSPAN. I have no objection to that.

You know, certain private agencies like Consumers' Union, which endeavors to analyze various type of products, I'm wholly in favor of.

Senator PROXMIRE. How about quarantine laws? Meat and poultry inspections?

Mr. GREENSPAN. Those are health statutes and I agree with them.

Senator PROXMIRE. Food and drug laws?

Mr. GREENSPAN. Yes.

Senator PROXMIRE. The National Transportation Safety Act, Consumer product safety laws—

Mr. GREENSPAN. I can't comment on these individually. I would be opposed to many of the elements within those.

Senator PROXMIRE. On what grounds?

Mr. GREENSPAN. On the grounds that they don't really help the consumer.

What they may well do is to eliminate what I think is a very important protector of the consumer, the competition that does exist to maintain quality products. If you put a guarantee in—first of all, if a guarantee is put in a marketplace which is not capable of being fully enforced and a great number of these things are, I think the consumer is often misled that when something is sold often by shoddy producers, that is somehow sanctioned by the Federal Government regulations.

Senator PROXMIRE. Then there is legal recourse. There is a legal penalty. There is an opportunity for the Government No. 1, to require the products not be shoddy; that it not fall apart and not be dangerous; and there's a basis for the consumer to recover and there's a kind of penalty that acts as a discipline.

Mr. GREENSPAN. This is the reason why I think there should be significant expansion in the fraud statutes because what we are talking about is fraud. That is, somebody is selling something and misrepresenting what is.

Senator PROXMIRE. How about the consumer protection agency? This is something that's before the Congress at the present time and, as you know, would provide representation for the consumer before the regulatory agencies the argument being that we have a long history of regulatory agencies being taken over by their constituency, just the thing you were talking about, I presume, before.

So you need a vigorous defense of the consumer before these various agencies and any number of others. What's wrong with that?

Mr. GREENSPAN. Maybe a problem is the constituencies that now run these agencies. I am not certain that making two steps forward is as good as taking one step back.

Senator PROXMIRE. Do you oppose the so-called consumer protection agency?

Mr. GREENSPAN. Senator, I haven't studied it. I neither support or oppose it. I don't unfortunately at this moment know enough about it to answer the question.

Senator PROXMIRE. Senator Biden, I don't want to hold you up. I've got a few more questions.

You had one question you wanted to follow up with or did you have more?

Senator BIDEN. But I plan on staying.

Senator PROXMIRE. Well, let's get an answer now to Senator Biden's question.

Could you give us an example of recommendations that are anti-inflationary, that would affect your corporate ties.

Is that what you asked?

Mr. GREENSPAN. As I remember the question, it's basically this: That, granted, I sever all of my immediate relationships with the company and granted that I don't obtain any financial rewards while in Government service, is it not a problem that when I go back having, let's assume, not the same clients but a broad spectrum of similar types of clients, that should I oppose some of their measures while in Government service, would I not find in coming back to my consulting firm, find a negligible number of clients as a result of that?

Senator BIDEN. I think that is fair. You raised it another way. you just raised the question of agencies where the constituency runs the agency, and in effect they are a one-man agency.

Senator PROXMIRE. A one-industry agency.

Senator BIDEN. Right. Potentially. As some of my former criminal clients used to say, "You are going to be a powerful dude."

Mr. GREENSPAN. In a certain sense, there is no answer to that, and

that problem, as I see it, does exist. All I can say to you is this, that upon confirmation, I will be under oath, swearing to fulfill my obligations, and I take them very seriously.

It may be that in the process of being council chairman that I would of necessity confront issues which would be highly negative to particular people who are clients of my firm and all I can say to you is, "So be it."

Senator PROXMIRE. Can you give us an example?

Mr. GREENSPAN. Yes, Let's assume I do have some steel clients. I would oppose steel quotas. I opposed them while they were clients of mine, and I would oppose them now, and I would oppose them while in Federal office. I don't think that my ideas change because of the particular job that I hold. I take ideas seriously.

Senator BIDEN. I want you to know, Mr. Greenspan, that it is within the same context that I asked the question, the exemption you would have to be granted under the U.S. code that we would be in effect voting on you today, and it would require that I as one individual in this committee determine that the interest is not so substantial as to affect the integrity of the services that a Government may expect from such an officer or employee, and that is not something that I take lightly. I don't mean that—I am not questioning your integrity—

Mr. GREENSPAN. No, I am serious.

