

Business and Government



FOURTH ANNUAL REPORT
to the PRESIDENT *by the*
COUNCIL *of* ECONOMIC
ADVISERS • *December 1949*

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Letter of Transmittal

COUNCIL OF ECONOMIC ADVISERS,
Washington, D. C., December 27, 1949.

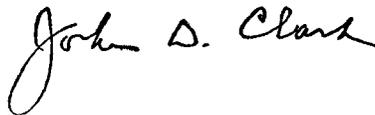
The President.

SIR: The Council of Economic Advisers herewith submits its Fourth Annual Report in accordance with the requirements of Congress as set forth in the Employment Act of 1946.

Respectfully,



Acting Chairman.



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The Council's First Annual Report to the President discussed the political philosophy of the Employment Act of 1946 and the economic philosophy of sustained employment. The second dealt with the meaning of maximum production and the means of attaining it, and the third considered the environment within which the Council operates. These three efforts brought indication that revelation of our general economic thinking was appreciated. They also provided background for the Economic Reports of the President and the Economic Reviews by the Council, which appear in January and July of each year. In this Fourth Annual Report, we discuss the relations between business and government because we find this subject of significance at all times and close to the forefront of general interest now.

We use the term "business" to refer to business management, recognizing that our system of free enterprise includes also workers, farmers, consumers, and their organizations. They equally are confronted by the system's problems; they too are responsible for its achievements; they too have dealings with government and are concerned about public policy. Before long we hope to discuss their relations with government.

I. Free Enterprise and Free Government

COMMUNISM, SOCIALISM, AND THE AMERICAN SYSTEM

The balanced emphasis which the Employment Act places upon the merits and responsibilities of free enterprise and free government is typically American and yet of universal import at this midpoint in the twentieth century. In the last century the philosophic base was laid for extremist doctrines that these two freedoms were irreconcilable, and that one or the other would give way under the impact of industrial concentration, disparate wealth, and popular communication. More recently, these extremists rose to command in many lands. On the right, powerful economic groupings allied themselves with counterrevolutionary movements to destroy free government. On the left, powerful statist revolutions swallowed up free enterprise. We now know how similar are the weeds growing from these different seeds, and how their pollen stifles genuine economic progress, intellectual inquiry, and spiritual aspiration. These manifestations create international problems. But they do not require much analytic annihilation because they make no appeal to the minds or hearts of the American people.

Then there are the current efforts by other peoples with a long tradition of democracy to combine free government with very substantial diminution of free enterprise. In our view these other free peoples will approach their own special problems according to their own needs or beliefs; but our problems are not theirs and we have different methods which are all our own.

During the nineteenth century there were many thinkers even in the United States who, appalled by the prevalence of poverty in a land of plenty and by the crude manifestations of industrialism in the raw, argued sincerely that neither our people nor their government could remain truly free so long as business enterprise remained free. But there are powerful reasons why this thesis is no longer given serious consideration. Although many of our problems remain unsolved, our unique combination of free enterprise and free government has moved so rapidly toward raising the general standard of living that the fair hope of more progress by the same methods immensely outweighs the costs and risks, the divisions and tensions, and above all the uncertainties, of radical change. All history shows that freedom in the long run may best be safeguarded through moderation in the adjustment of seeming conflicts. And the American system is so fortunately situated that it furnishes to the world a beckoning example of this kind of moderation.

The case for moderation grows in appeal because, whatever the situation in other lands, the only conditions which could seriously undermine free enterprise here would also jeopardize free government and possibly do it irreparable damage. In sober retrospect, not even the great depression of the 1930's altered the basic character of our economic system or reduced the commitment to it by the people and also by our most "advanced" philosophers, economists, preachers, and other social thinkers. It follows that nothing less than another depression even more devastating could break us away from this basic commitment. And any such economic convulsion could unleash forces of social tension, domestic friction, and pure political adventuresomeness which might leave us for a time without the essence of free government. Thus, those whose concentration of interest is upon free enterprise and those whose concentration of interest is upon free government are held together by unseverable bonds. No genuine liberal—and most Americans call themselves that—would welcome an economic crisis in order to have a chance to remold the economic system nearer to his heart's desire. We all know what happened to the liberals elsewhere who waited for or courted that opportunity and got totalitarianism instead.

Many of our domestic problems revolve around the application of moderation, compromise, and reconciliation in defining the respective rights and responsibilities of free enterprise and free government under a popular democracy. There are many ways of stating this root issue. How can enterprise remain free enough to be dynamic without

moving from freedom to license? How can government be strong enough, as Lincoln said, to maintain the essential interests of the people without invading their liberties? How can stability be equated with growth? Liberty with law? Individualism with cooperation? How can we steer between the dangers of absolutistic freedom and the deadliness of absolutistic security? However put, these questions involve business and government and seek to broaden their areas of agreement and to strengthen their complementary interactions.

Nobody can resolve this omnipresent issue with a single formula, symbolism, or definition. But there is room for a broad effort to formulate or restate a philosophy of the relationship between business and government. A philosophy voices that agreement on a few fundamentals, alive in the minds of the people, without which there can be little unity or progress. Without universal accord in America about free speech, for example, we could not benefit by debating our disagreements about so many other things. In our economic life no less than in our political, there is need for some common philosophy to hold us together; and since constitutions and courts are not so well suited to this purpose we must resort to the voluntary projection and constant cross-fertilization of ideas.

Economists may take some initiative here because economic problems occupy or even overcrowd the stage on which the drama of adjustment between business and government is going forward. And this Annual Report of the Council to the President is a convenient location for such discussion, in contrast with the Economic Report of the President and the Annual Economic Review by the Council (both scheduled for early January) which must necessarily be steeped in facts and particularistic points of policy.

What we now say is by definition general. Logical deductions from it will not reveal the content of specific programs which may be proposed in 1950 or any other year. Nonetheless, it is our earnest desire that this report will have some influence upon attitudes both in business and in government, and that it may uncover the solid ground on which they can deal with each other in ever-increasing harmony and trust.

A NEW GENERATION NEEDS NEW IDEAS

The particular urgency of this subject exists because there has now grown to maturity a whole generation of Americans touched by the influence of extremists who look upon conflict between business and government as normal. Conditioned by the depression era, extremists on one side have said that our business system broke down through fatal defects and that government took the whole leadership in putting it together again; while extremists on the other side have blamed government for all the tribulations of business. The new generation of Ameri-

cans should always remember that the breakdown resulted from errors on the part of both government and business; that both joined in forging some of the most practical measures for recovery; and that both must admit imperfection because the recovery was incomplete until the war restored maximum production and employment.

This new generation of Americans has also observed that some of the national programs directed toward economic change have initiated from government and been opposed by some spokesmen for business. But the extremists on either side should not overlay this observation to range either government or business along with the angels or the devils. Rather it should be recognized that it is a primary function of government, representing the whole people, to view the economy as a whole and to propose general measures. It is the function of business, as the main operators of the going economic system, to be conservationist if not conservative and to be wary about discarding workable machinery before better machinery has been clearly tested. In the interaction between these two functions, which is essential if we are to preserve both free enterprise and free government, the clash of viewpoint and the reconciliation of means to ends are in themselves beneficial, particularly when undertaken in good spirit.

We have now moved far enough away from the depression of the early thirties to start looking ahead, and to appraise the heartening evidence that free enterprise and free government have blended their varying strains into a rewarding effort. The conduct of the war was an example never to be forgotten. The moderate character of the 1949 recession, and the upward turn which followed, would have been impossible without business policies as well as public policies based upon greatly increased understanding of economic affairs.

The time has come to develop the prospects of the American economy for further economic progress and human happiness. Unlike other countries we were not decimated by war; we do not suffer from underdevelopment or impoverishment of basic plant and equipment; and we have the operational and financial skills, the splendid labor force, and the solid institutional structure to realize in full the promise of America.

The only thing that could stand in our way—provided that lasting peace is achieved—would be excessive internal discord. This would not stop our economic progress in the long trend, but it could slow it down greatly and leave us subject to costly fluctuations which we probably have the technical know-how to avoid or mitigate.

At this juncture, there may be value in a candid stocktaking of current relations between business and government. We shall place the greater emphasis upon the vast progress which has already been registered and upon the assets which have consequently accrued. But we cannot neglect some of the problems yet unsolved.

II. Trends in Government's Attitude Toward Business

The attitude of government toward business has always been favorable, in the sense that responsible public servants have always wanted our free enterprise system to thrive and prosper. The course of events shows that many of the public policies adopted over the years have contributed toward the strength of the economy, although they are always subject to refinement and improvement. Governmental thinking has never been static, and it may be helpful to try to discern recent trends under the impact of experience.

