



A TEN-YEAR PROGRAM FOR SOUND ECONOMIC GROWTH

Mr. Leon Keyserling

NOTICE

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Reviewed by: Colonel Tom W. Sills, USA

Date: 25 February 1960

INDUSTRIAL COLLEGE OF THE ARMED FORCES
WASHINGTON, D. C.

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Reporter: Ralph W. Bennett

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COL. SMYSER: General Mundy, General Houseman, Gentlemen: Our Economic Stabilization Unit of study begins quite appropriately at a time when the newspapers and periodicals are filled with articles about our national economy. We have just had President Eisenhower's economic report; and currently, Congress is conducting hearings and preparing their economic report.

Much of the comment and discussion about the national economy is concerned with two things: inflation and economic growth. At this time of competitive coexistence, the rate of growth of our economy in relation to that of the Soviet Union causes apprehension. Accordingly, it is entirely fitting that we open our lectures in economic stabilization with a lecture on a ten-year program for sound economic growth.

Our speaker this morning, Mr. Leon Keyserling, is well qualified to talk to us on this subject. In his many articles and publications he has advocated national policies and national responsibilities for using the unparalleled economic capability of our country to meet the Soviet challenge. He was Chairman of President Truman's Council of Economic Advisers, and currently he is President of the Conference on Economic Progress.

Mr. Keyserling, it is indeed a pleasure to welcome you back to the Industrial College of the Armed Forces.

MR. KEYSERLING: I'm certainly glad to be here. I was informed,

much to my surprise, that this is about the sixth time. When the person who introduced me started talking and said that it was very fitting to open this series with me, I thought he was going to say that it was very fitting to open the series on economic stabilization with somebody who doesn't believe in economic stabilization.

I think in one sense this is certainly true, because the law of life is not stability. The law of life is growth. Or, to put ^{it} in a more paradoxical way, stability depends upon growth. And we in the United States, during a period in our history when we have needed to recognize this more than ever before, and, in fact, when our survival may depend on it, have become so frozen to the idea of stability in the static sense that we have lost much of the dynamic character which should give us our great advantage over the totalitarian challengers, and also enable us better to meet our needs at home. We have lost the great part of this dynamism by becoming wedded to the concept of stability; and, not paradoxically but naturally, this has given us less stability to boot. So, instead of achieving a lesser objective at the sacrifice of a greater objective, we have achieved neither.

Now, of course, some people may ask, despite the very generous introduction, what qualification I have to talk about some of these subjects; and I'm going to say a word in my own behalf.

For example, on this matter of how much our economy ought to be outlaid for national defense, I don't pretend to be a military expert. So how can I have any views on this subject? Well, I go down South

and I have a little nephew whom I call Captain Billy. I go down to see him and he tells me that there's a fellow across the street who is an awful bully, very unruly and very dangerous. He says: "Uncle Leon, I'm in training and I'm strong enough to beat that fellow." Then I go down to see Captain Billy a few weeks later and he says: "Well, I'm not strong enough to beat this fellow, but I'm strong enough to tie him." Then I go down to see him a few weeks later and he says: "I'm not strong enough to tie him, but I think I'm strong enough to deter him." Then I go down a few weeks later and he says: "Well, I don't know whether I'm strong enough to deter him any more, but I'm strong enough to give him pause." And then I go down a few weeks later and he says: "I don't know whether I'm strong enough to give him pause, but I'm certainly sure that he may have changed his intentions." And then I go down still later, and Captain Billy, who by this time has put on a lot of extra fat, says: "Well, I don't know what difference it really makes anyway." Now, I don't have to be an expert in pugilism to be rather concerned about Captain Billy under these circumstances.

Second, I want to make the point that I don't want any of you to become nonplussed by the seeming differences of viewpoint among economists. I think one of the hardest things we have to deal with as we read the hearings up on the Hill, where many economists are paraded before the country, when we hear the viewpoints of economists inside and outside of the Government, is, how can the informed layman--and in a democracy, policy always has to be made in the final analysis by

the informed layman and not by the specialist--know where to go and where to turn when there is so much difference?

Well, I have a very simple formula for this. There really isn't any difference. There's only the difference between the good economists and the bad economists. Unfortunately, the good economists are very few in number.

But, stating it more realistically, there isn't really an economic difference. There's a difference in what economics is all about.

Now, I say that economics fundamentally is about the logistics of real wealth. Economics is about what a nation has by way of productive power and what it does with it. This is true whether you're talking about a slave society behind the Iron Curtain or the Bamboo Curtain, or a free society in Western Europe, or a free society in the United States. In the final analysis, the purpose of all economic thought and all economic policy is to increase your production, and especially your production per capita, through the application of constantly improved technology and managerial skills, and good will in a free society; and, second, to use it wisely. Using it wisely, of course involves subjective judgment, because different people differ as to wisdom. But, nonetheless, these are the two purposes of any economic society.

Prices, wages, tax policy, monetary policy are merely various instruments toward the achievement of these two economic purposes of marshaling your resources and using them wisely for the purposes of the country and the purposes of the nation.

Now, the two kinds of economists are those who concentrate on the first problem and think of the second problem as one of instrumental use, and those who have gradually become so intrigued with the intellectual interest of the second problem, or so proud of the specialties which they have developed for the treatment of the second phases of the problem, that they forget about the first. And so they debate about desirable price, wage, tax, profit, and monetary policies in a vacuum, without relating it back empirically or quantitatively to what is actually happening to the use of our resources. And therefore naturally they differ, and therefore naturally a lot of what they say is irrelevant, and therefore naturally almost all of what they say is dangerous.

And that is why we get such extreme conflicts as one hears now. Whereas we have been told for many years by one school of economic thought that a budgetary surplus was restrictive, that it held back the level of activity and therefore was anti-inflationary, we are now told that a large budgetary surplus, particularly if it is applied to the reduction of the national debt, is stimulatory because it provides business and the consumer with more funds. And therefore, contrary to the whole theory of fiscal policy which I thought was accepted by almost everybody, we are proceeding on the assumption that the bigger surplus you have, the faster rate of economic growth you will attain and at least the most sustainable it will be.

