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**AUSTRIAN INCOMES POLICY: LESSON FOR
THE UNITED STATES**

HEARING
BEFORE THE
JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES
NINETY-SEVENTH CONGRESS
FIRST SESSION

—————
JUNE 2, 1981
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Printed for the use of the Joint Economic Committee



U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1981

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(Created pursuant to sec. 5(a) of Public Law 304, 79th Cong.)

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(II)

CONTENTS

WITNESSES AND STATEMENTS

TUESDAY, JUNE 2, 1981

	Page
Reuss, Hon. Henry S., chairman of the Joint Economic Committee: Opening statement.....	1
Schober, Hon. Karl, Ambassador to the United States from Austria.....	2
Seidel, Hon. Hans, Minister of State, Federal Ministry for Finance, Austria.....	3

SUBMISSION FOR THE RECORD

TUESDAY, JUNE 2, 1981

Seidel, Hon. Hans: Prepared statement.....	6
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(iii)

AUSTRIAN INCOMES POLICY: LESSON FOR THE UNITED STATES

TUESDAY, JUNE 2, 1981

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met, pursuant to notice, at 10 a.m., in room 2167, Rayburn House Office Building, Hon. Henry S. Reuss (chairman of the committee) presiding.

Present: Representatives Reuss and Richmond.

Also present: James K. Galbraith, executive director; and George R. Tyler, George D. Krumbhaar, Jr., and Kent H. Hughes, professional staff members.

OPENING STATEMENT OF REPRESENTATIVE REUSS, CHAIRMAN

Representative REUSS. Good morning. The Joint Economic Committee will be in order for a further discussion into the cause and the cures of inflation.

It's a particular pleasure that I welcome this morning our guests from our great and friendly neighboring country of Austria to discuss efforts in their country to moderate wage and price increases.

This is an historic occasion for the Joint Economic Committee in that it's the first time that we have been honored to formally hear testimony and exchange views with representatives of a foreign government. This morning's hearing reflects our committee's uneasiness with our efforts to moderate inflation while simultaneously achieving economic growth.

Over the past 10 years, the United States has experimented with a variety of techniques to suppress wage and price increases—outright wage and price controls, tight-monetary policies, taxing and spending policies designed to slow economic growth, and more recently productivity boosting tax reductions.

During this same 10-year period, some mature economies have been able to successfully avoid the inflation or unemployment or both that has confronted the United States. These countries have been able to digest repeated OPEC oil price increases, rising prices for agricultural commodities, and the vagaries of floating exchange rates, while still attaining healthy growth rates with little inflation.

The purpose of this hearing is to explore what lessons can be learned from the successful Austrian experience in this regard. We are fortunate enough to have as our witness today Prof. Hans Seidel, the Austrian State Secretary in the Federal Ministry for Finance, who

will review for us the techniques and results of Austria's efforts to moderate wage and price increases. And we are also particularly honored to have with us Mr. Karl Schober, who is the Ambassador of Austria to this country, who will introduce Mr. Seidel. Mr. Schober has had a most distinguished record in both finance and diplomacy. He was Austria's delegate to this country back in the great days of 1948-49 when the Marshall plan was being put together. He has served his government with distinction both in Vienna and various important diplomatic posts, and he is a leader in the Washington diplomatic community. We are delighted to have you with us, Mr. Schober.

**STATEMENT OF HON. KARL SCHOBER, AMBASSADOR TO THE
UNITED STATES FROM AUSTRIA**

Ambassador SCHOBER. Thank you, Mr. Chairman.

When you informed me that the Joint Economic Committee of the Congress of the United States would like to look into the Austrian experience with incomes policies and asked for our testimony on this subject, we readily agreed to comply with your request.

Before I present to you Prof. Hans Seidel, Minister of State in the Austrian Federal Ministry of Finance who will explain the techniques and results of the Austrian efforts on this field, permit me to make a very few general remarks.

First, let me say that we are very pleased and honored by the interest this committee is taking in our home country. After all, Austria is a small country. It usually does not make headlines and rarely commands the concern of those concerned with the crises in the world.

After the devastation of World War II, we had to rebuild our economy almost completely. We were greatly helped by the Marshall plan and aid so generously given by your government. Today, Austria is a modern, industrialized state, having to cope with all the problems such states are facing, such as a growing oil bill, environmental protection, trade, wage and price control, et cetera.