No one person can speak with absolute certainty or comprehensiveness about these trends. The minds of various men and women in our public service are not melted down and fused into a single instrument. Policies and pronouncements, even when by the President or by the Congress—and many others decide issues and make statements—reflect a range of training, temperament, and viewpoint as wide as those in any other sector of our national life. However, while the Council can speak only for itself, we believe that from our strategic point of observation we can detect a prevailing trend of thinking about our business system and its problems.

FROM THEORY OF STAGNATION TO PRACTICE OF GROWTH

The first trend in the attitude of government toward business seems to the Council to be this: the doctrine of secular stagnation no longer finds place in any important public circle with which we are familiar. During the depression years, a significant body of thought held that the forces of business expansion had spent themselves and that government must provide the dynamic force for renewed growth. The thought may have had some relevance then; and the persons who held it developed some useful devices. But today the doctrine of secular stagnation has been replaced, in our judgment, by the firm conviction that our business system and with it our whole economy can and should continue to grow. This is illustrated by the statement of President Truman that we can achieve a 300 billion dollar economy within a very few years. We regard it as an historic event when the occupant of the most persuasive office in the world acts upon the proposition that our business system has further opportunities which transcend even those it has seized upon in the best previous decades. A member

of the Cabinet, the Secretary of Commerce, has recently applied the same realistic approach over a longer time span.

This sentiment on the part of important officials would be significant without independent verification, because it would have a controlling effect upon their attitude toward the business world. But we also note the recent corroboration of these growth assumptions by non-governmental economists who are highly regarded by businessmen as being unusually conversant with their problems.

FROM "MORE FOR SOME" TO PROGRESS FOR ALL

The second important trend which the Council senses in the attitude of government toward business is the realization that efforts to promote expansion of the total production and income of the economy are more significant than measures to "redistribute" the current product. In an economy foredoomed to inability to provide an adequate or rising standard of living for all industrious families, there might be some reason for according the resharing of output priority over efforts to increase output. The rationing resorted to by people in time of famine is an extreme illustration. But the notable expansion in production which our economy has achieved in the past and can certainly repeat or excel in the future, coupled with the observed fact that this so much lifts the general standard of living, should receive foremost consideration in economic programs and policies.

Of course, we cannot postpone efforts to improve the lot of the underprivileged until they can be lifted to reasonable levels by the lever of general growth. And measures directed specifically toward improving the productivity and incomes of low-income groups have favorable impact upon the whole economy. At the same time, primary emphasis upon general growth offers a more workable formula not only for the business community but also, the Council believes, for other groups as well. For once it is appreciated that the general growth of the American economy can create within less than a generation a truly good standard of living for all, then there is reduced to manageable proportions the ancient conflict between social equity and economic incentives which hung over the progress of enterprise in a dynamic economy.

FROM SOCIAL THEORY TO ECONOMIC "BALANCE"

The third important trend in the Government's attitude toward business, as viewed by the Council, arises from fuller realization that the flow of income to different parts of the economy should be viewed as an economic no less than a social problem. Certainly a people's ultimate objectives are social, being concerned with well being, and social thinking will never lose its utility. But the application of more precise

economic analysis to problems of income flow will yield benefit to all by reducing the problems of ways and means to soluble terms.

The use of economic analysis to refine and sometimes reformulate social theory will help to broaden the areas of understanding and agreement, without which the tensions and conflicts in a free economy of large organized groups might in the end become unbearable. That unsocial socialist George Bernard Shaw argued in one of his famous books written for American women that the only sound income distribution was absolute equality, since nothing else could be called "fair" in the absence of any precise measurement of the relative productivity or relative need of everybody in the community. While this is a *reductio ad absurdum*, it illustrates that contending individuals or groups in a free society could never arrive at viable agreements as to what share of national income each should get by the unalloyed application of social principles. Any effort to apply such principles fully or even excessively would involve the whole nation continuously in fracas and confusion.

Concentration upon the central objective of a stable and expanding general economy identifies more manageable although still difficult approaches to the problem of income flow. It then becomes possible, albeit not easy, for businessmen, workers, and farmers to seek that share of the total product which is most conducive to the progress of the whole economy and thus to their own best interests in the long run. The same approach should be used to evaluate those government programs which channel the flow of income from one spot in the economy to another, to test whether these programs promote general stability and expansion or rob Peter to pay Paul.

The nub of the problem of economic "balance" is to encourage sufficient funds and incentives for the growth of productive facilities which fully absorb our technology and manpower, while promoting sufficient flow of income to ultimate consumers to clear the markets of goods and thus to avoid periodic "overproduction." The Secretary of Commerce has put forward this idea of "balance" so cogently that it deserves repetition:

As we look down the road ahead, what do we see? Standing squarely and obstinately ahead of us on the road to a richer America is one great question mark. How shall we divide equitably among consumers, labor, management, capital, agriculture, and government their shares of our production? People are called liberal, radical, conservative, or reactionary depending upon the way they approach this most difficult of all our economic problems. Some pessimists say that there is no solution to this problem but the one resulting from the struggle between organized groups. They say that capital always wants more than its fair share of production, that labor will never be content until it takes all of the profit out of business, that farmers will not rest until all other groups are supporting them, that government officials will not be happy until they manage the whole economy and become the only privileged class in America. I am not so pessimistic. Many businessmen understand that business success depends upon well-paid, self-respecting workers and upon the ability of the public at large to buy what business produces. Many workers understand that business cannot operate at a loss, and that some return on capital

investment is proper. Many farmers realize that other groups are entitled to consideration and that the farmer is not cultivating a fenced-off lot.

We have not yet reached the time when these groups forget their special interests and talk out their differences in a spirit of sweet reasonableness. However, we have made and are continuing to make progress. Most Americans now understand the importance of business investment as well as the importance of mass purchasing power. We have passed the time when intelligent Americans use the word "profit" as a curse. I believe all of us can agree on the fundamental principle that profit is good when it is reasonable and when it is used to produce more of the things we need.

To this problem we must apply the idea of balance. What division at any given time will promote the smooth operation and further the balanced growth of our economy? To answer this question we must know as much as possible about our economy and we must also be willing to abide by the facts. In other words, we should bring to the solution of our problem scientific analysis and a scientific attitude of mind.

When this general idea of economic "balance" is translated into the factual analysis which alone can give it practical significance, it becomes crucial that the business world appreciate the motivation underlying such analysis. We may illustrate by citing some of the previous work undertaken by the Council. During the postwar inflationary boom between 1946 and 1949, we took the position that the bunching of unusually high profits and an unusually high level of business investment, accompanied by price-income developments which did not seem to promise sufficient consumer demand to maintain maximum employment and production when certain temporary props were removed, should not be viewed with equanimity. This did not mean that we were adverse to profits or profit-makers or were throwing partisan weight on the side of the consumer or wage earner.

Such was not our position. We simply foresaw in 1947 and 1948 that the "balance" between investment and consumption, while compatible with a very high level of activity in 1947 or 1948, could not be sustained indefinitely and that a new "balance" would need to be struck for a growing peacetime economy. We were concerned that, as profits declined during the transitional striking of this new "balance," business might have become fearful and contracted investment and employment unduly. This would have accentuated the downward spiral. Instead, we urged recognition that a temporarily lower level of return than the 1947 or 1948 level was inescapable for a while. If this was recognized, then, when the economy had passed safely through the adjustment tests, profits and investment along with consumption could again resume an upward course as the economy in general moved upward on a noninflationary basis.

Nor were our comments about the relationship between prices and consumer incomes during the inflationary boom intended to suggest that consumption between 1946 and 1949 should have been higher when there were no more goods to consume. The point rather was that looking forward to 1949 and succeeding years, when bottlenecks would be broken, productivity increased, and the plant and equipment improvements of the reconversion period fully felt, the price-income structure would have to readjust to the expanding volume of

consumption needed for maximum production, employment, and business opportunity. We advised business that some of these price-income adjustments should be started early and made gradually, for experience indicated that if too long delayed and then subsequently bunched over too short a period of time the consequence would be a dangerous decline in business activity. This in turn would cause profits and investment, the most volatile parts of the structure, to decline even more rapidly.

Fortunately, the practices of more and more representatives of the business community are coming to conform more closely to the tenor of what we have said. In the early 1949 recession, the majority of businessmen did not react to lower profit margins or prospects by the erstwhile traditional acceleration of cutbacks, rapid price deflation, wage reductions, and layoffs. Some occurred, but they generally took place with moderation and discernment. Many businessmen realized that we were working our way toward a better "balance," and that if they maintained steady nerves through a short but perilous phase the fundamental strength of the economy would turn us again upward. This does much to explain what transpired during the second half of 1949, although the march to maximum production and employment is still to be completed.

Our conclusion that in the long run a "balanced" economy would require the expansion of consumption opportunities at an even more rapid rate than the expansion of investment—although both should grow—has been matched by the similar findings of many nongovernmental economists. It is not the Council's purpose here to vindicate its own specific conclusions. We merely point out that our approach departs from the earlier and narrower perspective sometimes applied by economists; and that many of our profession are now in accord with our views.