Senator BIDEN. And I am not trying to be pugnacious with you. When in doubt in the past, I have erred on the side of voting "no."

Mr. GREENSPAN. Senator, your concern is essentially my concern and one of the reasons that I have been very reluctant to come on board, because I know this view exists. I am proud of having created a type of business, the type of business I have. While I have nothing against making money, that is not what I am in business for. I am in business as a profession to do the type of job which I love doing. Largely as a business procedure, I have never put myself in the position where any individual client or group of clients can in any way affect what I do or what I say in private life.

Senator BIDEN. Again, I want to explain why I asked the question.

With the chairman's permission, I would like to ask one more question, completely changing the subject.

You mentioned in response to a question by Senator Stevenson that the oil price jack-up was not a product of the free market phenomena.

Mr. GREENSPAN. That is correct; it was not.

Senator BIDEN. My question is, then, if it in fact isn't, doesn't response to that require something other than a free market response? Or shouldn't that be considered? I understand essentially the reason why you don't like the idea of rollbacks or setting prices. It flies in the face of your concept of the free market.

Mr. GREENSPAN. Well, no. If you are saying to me does one confront a particular problem with a free market solution under all conditions, no, you do not.

Senator BIDEN. Or specifically under this condition.

Mr. GREENSPAN. What the specific response to this is in the full

context, I don't feel as though I am in a position as yet to say, but you are asking the question do I, if confronted with huge price increases in which you are looking at essentially Government monopolies in the oil-producing countries, do we respond in—automatically—as though nothing had happened? I would say, “No, we don't.”

Senator BIDEN. The real reason for the question was that your response to Senator Stevenson was fairly classic, in which you stated that the market would seek its own level; it is going to be going down, and you talked in terms of competition, and again you stated what I firmly believe, that the increase has no relationship to competition whatsoever, and I am always—the argument eludes me that is made by a president of a major oil company in trying to convince me of the merit of his position.

Foreign crude was, from the Persian Gulf area, was about \$11½ a barrel, and this particular company had new domestic crude which was under control and he had that at \$11½ a barrel, and I asked why and he said, “Well, foreign crude is \$11½ a barrel, and we have to compete.”

I said, “I don't understand what the hell you are talking about.”

Just prior to that, he went on to make the same statement that you made, that the increase bore no relationship to the free market or to the competition. Yet, he is meeting that increase as an oil company executive in the name of the free market economy. That is how he justifies it, but really what it is, it seems to me, is just a gigantic rip-off, and that is why I raise this question. Why don't we roll back that price?

Mr. GREENSPAN. Do we want to create a system in which we have maximum expansion of oil production resources?

During the energy crisis, there were considerable questions with respect to what was an equilibrium oil price. In other words, what was the price which was required to create sufficient revenues or profit in an endeavor to maximize oil exploration, drilling, and production, basically, to avert problems we were having with the reliability of foreign oil.

Now, unfortunately, we don't know what that price is. We can make a number of estimates as professionals; mainly, rough guesses as to what is involved. The range or error in our understanding of what that price is, is very substantial. The nature of the problem as I would phrase it is basically this:

I don't think we can risk at this stage not to engage in “overkill,” on the question of producing energy sources.

If you ask me my professional opinion the current price may be above equilibrium, I suspect that it is, but the amounts involved, say, going back to pennies per gallon at the pump, are so small, that we have to lean over backward just looking at a sort of a cost-benefit analysis of the problem. Granting that our knowledge is quite deficient on the question. It is in our interests, to err on the side of too much rather than to little.

Senator BIDEN. You talk in terms of the amount involved and in terms of the pennies per gallon.

Mr. GREENSPAN. In terms of what I think the equilibrium price would be.

Senator BIDEN. In terms of pennies per gallon. Isn't it true that the aggregate increase of the cost of energy to the consumer is one of the primary factors in our inflationary picture, or a significant factor, as significant as deficit spending, and it ought to be considered in those terms?

Mr. GREENSPAN. Yes, and no, Senator. It is affecting the price level in the short run, unquestionably. That it can be considered a long-term major inflationary trend, I would say it cannot be, because I would argue, as I have argued before, the absolute average level of all prices is a function not of specific prices in the market place, but of so-called unit money supply.

Then, in the longer run what happens is that if oil prices stay high, other prices tend to fall relatively. In other words, the average sort of balances. There is no question that in the short run it does not.