Now, this doesn't result from a lack of logic. It results from a failure to observe the aphorism of Mr. Justice Holmes that a page of exper-

ience is worth a pound of logic. Nobody, almost nobody, is saying that if we are going to have an economic theory, we should build a model of how the economy is actually operating and look at it and see what went wrong in terms of our basic principles, and then reconstruct the theory on the basis of this observation.

Now a word about conservatism and liberalism, because I'm classified as a liberal economist. I'm not a liberal economist. I'm an observational economist. I can't imagine anything more conservative than what I just said, and I'm not interested in labels. I don't mind being called a liberal economist. I'm rather proud of it. But what could be more conservative than saying that the real wealth of nations is in what you produce and how you use it, and not in bookkeeping; and that the real way to arrive at a sound economic theory is to look pragmatically at what is happening and readjust your theory gradually to the observation of the changes that are taking place?

Now, you can call that liberal, conservative, socialist, planning, anything you want to, but that's what I stand for. I make these introductory remarks so that what I say will fall more clearly into line.

In these terms let's look at what has been happening to our economy since the end of the Korean War. And I don't take since the end of the Korean War for any political purposes. It happens that a new Administration came in then. I take that period because the ending of the Korean War challenged us again with the problem of what kind of economic job we could do in a long period between peace and war, which

is the only type of period which is relevant to our problems now. Providence doesn't know, at least we don't know, when we're going to be in a period of real peace. We certainly don't know when we're going to be in a period of real war. And therefore the performance of our economy in this middling period is most relevant to our problem today and as far ahead as we can see. And, second, the new technology which has emerged during this period is more relevant to our economic problems than anything in the past.

Third, to be perfectly frank with you, I think there have been certain economic changes in national policy during this period, which I think are profoundly wrong, both on the monetary side and on the budget side. And, lest you think I am political in this, I refer you to the hearings before the Joint Economic Committee in 1952, when I was the top economic officer of the Government and when I took profound difference with the changes in monetary policy then in their inchoate shape and debated it mostly with Democratic Senators. So there is nothing political about this.

Now, what has happened to us during these seven years is very easy to state in these quantitative terms: We've had an extremely low rate of economic growth. Our average during the past 50 years in real national product increase per year has been about 3 percent. Our average during these seven years has been 2.3 percent, which is a hell of a lot below 3. And the 3 percent figure is entirely irrelevant, because this isn't even the experience record.

The 3 percent is compounded of an accelerating rate of economic growth based upon an accelerating enlargement in technology. And therefore, to measure our potentials against a 50-year average is just as ridiculous as if we tried to project ahead ten years what's going to happen in medical science on the basis of the average of the last 50 years, or what's going to happen in military weaponry based upon the average of the last 50 years. We don't live in that kind of an economic world, any more than we live in that kind of a scientific world or military world. And, as a matter of fact, since the economic performance is a compound of more imponderables than science or military life, taking a 50-year average is even more ridiculous.

If we look at the more recent period, take, for example, the seven years prior to the ending of the Korean War, which again is rather similar to the current period, because about half the time was peacetime, with a military budget of 13 billion dollars, and half the time was limited war, which gives you an average compound mix somewhat similar to what we've had more recently, we had a growth rate of 4.7 percent a year without the kind of pressure upon our productive resources that we had in full-time war. As a matter of fact, hours of labor were reduced during the Korean War. We had very little pressure on resources. We had inflation for other reasons, which I'll come to.

So we've had this 2.3 percent growth rate. The customary argument developed in favor of this growth rate, which represents the latest mental gymnastics of my friends in the Federal Reserve Board and

elsewhere, is that it is better to have this lower rate because it is a sustainable rate; that if it's higher, it won't be so sustainable. Well, I look back over the last seven years to see what's been sustained and what I find is this: I find that the 2.3 percent rate is composed of a down-turn of 2 percent from '53 to '54, an up-turn of 8 percent from '54 to '55, an up-turn of 2 1/2 percent from '55 to '56, of 1 percent from '56 to '57, another down-turn of 3 percent from '57 to '58, another up-turn of 6 1/2 percent from '58 to '59; and now the businessmen are speculating whether the next down-turn will be in late '60 or, because of the steel strike, will be deferred until late 1961. So what's sustainable about this? We have had recession half the time and advance half the time. Nothing has been sustained.

As a matter of fact, the very low growth rate is the reason why nothing has been sustained, because when you grow that slowly, when you grow so slowly that you're not moving fast enough to absorb the additional labor force and the accruing technology, which is moving forward at a bursting pace, more than we realize, you gradually accrue a differential between your actual product and your potential product which becomes so large that you get another recession. So that saying that a 2.3 percent growth rate is sustainable, which is the latest fashionable argument, is like saying that for an airplane to sustain itself best going in the air, it ought to go 23 miles an hour.

Now, what have been the consequences of this low growth rate? The consequences of the low growth rate, very simply, are that, while

of course, we are higher at the top of every boom than at the top of the previous boom, and therefore the politicians tell us we're better off than ever before because we're higher than ever before, this is absolutely meaningless. It's like the little boy in school that stayed two years in the third grade, two years in the fourth, and two years in the fifth; and when he got in the sixth, his mother went around town saying he's higher than ever before. When ever before was such brilliance demonstrated?

Actually, at the peak of the boom in 1959 you have a product potential about 10 percent higher than at the peak of the previous boom two or three years earlier; and if you're one percent higher, instead of saying you're higher than ever before, you ought to say you're 9 percent behind. And if you look at your unused resources rather than at your used resources, which is the really vital thing, this is perfectly obvious, because at the peak of each of these up-turns that we've had since the Korean War, we, of course, have had less unemployment of plant and manpower than at the depth of the previous recession; but we've had more unemployment of plant and manpower than at the peak of the previous boom, which is the really proper method of comparison. In other words, in a ragged up-and-down performance we are gradually accruing more chronic unemployment in wastage of plant and manpower, not year by year but two years by two years or three years by three years, which is the only thing that counts.

Now, what is this costing us? Different economists will have

different computations, but again these differentials are insignificant for the purposes of the general proposition. What it is costing us, very simply, is that over the past seven years we have had 200 billion dollars less of national production, measured in 1958 prices, uniform prices, than if we had maintained a sustainable rate of growth--I underscore "sustainable"--because 4 or 5 percent a year would have been sustainable, while a 2.3 percent average is not sustainable. We would have had about 200 billion dollars more of national production. We would have had about 15 million more man-years of employment.