TOWARD MUTUALITY OF INTERESTS

The fourth advance in the attitude of government toward business, as appraised by the Council, derives from the three already listed. The problems of our economy appear no longer primarily as problems of protecting the shippers of the West from the "interests" of the East, or the farmers of the South from the bankers of the North, or the workers in general from the industrialist class, or the consumer from the farmer. To be sure, government still has the function of preventing any one group from taking unfair advantage of another, and laws and administrative devices are necessary for this purpose. But national economic policy should center mainly upon the basic interdependence of the long-range interests of various groups. If we are to endure and grow as a nation, the things which unite us must become infinitely more important than those which divide. The function of gov-

ernment is, without favor or preference, to test each of its own actions by the long-run common good. Moreover, government should stimulate that thinking and analysis by business and other elements in our free-enterprise system which will help them to advance the general economic welfare and thus to reduce the requirements for public supplementation.

In an expanding economy, the lifting of low-income families to a far higher standard of living, the improvement of agricultural programs consistent with the needs of urban consumer incomes and also promoting parity of income for the farmer, the provision of adequate funds for a rewarding level of business investment and profits, and the meeting of our domestic welfare and international security requirements, are not incompatible objectives. Attainment of each objective is inseparable from attainment of the others.

REGARDING BUSINESS SIZE AND PRACTICES

The Council finds the fifth trend in the attitude of government toward business related to the size, structure, and behavior of business organizations. No thoughtful person within government wants to abandon or vitiate the "antitrust policy." The stultifying results of excessive cartelization in some other lands gives renewed evidence of the prescience of those who wrote the Sherman and Clayton Acts and established the Federal Trade Commission. Still, it is important to realize that our industrial problems have changed continually and require recurrent examination. Under our system of law and administration, many adjustments to new situations are made interstitially without organic reconstruction of the legal framework. These adjustments have been going forward over the years. The process is never finished.

In a stable and expanding economy, there is room both for well conducted big business (with its unique facilities for scientific and developmental experimentation) and for small business with its display of individualism and self reliance. Small business should be protected from any predatory practices by its larger neighbors, and all business should be protected against unfair competitive practices by units of any size. Yet the truth at least in part is that small business is threatened not primarily by big business but rather by big instabilities in the economy. When the economy attains full prosperity and is moving upward, small business in general does very well; but when the economy hits the toboggan many small businessmen are ruined not because they are less efficient than big business but because they are weaker and have fewer sustaining resources. An economy that grows steadily, as our economy can, would provide manifold opportunities for small business. Small business has some unique problems of obtaining financing, and more efforts should be directed toward solving these problems.

We are still a long way from having completed the necessary rethinking of problems involving business size and practices. Much more

work needs to be done. It should proceed in a spirit of fair objectivity toward business both large and small.

FROM MERE POLICING TO AFFIRMATIVE FACILITATION

The Council would describe the sixth trend in the attitude of government toward business as being away from the purely negative or policing function and toward the affirmative or facilitative approach. Our economy has become too complicated for government to function best simply by placing "don't" signs all over the lot. Some things, of course, the government must continue to prohibit or regulate—and regulation may be focused in part upon affirmative objectives. But the central problems of economic "balance" require adjustments which cannot be achieved mainly by regulation. For example, regulation is inadequate to correct an economic situation in which business might not receive the incentives to stimulate a high enough level of investment. Yet an inadequate level of investment can probably wreak economic havoc. Consequently, the fiscal, credit, monetary, and other facilitative operations by which government may promote an environment conducive to business expansion are at least as important as the more traditional watchdog functions. Those government policies and programs which affect farm income, industrial wages, or consumer incomes are also of prime importance and call for increasingly thorough and objective analysis.

AWAY FROM SPECIFIC CONTROLS

The seventh trend which the Council observes in the attitude of government toward business relates to specific controls. The war made these controls necessary. In our judgment, they were abandoned too soon and could have been helpful in curbing the inflationary boom, and rent control is still necessary. A better understanding between business and government might even make it possible to have a broader range of restraining measures available in reserve without concern that they would be used prematurely or excessively. However, in the current and foreseeable economic situation, it is far less important even to contemplate the restoration of the specific controls than it is to realize that they do not for the long pull answer the basic economic questions confronting the American economic system. In peacetime, the mere authority to fix prices or wages does not in itself answer the question of what relationship between prices and wages will be fair to all concerned and most conducive to economic stability and growth. The answer resides in improved economic understanding rather than in fiat. Nor, in peacetime, does the mere presence of control authority upon the statute books obtain the popular understanding of price-wage problems essential for their workable adjustment; and if this popular understanding exists, we should in peacetime find better ways than specific controls to translate

it into action. The Government should use its fiscal and monetary powers to promote economic "balance," and supplement these with such well accepted programs as farm price supports, social security, minimum wage legislation, developmental programs, etc. The other phase of the task of promoting "balance"—which resides in the continuing adjustment of prices and wages and profits—should be left to the actions of managers and workers within our business system itself.

FROM "COMPENSATORY" THEORY TOWARD MORE RELIANCE ON
ENTERPRISE. AND A WORD ABOUT KEYNES

The eighth, and in the Council's judgment the most important trend in economic thinking within government as we observe it bears upon the respective scope and weight of public action and private action in promoting stability and growth. During the mid-1930's particularly, there grew up an influential school which held that our free enterprise system was necessarily subject to violent fluctuations which could not be ameliorated substantially *within* the system. It held that only government action, mainly through enlarging or contracting the volume of taxation and public spending, could fill in the gaps in employment and production when these became large or curb inflation when it became dangerous.

The experience in the 1930's, however, demonstrated that when the private economy ran sufficiently far downhill "compensatory" action by the government became entirely necessary but *was not alone sufficient* to restore and maintain satisfactorily high levels of general economic activity. The reason for this was not simply that the "compensatory" action was not big enough. The fact was—and still is—that the range of useful projects susceptible to undertaking by government cannot be sufficiently voluminous to counteract fully a general depression—even when coupled with tax reduction. Further, public action beyond certain levels or in certain fields may be offset by declines in private spending and investment, so that the net gain is not equal to the total number of public dollars spent. Similarly, in fighting inflation, mere increases in taxation and reductions in public spending, while useful weapons, are difficult to employ fully enough to curb inflation without bringing on an excessive deflation. Nor do these fiscal measures alone deal adequately with the internal maladjustments in the price-income structure which are primary sources of danger in the kind of inflation that we have recently witnessed.

This leads to the conclusion that "compensatory" public action can help to iron out minor fluctuations of the business cycle and must indeed be used if big ones develop, but that complete recovery from a substantial downswing depends primarily upon the revival of private investment. And because that revival becomes progressively harder to accomplish as the economy moves further downward, the main concentration of economic policy should be upon encouraging stability and

growth within our free enterprise system itself. This is doubly true in a prosperous period like the present, when action is feasible before the eleventh hour.

Many government policies, if appropriately designed, can place foremost emphasis upon encouraging steady business expansion and thus minimizing the fluctuations in business activity. This approach is sometimes referred to as creating a climate favorable to business. This is true although the responsibility does not lie wholly with government. Within enormous areas of action and decision, business holds within its own hands the factors which condition its course. This is the essential nature of a free enterprise system, and business should be encouraged when government recognizes this cardinal fact.

Despite all efforts by business and government to promote steady growth, "compensatory" policies form an important part of the techniques to be used for stabilization purposes. The difference between the exaggerated use of the "compensatory" approach and the Council's approach is a matter of degree or emphasis. This problem is further treated in a later section of this report which stresses the need for somewhat more stability in national economic policy.

Sometimes the purely "compensatory" approach is referred to in popular discussion as "Keynesian economics." In fact, Keynes placed more emphasis upon structural problems than upon the cycle. Lord Keynes was too sizable an economist and too enterprising a technician for us to attempt to evaluate his great work in a report of this kind. We shall content ourselves here with saying that, insofar as any popular version of the "Keynesian economics" identifies it with the school which placed exaggerated stress upon "compensatory" action, that school is neither representative of our own thinking nor in our opinion characteristic of any important segment of government thought today.

III. Trends in the Attitude of Business Toward Government

As government economists, it would be presumptuous for the members of the Council to attempt a description of business thinking as fully as we have attempted an appraisal of the prevailing government attitude toward business. But it may be helpful to sketch briefly our own impression of business attitudes, particularly because public appraisal of these attitudes obviously interacts upon government's attitude toward business. We discern a trend which is distinctly propitious to mutual accommodation and adjustment.

GAINS THROUGH BUSINESSMEN IN PUBLIC SERVICE

American business is highly pragmatic, and its point of view has been vitally affected by the war effort which brought to countless businessmen a new experience in public service. There they observed at close range the operations of the whole economy, the interdependence of its parts, and the common problems of all. True, the war economy and its problems, as well as the solutions devised, were drastically different from anything wanted in peacetime. Yet many businessmen in Washington during the war developed points of view which have immensely influenced their subsequent thinking.