Without boasting, I think one can say that the Austrian economy weathered the difficulties of the 1970's relatively well. Just to mention a few facts, having made full employment the first priority, we succeeded in keeping unemployment below or around 2 percent. The inflation rate was 3.7 percent in 1979, and 6.4 percent in 1980. The Austrian schilling is one of the hardest currencies in the world. Our economic growth rate was 5.2 percent in 1979 and 3.5 percent last year. In the period from 1966 to 1979, prices doubled but wages tripled. Our GNP per capita, which in 1970 was 60 percent lower than yours, is now only 13 percent lower. And finally, a most unique record, although Austrians have the full right to strike, they went on strike very rarely during the last decade; we enjoy an almost unparalleled social peace.

The explanation for this Austrian miracle, as it is sometimes called, lies in a well-functioning mechanism for discussion and settlement of basic economic and social issues. This mechanism, called the Commission of Parity, provides for an institutionalized and continuous

dialog between all the economic forces of labor and commerce on a decisionmaking level. The role and the effective representation of those forces as well as of our government in this mechanism go a long way to assure that compromise is always found and that strikes are practically eliminated from our economic life.

But now, Mr. Chairman, permit me to present a most competent expert to give this committee the information you requested. Prof. Hans Seidel is a graduate of the University of Commerce in Vienna, who, in 1946 joined the Austrian Institute for Economic Research, to which he still belongs today. In 1962, he was appointed deputy director, and in 1973, director of that institute.

In 1957, he spent some time at the International Monetary Fund here in Washington on a sabbatical visit. In 1965, the title of professor was conferred upon him and in 1969 he was made an honorary professor of the University of Vienna. He is frequently called upon to act as an expert at Government functions. In January 1981, Professor Seidel was appointed Minister of State in the Federal Ministry for Finance. Thank you, Mr. Chairman.

Representative REUSS. Thank you very much, Ambassador Schober; and, Professor Seidel, we are honored to have you with us. You have been good enough to prepare a statement and we would appreciate your now giving us the statement so we can proceed to some questions and a dialog.

**STATEMENT OF HON. HANS SEIDEL, MINISTER OF STATE, FEDERAL
MINISTRY FOR FINANCE, AUSTRIA**

Mr. SEIDEL. Mr. Chairman, it is a pleasure for me to speak before this distinguished committee. I have prepared a short statement and, with your permission, I will read the most important parts of it.

To begin with, what is the purpose of incomes policy in Austria? As in most other countries which used this technique, incomes policy originally was introduced to reduce the inflationary bias of a full employment policy. By an appropriate mix of demand management and incomes policy we thought that we could have both a high level of employment and a reasonable degree of price stability.

By the way, that does not mean that we neglect the supply side of our economy. We think the words of an American economist are true, that God gave economists two eyes, one to look at the demand size and one to look at the supply side. So originally we thought incomes policy was a method to reduce the rate of inflation with a given growth of resources.

With the reduction of trade barriers during the process of European Integration in the 1960's and 1970's, a shift of emphasis was necessary. Many industries became price takers. They had to take the price of the world market. Under these circumstances, incomes policy was not well fitted to have a big influence on prices, but it was designed to insure or at least to support cost competitiveness vis-a-vis foreign producers. Wage increases should not undermine the profitability of the exposed sector at the given exchange rate.

Incomes policy is a very loose concept. Many different forms can be distinguished. Perhaps the best way to introduce the Austrian version is to explain what it is not.

First, incomes policy in Austria is not a short-term device to overcome temporary difficulties. We do not switch between policy-on and policy-off periods.

Second, incomes policy in Austria does not use mandatory controls, government intervention is kept to a minimum.

Third, there are no explicit, openly announced quantitative wage guidelines, although there is a widespread understanding which wage increases seem to be consistent with sound economic development.

Fourth, and I think this is an important point, incomes policy in Austria is not regarded as an instrument for changing the personal or functional distribution of incomes. It is based on the idea of maintaining approximately constant shares of labor and capital in the national income.

I wanted to stress these four points at the beginning because they show that some standard arguments against incomes policies cannot be raised in the Austrian case. For instance, it is usually said that after a wage freeze there will be a wage explosion. That type of argument cannot weigh against Austrian policy which is a more durable kind.

Now what really is the Austrian wage and incomes policy? It's a little difficult to explain, but I will try to do my best.

I think incomes policy in Austria has to be regarded as an essential part of the broader concept of what we call "Social Partnership," a durable cooperation between the representatives of labor, business, and agriculture. The idea of cooperation has its roots in the political and economic history of our country. We had civil war and mass unemployment. We had the bad experience of the Nazi period, and we had economic collapse at the close of the Second World War. All these factors strengthened the desire of the different social and political groups to work together and to solve outstanding problems by making compromises.