So much for the overall. Now, as to the uses, of course, economists can draw different patterns of what uses this higher production might have been put to. My method of diversification of this additional product is to look pragmatically at what I call a sustainable pattern, which is what the Reserve Board is talking about, but they're talking about it without looking at the facts.

According to the sustainable pattern I get the notion that what we should have had over this period is about 51 billion dollars more of private investment in tools and technology to build our fundamental productive power, about 127 billion dollars more of private consumption for raising the American standard of living; and on the public side it's a little harder to measure because you have a lot of differentials between goods and services accounts and other kinds of accounts. But realistically what it comes to is this:

With the wise deployment of the fuller use of our resources, we

would over this period, at existing tax rates, have had about 65 billion dollars more of Federal, State, and local revenues, which is not dollars but wealth, because I don't get the 65 billion dollars out of raising tax rates and redistributing products from one part of the economy to the other. The 65 billion dollars is merely the portion of this additional at 200 billion dollars of wealth production which/the existing tax rates would be allocated to public purposes; and it would still leave over 135 billion dollars more for private investment and private consumption.

Now, what we could have done with that 65 billion dollars, very simply, is this: We could have used about 19 billion dollars of it to retire completely, or, rather, to eradicate completely, the deficit in the cash budget over this whole period. That's bowing respectfully to those who believe that inflation has been caused by deficit, which it hasn't. But at least we would have done that. We wouldn't have had the deficit. And the remainder would have been available for national defense, science, education, the basic national priorities of the nation.

Now, I'm not dealing now with really debatable issues, because the only thing that economists could debate with on this score is whether the 200 billion figure ought to be 175, whether the 15 million man-years of lost employment opportunity should have been 13 or 18. Actually, if we were awake to the world challenge, as the excellent people/are bring-^{who}ing to the attention of Governor Rockefeller what I've been saying for for a number of years have said, we shouldn't be talking about the 4 or 5 percent growth rate that I'm talking about. We should be talking about

6 or 7 or 8; and these figures should not be 200 billion and 15 million, but should be maybe 250 billion and 18 million. But I'm taking a very conservative, middle-of-the-road approach on this.

Now, let's look at some of the confusions on this score. One of the biggest confusions is on the part of the people who tell us heroically, to the great damage of the American system, that our Presidents or our Presidential candidates have to have the heroism to tell the American people that if they want more national defense, if they want more education, if they want more science, they have to cut back on their private living standards.

Now, this is absolute pap and nonsense. It's psychologically confusing. It's politically ridiculous. It's functionally unworkable in a mixed situation between peace and war; and it's not true.

The state of our economic confusion is indicated by the fact that the biggest best seller that we've had in the field of economics in the last two or three years, written by a very good personal friend of mine, is on the score of economic analysis one of the loosest, sloppiest, wrongest books that have been written in the past forty years, because what it says, very simply, is that economic growth is no longer important because we're so affluent that all we have to do is to divide up in a different way what we've already got, and impose enough sales taxes on low-income people to pay for national defense and for schools.

Now, how you are going to do this, ^{politically} in a free society that is fighting not a hot war but a cold war I don't see. But, more important, how are

you going to do it economically? Because if these people who want to write best sellers would instead look at some of these quantifications that I've talked about, and look at some of the logistics of economics, they'd say this: "All right. We've had this 200 billion dollars deficit in national product, and we've had these 15 million man-years of excessive unemployment. We needed over this period 40 or 50 billion dollars more of public outlays, including national defense. Let's just change the accounts and making the model for the past, make the public spending 50 billion dollars bigger and the private spending 50 billion dollars lower."

Well, this would make some sense if you had had full use of resources. But if you apply this to the pattern of performance which you've actually had, you would still have the 200 billion dollar deficit and still have the 15 million man-years of unemployment, and he would still be going out to Michigan and telling his State, which has had an average employment in the automobile industry of about 60 percent over the last seven years, and an average level of unemployment of about 500,000, that the way to get more schools, which depend upon tax revenues, is to have still fewer automobiles and still more unemployment.

Now, for people who want to pretend to be moralistic when they are only confusing, it sounds very wonderful to say, "Aren't schools more important than tail fins?" Of course they are. But there's no conflict between the two when your shortage of resources for public purposes is a by-product of the overall wastage in your economy and the

overall deficit in tax revenues resulting from a poor private performance.

If we had been operating during the last few years at anything like optimum use of resources, I would be the first to say that, if that did not yield an adequate level of national defense or of schools or of science, certainly we must cut back on private consumption in order to achieve these higher priorities. This means higher tax rates, it means repression of private living standards, and we've got to do it; and the American people would understand and take it.

But to talk this way under circumstances as they have actually existed is economic nonsense; and, more important even, it exhibits a complete lack of understanding of the worldwide struggle we're engaged in, because here for the past ten or fifteen years we've been saying to our people, in fact saying to them too much: "Look, the Russians have been able to build a big industrial base and have been able to build a big military machine by repressing consumption and the standards of living of their people." This in the long run, we've been saying, is going to weaken them because you can't go on forever in any kind of modern world, even under a totalitarian system, suppressing the advancement of private living standards, and this will corrupt them from within.

Well, of course, this has been a manifestation of our belief in the United States that it is patriotic to tell everybody how weak your opponent is. I had a few years ago to challenge the proposition that they couldn't develop an atomic bomb for ten years, and then I had to challenge the proposition that they couldn't develop a science because

they were barbarians. And then I had to challenge the proposition that they couldn't develop education because dictators weren't interested in the education of the people. And then I had to challenge the proposition that they weren't going to expand consumer enjoyment because, unlike the barbarians of Rome, their system is interested in the expansion of the living standards of their own people. They believe that they have a better system for that purpose, and I don't believe it's better. But neither the philosophy nor the drive nor the politics of that system is disinterested in advancing the living standards of the Russian people.

What they have done under a slave system is to do what the under-developed free societies would have liked to be able to do under a free system; namely, to defer the expansion of living standards so as to build capital equipment; and a free under-developed society finds it very hard to do this, because it doesn't get the political assent.