The net result has been an increased appreciation by business that business and government are not enemies but friends; and that persons permanently in the public service have the same virtues and faults as Americans elsewhere and are equally committed to free enterprise as well as free government. The government service needs additional inducements to bring more skilled businessmen into that service in peace no less than in war. The idea that a businessman working for government is "serving two masters" (even when he has divested himself of private interests which might conflict with his public duties) is a relic of the earlier thought that the sole or main purpose of government is to police business. The problems of economic policy have shifted their center of gravity away from this earlier concept toward an area where the problems of business and government interpenetrate and require complementary action. It is therefore desirable that the most practiced exponents of industrial management should participate in government. This is equally true of the practiced exponents of American trade and industrial unionism, as well as of those who have been closest to the problems of the farmer.

Through the war experience, and in other ways, businessmen have come increasingly to realize the immense influence of public policy upon the American economy. The prevalent view that government should adopt policies which "create a favorable environment" for business is a far step from the earlier notion that government should just "let business alone." For that could happen only if government had no policies which affected the business environment. In addition, there is an increasing measure of agreement about many policies now in effect. Farm price supports, social security, Federal Reserve operations, and Treasury debt management, to mention a few, have passed into the realm where the debate is no longer at the central core but instead on the periphery—dealing with improvements or modifications in detail.

This realism on the part of businessmen about the role of government in modern economic society is accompanied by a mature view concerning the need for a variety of policies blended in just proportion. This has replaced an earlier view that some one trick or gadget would maintain the economy in good health. Very few businessmen now believe that the whole answer lies in some minor change in interest rates, in whether the Government supports its bonds at par, in whether some particular tax reform is adopted, in whether the labor laws are amended or repealed. Instead it is recognized that big government is even more complex than big business, and that the same skepticism of panaceas and the same balanced judgments on a wide range of problems and procedures which characterize the successful business manager are equally necessary on the government scene.

REJECTION OF MERE SLOGANS—THE PENSION EXAMPLE

Recognition by businessmen of the complexity of the modern economy has made a majority of them increasingly distrustful of mere slogans or shibboleths as a guide to the relationship between enterprise and government.

By way of example, mere slogans would lead all businessmen to believe that privately negotiated pension systems are preferable to the expansion of Federal old-age security because the former is "free enterprise" and the latter involves "government." But this is not happening. Many businessmen, on entirely unselfish grounds, are questioning whether the random development of unequal pension systems in scattered industries would really leave the business system more truly free than the systematic development of uniform old-age security. And they are asking other questions. If thoughtful business and labor have both been concerned about the wide disparities in the wage structure, will this problem be lessened as an equal or greater disparity arises in business costs for pension plans developed sporadically? If labor mobility is a prime characteristic

of dynamic free enterprise, will business or workers have more freedom when nontransferrable pension benefits weld particular workers to particular jobs? If business success depends upon flexible adjustment to changing circumstance, should business entangle itself in cost ventures which necessarily project a generation or longer into the future?

The Council is certainly not prepared to censure the drive toward privately operated old-age security, which has arisen from delay in enactment of changes in the Federal system. It seems to us that many workers and employers have had no choice but to do what they have done. Nor do we take the doctrinaire position that some thoughtful combination of public and private insurance against old age may not usefully emerge, although we incline strongly toward immediate expansion of Federal old-age security as the more urgent requirement. Our main purpose is to illustrate that certain functions performed by government may be more consistent with the practical welfare of free enterprise—including both management and labor—than excessive efforts by private business to perform those particular functions. And because more businessmen are adopting this pragmatic view, the prospects are increasingly bright for workable alignment of the functions of business and government.

ENLARGED UNDERSTANDING OF WORLD CONDITIONS

There are also general forces of compelling magnitude which contribute toward a better understanding by the business community of the problems of government. This is evidenced in a statement made by Mr. J. Cameron Thomson (on behalf of the Research and Policy Committee of the Committee for Economic Development) before the Joint Congressional Committee on the Economic Report on November 23 of this year. Mr. Thomson said:

The idea that great economic instability is inevitable in a free society is one of the most dangerous ideas at large in the world today.

Most businessmen in recent years have not denied that *great* instability could be avoided. The debate raged only as to whether such instability was not preferable to even the minimum amount of government action—in addition to extensive private action—conceded to be necessary for its avoidance. We think that this debate is receding, with so many businessmen sharing the viewpoint expressed by Mr. Thomson that we cannot confront the world with another American depression and still maintain our position or security in the world of the future.

The informed businessman of today is acutely aware of the menacing challenge to free enterprise and free government which confronts the West. He knows that this challenge must be met by firm and comprehensive countermeasures, largely in the area of our international economic policy. He knows that the United States must take the leadership in these measures, which are fundamentally economic in

character. He knows that for both historic and practical reasons government must help to mobilize and give leadership to the programs involved. Thus the businessman appreciates that perhaps the most important phase of public policy today is directed toward the literal salvation of the one kind of world in which the businessman can breathe.

In the struggle to preserve freedom, the businessman needs government; and government needs the help of businessmen in the development of practical programs. These are no times for bickering or prejudice. Ironically, the actions of those who believe that free enterprise and free government are incompatible, and that one or the other or both must be destroyed, are prompting free enterprise and free government in America to close ranks and to work together in the supreme cause of human freedom.

IV. Further Needs in Government Economic Policy

Despite much progress in the relations between business and government, there are still some gaps in national economic policy as viewed by the Council. The word "gaps" is used advisedly to indicate our belief that improvement in current operations should proceed at least apace with ventures into new fields. This does not mean that no new programs are needed, or that the nation can pause in building upon solid foundations. While this report is not the place for specifics, we have said that measures such as social security should now be expanded. But one way to safeguard progress is to consolidate the gains which have been made.

NEED FOR FURTHER HARMONY AND CONSISTENCY

A cardinal task, as the Council sees it, is to achieve even more harmony and consistency among those outstanding programs of government which greatly affect the whole economy. During the critical mid-thirties, when some of the structure of current national policy was built, there was no time to develop symmetry for the various wings of the structure or to connect them with the center. This was inevitable during an economic emergency, but there is no such emergency now. The privilege of men and agencies within a free government to give differing advice should be cherished. But this does not mean that the final execution of public programs touching upon the whole economy should not achieve that internal consistency and that harmonious relationship to defined common objectives which any large undertaking demands.

In the context of this problem, much good may be derived from the comprehensive work of the Hoover Commission and from the steps which the President and the Congress have already taken to implement it in part. More efficient use of personnel and of instrumentalities can register great gains for the taxpayer and for the country. But administration is an arm of policy, not the heart. For every dollar affected by the use of personnel, there may be a hundred or a thousand dollars affected by basic economic policy. It is here that the most costly mistakes could be made or the most useful services rendered. Here also manifold gains have already been affected, but there is need for still more progress.

This progress toward still further harmony and consistency in governmental economic policy does not in the judgment of the Council call for the establishment of more agencies or committees. It calls instead

for a unifying framework within which each separate economic policy may be tested against its effect upon the general economy and upon the promotion of maximum opportunities for employment and production in free, competitive enterprise. This depends in turn upon the further use of machinery which the Congress has already made available and which the President has always been ready to use—the machinery of the Employment Act of 1946. Progress in this direction is reviewed later in this report.

NEED FOR MORE STABILITY

As government economic policy becomes increasingly consistent, it should also become somewhat more stable. The prudent American family makes some arrangements lasting 20 or 30 years; a moderately large business may look 50 years ahead; and a local government sometimes looks a century ahead. The biggest venture of all, our Federal Government, should strive gradually to modify its habitual practice of carrying almost all of its major policies and programs on a year or year and a half basis. The credit and spending and regulatory and tax policies of the Government are so highly conditioning to the whole economy that the degree of stability of these policies affects the degree of stability throughout the whole business world.

Some short-run shifts, indeed, are necessary to enable the Government to alter its position and thus to “compensate” for changes in the private business situation. But we have already in this report indicated that if the Government moved gradually toward placing somewhat more of its own activities on a somewhat more stable and longer-range basis, this might add greatly to the stability of the whole economy. The placement of some public programs primarily upon this basis rather than upon a “compensatory” foundation would also hold these programs truer to their intrinsic purposes. The intrinsic purpose of public works is not to take up slack in employment, but rather to build up our national wealth by procuring certain end products which the country needs but which cannot be produced in any other way. Similarly, a decision to expand our educational facilities should be related closely to the priority value which we place upon education, rather than to the usefulness of school construction in taking up a business slack. All or some of these programs may to a degree be expanded and contracted in response to variations in private business. But the variation should not be carried so far as to interfere with the primary purpose of these programs.