In order to make the idea of cooperation workable, one needs an institutional framework. The Austrian solution is based on the fact that our main interest groups have developed strong centralized organizations which are able to solve differences of opinion within the group. Each organization, shall we say, speaks only with one voice. That means there already is a complicated decisionmaking process within each group.

Now there are many organizations representing interest groups. The so-called "Chambers" for commerce, labor, and agriculture were established by law. Membership is compulsory. Expenditures are financed by taxes. This type of interest group representation has no parallel in most other countries. In addition to these Chambers, workers are represented by the Federation of Trade Unions, in which union membership is voluntary. So we have a system of double representation of interest groups—one voluntary and one compulsory.

I think it's really important to stress that the tight union federation in Austria is a centralized organization which leaves less room for interunion competition than in most other countries. There are only 16 different unions. The Federation controls the finances of the unions; the methods by which members elect their representatives leave those officials free from direct rank-and-file pressure.

The fifth and last group is the Industrialists' Association, with voluntary membership drawn from big business.

There are five strong interest group representations and these groups have developed institutions and procedures for discussing and as far as possible solving economic problems. The institutional framework at first might seem to be rather complicated, but it has developed on the idea of a social contract along the following lines: The trade unions are willing to abstain from using their full bargaining power in wage settlements if they get something for it. Especially, they want to have some influence on the formation of prices for products in oligopolistic markets, and they want to participate in decisions on general economic policy.

Based on this concept, a joint price and wage commission was set up. In 1957, it consisted of four government representatives and eight representatives from the main Chambers and from the Trade Union Federation. The Commission works on a voluntary basis. It has no legal authority nor means of applying direct sanctions. Decisions must be made unanimously.

The joint Commission has three subcommittees, one for prices, one for wages, and one for general economic issues, the so-called Economic and Social Advisory Board.

These committees work as follows: the Wages Subcommittee authorizes a particular trade union to start wage negotiations but cannot directly influence the content of wage agreements. So the subcommittee is not able to say that wage claims are too high, although it may postpone the start of wage negotiations. Moreover, wage claims are submitted to the committee through the Trade Union Federation. This procedure permits the coordination of the claims of the various unions before presentation to the subcommittee. So there must be some understanding of what the wage increases will be before the wage negotiations are started.

The second subcommittee, the Price Subcommittee, controls the prices of about 200 standard articles. The number of applications handled per year varies between 150 and 350. As a rule, the committee regards price increases as justified if the entrepreneur can demonstrate with plausible arguments that costs have increased. If there is no unanimous decision by the committee, the entrepreneur is entitled to raise his prices as requested after a short delay.

The price control law provides for imposing some sanctions on entrepreneurs who raise their price by more than the approved amount or who do not submit their claims for approval. In practice, these sanctions are never used.

The third subcommittee, the Economic and Social Advisory Board, consists of experts who make recommendations on economic problems submitted to them by the presidents of the nongovernment bodies. The experts are economists employed by these bodies. They combine expert knowledge with interest group representations.

That ends my description of the introduction arrangement. I now want to make some comments on the question of how effective incomes policy in Austria has been.

That question is not easy to answer. Some would even argue that it is not appropriate to use quantitative criteria such as macroeconomic data. All that matters, these people would say, is a friendly climate for negotiations, good labor relations, and the creation of an atmosphere of political stability. My introductory remarks already

have shown that I do not share this opinion. Social partnership according to my view, not only means that we all sit in the same boat; it also means that we are willing to steer the boat in a direction upon which most of us agree.

There are many facts which are relevant to the question of how well incomes policy has worked. I just want to mention three of them. Some others were presented to you by Ambassador Schober.

First, there are almost no strikes in Austria. We are, so to speak, on the bottom of the international strike league. The disruption of production associated with long lasting conflicts in the labor market has been avoided. I want to add that for a country with our geographic position, it is very important for political reasons that you have good labor relations where strikes are the exception and not the rule.

Second, during the stormy seventies, the overall performance of the Austrian economy was quite satisfactory. The annual growth rate on average was 1 percent higher than in the whole OECD area; inflation was lower than in the other industrial countries; and unemployment kept at low levels.

The most remarkable development in the seventies in the context of this hearing, and of my argument, was the rapid decline of inflation after the first oil price shock. In 1975, we had an inflation rate of nearly 10 percent, but this rate was reduced to 3.5 percent in the years 1978 and 1979 without creating unemployment on even a temporary basis. Most economists would argue that such a reduction in the inflation rate would be only possible by increasing the rate of unemployment.