Now, don't misunderstand me. I'm not saying that the Russian system is better or more preferable, because I believe the price they have paid for these forced assents is too high. But the pattern of what they have done economically is ^{not} a foolish pattern. I don't like the way they have achieved it. They built their industrial base first. They built their war machine first. And now they can sustain and advance this ~~industrial base~~ war machine with their left hand and the industrial base with their right hand, and they can and will advance consumer living standards through a high rate of economic growth. And this is going to be both a challenge and an example to the free world. And what kind

of time is this for our best American thinkers inside and outside of Government to be telling the United States that we must beam to the world that we have to withdraw from the fundamental competition in living standards in order to compete with them in the military or industrial base, and where, incidentally, through default on one front, we're not competing with them on any of the three fronts because the three fronts are interrelated. Now, seriously, what could be more nonsensical than that, in political terms, in economic terms, psychological terms, strategic terms, and bare terms of the logistics of the quantities of economic development and power? We should be outdoing them on all three of these fronts, because all three of these fronts are important in just proportion.

Now, let me illustrate that for a moment with respect to the future, and then say a few words about policy.

What is past, of course, is only prelude. Here we are in this 1960 boom, screaming again that the great problem is the prevention of inflation, that the great problem is to have our economic growth low enough for it to be sustainable; and we are adopting exactly the same policy that we adopted in 1955 and in 1957 under exactly the same circumstances.

How well do I remember in early 1957, before the Finance Committee of the United States Senate. I was there with Secretary Humphrey and Mr. Burgess and Mr. Martin. This was in the spring of 1957 and they were all worried about the inflation. None of them saw any prospect

of a recession. They said: "The only reason we're having the inflation is because our economy has the highest prosperity ever and our resources are overstrained." I said: "We're moving straight into an economic recession. Nothing is overstrained. We have surpluses of farm products, surpluses of cars, surpluses of gadgets, surpluses of everything." And when they were challenged, the only thing they couldn't find a surplus of was one kind of steel pipe. And we were moving into a desperately serious under-utilization of our resources, and they were worried about overstrain. And I said: "This 1957 boom is like the 1955 boom. You haven't met the problem. You are in a long-term period of low economic growth and chronicwise in disuse of resources."

We're in exactly the same kind of situation now in 1959, and again they are tightening up on the money supply and tightening up on the budget and running a big surplus, which now for some reason they say is stimulatory. But every banker and every businessman and the stock market knows that a 4 1/2 billion dollar surplus is repressive, and that you ought to have it if your resources were overstrained, but not when you're heading straight into another recession that's going to be bigger than the last one, and saying that you can't afford the national defense and the science and the education which would come from the full release of your productive resources. So the informed businessmen aren't debating whether we have achieved a sustainable rate of economic growth. They are only debating whether the next recession will come in late 1960 or early 1961. And from the larger viewpoint, what in the dickens difference does it make?

Now, looking ahead, we face the prospect over the next seven years-- and I say "seven years" and it might be five years--that with these kinds of policies and this kind of approach we will repeat the record since the Korean War. We will average again a growth rate ranging between 2 percent, 2 1/2 percent, and 3 percent as against 4 1/2 or 5. And my estimates of the differentials are very low, because I am merely projecting a growth rate compatible with the technology already developed. I'm taking no account of the fact, which my individual studies indicate, that the American people and their leaders have absolutely no recognition of what's happening to technology now. Why, on the farm the increased output per acre or per man-hour is just increasing at an indescribable rate. The same thing is true in the factories.

There is one automobile company now that can produce without more hours of labor more automobiles than all the automobile plants in the country produced, not this year, but in 1955, when they produced the most. And I cite this just to give you some indication of the tremendous technology that can't permanently be swept under the rug; and I'm not even taking that into account in my estimates. But just based on the past technology, if we have this lower growth rate rather than the optimum growth rate over the next few years--I'll only go ahead to 1965-- we'll have a differential of about 350 billion dollars of national product; and we'll have a differential in existing tax rates in Federal, State, and local revenues of 100 billion dollars. And therefore at existing tax rates we'll have 100 billion dollars less of Federal, State, and local revenues for national

security and schools and science and roads and all the things that represent our great national priorities.

And yet under these conditions we're told what we can't afford, and we're told that we have to try to maintain a sustainable rate of economic growth by perpetuating a constantly rising chronic unemployment of plant and manpower which will carry us to about 8 or 9 million unemployed within a few years, rather than the 5 million that we have now when we count it correctly; and this is the ultimate source of wealth.

Now, what do we need to do to get going on this road? The first thing that we really need to do is to recognize the problem. And then it becomes relatively simple, because the whole trouble now is not with the mechanics of the deployment of specific measures. The whole trouble is with the utter and complete unrealism of our economics except in times of total war. We would never say in total war that we wanted to build our armaments or build our production at half the rate of which we were capable so that it would be sustainable. We would ask ourselves how we were going to sustain the nation if we got into such nonsense. And we would never in time of war measure our capacity to do anything on the basis of a flow of a commodity, which isn't really very good now even for filling teeth. And yet we talk now about basing our whole international economic policy of the flow of gold.

Let me tell you right here and now that I certainly don't want to be defeatist about the United States; but as a student of civilization we cannot compete with the realism--we don't need the ruthlessness and we

don't need the brutality--we cannot compete with the realism of systems that measure wealth by manpower, and electric power, and transportation, and science, and technology, used, when we talk this nonsense about measuring our performance by certain superstitions applied to the controls of economic life--prices and wages and profits and Federal books--rather than talking about whether we are or are not using our resources. A nation that says that it is correspondingly able to do less as more of its resources become unemployed because the more of its resources are unemployed, the less revenues flow, is upside down. And this is not liberal economics or socialist economics. It's plain, ordinary common sense to anybody concerned with the preservation of the country.

Now, which of our policies do we have to change? First of all, we have to change our attitude toward inflation, not on the valid ground that the matter of the change in the value of the dollar is not per se important. We have had almost no economists in this country with enough guts to say that what you really have to examine is not the change in the value of the dollar, but how the change in the value of the dollar acts as resources toward building or corroding economic strength. To put it in another way, if a 3 percent annual decrease in the value of the dollar yielded a 6 percent real growth rate, while a stable dollar yielded a zero growth rate, manifestly it would be better to have the 3 percent corrosion in the value of the dollar, because the dollar was worth most in 1932.