Senator PROXMIRE. May I ask this for a minute?

I think I can wind up my part of the questioning in about 10 minutes.

Senator BIDEN. I can wind up with just one thing, Mr. Chairman.

Everybody who holds your position talks in terms of pennies per gallon when we are talking about oil prices and not the aggregate increase. When we talk in terms of the budget, they take the opposite point of view, and, you know, I am just saying what is good for the goose is good for the gander, and I really am tickled to watch these conservatives here in my sector, along with some of my liberal friends on the way they approach these issues now. I watched the conservatives jump on the bandwagon for beef subsidies and to give the arts \$400 million, but Senator Proxmire is trying to cut that. I watched those same guys who get up there and pontificate about the welfare system jump in and spend what I estimate to be an additional \$10 billion so far on things that were counter to their philosophic concept that they espouse when it comes to social programs.

All I am saying is that I understand what you are not, is a phony, what I understand you are is a straight talker and a straight shooter. That is why I am glad that the President picked you. If he picks a conservative, I want him to pick a straight one and a bright one. I understand you are a straight one and a bright one, which is something that has been in short supply, not only in the Administration, but around in the conservative and liberal camps. That is the only reason for my questions.

Senator PROXMIRE. May I say to the Senator from Delaware that I think Mr. Greenspan is both straight and bright, but I am not so sure if you are going to pick an executioner that you want to pick one with the sharpest possible ax.

Let's pick a guy so incompetent that he is not going to get a program we don't believe in done.

Senator BIDEN. You want it clean. If I go, I want a clean knife, just, "Bang."

Thank you, very much, for tolerating my questions. I have literally 25 more.

Senator PROXMIRE. Why don't you put them in the record, and Mr. Greenspan can perhaps answer them when he corrects the record.

Senator BIDEN. That would be fine.

[The questions and answers follow:]

QUESTIONS FOR ALAN GREENSPAN FROM SENATOR BIDEN

Question 1. In last Sunday's New York Times, government officials were quoted as saying that unemployment would exceed 6% this year. The same article indicated that even under such circumstances the Administration intends to hold to a majority of moderate restraint, for several years if necessary, in order to reduce inflation.

(a) Is this the policy you would advise the Administration to pursue?

(b) Do you believe there is some point, without being precise to one tenth of one percent, where unemployment would be so high that you would recommend an altered course of action?

(c) If so, what action could be taken that would heat up inflation least?

Answer. If somebody could perceive a more viable long-term program to bring down the rate of inflation which has as high a probability of success as the policy of moderate restraint, I would certainly urge that it be considered. At this point, no such alternative policy has been offered.

The danger to this nation stemming from continued inflation at current, or higher, rates must not be underestimated. All people, employed and unemployed, are hurt by inflation. The issue is essentially a question of which policies will inflict least hurt on the fewest people. Further inflation would severely hurt a far greater proportion of the nation's population than would the increase in unemployment that might be generated by antiinflationary moderate restraint. It is a sad state when such conflicting choices confront us. Unfortunately, we cannot go back and redo the tragic policies which brought us to this point. We are here now. The question we must confront is what are the real alternatives still open to us.

I don't think the unemployment rate, per se is the only element involved in such a decision. The higher unemployment rate must be evaluated in relationship to the degree of success which the policy may be having in suppressing the financial bloat which has been ravaging our system. This is absolutely necessary in order to dampen unemployment.

In the current context of high inflationary pressures, attempting to cure unemployment by reflating would present too high a risk to the economy, in my view.

Question 2. There have been suggestions that if we are to suffer high unemployment in the short term, in order to reduce inflation in the long term, we ought to have government sponsored programs such as higher unemployment benefits, public employment programs, and job training programs.

(a) What do you think of such proposals to handle unemployment programs?

(b) Might they not be just as inflationary as if the people had private industry jobs?

(c) If we increased the Federal Budget to do this, does this mean even greater cuts in other programs?

Answer. If increased federal expenditure are directed towards such programs, ways must be found to offset the inflationary implications by cutting back other federal spending.

In evaluating these programs, the focus always must be on the key cause of inflation, which is the excessive rate of monetary growth designed to accommodate Treasury spending and Federal deficits. To truly help the unemployed, any aid program must not generate greater inflation at the same time.