Our public programs are supported out of the production record achieved by the economy as a whole. We should ask ourselves what is the productive potential and capacity for growth of our economy over a reasonable span of years, assuming that we are fairly successful in maintaining full utilization of our material and human resources. We should then ask ourselves what part of our output of materials,

money, and effort—over a similarly reasonable span of years—we want to devote to specific purposes such as public improvements and education. The Council admits that this involves social as well as economic judgments; but nonetheless the problem has elements which prompt economists to suggest an orderly method of arriving at results although they do not presume to dictate what these results should be.

The Council thus leans toward some further development of reasonably stable policies, in a few major conditioning areas, to cover a moderate span of years. Allowance should be made for the growth potential of the economy, instead of basing policy upon the assumption that the economy will linger indefinitely near a point reached after a half year of recession or fail to move again toward maximum levels of employment and production. This stability and confidence, displayed by government at so important a sector of the economy, might favorably condition also the free enterprise sector.

The argument may be advanced that more stability in some public policies is impractical because “we cannot see that far ahead.” The problem is admittedly one of degree. But it is easier to predict safely that our economy will grow in the long run than that it will grow in 1950, although we believe the latter also to be true. This is not to say that short-range adjustments have no place in a rounded economic policy; some of these short-range adjustments may now be needed, but they should not be asked to carry too heavy a load. If, despite the effect of some reasonably constant public policies, serious downturns in general economic activity should occur, it may still be practical to readjust public policy upon observation of the event. Economic downturns do not progress so rapidly that they leave no time for effective changes in policy. However, we repeat the more important consideration that temperate progress toward somewhat more stability in government policy would promote more confidence and stability throughout the whole economy and thus help to hold the manifestations of instability to manageable proportions.

One caution is called for. The foregoing discussion develops principles for gradual application, but it cannot be accepted as a necessary guide to specific policies during the coming year. For example, while we should aim in the long run for reasonable stability in tax policy, the great changes in the tax structure over the most recent years and the double reversal of economic trends in 1949 may make it necessary to alter the tax structure somewhat before a basis for stability in future years will have been laid. But this does not vitiate the principles which we have set forth; it simply proves that the objective cannot be fully accomplished overnight. The Council hopes that the specific policies soon to be announced for 1950 will show some progress toward the goal of improved stability and that this goal will be increasingly pursued in subsequent years.

NEED FOR CORRELATION OF WELFARE PROGRAMS, ESPECIALLY SOCIAL SECURITY, WITH GENERAL ECONOMIC POLICY

The need for still more harmony and consistency in national economic policy, and for its placement on a somewhat more stable basis, has cogent applicability to programs such as social security. A still better understanding between business and government would result if the excessive separation were lessened between "economic" and "social" programs—between a government interested in encouraging the growth of the economic system and a government interested in "welfare." Those who quite appropriately raise the question of how much "welfare" is going to cost, or whether our economy can stand that cost, clearly recognize that programs of social security which involve billions of dollars in taxes and in public outlays cannot be divorced from economic considerations.

The support of people who are too old to work or who are unemployed or ill does not create wealth. It is not like the production of goods and services. For the most part, it enables certain individuals to consume wealth which is being currently produced by others. The real question is how much of current production may be diverted to support this particular type of consumption (above a base subsistence level, for that level of support the economy must bear in any event) without sacrifice of relatively more important objectives. This makes social security an economic problem in the same degree as striking an appropriate balance between business investment and ultimate consumption, or between defense and foreign aid programs and the requirements of our domestic economy.

Sometimes it is said that, whatever amount of income may be flowing to the old or to the unemployed, it is economically desirable because it creates purchasing power and thus provides demand for the products of industry. But no *additional* purchasing power is created if this income is simultaneously taken in equal amount from those who are still employed. In fact, there might be future deflationary elements in a social security system which for too long provided a large excess of forced savings going into reserves over current payments to the aged. Payments to the old or the unemployed which resulted from deficit financing would create purchasing power of a sort. But purchasing power generated in this way, while it would be better than no purchasing power at all, would not have equivalent economic value to purchasing power generated by production efforts. For similar reasons, cutting the workweek simply to provide jobs for more people—which is a form of sharing unemployment—would never be as beneficial as obtaining the full use of our productive resources, even though it might be a necessary expedient if we failed egregiously in the more important task. Likewise, the age at which workers retire or the size of the benefits they receive should not be determined by the fallacious idea that this is a good way to create more pur-

chasing power by adding the purchasing power of those who are not working to the purchasing power of those who are working. We should start with the assumption that our economy will be most productive by providing useful jobs for as many people as are able and willing to work. In that event the national policy with respect to the general age of retirement would be based not upon an artificial method of leaving more job opportunities for others, but rather upon a decision that the functioning economy can afford to support people who have reached a certain age without requiring that they work further.

Social security programs are viewed in a distorted perspective unless it is realized that their justification rests upon two grounds. First, that the cost of caring for the old, the unemployed and the sick always falls upon the economy; and that bearing this cost in a systematic way is more efficient than bearing it through charity or improvisation. Second, that as an enlightened nation we are willing and even eager to divert a portion of our annual output away from capital replenishment and away from consumption by current producers in order to make life more livable for those who are unable to produce through no fault of their own. The appropriate test for the size of a social security program is how much of our resources on balance we wish to devote to this humane purpose, taking into account all the competing purposes and needs of our kind of economy. It is true that the social insurance programs make our economy somewhat stronger by cushioning it against fluctuations by their "built-in stability" effects. But the larger question is how much of these programs a strong and rich economy can and should afford.

The true nature of the social security problem being what it is, the concept of "saving" for social security is in one sense useful and in another sense misleading. It is useful to recognize that we must save in order to enlarge our productive equipment. Without such enlargement, our economy would not be able to turn out more goods from year to year and therefore would not be able to afford the progressive expansion of social security. But it is misleading to assume that through any process of bookkeeping, either personal or national, millions of people can "save" the food, and clothing, the medical care and recreational allowances which they will be consuming 30 years from now when they retire. What they consume when they retire will be produced not by themselves but by the working force at that time, and what they save now should be channeled insofar as feasible into current investment opportunity.

The Council strongly favors the national system of social security which involves contributions from employers and from workers on a systematic basis, and which also involves contributions by government. This is the best way to protect people in their old age as a matter of right, and not to leave what may happen to them later on subject to unforeseeable policy decisions in the future. Yet our discussion of the social security problem implies that gradual efforts should be made to

improve the contributory system so that at least part of the contributions would be more nearly on a "pay as you go" basis. By this, we mean the gradual development of a closer balance between social security receipts and payments from year to year. The ultimate objective should be toward making withdrawals from the economy for the purpose of social security roughly balance the contemporary cost of benefit payments, although it might always be desirable to maintain some "reserves" of significant size. We also believe that, as coverage becomes more general, a larger part of social security receipts should be obtained through general revenues rather than payroll taxes.

This gradual development would be sound economics for reasons already given; and it would also provide a better gauge as to the magnitude of future social security benefits which we can afford to enact into present legislation. For if enactment of legislation now involves the commitment that X number of people who will not be working 30 years from now will receive Y number of dollars of old age benefits per month, the real test of whether the nation can afford such a program is not XY dollars per month measured against the *current* size of the economy but XY dollars per month measured against the productivity of the economy *30 years from now*. Social security expansion now, insofar as it applies to persons who will not retire for many years, should make considerable allowance for an assumption of continuing secular economic growth. Almost all of our national policies in the long run depend upon the validity of this assumption. For otherwise we face continually rising unemployment, under-utilization of our resources and technology, and increasing disturbance to our whole economic system.

The Council's main reason for offering this analysis is to promote the application of sound economic principles to social security matters. It is not our function in this report to argue for a social security program of any particular size. Yet it seems clear to us that the application of sound analysis reveals that our nation can afford a considerably expanded social security program without impairing our economic stability or weakening our growth potential.

COORDINATION OF NATIONAL ECONOMIC POLICY IS NOT "CENTRAL PLANNING"

The Council's interest in the orderly evaluation and systematic reconciliation of public policies should not be misconstrued as any leaning toward "blueprinting the economy" or "central planning." Except for the reference to social security to clarify certain points in our analysis, we have not here dealt with any specific additions to governmental programs. We have only stressed that, *whatever* the scope or extent of government programs, there should be applied to them those principles of consistency and harmony which are valid in the case of any material undertaking of business as well as government. The use within gov-

ernment of that "budgetary" concept which is applied by any large corporation in the measurement of its competing needs and prospects is compatible with the maintenance of a flexible and pragmatic spirit in government as well as in business.

In the long run, this approach should lead to the simplification rather than to the proliferation of public programs. For the more successful government becomes in weeding out inconsistencies and adapting means to valid ends, the more the taxpayer will be saved in direct administrative costs. And the more effectively government weighs the effect of its established programs upon the whole economy and upon the course of business development, the more confident and prosperous our business system should become. This, in turn, may help to protect us against those serious economic downturns which provide the main impetus for certain types of public intervention in response to public need.