These and other observations are clearly not sufficient alone as evidence for the effectiveness of incomes policy in Austria. Other factors surely have to be computed into the so-called success story of Austria. Nevertheless, most economists who have analyzed the Austrian case have argued that incomes policy in Austria has been reasonably successful, although many of them have added that the Austrian system is not exportable.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Seidel follows:]

PREPARED STATEMENT OF HON. HANS SEIDEL

Incomes Policy in Austria

It is a pleasure for me to speak to this distinguished Committee.

Incomes policy in Austria, like in other countries which used this technique, originally was introduced to reduce the inflationary bias of a full employment policy. By an appropriate mix of demand management and incomes policy we thought that we could have both: a high level of employment and a reasonable degree of price stability.

With the reduction of trade barriers during the process of European Integration in the sixties and seventies a shift of emphasis was necessary. The growing importance of the so-called "exposed" sector of the economy (more and more industries were subject to international competition) reduced the scope of a national price policy. Many industries became price takers: the prices of their products in the domestic and foreign markets predominantly were determined by world market conditions. Under these circumstances incomes policy was designed to ensure, or at least to support cost competitiveness vis-a-vis foreign producers. Wage increases should not undermine the profitability of the exposed sector at the given exchange rate. This line of arguments implies that the exchange rate was used as a policy target.

As a matter of fact, the Austrian shilling in the seventies for good reasons was kept in a constant relation to the Deutsche mark, although divergent economic policies were taken in both countries. The Austrians placed more emphasis on a full employment policy of a Keynesian type and did not use quantitative monetary targets. Incomes policy was supposed to fill the gap and keep the development of labor unit costs in line with cost increases in Germany.

Now, incomes policy is a very loose concept. Many different forms can be distinguished. Perhaps the best way to begin a description of the Austrian version is to explain what it is not.

(a) Incomes policy in Austria is not a short-term device to overcome temporary difficulties. We do not switch between policy-on and policy-off periods. Instead, incomes policy is regarded as a permanent task with long-term consequences.

(b) Incomes policy in Austria does not use mandatory controls, government intervention is kept to a minimum. Only in the immediate post-war period did price fixing play an important role.

(c) There are no explicit (openly announced) quantitative wage guidelines, although there is a widespread understanding, which wage increases seem to be consistent with a sound economic development and that the claims of individual unions should stay in line.

(d) Incomes policy in Austria is not regarded as an instrument for changing the personal or functional distribution of incomes. It is based on the idea of approximate constant shares of labor and capital in the national income.

I want to stress these four points at the beginning, because they show that some standard arguments against incomes policies cannot be raised in the Austrian case, e.g., the high administrative political and economic costs associated with rigid price and wage controls, or the danger of wage explosion after relaxing or abolishing guidelines or restrictions.

Let me continue with positive aspects of my subject. Incomes policy in Austria has to be regarded as an essential part of the broader concept of what we call Social Partnership, a durable cooperation between the representatives of labor, business and agriculture. The idea of cooperation has its roots in the political and economic history of our country. The civil war and mass unemployment in the thirties, the disastrous and disillusioning experience of the Nazi period, the occupation and the economic collapse after the Second World War: all these factors strengthened the desire of the different social and political groups to work together and to solve outstanding problems by making compromises.

We had a coalition government for two decades after the Second World War, and the system of Social Partnership, which was responsible for many important economic policy decisions throughout the periods, still works, although occasionally misunderstandings and tensions occur. The one-party governments since the mid-sixties held close contacts with the social partners or at least avoided actions, which could undermine Social Partnership.

Incomes policy requires a specific institutional framework. The Austrian solution is based on the fact that the main economic interest groups have developed strong centralized organizations, which are able to solve differences of opinion within the group. Each organization, so to say, speaks only with one voice.

There are many organizations representing interest groups, but only five do matter. The so-called "Chambers" for Commerce, Labor and Agriculture were established by law, membership is compulsory, expenditures are financed by taxes. This type of interest group representation has no parallel in most other countries. In addition to the Chamber of Labor, workers are represented by the Federation of Trade Unions, in which union membership is voluntary. The Federation is a centralized organization, which leaves less room for interunion competition than in most other countries. There are only 16 different unions, the Federation controls the finances of the unions, the methods by which members elect their representatives leave those officials free from direct rank and file pressure. The last organization to be mentioned in this respect is the Industrialists' Association with voluntary membership and specialization on big business.