But we can put all this aside, because it's irrelevant except as a

measurement of a lack of guts of people who won't even talk about it. They're not making any empirical observations of what kinds of price trends would be conducive to our real economic strength. But let's put that aside. I will accept the fetish of the stable dollar and I will make a separate point.

I raised the question a few years ago that if an automobile burned the least gas ^{per mile} going 50 miles an hour and this is the most efficient rate of operation, and burned more gas per mile going 90 miles an hour, wouldn't it also burn more gas per mile going 23 miles an hour? The answer is obviously "Yes." I said: "Well, then, by the same token, if you learn in going 90 miles an hour that this is inflationary or wasteful and that you have to slow down to 50, does it follow that if you're going 23 miles an hour you have to slow down further to burn less gas per mile?"

Now, this is a perfectly apposite, exact, practical, observationally provable observation about the American economy. The only kind of inflation we've had in the United States in the past seven years has been an inverse correlation to all of the classical measurements of the causes of inflation, based upon the wartime experience when we were going 90 miles an hour, although, as I said, growing 9 percent in real terms and imposing an excessive strain on our resources. All of the inflation that we have had in the past seven years has come from going too slow. Let me illustrate.

If you have a plant that is operating at 50 percent of capacity,

and you attain 70 percent of your labor force for perfectly good reasons-- you want to share unemployment; you don't want to turn them out on the streets--you divide the 70 into the 50 and you get a low productivity figure. It has nothing to do with technology. This is high cost due to economic slack. Your technology may be racing ahead, and that's what has been happening in the last few years when we've heard all this nonsense about low productivity. In a technological sense our productivity has been increasing faster than ever. We've simply gotten a low productivity figure by economic slack, and then we've said: "The low productivity is inflationary. Let's slow things up some more." And in an administered price and wage system, where the employer tries to compensate for the high level of unemployment in the plant by higher prices, and the labor group tries to compensate for the high level of unemployment by higher wages, you get higher cost per unit and this is inflationary.

Now, this is not theory. I've done what nobody else bothered to do. I said: Let's take all these periods --and I've gone back fifty years and I've taken all the different periods--and they show very clearly that from 1951 to 1953 you had virtually stable prices with a high rate of growth and so forth and so on, and that the so-called new inflation was entirely caused/by economic slack; and the reaction of the factors in the economy to the economic slack, and that there was an absolute inverse correlation between the tightness of the money supply and the price inflation, and an absolute inverse correlation between the surplus in the Federal budget and the price inflation, because, since the repressive budgetary

policy and the repressive monetary policy caused economic slack, and therefore caused the kind of inflation that was due to economic slack, the classical remedies for inflation will cause more inflation because we weren't in the classical inflationary situation.

You don't have to be an economist to realize this. All you have to do is look at the figures. Any conservative businessman would assert this if he stopped to think about it--that if you go too slow it's costly, just as if you go too fast; that if you crawl it's more exhaustive than if you walk, just as it's more exhaustive if you run. We've been crawling and then talking about a sustainable rate of progress.

So what do we need to do? Very simply, we need to adjust our tax policy and our monetary policy and our budgetary policy to the needs of the nation. We need to have a national prosperity budget which quantifies our productive powers, our national objectives, and how our monetary policy and our tax policy supplement and reinforce the achievement of these quantitative goals.

Now, this isn't alien or dissident. We did this in wartime. People say, "Oh, well, but that's planning." Well, what do we mean by "planning"? If we mean by "planning" the complete planning that the Russians have, we're not for it. If we mean by planning the degree of planning that we had in wartime, we don't need it. But if we mean by planning that the traditional policies of Government, which are executed anyway, should be executed on a long-range basis and be consistent with one another, should be geared to objectives, what is the sense of a tax policy

that isn't geared to the objective of resource use? Taxes are designed to transfer resources. What is the sense of a monetary policy that isn't geared to resource use? Monetary policy is designed to deal with resources. And what, above all, is the sense of a monetary policy and a tax policy that conflict with each other and are internally inconsistent every other day, and which will remain internally inconsistent until we chart these long-range goals for production and employment?

Now, one final word. I read in the newspapers, as another indication of our utter confusion, that my successor as Chairman of the Council of Economic Advisers--and I'm not speaking politically--is being mentioned as the chairman of the committee which the President is going to appoint to set the kind of long-range economic goals that he talked about a year ago, that some of us have been talking about since the Employment Act of 1946, 14 years ago, placed upon the Government the mandate to do this. So when he took over as Chairman of the Council in 1953, he stopped doing it, the economic reports to the President stopped ^{about} talking, needed levels of production, employment, and purchasing power, and stopped relating the policies to these goals; and the reasons given by Professor Burns was, first, that economists didn't know enough to do this; and, second, that it was a delusion anyway because if you did it, the people would expect the Government to help achieve these goals; and if the Government was expected to help achieve these goals, they would be used for political purposes or we would lose our freedom.

Now, a few years later, he or somebody else is going to chair

a committee to do exactly this kind of thing outside the Government. I don't know what great amount of additional economic knowledge has accrued in these few years. I don't know whether the statement is that it doesn't matter if you do it outside the Government, because then nobody will expect the goals to be achieved, and therefore it won't be dangerous. I don't think that's a very great position for a great democracy to take in the face of the greatest peril it's ever faced--"Let's do this so long as it's an academic exercise in nothingness, but let's not do it if we can make it significant." This I just don't understand.

And I hope that this does not overstate the role of a free Government in a free society, because let me tell you for sure that our biggest problems today domestically and our biggest problems throughout the world are problems that we have to meet ^{as} 180 million people together and not as 180 million people separately, and as a nation and not as 50 States. We don't have the kind of problems that can be solved individually. Our farm problem is not based upon what the farmer needs to do. He's becoming very, very productive, and the only thing he can do on the farm is become more productive. And it's not based on what the worker can do individually, because, despite all the talk about feather-bedding, he's becoming more and more productive, whether it's due to his own efforts or due to technology. You don't have surpluses because people are becoming less productive.