V. Further Needs in Business Preparation for Stability and Growth

Along with further progress in those government policies which affect business, the record of recent years leads the Council confidently to anticipate further progress in business thinking and practices. This will help our business system to maintain that major responsibility for the condition of our economy which is ascribed to it under the American combination of free enterprise and free government.

FURTHER ACCEPTANCE OF "MAXIMUM" OBJECTIVES

First of all, our business system needs to embrace even more fully—as its enlightened leadership has already done—the goal of continuous maximum production and employment. This is not to say that so high a goal is readily obtainable. Possibly some periodic setbacks of moderate size are the price we must continue indefinitely to pay for the freedom and flexibility which make our system so dynamic in the long run. But this is entirely different from saying that the setbacks are desirable as well as difficult to avoid. Very few businessmen really believe that the drop in the industrial production index by about 16 percent, and the increase of unemployment by about 1½ million, which took place in 1949, left them with a more confident feeling than if a better balanced expansion in 1948 had prevented this decline. We are recovering from that downturn because of the strong elements in our economy, and not because of the deficiencies which generated the downturn. As our system learns to develop still stronger elements, even if it does not succeed in maintaining continuously maximum levels of activity, the downturns can become more moderate and the upturns can become more certain.

Nobody should confuse the classic theory of how downturns occur with the erroneous belief that they are helpful. Saying that a downturn in production and employment is an adjustment of supply to demand may be true; but supply and demand were thus "adjusted" even in 1932. Saying that a downturn is inevitable, when backlogs of demand accumulated during a war period are worked off, may be a correct observation about the past; but it is simply another way of saying that we have not yet learned how to make full use of our productive capacity in peacetime. It is better to aim constantly toward maximum production and employment, because this will in the long run make our think-

ing clearer and our achievements greater, even though we have not yet learned enough to reach this objective fully every year.

FURTHER REALIZATION THAT PUBLIC SENTIMENT AFFECTS THE ECONOMY

Occasionally it is said that a level of employment below the maximum is desirable because it makes workers more efficient and improves productivity. Quite aside from the lack of scientific verification of this proposition, the Council feels that even more businessmen will come to recognize—as so many now do—that public sentiment toward mass unemployment is just as much a part of our economic life as the public's attitude toward buying particular goods or spending particular portions of its earned income. And whether unemployment is "too high" depends as much upon what the unemployed think as upon what business thinks, just as whether prices are too high depends as much upon what the buyer does as upon what the seller says. Social and psychological considerations will come to enter more and more into business action because they are a part of the environment in which business is done.

Since mass unemployment tends to build up resentment (whether rightly or wrongly) against free enterprise, it injects a threatening element into business life and prospects which is enormously important. Efficiency, even if it could be purchased at the price of so vast a danger to our business system, would not be worth the buying. Our economic system is strong enough to be sufficiently efficient without undergoing this oppressive risk. And because every mass increase in unemployment tends to shift the location of authority and decision from business toward government, business has additional cause to strain every effort towards its prevention.

NEW BUSINESS ATTITUDE TOWARD "POLITICS"

Of course, government is a "political" process, just as the Constitution of the United States is a "political" document. But no businessman should resignedly take the position that it is futile to attempt to influence public policy because he is outnumbered by workers and farmers and "the government counts instead of thinks." Neither business nor any other group can offer any workable substitute for the processes of democracy, because there is none. Further, democracy is the system which affords the best opportunity for those with the qualities of thinkers and leaders to make their weight felt although they are outnumbered. These qualities exist in abundance in the business world.

Some of the best friends of business, who are neither in government nor in business, are now urging businessmen to assume increasing responsibility for participation in public affairs. This is a good thing.

CAN BUSINESS ACTION ACHIEVE SUFFICIENT CONCERT TO PROMOTE
STABILITY?

Successful efforts to combat serious economic downturns must be concerted. They must be on a massive scale, because the economy is huge and acquires tremendous momentum when it starts definitely upward or downward. The main advantage offered by government policy in resisting economic fluctuations is that government can act on this massive scale. The extent to which free enterprise can enlarge its necessary contribution to economic stability hinges upon methods whereby business itself may act more effectively and thus deliver a more massive blow against the forces of deflation.

The dilemma is this: businessmen *individually and separately* may react to the beginning of a downturn, or even to its prediction, in sufficient numbers cumulatively to accentuate the downturn. But no sufficiently satisfactory way has yet been found for businessmen *individually and separately* to respond to the beginning or prospect of a downturn in a manner which cumulatively holds the economy stable or propels it upward. This is the real meaning of the importance of "business psychology." Businessmen at certain stages in the economic process take so seriously the first signs or predictions of a downturn that the prediction may become, as the Council said in its First Annual Report, "the engine of its own verification." If businessmen under such conditions could follow *in sufficient numbers* policies contributory toward stability or growth, or at least act in a manner consistent with the proposition that the long-range trend of the economy is upward, this might provide a key to the dilemma.

There are two lines along which such action by business may be facilitated. The first is by more common study and education of how the economy works and what policies may be most salutary at various stages in the economic process. If the results of such inquiry were sound and obtained sufficient acceptance, individual businessmen might act (without the kind of concert which could be against good policy) to cumulate the forces of stabilization and growth instead of cumulating the forces of downturn.

That this is not too much to work toward is demonstrated by the economic history of 1949. The Council finds one explanation of why the recession of the first half-year was so contained in size and duration in this fact: businessmen all throughout the postwar period, and particularly during 1949, exhibited far more economic understanding translated into practice than in those past periods which presented them with somewhat comparable difficulties. To be sure, there were mistakes of price policy and other policy during the inflationary boom. But in contrast with the period following World War I, the management by

business of its inventory and pricing policies was definitely superior. Similarly, the fact that business knew enough not to react to the first signs of the downturn by wage cuts or by layoffs (beyond the minimum in the face of dwindling markets) was a sustaining factor along with the sustaining influence of many public policies. There is no reason why this behavior pattern exhibited in 1949 cannot be accentuated in future years.

However, the Council does not feel that the forces making for a downturn in early 1949 were sufficiently powerful to put our business system or our government policies to as severe a test as may occur at a later period. Consequently, we feel that in order to be safeguarded against the possibility of more ominous danger at some time in future, the process of study and education and understanding needs to be carried much further by every feasible means.

Moreover, we feel that such study and education and understanding may not be enough—even when added to vigorous public policies—unless it is accompanied by improved institutional arrangements which will come nearer to assuring consistent and massive private action on a much broader scale than was exhibited even in 1949. Therefore, as a second line of action, we favor further exploration of how these institutional arrangements may be developed and made most effective to expand business activity without that kind of collaboration in restraint of trade which the Sherman Act wisely condemns. In the final section of this report, we make some reference to meetings of management, labor, and others to explore some guiding principles for private economic policy on a voluntary basis.

These considerations, and in fact all that we have said in this report, shape our thinking about the kind of fundamental study and analysis most relevant to foreseeable economic problems in the United States. We now turn to a somewhat more detailed description of the kinds of economic study which we believe should engage economists, businessmen, labor and farm organizations, and all those most deeply concerned about economic stability in the months and years ahead.

VI. Focal Points for Economic Study

In carrying out its own responsibilities under the Employment Act, the Council has found itself of necessity the carrier and purveyor of the kind of improved economic analysis to which reference has been made throughout this report. We have also been acutely aware of the gaps and deficiencies, because we have been challenged to arrive at judgments upon matters where current facts and analysis have provided only a very partial guidance. Our desire is to stimulate individual and organized research through every available means.

By stating with some definiteness the difficulties which we have encountered or anticipate, we hope to provide further stimulus to those lines of study and education which may be helpful to both business and government. Those who have read the various reports under the Employment Act will have identified some of these difficulties. But many of them are in the future, since the life of the Council has thus far largely coincided with a period of high employment achieved by war-initiated momentum. This period, it is true, has presented serious problems concerned with inflation and its aftermath. But for the problems of the future, these earlier reports have been only trial runs. Largely concerned with immediate problems of postwar adjustment, they have not adequately explored the long-run problems of stability and growth.

THE PROCESSING OF FACTS

Our economy consists of myriad interacting elements. The problem of analysis is to reduce them to manageable categories of thought, to trace the paths of interaction, and to identify strategic points at which particular actions will lead to desired results.

At the base of the pyramid lie numberless facts. The principal way to impound economic facts is through statistics. The effort to carry forward our work would have proceeded in darkness and disorder had it not been for the tremendous programs of collecting statistical data which have been put into effect over the past generation. Many private organizations—business, labor, universities, research institutions—have participated in this development. But in very large measure it has been and must be the statistical activities of the Federal Government which provide the necessary data. The cost and complexity of adequate statistical services far exceed the resources of any private agency.