These five strong organizations—the three Chambers, the Trade Union Federation and the Industrialists' Association have developed institutions and procedures for discussing and as far as possible solving economic problems. The institutional framework seems to be rather complicated, but it can be understood easily if the position of the representatives of labor, who at least formally bear a large part of the burden of such a policy, is taken into account. This position can be explained as follows: The trade unions are willing to abstain from using their full bargaining power in wage settlements, if they get something for it. Especially they want to have some influence on the formation of prices for products on

oligopolistic markets. And they want to participate in decisions on general economic policy.

Based on this concept, in 1957, a Joint Price and Wage Commission was set up. It consists of four government representatives and eight representatives from the main Chambers and from the Trade Union Federation. The Commission works on a voluntary basis; it has no legal authority nor means of applying direct sanctions. Decisions must be made unanimously.

The Joint Commission meets once a month. Before the meeting the presidents of the nongovernment bodies in a "Presidents' discussion" try to reach an agreement on current issues. Many important decisions have been taken in these discussions, e.g., the introduction of the 40-hour workweek.

The Joint Commission has three subcommittees, one for prices, one for wages and one for general economic issues (Economic and Social Advisory Board).

The Wages Subcommittee authorizes a particular trade union to start wage negotiations, but cannot directly influence the content of wage agreements. The outcome of the negotiations has to be submitted to the Commission for approval, but is usually accepted without modifications. Wage claims are submitted to the Committee through the Trade Union Federation. This procedure permits the co-ordination of the claims of the various unions before presentation to the Subcommittee.

The Prices Subcommittee controls the prices of about 200 standard articles. The number of applications handled per year varies from 150 to 350. As a rule, the Committee regards price increases as justified, if the entrepreneur can demonstrate with plausible arguments that costs have increased. If there is no unanimous decision by the Committee, the entrepreneur is entitled to raise his prices as requested after a delay of 6 weeks.

The Price Control Law provides for imposing some sanctions on entrepreneurs, who do raise their price by more than the approved amount or who do not submit their claims for approval. In practice these sanctions were never used and the system worked on a purely voluntary basis.

The third Subcommittee, the Economic and Social Advisory Board, consists of experts who make recommendations on economic problems submitted to them by the presidents of the non-government bodies. The experts are economists employed by these bodies. They combine expert knowledge with interest group representation.

The long tradition of Social Partnership and incomes policy in Austria to no small degree can be attributed to the flexible handling of problems as they occur. Voluntary and unanimous actions were preferred. No quantitative or overambitious incomes policy targets were set, although in critical circumstances there was a widespread understanding which wage increases were desirable. The increase in negotiated wages usually did not differ very much between various groups of employees, but effective earnings were flexible enough to attract labor, where it was most needed.

How effective then has incomes policy in Austria been? That question is not easy to answer. Some would even argue that it is inappropriate to use quantitative criteria such as macro-economic data. All that matters is a friendly climate for negotiations, good labor relations and the creation of an atmosphere of political stability. My introductory remarks already have shown, that I do not share this opinion. Social partnership does not just mean that we all sit in the same boat. It also means that we are willing to steer the boat in a direction, upon which most of us agree.

Reliable empirical evidence, of course, is hard to get, partly because incomes policy has been used for such a long time without interruption. Therefore, the normal way of testing assumptions; namely, to compare policy-on periods with policy-off periods, is not possible. Instead external criteria, such as comparisons with other countries, must be used.

There are many facts, which are relevant to the question concerned. I want to mention only three observations and make some brief comments on them.

(a) There are almost no strikes in Austria. We are on the bottom of the international strike league. The disruption of production associated with long lasting conflicts on the labor market has been avoided.

(b) During the stormy seventies the overall performance of the Austrian economy was quite satisfactory. The annual growth rate on average was 1 percentage point higher than in the whole OECD area, inflation was lower than in the other industrial countries with the exception of Switzerland and Germany, and unemployment could be kept at low levels. The rate of unemployment was fluctuating

around 2 percent of labor force. The favorable trade-off between unemployment and inflation certainly was not only the result of an efficient incomes policy, but it did play a predominant role in the policy mix Austria was using in the seventies.

(c) The most remarkable development in the seventies in the context of this paper was the rapid decline of inflation after the first oil price shock. The rate of inflation could be reduced from nearly 10 percent in 1975 to 3½ percent in the years 1978 and 1979. The stabilization policy was successful without creating unemployment even on a temporary basis. Most economists, who believe in a dynamic Phillips curve, would assume, that such a reduction of inflation is only possible, if the rate of unemployment overshoots considerably the so-called natural rate.