And the Governors in the States likewise. And I am perfectly willing to have the head of the NAM talk about what the NAM should do

and the governor talk about what the governor should do, and a mayor talk about what the mayor should do, or even to have the Farm Bureau talk about what the farmer should do, and the AFL-CIO talk about what they should do or what they want. But I don't think that the leaders of the nation can spend most of their time talking about what all these other people should do and conduct a march against Washington, instead of asserting and affirming the great responsibilities of the nation. And the responsibility to provide for the national security, the responsibility to manage tax policy, the responsibility to manage monetary policy, the responsibility to manage the general economic environment in which all these other factors are operative is nationwide.

Now, you can call this planning if you want, but I would certainly like to know how the Russians really feel if they hear the American people saying, "Let's leave this to Alaska." I'm wondering who's going to be in Alaska if we leave this to Alaska. I think some of these things have got to be left to Washington.

And I think, if we're going to steer between the Scylla of totalitarianism and the Charybdis of aimlessness, and hit that happy middle ground between Scylla and Charybdis, you've got to have a lot more thoughtfulness, a lot more more coordination, a lot more planning under freedom, a lot more centralized responsibility, a lot more action of the United States as a nation, than we have now or than we have had for a long time; and the fateful decision on this score will have a lot to do with how long we are here.

Thank you very much for your attentiveness.

COL. SMYSER: Mr. Keyserling is ready for your questions.

QUESTION: Mr. Keyserling, increased production up to this 50-miles-an-hour rate that you recommend, it seems to me, implies an increase in consumption even over and beyond our increase in population. What form do you visualize this consumption should take? More television, automobiles, better housing, or what?

MR. KEYSERLING: You have two basic types of consumption that need to increase--public consumption and private consumption. Unfortunately, our befuddled economics has become accustomed to calling public consumption "public spending"; and therefore the whole thing gets confused because you are juxtaposing public spending and private consumption. Public spending is public consumption and private spending is private consumption. If you send your child to a private school, you are engaging in the private consumption of education. If you send your child to a public school, the nation is engaging in the public consumption of education. Both consume a certain portion of your productive resources for certain purposes.

Now, my thesis is that we have to increase both public consumption and private consumption in proper proportions. Now, what are proper proportions? This is what policy is about. That's why I say that here's what I mean by planning: When you set a Federal budget at 80 billion dollars, you are determining as a matter of policy what part of your national production you want to allocate to the purposes contained in the

budget. You don't avoid this planning problem by setting it at 80 rather than 85 or 72. You have the problem anyway. You can't avoid it. And you have it in peacetime as well as in wartime. The question is what your criteria are.

Now, I say that your criteria should be, first, What is our national product capacity at reasonably full use of our resources? That's point one.

Point two, what part of that do you want to allocate to your highest national priorities, which actually are, for the most part--I mean, and clothing aside from food and shelter, which we have a reasonable amount of in this country--the highest priorities are the things you try to do through your budget, I mean the Federal, State, and local budgets, like national defense, education, science, and so forth. So you say, "Here are our national needs and we think we ought to put about 17 or 18 percent"--or whatever it is--"of our national product at full production into these budgets." And I would construct the Federal budget on this basis.

Now, if ^{your} national growth actually turned out to be less than you computed, you wouldn't have made a mistake in your Federal budget, because if your national product should turn out to be less, the budget deficit resulting from that disuse of resources would help to prevent the disuse from being greater. It would be stimulatory in the traditional sense. And you certainly shouldn't cut back on your big priorities because you have economic slack.

And this shows the nonsense of a lot of our economic thinking,

because on that theory, the more slack you have, the less you can afford. Or, stating it from the opposite point of view, some other people say the more slack you have, the more you can afford, because there are resources to be taken up. I say, neither. I say what you can afford by way of your national priorities is what part of your resources at full employment you want to put into them. In this way you construct your public consumption budget.

Now, coming over to private consumption, your economic analysis provides you with general guides as to targets for private consumption. And in answering your question I would say that private consumption runs across the whole gamut of consumer spending.

I would not attempt--and here's where I'm not/^{so much}for planning as some of you might think--to dictate to consumers, directly or indirectly, what the pattern of private consumption should be. And that's where again I disagree with some of my economists who say that we don't need growth; that all we need is better qualitative values and who want to tell the American consumer that he should like one kind of book more than another or one kind of entertainment more than another. I say, ~~provide~~ use your economic policies to provide a level of private consumer power roughly equivalent to the private production, which is your total productive capacity less your priority takes through public programs, and let the consumer spend as he will.

Now, what policies do we have for that purpose? First of all, we have tax policies, because, obviously, tax policies very importantly

affect the pattern of private consumer power. The tax policies should be adjusted to these quantifications. Our tax policy now is conducted in an absolute and complete vacuum.

Similarly with our monetary policy. Through our monetary policy we have been imposing increasingly repressive burdens upon the things we ought to have more consumption of and not holding back the things that we ought to have less of. The tight money policy has restrained general private consumption when we needed more of it, has restrained local schools and education and other public improvements when we needed more of them, and had no effect upon an investment boom that from time to time got out of line with consumption and thus resulted in slack capacity. It had no effect upon them, because the big investors don't depend upon monetary policy or interest rate policy. In other words, any empirical observation would show that the policy wasn't attuned to any rational pattern of resource use. So you would adjust your policy. And I would adjust the social security policy. I don't think we have enough consumption on the part of our old people.

I think that instead of talking about the danger of price and wage controls or the need for them and some of these other things, I would say that if we took the established policies of Government--tax policies, money policies, social security policies, certain regulatory policies--and adjusted them to these kinds of quantifications, which is ^{actually} ~~essentially~~ an unfulfilled mandate of the Government now under the Employment Act of 1946, we would get pretty good results, and we could correct as we

went along. And we would have a balanced budget to boot, because it is impossible to develop a model which gives you reasonably full employment at existing tax rates and doesn't provide you with a budgetary surplus. The budgetary deficit is entirely the product of economic slack. And actually, with the 2.3 percent growth rate that we've had over the past seven years, we've had on an average annually three and a half times as big a budget deficit, despite the repressive budget policy, as we had during the previous seven years, despite the Korean War, with a 4.7 percent growth rate.