As soon, however, as our work was initiated, it became clear that existing statistical services although extensive were inadequate. This was indicated in a committee print of the Congressional Joint Committee on the Economic Report, *Statistical Gaps*, issued in 1948. It presented a series of recommendations concerning the need for more complete Federal statistics in several fields, summarized as follows:

(1) Periodic surveys of consumer purchasing power and demand, sufficient to show—

(a) the distribution of income and saving available for expenditures by geographic areas and among various consumer groups and income brackets, and
(b) current and prospective patterns of consumption and expenditures.

(2) Collection of information on wage earnings of employees in activities not covered by our social security system.

(3) Improvement of the information on returns to capital and management of unincorporated businesses.

(4) Collection of more information on employment and unemployment, adequate to reveal geographic differences in employment trends and unemployment rates, and to provide data on occupational and other characteristics of the unemployed.

(5) Development of more complete and current information on financial trends in business, providing industry totals, data on business operations by size of business, and information on business concentration.

(6) Taking of an up-to-date census of wholesale and retail trade and services by means of which the current statistics on business and distribution may be improved and made more reliable.

(7) Development of adequate concepts for measuring productivity and the collection of data to supply information on the course of changes.

(8) Development of data on costs of construction and improvement of data on the volume of new housing and nonresidential construction.

(9) Improvement of inventory statistics by covering a larger and more reliable sample which would permit a break-down of inventories at the various stages in the industrial process.

(10) Collection of detailed information on the relationship of requirements for materials, capital equipment and energy to the volume of production, to permit evaluation of the industrial consequences of production programs.

(11) Collection of fuller information on business intentions with regard to capital expenditures and related data.

(12) Collection of more current and detailed information on expenditures of State and local governments, for use in preparing estimates for the Nation's Economic Budget.

This list is merely illustrative of the wide informational base upon which broad economic policy must be built.

Statistical facts, however, are just the beginning—the raw materials. They must be made to mean something. Thus, the next great step lies in the field of analysis. What relations between particular sets of facts are of strategic importance? How do we relate the past relations to future relations? How should we try to shape the collection of future facts?

In attempting to answer such questions, we come squarely to the functions of economic analysis. And oddly enough, much of the most useful economic analysis is not based upon detailed facts. It is concerned with the molds, or schemes of relationships, into which facts should be poured. A concept of national income, of consumer income, of savings, of investment, of economic input and output—all these and others are necessary before statistical facts can be made to mean anything in relation to one another. We need a clear conception of the nature and role of credit, of the impact of wage changes upon costs, prices,

and incomes. We need clearly to see why a scheme of competitive enterprise works, and wherein its problems lie. The analytical framework can be, and has been, expanded and improved by economic statisticians. But it is largely economists who have devoted themselves to the broader framework of economic relations. Creative scientific thought and investigation precede the ability to build a radio, a bridge, or a bomb. And so it is with economics. In order to be more explicit, and to identify certain respects in which further economic analysis is needed, we shall now consider certain broad areas within which the Council's work falls.

FORECASTING

The first of these areas is the appraisal of current and foreseeable trends, commonly called forecasting. The immediate past is always fairly well visible to the naked eye with the aid of existing, though still inadequate, statistical data. The course of employment, business activity, credit, investment, consumption, etc., can be discerned, and their shifting relations followed for a past period of time. But what of the future? What is to be anticipated? And if the outlook is not satisfactory, with what confidence can preventive remedies be put into effect prior to the event? This is the rock upon which many people have foundered in their effort to see how any generalized economic policy might be made to work.

While it cannot be denied that the art of economic forecasting is far from well developed, this shortcoming may easily be exaggerated. Expert attention to the course of events can give an informed opinion of where they are tending. On this basis, preparation can be made for meeting developments which lie within the range of probability. This is what the Council now has to do, and all those responsible for the development of private or public economic policy cannot avoid formulating some view of the probabilities in the case. Nevertheless, the deficiencies are real and every effort needs to be made to diminish them.

Various useful experiments are now under way. One of the most promising is the wide sampling of business anticipations and of business intentions with respect to investment. Fluctuations in business investment have in the past been very marked and are breeders of instability elsewhere. Knowledge of the prospects in that direction is one of the most important keys to the short-run outlook. It is, of course, true that business plans can be changed rapidly, and prospects as seen by private firms must be checked against all other indicators of trends. But the possibility of a much improved approach to forecasting is undeniable. The Department of Commerce and the Securities and Exchange Commission are jointly engaged in developing improved procedure in these fields, as are also several private agencies, particularly Dun and Bradstreet and the McGraw-Hill Publishing Company. They

promise to become increasingly useful as techniques are perfected and statistical samples broadened.

Another promising type of inquiry is that which samples the financial position and anticipated purchases of consumers. The principal pioneer in this field is the Survey of Consumers' Finance sponsored by the Federal Reserve Board. From it may be inferred changes in the intensity of consumer demand in different directions as, for example, toward housing, automobiles, and other durable consumer goods. As with business investment, consumer plans can change rapidly if income prospects change, that is, if the whole economic situation changes. But in conjunction with other indicators, such information is extremely enlightening. The techniques which are being developed are likely to be found useful by private market research agencies, bringing a marked increase in the available information.

There are a good many types of statistical forecasting systems being experimentally used by private agencies, particularly financial and investment houses. Some of them may be very imperfect, but in the aggregate they include a large amount of intelligent effort to assess the factors which are shaping the future. The more widely such intelligent attention is directed to these factors, the greater will be the opportunity for well informed business decisions.

DEFINING OBJECTIVES

The second broad category of work identified by the Employment Act, and certainly central to economic policy, has to do with defining objectives. The Act calls this setting "needed levels of employment, production, and purchasing power" in order to promote maximum levels. The fields of inquiry implicit in these simple words are so numerous as to be almost beyond description. But what is involved may be indicated by selective examples.

One group of subjects may be called the institutional structure of the American economy and the means to its improvement. This may be illustrated by the structure of the investment markets. One overall fact that seems reasonably clear in regard to the sources of funds is that business and social evolution has wrought some irreversible changes in the mechanism of private investment. The role of the wealthy independent investor is diminished, while the importance of business savings and indirect institutional investment of individual savings is increased. Constructive effort to meet the problems involved in this adjustment calls for intensive research into existing and potential new means by which the savings of the security-minded small saver can be made available for business investment without excessively burdening risky enterprises with debt.

The central importance of this problem is apparent on its face, since one of the surest ways to halt progress and magnify unemployment is

for a large part of the saving of the people to fail to find an outlet in new productive capital. The study of this problem is one which deserves wide attention by economists and by those agencies engaged in administering the people's savings. Such studies can broaden out to include the whole credit structure of the country, including that part which is directly administered by the Government, with a view to adjusting it to the expanding and changing needs of the country.

Problems of institutional structure arise in many other fields, for example, in the labor-management field. The whole economic well being of the country is closely related to the outcome of collective bargaining agreements. The basis for decisions compatible with the public interest, under modern conditions, requires continuing intensive study by economists, by government, and by the parties to the bargaining process. Similarly challenging problems arise also in the field of market structure where the price and production policies of large-scale business have a very direct bearing upon the health and progress of the economy.

Institutions exist for a purpose. One way of stating the purpose is that they are for achieving goals. The primary goal under the Employment Act is that our working population and other resources should be as fully and efficiently employed as possible. But this goal embraces in fact many goals. It comprises all the conditions which are significantly relevant to the central purpose. Consequently, in addition to concern with the improvement of institutional structure, economic study and policy should concern itself with another group of subjects under the broad category of goals, or needed rates of growth in various directions. There are various ways of approaching this subject, and one of them is to assume that, if things can be kept going well in the short run, the long run will look after itself. There is some point in this thought, but not so much that the Council has thought it proper to forego all inquiry into the capacity of the economy for growth. On the contrary, we have felt it important that explorations be made, in quantitative terms, into the productive potential of the economy as time goes on, and into some of the interior adjustments within the economy which that development will entail.

The Council's own experiments in this field have been conducted in the form of hypothetical projections of the Nation's Economic Budget. But they can be conducted in other ways, and the more ways the better. In any case, they all involve an advance estimate of our productive resources at various stages of development and the amount and character of their productive yield, upon certain stated assumptions. A path-breaking contribution to studies of this sort was the comprehensive volume, *America's Needs and Resources*, prepared by the Twentieth Century Fund.

In a way, it is not entirely satisfying to call the outcome of such projections "goals." They are not like the goals of a Russian five year

plan. They are not "plans" toward the achievement of which every resource of public authority will be directed, and for failure of which heads will fall. In one sense, they are bench marks of progress, evidences of the attainable. But in another sense they are simply an instrument through which we can more carefully study the conditions of progress. Does one anticipate a growing or declining relative place of government in the economy? And why? What factors suggest a changing proportion between the production of capital goods and consumer goods? Is it possible to measure the levels of investment needed to support stable progress? The mere effort to make the projections leads the mind to ask fundamental economic questions. While some of the answers are necessarily very general or tentative, they are not without meaning or utility.