If programs to aid the unemployed are initiated, they should be very carefully crafted in order to assure that they remain temporary. They must not be devices which merely create a permanent increase in government employment. Unemployment benefits are sensitive to changes in unemployment. There is a clear automatic shutdown as unemployment fades. However, it would be exceedingly difficult to construct public employment programs which would be equally sensitive to changes in unemployment. There would be a considerable lag between the time when action was initiated and the time when

the public service employment was actually implemented. Thus, the employment could be underway just when it was no longer needed. Furthermore, it is hard to conceive of people being laid off from these public service jobs to seek jobs elsewhere when unemployment has been reduced. Accordingly, I would lean far more in the direction of unemployment insurance rather than public service jobs. As to which jobs are more inflationary, that depends upon a comparison of their pay-productivity relationships. If production per unit of wage is higher in the private sector, then public service jobs would be more inflationary.

Question 3. There seems to be action again to establish an Agency to monitor inflation. It has also been suggested that the President should have standby authority to impose price or wage controls in a selective way as a result of the monitoring. Would you recommend this kind of monitoring and stand-by control?

Answer. I am not in favor of such legislation. I believe it risks moving back to a rigid mandatory wage and price control system.

Question 4. Most people seem to agree that oil prices and the massive money movements to oil producing nations is a major factor in the unsettled financial affairs of the non-communist world. Realistically, what do you think can be done to bring the oil price problem under control?

(a) Do you think there would be any benefit to a joint group of oil-consuming nations to bargain with oil producers? Would this really achieve anything?

Answer. Unquestionably, high world oil prices are generating a tremendous and unsustainable growth in debt for numbers of oil importing countries. The magnitude of these unilateral debt flows cannot go at their current pace for a protracted period of time without severely damaging the financial capability of major segments of the industrial world.

This process is already tending to curtail oil consumption. Unless world crude oil production is cut back, the existing excessive world inventories of crude end products must eventually bring prices down. However, if the oil exporters decided to curtail production, they could artificially sustain the level of oil prices. This is not an economic problem, but rather an international political problem.

If a joint group of oil consuming nations could act in concert to bring down prices, I would certainly favor it. Unfortunately, in such a confrontation I suspect that the staying power of oil producing nations is much greater than that of the oil consuming nations. Many of the oil producers do not need to maintain production since they already have accumulated significant revenues. In contrast the oil consumers simply cannot stop importing. As a consequence, the sheer power balance is badly skewed against any joint oil consumer groups.

Question 5. There are a number of laws and practices that may tend to keep prices up. Among those that occur to me are the so-called Fair Trade Laws in 15 states; the Davis Bacon act that requires payment of prevailing wages on Federal contracts; and programs to subsidize American shipping. What would be your recommendation to the President on these and similar practices?

Answer. Should the President ask me, and I must emphasize to you that I am by no means sure that he will, I would express my personal belief. I am against such laws and practices which hamper free markets and tend to keep prices artificially high.

Question 6. There has been much talk and speculation about the stability of financial institutions around the world.

(a) Do you believe there is a serious problem in this area?

(b) What do you think can be done—on an international basis—to prevent such failures or assure a unified international approach to preventing major failures of financial institutions that might have international ramifications?

Answer. Yes, I do believe there is a serious problem. This is, in fact, one of the very urgent priorities at the moment.

I believe that our data must be improved considerably in order to enhance our understanding of the interrelationships which affect international financial flows. I don't think a sufficiently efficient preventive system can be set up until a much better diagnosis is available of precisely where the strains and difficulties are. Only then will it be possible to trace the potential consequences of different types of financial breakdowns as the secondary effects ricochet throughout the world.

By its very nature, such analysis and such efforts cannot be public knowledge. Therefore, at this moment I could not comment on the precise state of either. Nevertheless, it is clear that the considerable interrelationship of national financial systems necessitates a sensitive international cooperative approach.

Question 7. Roy Ash, the Director of OMB, has been quoted as saying that OMB intends to conduct a "sweeping review" of Federal regulatory legislation in such areas as occupational safety, anti-pollution controls, health and similar areas. He feels this regulatory legislation adds to costs and therefore is inflationary.

(a) Do you support a program of relaxing Federal regulatory standards? Do you believe this would reduce business costs and help hold prices down?