So the argument is really rather off the point, that we have to choose between growth and stability, or that we have to choose between budget deficits and national deficits. This isn't really true. The real truth of the matter is that in any situation short of total war, the policy that is best for growth is best for stability, and a policy that is best for an abundant fulfillment of our national economic needs is best for the abundant fulfillment of our Federal budgetary needs; and a policy of economic growth and a policy of balanced budgets and a policy of price stability therefore coincide. And empirically we ~~haven't~~ haven't gotten one or the other. We've gotten none of the three. We've had the biggest inflation we ever had in peacetime. We have had the biggest deficit we ever had in peacetime. And we have had one of the lowest rates of economic growth that we ever had in peacetime.

QUESTION: Could you relate what is happening in West Germany and lately in France since DeGaulle took over to their policies with regard

to rate of growth?

MR. KEYSERLING: Well, what's happened in Western Germany, since first of all, is that if you take the whole period ~~from~~ the rebuilding of Western Germany since World War II, they have had a very much more rapid rate of growth than we have. There are a variety of reasons for this.

I do not think that the need for rebuilding is one of the reasons. I think this is a great fallacy. I think your rate of growth is dependent upon your productive force; and if you don't use that productive force for rebuilding, you ought to be using it for new building. There are plenty of unmet needs. This whole idea that you can grow fast only when you are undeveloped, or when you have to rebuild, is an expression of the lack of imagination and creativeness of economic policy.

We have just as much room to do new things as India or Germany. We just happen to have the advantage of starting from a higher plateau. But once we admit that we're on a higher plateau, we haven't got as much room, this is the very essence of our falling behind, by saying that all the others who are behind us can ^{grow} faster, because we're ahead of them; so they'll be ahead of us. Yet this is what we hear all the time, and this is the absolute corruption of our economic policy. We hear that an ^{under-developed} ~~undeveloped~~ country can grow faster. This isn't so. It isn't supported by analysis or experience or anything else.

Your technology increases at a geometric ratio and we can grow faster than any country in the world right from here on out. Of course,

if you get fat and soft and lazy and say you don't need to, because you're ahead--and if you listen to economists who go up on the Hill and argue about whether the Russians are going to be ahead of us in 11 years or or 17 years 13 years--who ever heard such nonsense? What difference does 11 years as against 17 years make in a world contest among nations? It's already more than 20 years since World War II ended, or since it began; and how long is that? So they're arguing about whether it's going to be 11 years or 17 years or 19 years and therefore we don't need to worry.

Western Germany has had a faster rate of growth than us because they have mobilized their resources more effectively and put them into a more coherent pattern.

I also think that the policies that produced a higher rate in Western Germany have been suited to a period when they had a great amount of capital replenishment, and therefore could have an investment program coming to a much larger percent of their national product than is sustainable in the long run; and that some of the conservative economic policies that have been in vogue since World War II have been suitable for that purpose. But Germany, unless it adopts a more liberal economic policy in the sense that I have defined it, is going to run into increasing unemployment and increasing trouble now that its capital equipment is rebuilt, and it has to think more about the problem of distribution.

Now, as to Western Europe aside from Germany--France and England--they have all been growing at a faster rate than we have, considerably faster. Their growth rate has slacked off in recent years.

I think they suffer in varying degrees from the same difficulty that we do--of too much homage to the classical economic formulas. The so-called conservative monetary policy has had a great run for its money in recent years. It has worked very poorly everywhere. It hasn't contained inflation. It has slowed down the rate of economic growth. It's been in great vogue among the bankers--and I have nothing against the bankers, but we've certainly come to a sorry pass as a nation when we are so stupified that the great financial institutions have the gall to put advertisements in the newspapers to the effect that the way to stop inflation is to hit the wage earner on the head, depress the farmer, and double the payments that we get for lending the people their own money. When people have the simple gall to do that, it's a recognition of the low state of our economic thinking. And they have had the gall to do it. They've gotten away with it. And, of course, during 1959 and 1958 the profits of the bankers have been ^{perfectly} fabulous. I have no objection to banking profits on a sound basis.

Incidentally, everything I say can be checked with the facts. Somebody said to me outside: "This Captain Billy that you were talking about--does he have red hair?" I said: "Yes" because this gentleman was stationed down near my home town and knew my brother, who's a practicing physician down there, and I do have this little nephew with red hair whom we call Captain Billy.

Now, likewise and more importantly, this monetary thing can be checked. There has been a tremendous increase in the illegitimate

earnings based upon the use of a national monopoly created by the Government--the banking system--for private purposes.

Now, I'm not against private enterprise when I say that if the Government of the United States 46 years ago deliberately passed the Federal Reserve Act to permit and encourage the banks and bankers of the United States to exercise a uniform decision and control over our credit system and our money supply and our rediscount rates, and, indirectly, therefore over our interest rates, that when the Government took that step, which I think needed to be taken, then to maintain at the same time that in order to avoid politics this fantastically powerful instrument of national action should be independent and clear of Government, is a strange kind of thinking. And, again, I say, my position is very conservative. I can think of nothing more radical than saying that the Government should set up such a banking system and then have it run by a central market committee of bankers in New York. ^{It's} just as radical as to say that because our tax system should be non-political, we should have our tax system run by a group of bankers, businessmen, and labor leaders and professors, rather than by the Government; or that if we had price and wage ~~controls~~ ^{controls} during the wartime, since we want them to be non-political, let's set up a group of labor leaders and businessmen to administer the price and wage controls. If that's what you mean by non-political, I'm for politics.

And to have an independent monetary system when you have a national debt of 280 billion dollars, when you have to coordinate your fiscal

and your monetary policy, if you were writing on a blank sheet, as Woodrow Wilson said when he first set up the Federal Reserve System, you have to take people out of an asylum to write that on the blank sheet. It doesn't make any sense at all, regardless of what you think about the particular policy.

A few years ago the Federal Reserve Board was saying that they didn't believe in independence; that it was absolute nonsense; that all they meant was independent of the President and they didn't mean independent of Congress. This was my friend Bill Martin's position-- didn't mean independent of Congress. Well, last year the Federal Reserve Board wanted the ceiling raised on interest rates of certain types, and Wilbur Mills, of the House Ways and Means Committee, had legislation to give it to them and he just wrote in there a little provision of a general ~~innocuous~~ ^{innocuous} character expressing the interest of the Congress that the Federal Reserve Board take some account of economic growth and various other problems. And Martin said: "No. This is getting the camel's nose under the tent. This is the beginning of Congressional concern with the operations of the Federal Reserve System." So the whole argument that we were independent of the Congress but weren't so blatantly disregarding of the democratic process as to say that we should be independent of the Congress became converted in 1959 into the argument that we should be independent of the President and the Congress. And how are you going to run a country that way?