But more is accomplished by this occupation. It moves us toward a closer inspection of the logic of various public programs of a developmental character. Upon what assumptions is the size of programs of resource development based, and how are they related to other assumed developments in the economy? With what state of economic development is a housing program equated? Upon what base of national income can social security obligations be projected? Such tests of relevancy are presented to public programs reaching far into the future.

One further purpose is served. The American economy cannot reach its potential unless its possibilities catch the imagination of those who plan for the future and invest in it. If investment decisions are made on the basis of "experience" alone, the backward view, they may not adequately correspond to what the future can support. The possibilities are not infinite but they are great, and numberless farsighted private decisions will have to be made to capture them.

The adequate exploration of the future calls for the best talents of many minds. Economists and statisticians can work out the models and fill in many details, but the attention of experts in many fields is needed. The improvement of our economic institutions, the patterns of growth in our resources—these are subjects which will repay dividends to detailed analysis in the form of a more comprehending approach over the years.

POLICY MAKING

The third broad category of tasks falling to the Council is that of appraising and recommending policies and programs. The two other categories of our work, as discussed above, are technical in character. While they give rise to disagreement, it is disagreement mainly on technical questions of analysis. But this third category is in vital respects of a different sort. It is public action that is under discussion. These actions in some measure affect everybody, in their self interests, in their most deep seated ideas of what is good and what is not. Economic action in a democratic society is distilled out of varied viewpoints.

The work of the Council necessarily involves controversial issues. But in this report we deal with that primary aspect of the Council's concern with policy which is technical in character. The process of arriving at informed judgments concerning measures which will contribute to economic stability is to a high degree an objective process. It involves economic analysis of the consequences of various lines of action. It requires the choice between alternatives on the basis of that analysis.

The pattern of sound economic policy is not easily discerned. There are other ends of national policy besides economic stability and growth. Some of these have to be accepted as data. The size of the defense program required for national security, for example, involves factors which the economist cannot even weigh, although it involves other factors where his techniques may be useful. Yet even within these bounds the task is complex. Particular measures may have short-run effects of one character and long-run effects of another. Or they may have conflicting types of short-run effects. In an inflationary period the building of more houses may force prices up by competing for scarce materials, but it may also relieve a critical housing shortage. Which consideration has the greater weight? A blend of judgment is constantly needed.

The problems of practical economic evaluation extend even further. How is it best to do the things which ought to be done? Means and ends are almost inseparable in their impact upon economic activity. Enough has been said to suggest, though only broadly and with little detail, that there are almost endless spheres in which the talents and skills of economists and other experts could be brought usefully to bear upon the problems of economic stability and growth. We hope that both with and independently of our stimuli there will be much more effort by others in many fields, and that the results of their work will flow freely for the benefit of all.

The task, however, goes further. Economic policy is not the exclusive province of economists, or of the Council or the Congressional Joint Committee. The impress of facts and of acute and disinterested analysis must be widely felt. It must be felt in the Congress, throughout the executive agencies, in the circles of business and farm and labor leadership, and out into all the byways of the country. The problems must be widely known; technical foundations of policy must be widely understood; the disinterested and professional character of the underlying analysis must be established. If this foundation can be built, economic measures designed intelligently in the public interest should increasingly find their way into the stream of public and private action.

VII. Recent Developments in Council Operations

This report has already made it abundantly clear that work under the Employment Act is a cooperative venture in the broadest sense. It involves business and government because both have basic responsibilities for the stability and growth of our economy in a free society. It involves organizations of workers, farmers, and consumers, which are of equal importance to business management although in this particular report we have stressed the functions of the latter. (On later occasion, as we have said, we may deal in equal detail with the relations between government and these other organizations in our private economy.) It involves the interplay of numerous agencies and instruments of government. It involves the President and the Congress. It implicates the economics profession, whose members prepare so much of the resources of scientific research underlying the practical tasks of the Council. Perhaps the hardest task of the Council as a small body is to develop relationships between itself and others which will keep moving in both directions a constant flow of information, stimulation, and improved thinking. The best way to describe the progress in our operations, therefore, is to outline some of the recent trends in these relationships.

WORK WITH PRIVATE ECONOMIC GROUPINGS

The Council has continued during the year its frequent meetings with representatives of business, labor, agriculture, and consumers. During our first years, these meetings were devoted mostly to general discussion of the economic outlook, supplemented by somewhat random consideration of specific problems which our visitors might raise with us around the conference table. But beginning with the last quarter of this year, we have instituted a new idea for which we have high hope. We have suggested to our conferees that together we undertake to designate one or two special problems for consideration at our next succeeding quarterly meeting, and that in the interval their staff resources as well as ours undertake to work up specific studies which might be circulated in advance of discussion. In addition to the manifest merit of this pooling of resources, we hope that the psychological advantage of *working together* as well as *talking together* will intensify the realization that the purposes of the Employment Act involve the whole nation and certainly cannot be furthered in an ivory tower.

In the course of our development of this plan, some of our conferring groups have suggested that, instead of meeting separately with representatives of various sectors of the economy, we should undertake joint meetings and perhaps joint studies with representatives of industry, agriculture, labor, and consumers functioning as a single team. There are some practical difficulties involved in this method of approach, but the Council does not deem them insurmountable. Certainly the argument that such meetings lead to hot disputation instead of calm analysis can carry little weight among those who realize—as this report has sought to stress—that the reconciliation of conflicting views and seemingly conflicting interests is the hallmark of free enterprise and free government.

We hope that procedures along these lines may be perfected, and that one of the most important collateral benefits will be the encouragement of mutual efforts along the same pattern but on a more decentralized basis throughout the nation. In such efforts the Council will not generally be able to join because of limitations of time and staff, but it is encouraging to note that already in some states agencies somewhat similar to the Council are being considered or have already been established.

WORK WITH GOVERNMENTAL AGENCIES

The network of the Council's relationships with other agencies of government has been described rather fully in previous reports. Particularly during the latter part of this year, these arrangements have been carried further. In the preliminary development of materials for the forthcoming January reports, members of our staff assigned to specific topics have initiated working committees tying in with other parts of the government devoted to research or operations in the various fields. Different groups have been studying the requirements for and the impediments to a high level of business investment; the interrelationship between international and domestic economic policy; the progress of the program for treating spot areas of unemployment; the relationship between agricultural adjustment and the general economy; the coordination and timing of the wide range of public works and developmental activities in the perspective of economic trends both secular and cyclical.

The Council should not be simply a reviewing body which looks over the proposals made by operating agencies and recommends to the President how these proposals may be fused into a consistent and sound economic policy. Our work to be effective must commence at a much earlier stage in the process. It should include participation in the developmental thinking about those policies and programs which are of central concern to the whole economy. Only thus can other agencies receive our assistance at an early enough stage for it to be fully effective; and only thus can we be brought in contact with their work at an early enough stage for us to comprehend it fully and be benefited fully by their thinking and experience. We feel that during the course of the

coming year, encouraged by the splendid cooperation thus far received, we shall be able to move toward the fuller professional service which the reading of the Employment Act and of its legislative history shows so clearly to have been the expectation of the Congress.

Practically every program and policy of government passes at some stage through the Bureau of the Budget; and those matters which importantly affect economic affairs channel also through the Council. This does not involve duplication, because the functions of the two agencies are manifestly different although closely interrelated. Yet the problem of adjusting other economic policies to the hard facts of the budget, and the correlative problem of adjusting the budget to the hard facts about the economy, mean that the Council must maintain closer year-round contact with the Bureau of the Budget than with any other agency. This contact has been greatly facilitated by the cooperation which the Bureau has extended to the Council.

RELATIONS WITH THE CONGRESS

The signatories of this report have never found any reason to believe that our special service to the President under the Employment Act could be inconsistent with that degree of cooperative servicing of Congressional Committees—particularly the Joint Committee on the Economic Report—which has become the traditional practice of policy advisers to the President who are set up under law, entrusted by law with a specific field of study and advice, and responsible under law for explicit participation in reports and recommendations transmitted to the Congress. The “problems” which such advisers face in occupying a confidential relationship to the President while cooperating with the Congress have been exaggerated, and in any event are not peculiar to economists; and it is less important that the Council be spared these “problems” than that the Congress, at least as much as the economic groups with whom we deal, have access to our open and full discussion of economic fact, outlook, and policy.

Our most recent discussions with members of the Joint Committee on the Economic Report have strengthened our belief in this principle and practice. We look forward to exerting every effort toward making our best contribution to the furtherance of one of the most important objectives of a free government—mutual respect and common purposes between those who serve in the executive and those who serve in the legislative branch. The only way to further these ends is to work together on problems confronting both.