The forementioned examples and other observations cannot be regarded as sufficient empirical evidence for the effectiveness of incomes policy in Austria. Nevertheless most economists, who have analyzed the Austrian case, have argued that incomes policy in Austria has been reasonably successful, although many of them have added, that the Austrian system is not exportable.

However, the external and internal political, economic and social conditions change. In the future some factors will make incomes policy more difficult than it has been in the past. The Austrian way is based on an economic system, which might be described as a fixed-price, flexible-quantity system. Under these conditions prices were sticky and did not clear the market immediately. Therefore there was some room for negotiations; e.g., mark-ups in price setting could be debated. In more recent years flexible-price markets have become more important and some markets have changed their characteristics. Exchange rates are fluctuating heavily, the prices for energy have increased enormously, interest rates, which have been low and stable over a long period, because high and volatile, a growing share of the economy is subject to international competition. All these factors not only reduce the scope for a national price policy. They also lead to shifts in income distribution, which seem to be hardly acceptable for some groups. That is one reason why social partnership cannot be reduced to wage determination alone. So there is a need to investigate, what type of incomes policy can and should be adopted under the conditions prevailing now and in the foreseeable future. Personally, I am quite confident, that the Austrian socio-economic system will meet the new challenge.

Representative REUSS. Thank you very much, Professor Seidel. Mr. Richmond and I have a number of questions to ask. You were polite enough not to do it, but I want to compare the economic performance of Austria with that of this country in order to make a point. In 1979 you had, despite the oil shock, inflation of about 3.5 percent and a very low rate of unemployment, something like 2 or 3 percent. In comparison, the United States in 1979 had 12-percent inflation and unemployment of over 6 percent. The point is, when you put Austria's economic performance up against this country's, one is certainly compelled to seek what there is about the Austrian structure which enabled your much better performance to occur.

And while you're quite modest, again, in not claiming "credit" for the incomes policy, I have to say that a successful incomes policy in Austria, as opposed to the United States, seems to me one reason you were able to avoid the Phillips curve tradeoff and we were not. I notice you're nodding your head. I do think we are on the right track there.

I have some specific questions to ask about the way your incomes policy and social partnership works. On price controls, as opposed to wage, if there's less than a unanimous decision, then there's only a 6-week delay in putting into effect the new higher price. Costs are allowed to be passed on. And then you say, "but for those who do raise their prices by more than an approved amount, there are sanctions, but in practice these sanctions were never used and the system has worked on a purely voluntary basis."

Well, that's certainly very fortunate, but didn't Austrian businessmen who were obeying the rules of the game complain? Didn't they say, in effect, "Look, we're being good guys but while being good guys we see others get outsized, illegal price increases and get away with it." Was that said and how was that answered?

Mr. SEIDEL. Well, to answer just that specific question, there are other ways to make entrepreneurs appear before the commission, so we didn't need the legal methods. There is a very strong representation of business and the chamber for commerce on the commission—not to force, but to convince entrepreneurs that they should appear before the commission and they should play the rules of the game. So it really doesn't happen that only part of the entrepreneurs accept the rules of the game and others do not.

If this would happen as a consequence of a large break in the business community, then the whole system will break down. But as I've mentioned in my prepared statement, even if all the entrepreneurs having influence on the prices in the market really are seeking price increases, their capability to influence prices is getting smaller because foreign competition is getting larger. So, for instance, the price of steel in Austria is practically determined by the Common Market price and we do not have our own steel price policy. So, increasingly, the limitations come from abroad and not from the domestic economy.

Representative REUSS. So your answer to my question very largely is that I raised a problem that really hasn't existed; that the Austrian Joint Price and Wage Commission has not had to use its mandatory enforcement powers on price violators because the chambers of commerce exercised peer pressure on the erring businessman and he in fact then moderated his price increase.

Turning then to wages; in your prepared statement, you set forth how it is that labor in Austria has been willing to hold back from using its full bargaining power and, in general, has bargained only for such wages as are generally in line with productivity increases and hence aren't inflationary. You pointed out two things which made labor willing to do that, and I will repeat your words: "Especially they want to have some influence on the formation of prices for products on oligopolistic markets. And they want to participate in decisions on general economic policy."

Now the way they got their influence on the prices of products is through membership on the Joint Price and Wage Commission; was it not?

Mr. SEIDEL. Yes.