QUESTION: Mr. Keyserling, you said that we ought to take

account of and accept a 3 percent inflation in order to get growth. Well, if the Government will accept a 3 percent inflation, won't all the executives also take that into consideration, and when you try to sell bonds, won't they say: "Well, the first 3 percent goes down the drain; so we've got to have an interest rate above that"? And if you can't sell bonds now at 4 1/4 percent for the long range, how is the Government going to finance this extra budget if they have to pay more for the money?

MR. KEYSERLING: Well, first of all, I haven't taken the position that we should have a 3 percent inflation to get growth. I have said that if a 3 percent inflation were the only way to get growth, and the only way to avoid the gross neglect of your most important national priorities, then you have to weigh one against the other.

Stated more succinctly, I would say that during World War II we might have had a little less inflation than we had, through a different set of policies, but that we couldn't have fought World War II without considerable inflation; and that if we had said that inflation was a greater danger to us than Hitler, as we are now saying that inflation is a greater danger to us than Khrushchev, we would have lost the war and we wouldn't have any dollars. That's all I'm saying.

But I'm not saying that the 5 percent rate of growth is dependent on 3 percent of inflation. I'm saying quite the contrary--that the policies which would be conducive to a 5 percent rate of growth would net in the long run less price inflation than the policies contributory to a 2.3 percent rate of growth. This is the whole basis of my argument. Not that we

have to choose between growth and stability, but that an optimum rate of growth is conducive to ^{optimum} stability, a hyperbolic rate of growth is conducive to price instability, and that a deficient rate of growth, although it produces some price stability during the period of recession, in the long run of the ups and downs, averaging a low rate of growth produces more net price inflation than a stable rate of growth at a higher rate.

QUESTION: Mr. Keyserling, I find it real easy to subscribe to the logic of your stated requirements for planning for this economic growth which we need. I do, however, come to a grinding halt when I visualize the problems that we have in getting any sort of long-range program, say, in the military departments, where we go from a year-to-year basis. How do you politically translate this requirement for a 10-year or a 7-year or a 4-year program for economic growth in an environment where your Administration changes every four years perhaps and the political complexion of your Congress may shift every two years? Is this politically feasible?

MR. KEYSERLING: Well, I appreciate your question. I don't just know what would be accomplished by any answer that I might give to that question, because if my answer were that we had a political system in a constitutional sense that were not adjusted to the world in which we now live, that answer wouldn't be worth anything, because we have that political system and we're going to stay with it; and we would still have to come back to the question, What are we going to do now that we've got it? So I don't see that the answer to the question, if that

were the answer, would get us much further than where we are now.

More affirmatively I would say that I do not believe that the flexibility or nature of our political system is an intrinsic and irremediable liability. I think it gets down to the old, overused, but nonetheless important word of courageous leadership. I think the kinds of policies that I am talking about have no popular political obstacles that cannot easily be surmounted by courageous leadership.

As a matter of fact, a good many of the policies that I'm talking about the public doesn't register any will on and doesn't have any opinion about. Take, for example, the policies of the Federal Reserve Board. There is no really politically insurmountable obstacle to their changing their policies. They could change their policies overnight. And there's no political obstacle to the President of the United States and the Cabinet taking a different position on these monetary policies.

As a matter fact, from the political point of view I can go around the country and sell 70 people on the outrages of the tight money policy for every 30 people they can sell for it, when you tell them the facts, because the American people are not intrinsically committed to the proposition that 20 billion dollars in a few years should be taken out of their pockets and put into the hands of a few financial institutions. And the American people are not intrinsically committed to the proposition that the way to stop inflation is by inflating the fat and starving the lean. There's no political intrinsic difficulty in changing this policy. It's a matter of leadership. It's a matter of the policies and attitudes of the

trustees of the American People--the Federal Reserve Board and the Government.

Tax policy is a little more complicated, but there's always a lot of pull and tug on a tax policy anyway. I don't think that a rational tax policy is intrinsically more difficult than an irrational one.

As a matter of fact, even on this whole price-wage front and the atrocious mismanagement of the steel controversy, I think the Government has done the worst of all things on all scores. And I don't think that a more viable and sensible policy would have been politically more difficult. It may have been. But, again, if we're going to say that courage has now no place in the lives of the leaders, I don't think we're where we were.

Now, every person in political life is ambitious, and every person in political life believes that survival is the first law of nature. I'm getting a little off economics here, but it's very relevant. But modern world history has demonstrated many examples of political leaders who, while they were ambitious, and while they wanted to succeed, and while they wanted to be prime ministers, nevertheless were willing to go out into the political wilderness. Winston Churchill, for example, did that most of his career. I think he was just as ambitious in his early years as in his later years. I think he always probably wanted to be Prime Minister. But he had certain basic principles that he fought for; and if they took him into the wilderness for a while, he went into the wilderness for a while.

This has been true in the United States also. We have had leaders
in the mean--
who compromised on many issues who were flexible to me/ and I'm
not talking about the President only. I'm talking about the Congress and
elsewhere--but still had certain unalterable minimum objectives for
which they would fight.

← Now, if we happen to have reached an age in the United States
where we don't have this any more in our political leaders, then I think
we're doomed. But I don't think that's true.

That's the only kind of answer I can give to your question, which
is a sort of very important and imponderable question. I think that if
the things that I am talking about are correct, and if they are understood,
and if economists and technicians and other people do their part in
pressing them, I don't think that the political task of selling this program
is at all unmanageable. If it is unmanageable, then I don't see any way
out.

COL. SMYSER: Mr. Keyserling, the great number of questions
that we have I think is indicative of the great interest in your talk, but
I'm afraid that our time has run out. On behalf of the Commandant and
the faculty and the students, I want to thank you for your visit here this
morning. I'm sure your remarks will stimulate us to some very serious
thinking about the problem of economic growth. Thank you, sir.

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