Answer. First it is important to recognize that no one has the right to indiscriminately pollute the atmosphere, create occupational hazards, or endanger the health or prosperity of other individuals. A company which dumps its wastes on property other than its own is being subsidized to some extent, since it is utilizing a costless way of disposal. I am in favor of the removal of such subsidies.

Business should internalize all of its costs. However, the rapidity with which such requirements must be met is another question. Many businesses have complained that these regulations require excessively fast compliance which is extremely costly in the short run. Hence, I would favor a review to ascertain what the tradeoffs in this area should be between financial costs and environmental gains.

There is no question that funds expended for occupational safety and/or antipollution controls do subtract from the capital funds which otherwise might be available to expand capacity. The latter outlays would help reduce inflation. In short, a balanced program between these two alternatives is necessary.

The precise balance between the two must be based on a thorough evaluation of the specific implications of the different options available to each firm or business.

Senator PROXMIRE. Mr. Greenspan, I hate to press you on this, but the President has asked for time at 9 o'clock tonight to make a speech to the country. Many people feel he may announce his resignation at that time. This is why I come back to the issue.

Under these circumstances, it would seem to me that it would be no disservice to you, you are obviously very popular up here on the Hill, and you have many enthusiastic supporters, including some who greatly disagree with you, if we held up acting on this nomination until we see whether or not the President is going to resign so President Ford would have a free hand to appoint his own Chairman of the Council. It might well be you. At least he would know what he was doing.

I simply say that that seems to me to be the course that the committee might pursue.

Mr. GREENSPAN. Yes.

Senator PROXMIRE. Now, I think I can get through this quickly, if we can have quick answers, and I will try to make the questions brief.

You haven't been asked at all about tax policy. Would you favor a tax increase now to go with the inflation problem?

Mr. GREENSPAN. Not in and of itself, Senator Proxmire.

The basic reason is that I think that we are confronted with a problem that I would define as too high a rate of increase in Federal expenditures, I am concerned that if you raise taxes, we will merely delay our coming to grips with the problem.

If we delay by raising taxes by one time or two times or something

of that sort, we will eventually arrive at the point where increasing tax rates no longer increases revenues for obvious reasons, and we are back to the same problem again of coming to grips with the expenditures.

So that as far as I can see, a tax increase is merely postponing the problem.

Now, if you ask me in the context of a major anti-inflationary program in which that is not a particular concern, and which one can presume is part of a larger package, then I would say that I would want to examine it.

Senator PROXMIRE. We have an erosion of the effective corporate tax rate. Dr. Otto Eckstein of Resources, Inc., has estimated, based on Government statistics, that it has gone from 43 percent in 1969 to about 35.5 percent now. This represents a shift in incidence of taxation away from corporations and stockholders, perhaps, to especially the payroll tax.

How do you feel about the equity involved, and should we begin to try to reform our tax structure to reclaim some of that?

Mr. GREENSPAN. I think we have to understand why that tax decline has occurred. I don't have the figures in front of me, Senator, but if you want them, I can see if I can make them available.

My recollection is, and I emphasize it is my recollection, that there were two major elements involved in that decline in average tax rates other than the tax cuts that have been legislatively enacted.

The first, of course, is the very dramatic increase in foreign affiliate income, which is included in the national income accounts after taxes, and as a consequence, the greater the proportion of so-called rest of the world or foreign affiliate income in the present profit figures, the lower the effective tax rate would be.

That is part of it.

Secondly, we have a very substantial number of what we call deficit corporations in the United States. That is, corporations which make no money and hence pay no taxes.

Senator PROXMIRE. Isn't that a permanent phenomenon? Is that something that has developed in the past 5 years?

Mr. GREENSPAN. I expect that what is happening is that the proportion of deficit corporations has decreased, and what that would tend to do is to lower the average effective tax rate.

Now, the reason I suggest this is, that when we are talking about the equity of tax policy, I think we want to look only at profitmaking corporations.

Senator PROXMIRE. Isn't this a product also of accelerated depreciation, and so forth, which has the effect of a tax reduction on stockholders?

Mr. GREENSPAN. There is no question. I was merely referring to the fact that other than the well-known changes in the law, there are specific statistical factors involved in that type of calculation.

Senator PROXMIRE. Is it possible to reform the tax structure to provide a progressive income tax, or do you think it is desirable to do it, a more progressive income tax which relies more on ability to pay, and eliminates the inequitable effect of some of these so-called

incentives and requires perhaps higher pay for long-term capital gains? A minimum tax, do you favor that kind of action, or do you think it would be counterproductive?