Representative REUSS. And so am I right in inferring that labor unions, through their membership on that commission, had some role in stiffening the back, let us say, of the chamber of commerce so that whether it's actually said or not in so many words, it was evident that if labor was going to stay in line the chamber of commerce was going to have to take care of its side of the economy and see that there wasn't a widespread increase in the prices of oligopolistic products. Is that a fair statement?

Mr. SEIDEL. Yes, I think so, Mr. Chairman. Originally, the representatives of labor in many cases were not satisfied with the outcome of the decisions in the commission. They wanted the legal possibility

to make use of their influence to point out if we don't reach a unanimous agreement within the commission, then they, the representatives of labor, could say, "Well, under these conditions we must have more strict rules or this system cannot work." But this is, of course, only one point where the trade unions and the representatives of labor can influence prices.

I think you asked a question about influence on economic policy?

Representative REUSS. Yes.

Mr. SEIDEL. One subcommittee, the subcommittee which we call the Social and Economic Advisory Board, is a Board in which economists from both sides meet, discuss their problems; they are expected to reach a compromise. So it's not just an expert group, but a mixture of political decisionmaking and expert advice. Of course, one has to take into account what type of government you have. If you have a Socialist government, the possibility of trade unions and labor to influence in a more direct way the economic policy is much greater than in this country. Nevertheless, whatever the government is, there are consultations among the representatives of the three groups—labor, agriculture, and business—and it is very important that the government not impose or not introduce measures which have not been approved by these groups.

At the moment, the Socialist government is designing an economic program. We won't decide this program in a vacuum, however; there will be negotiations about many parts of the program with the social partners. We will leave discussion, for instance, on the rather delicate question of how you promote investment to the Economic and Social Advisory Council. The chamber of commerce and the representatives of big business have a chance to put in their views there. There will be a constant discussion of problems and the government will avoid any action which will do harm to the type of social partnership which we have.

Representative REUSS. Now, in fact, in Austria since 1957, the year in which the joint price and wage commission was set up, there have been changes in government. For a while the more conservative group, the People's Party, was in power; and currently and at various times in the past the more progressive liberal group, the Socialist Party, was in power. But your testimony is, that irrespective of which government is in power, the general social contract was observed and labor had an opportunity to be heard, not only on wage and price questions, but on general social questions—the development of industry, credit policy, and social welfare policy. You're talking about such things, too—the whole gamut of economic matters?

Mr. SEIDEL. Yes. Let me give you just one example regarding interest rates for savings. Years ago, the level of those rates was primarily a question of some sort of a political and social compromise. Then the president of the trade union said that interest rates were too low compared to the inflation rate; we have to do something about it. And so interest rates were raised. That's just one example of their influence on general economic problems.

To give you another example, at the beginning of the 1970's, there was a general agreement, a basic agreement, between business and labor that work hours should be reduced to 40 a week. This basic

process had to be worked out by the experts and government didn't intervene in this partnership deliberation.

Representative REUSS. Congressman Richmond.

Representative RICHMOND. Thank you, Mr. Chairman.

Professor Seidel, the annual budget of the Austrian Government is how much?

Mr. SEIDEL. Of general government, the central government?

Representative RICHMOND. Yes.

Mr. SEIDEL. Our total budget is 300 billion schillings, but that excludes the expenses of the railroads and public-owned enterprises. Including those would yield a budget of about 200 billion schillings.

Representative RICHMOND. And you run a deficit of how much?

Mr. SEIDEL. We will run a net deficit this year of 25 billion schillings. That's approximately 2.5 percent of GNP.

Representative RICHMOND. 2.5 percent of GNP?

Mr. SEIDEL. 2.5 percent of GNP, a little less.

Representative RICHMOND. Ours is about the same. Yet, many Americans feel that the deficit our government operates under is one of the leading causes of inflation. Obviously, the greatest problem we have in the United States, next to our dependency on imported oil, is inflation. Why has the deficit of the Austrian Government not caused inflation in Austria? What is the present inflation rate in Austria?

Mr. SEIDEL. Well, I think we'll have 6.5 percent inflation this year.

Representative RICHMOND. 6.5 percent and last year I believe it was 5 percent, wasn't it?

Mr. SEIDEL. No. It was 6.4 percent. So these are 2 years during which we had high inflation rates because of the second oil shock.

Representative RICHMOND. Last year your inflation rate was roughly half of ours and this year it still will be considerably less than ours, even though you have a deficit in your government and we have a comparable deficit in ours. Can you explain why your inflation hasn't gone higher than that? You're even more dependent on outside oil than we are, correct?