Mr. GREENSPAN. The tax structure is so complex that I personally, and this is my view and obviously not the administration's, I would prefer to seek a vast cutting through all the exemptions and special elements within the tax code so that you lower the rate tremendously, as a number of people have suggested. That would be far more efficient. These alleged tax shelters and all these varieties of things serve no useful purpose that I know of, and—

Senator PROXMIRE. Well, do you agree? You have indicated at one time or another that you don't support the concept of a strongly progressive income tax.

Mr. GREENSPAN. That is correct, I do not.

Senator PROXMIRE. You do not?

Mr. GREENSPAN. The reason I don't is that you have to distinguish between equity and equality. The logic underlying the equity of the income tax per se, I find very elusive. Many people have tried to explain it to me in a broad philosophical sense, and I must say that while I have listened, I have not understood the underlying logic of it.

Senator PROXMIRE. Why isn't it simple? If people with large incomes need the additional amount of income that they get above, say, \$20,000 or \$30,000, or \$40,000 a year, less, substantially less than a person who has an income of, say, \$8,000 or \$10,000. The necessities of life, the ability to subsist and provide anything like a decent living.

Mr. GREENSPAN. First of all, this gets down to some very basic questions about the nature of what the question of equity is in the tax code, and I don't understand—

Senator PROXMIRE. No, it is just that simple notion. Isn't it justice to provide a larger proportionate tax on people with big incomes than on people with limited incomes, just from the standpoint of being able to live a decent life?

The utility of a dollar is so much less for a man who earns \$100,000 a year than a man who earns \$10,000 a year.

Mr. GREENSPAN. It gets to the point of the nature of the relationship between the individual and the government, and this gets down to a quite fundamental question of one's view of the nature of the political freedom and the relationship that exists between the state and the individual.

The concept of a government's unqualified claim on the property of an individual is something to which we as a free society don't subscribe. The concept that government has a preeminent claim on a person's income is something which is not consistent with a free society, it implies that it is our after-tax income which is in a sense vouchsafed to us.

Senator PROXMIRE. We have to collect a certain amount of taxes in order to provide for the national defense and in order to provide essential services. No matter how conservative a person is, he agrees in our complex society there is a heavy burden on the citizen. We disagree as to how heavy the burden should be.

You argue that because the Government doesn't have a right to property that the rich man shouldn't pay as high a proportion of his income as the poor man.

Mr. GREENSPAN. I would like to see all so-called, if you want to call them, loopholes, exemptions, knocked out, and everybody pay a tax.

Senator PROXMIRE. A flat tax, not a graduated tax?

Mr. GREENSPAN. What you would find under those conditions, I believe, is that the actual amount of tax as a percent of income is not going to change that radically.

Senator PROXMIRE. Let me go back to it again.

Would you, then, like to see a flat tax on all incomes?

Mr. GREENSPAN. That would be my ideal state, but I scarcely expect that to happen.

Senator PROXMIRE. But that is the direction you would want to have government policy move?

Mr. GREENSPAN. My view on this is perfectly clear. The rest of the people around me in discussing Government policy disagree with me, I must say, to the point where I am a minority of one.

Senator PROXMIRE. Again, I apologize for taking so long, but this is so important. You have argued that you would not specify where you would cut the budget. How about military? Would you cut that?

Mr. GREENSPAN. I see no reason to except any part of the budget.

Senator PROXMIRE. The military spending produces no economic good. You don't go into a supermarket and buy an aircraft carrier.

No. 2, the goods in short supply, steel, chemicals, and so forth, go in disproportionate amounts to the military.

For those reasons, shouldn't the military, shouldn't we look for cuts there?

Mr. GREENSPAN. I would certainly say that would be one major reason why one should not except the military from that analysis.

Senator PROXMIRE. Would you cut social security, or arrest increases?

Mr. GREENSPAN. Our problem with the Federal budget is that we need to arrest the rate of increase. The expectation of cutting back on this at this point, is unrealistic.

Senator PROXMIRE. Dr. Burns proposed yesterday that we provide, as have a number of others, and Mr. Simon indicated support for it, indicated a great interest in it, that we ought to provide a net for those who are unemployed whenever we reach a 6-percent level, a trigger of public service employment to go as high as \$4 billion a year, and provide 600,000 jobs.

Do you oppose that?

Mr. GREENSPAN. Four billion dollars? I think that would—

Senator PROXMIRE. It would be triggered only if we go to 6-percent unemployment.

Mr. GREENSPAN. That is using a blunderbuss on a problem that, as I understand it—

Senator PROXMIRE. With 6-percent unemployment, you can't do it with a peashooter.

Mr. GREENSPAN. Remember, when there is 6 percent unemployment on an average, nationwide, there is a wide range of dispersion. There are groups that experience 3 percent unemployment and those that experience 8 percent.

Senator PROXMIRE. And with black teenagers, it is 35 percent.

Mr. GREENSPAN. Sure. Averages are obscuring very large divergencies.

Senator PROXMIRE. You say use a blunderbuss. Four billion dollars is a lot of money, but it is about 3 percent of our GNP.

Mr. GREENSPAN. I think you can do what Dr. Burns says——

Senator PROXMIRE. I beg your pardon. It is three-tenths of 1 percent.

Mr. GREENSPAN. It is 4 billion dollars in the Federal budget, and if you are trying to cut the budget \$4 billion is not a small amount.

Senator PROXMIRE. It is about three-tenths of 1 percent of the GNP.

Mr. GREENSPAN. That is a large amount. Where I would agree, is that if you are confronted with the problem of cutting unemployment this is obviously far less inflationary than other avenues that might be followed.

Nonetheless, although I am not terribly familiar with it, I think that there are other elements in this public service employment thing which are significantly less costly; and we are trying to deal with the pockets or the areas where the unemployment problems are most severe.

If we go in this direction, I would certainly hope that it could be set up in a manner in which it certainly would turn out to be temporary, because there is always the danger, as you well know, Senator, that when we talk about temporary programs in which the Government is the employer of last resort, there is a tendency, if we are not very careful, that they will become the employer of first resort; and if such a program is constructed, I would think it would be incumbent upon us to be very clear that it be done in such a manner that it does not become a permanent program.

Senator PROXMIRE. They don't propose it as a permanent program, but triggered in and out. As unemployment drops down, then you would phase it out.

Mr. GREENSPAN. I understand that, but there are often programs in which the purpose is specifically stated, but its implementation does not work that way.

If it can be worked in the way in which it is stated, it is obviously a far less inflationary technique to reduce unemployment than going on a broad fiscal monetary way.

My concern rather than merely saying that the purpose of this program is temporary, is to be sure that the means by which such a program is constructed, if it is constructed, insures that that is what happens.

As you well know, putting it as a preamble in front of a program saying this is what is going to happen doesn't make it happen this way.

There is a danger that it could become a permanent displacement of State and local funding to employment.

Senator PROXMIRE. Well, I want to thank you very much. My problem with your nomination, Mr. Greenspan, is that it is very difficult, because you are honest, you are capable, and some of the things that you propose I enthusiastically applaud; but I have great, great difficulty with the fact that you are a free enterprise man who does not believe in antitrust, does not believe in consumer protection, does not believe in progressive income tax; and the latter may be consistent with a laissez-faire position, but you seem to be opposed to many of the social programs that we have been able to achieve.

Leonard Silk, one of the editorial writers on the New York Times, wrote a thoughtful piece in the New York Times Magazine on July 28. He has a short paragraph. He says the old-style laissez-faire capital system is dead. Yet the mixed economy, the mixture of Government and private interest which have replaced it, needs better methods of harmonizing pressure groups.

What is wrong with that philosophical approach? We have a mixture. With the greatest goodwill in the world, you are not going to go back to Adam Smith. You know that.

Mr. GREENSPAN. I am aware of that. My observations of the fundamental mechanisms by how this particular type of mixed economy works is one of the reasons why I am such a strong advocate of free enterprise capitalism. We have come to a point where the damage that is being done by our mixed economy policies is very patent. I needn't point to the fact that what we are in now is an extraordinary imbalanced, inflation ridden, very disturbing economic structure.

This is largely the result of our attempt to maintain the types of balances that Leonard Silk is indicating. I might say in passing, that while I often disagree with much of his commentary, he is a first-rate economist and one of the rare journalists in this business, who raises fundamental questions.

Senator PROXMIRE. My problem is that I disagree with your notion that inflation has been caused largely by this. I think it has had an impact. There is no question that our eyes are bigger than our stomachs. We have moved too fast in some of these areas. That is true. But you can't explain that 40 percent increase in 1 year in steel prices, that 30 percent or more increase in chemicals—50 percent in industrial chemicals, and 82 percent increase in oil prices, the 46 percent increase in nonferrous metals on anything, except it seems to me, except sheer, unadulterated economic concentrated power. That can do it. If you don't follow an antitrust policy, you are not going to be able to get on top of it.

Furthermore, one concluding note, and that is that I have given a series of speeches on what is right with America; and one point, one area that I have been hitting is what is right with the economy. It is time we looked at that. The fruitful things the New Deal has done and the so-called New Frontier and the Great Society have accomplished a very great deal. Since 1929, a 400 percent increase in real income—fourfold. People have four times as much. That is a terrific kind of achievement.

Since 1939 alone, it is a 395 increase. Real corporate profits after taxes up 300 percent since 1929. Industrial production up 380 percent.

In regard to average hours worked, we are working less than we did before. From 40 hours a week to 37 hours a week. People aren't lazier. We have a greater participation in the labor force. We have more people working, more women, more young people who wanted to start working. That is up from 56 percent in 1940 up to 61.6 percent.

I am not talking about those unemployed. I am talking about those seeking work and working. That has improved. The number of persons employed has more than doubled since 1929.

The poverty ratio has dropped in half since 1939, from 22 percent down to 11 percent. We have—we did have in 1950 only 37 percent of our retired people covered by Social Security. Now it is 95 percent—90 percent, I should say.

It is a marvelous improvement, really a great achievement, and it shows that with all the weaknesses and all the problems we have with inflation we have moved ahead. And I don't want to see us adopt policies that will dismantle it. I am afraid with your great ability and philosophy and the position that is associated with you, we might go backward.

Mr. GREENSPAN. Let me say this in answer to you, Senator. This is a great nation. Our success has been just extraordinary. We have come a long way. And while we do differ on how we got here and where we want to go next, I don't think there is a very significant difference in our general goal, that what we want to see is a viable, great American economy where standards of living continue to be the highest in the world and everyone shares in the prosperity, which has been the case in this country since our beginning.

Senator PROXMIRE. Mr. Greenspan, thank you very, very much. You are certainly an honest and capable witness, and I appreciate this so much.

It has been a very interesting morning for me. I apologize for keeping you for 3 hours. It is an unusually long session, and you did a fine job.

The committee will stand in recess until 2:30.

[Whereupon, at 1:25 p.m., the hearing was recessed, to reconvene at 2:30 p.m., this same day.]

[Biographical sketch of Mr. Greenspan follows:]

BIOGRAPHICAL SKETCH OF ALAN GREENSPAN

Since 1959 Mr. Greenspan has been President and member of the Board of Directors of Townsend-Greenspan & Co., Inc., economic consultants. He is also a consultant to the Council of Economic Advisers, the Department of the Treasury, and the Federal Reserve Board, and a member of the GNP Review Committee of the Office of Management and Budget. Mr. Greenspan is a member of Time Magazine's Board of Economists, Senior Adviser to the Brookings Institutional Panel on Economic Activity, Director of the National Economists Club, Vice Chairman of the Conference of Business Economists, and Past President (1970) and Fellow of the National Association of Business Economists.

He was born on March 6, 1926, in New York, New York. Mr. Greenspan received his B.S. degree, summa cum laude, and his M.A. degree from New York University, and has done advanced graduate work at NYU and Columbia University. In addition to his current activities, he has also been a member of the Commission on an All-Volunteer Armed Force (1969-70), the Com-

mission on Financial Structure and Regulation (1970-71), the Task Force on Economic Growth (1969), the Economic Advisory Board of the Secretary of Commerce (1971-72) and the Securities and Exchange Commission's Central Market System Committee (1972).

Mr. Greenspan joined Townsend-Greenspan & Co., Inc., in 1953 as a consulting economist after serving from 1948 to 1953 as an industrial economist with the National Industrial Conference Board. He currently holds directorships with the following: General Cable Corporation, Sun Chemical Corporation, Trans-World Financial Co., Dreyfus Fund, Dreyfus Special Income Fund, Dreyfus Liquid Assets, Inc., Standard & Poor's/InterCapital Income Securities, Inc., the Hoover Institution on War, Revolution and Peace, and the Bowery Savings Bank.