Mr. SEIDEL. Yes, that's correct. But you see, in order to stabilize prices or to reduce the inflation rate, we have a certain policy mix which means we are fixed—the Austrian exchange rates, the value of the schilling—to the German deutsche mark. That means, if inflation is low in Germany it couldn't be very much higher in Austria, for various reasons. So we try to use exchange rate policy as an instrument to hold down inflation. And if you do this in a small country, you have to be very careful what happens to wages because if wages continue to increase, then you will lose competitiveness in foreign markets. So the Austrian way to stabilize the price level and lower the inflation rate was and is to maintain fixed exchange rates with the deutsche mark and then convince trade unions that they have to accept the consequences of a so-called hard currency policy. That is the way we reduced the rate of wage increases between 1975 and 1979, although in that time we had a fairly high deficit. In 1975, for instance, we had a deficit of 4.5 percent of the GNP, which was fairly high, and it was only very slowly reduced to about 2.9 percent last

year. So the budget deficit in a small country probably has more influence on the balance of payment than on prices and wages.

Representative RICHMOND. Coincidentally, our budget deficit in proportion to our GNP is about the same as your budget deficit and really our inflation is almost double yours. I'm trying to find out what we Americans can learn from the conduct of the Austrian Government.

Mr. SEIDEL. Yes. You see, we are in a position where we had a fairly high growth rate. It was higher than in other countries. That, of course, meant that demand for imported goods was fairly high and we ran a balance-of-payment deficit on current account which was 20 billion schillings on 2 percent of GNP last year. We won't have a balance-of-payment deficit this year for cyclical reasons because there will be little economic growth this year and that will dampen import demand.

Representative RICHMOND. Professor, on another subject, Austria is by far the leading country in the world in support of the arts. I understand that your government allocates 100 schillings per capita for supporting arts of all types. Is that correct? At least that's what the mayor of Vienna told me recently. So the Austrian Government, in other words, allocates 700 million schillings to the support of the arts, which would mean 150 million schillings goes to the city of Vienna for the maintenance of your opera company, your museums, and all the other great tourist attractions you have in Vienna. Are those figures correct? They were given me by the mayor of Vienna.

Mr. SEIDEL. Yes, it's approximately 700 million schillings.

Representative RICHMOND. And you are by far the leader in the world on government support of the arts?

Mr. SEIDEL. Yes.

Representative RICHMOND. Do you also have private support of the arts? Do private people in Austria also contribute to their museums and their symphonies and their various art forms?

Mr. SEIDEL. Not to a very much degree. It's mainly government supported institutions.

Representative RICHMOND. In other words, people pay taxes and then the government takes part of the taxes and supports the arts. Is that correct?

Mr. SEIDEL. Yes.

Representative RICHMOND. It has obviously been a great success and benefit to Austrians and it has created incredible amounts of tourism. It is something that we Americans ought to examine very carefully because certainly the city of Vienna is a great tourist attraction because of the art forms you have there, the museums, the state opera company, your symphony orchestra, and so on.

Mr. SEIDEL. I agree.

Representative RICHMOND. This is something we are trying to get across to the American Government. Thank you.

Representative REUSS. On just that point, I would tell Professor Seidel that Congressman Richmond is chairman of a new institution here called the Arts Caucus which is a group of Congressmen determined not to forget the fact that cultural matters are part of people's lives just as much as bread.

In that connection, isn't it a fact that in Austria, either through government subsidies or union contracts, people who live in small cities and the countryside are able, either without cost or at a very small fee, to take periodic trips to Vienna and other centers to see museums, art galleries, hear music and operas which, because of their nature, can't be put on in smaller communities?

Mr. SEIDEL. Well, there are such actions, but I don't think that they are so important. I would add that not only do we have a big opera and museums in Vienna, we also have the Salzburg Festival and in most small towns there are some sort of theater, as well. So, not all Austrians have to come to Vienna to participate in our cultural life.

Representative REUSS. Turning to the Joint Price and Wage Commission, you spoke of the fact that about 200 commodities are currently subject to price regulation. Without listing all 200, generally what kinds of commodities are subject to controls and what kinds are not subject to controls at present?

Mr. SEIDEL. Not subject to controls are import prices, and this is a question of debate because well over 50 percent of the manufactured goods which we consume are imported. They are very important items in the cost-of-living index. What we do include in the regulations are mostly prices for industrial goods produced at home, manufacturing goods, and goods which are important for the economy where there is some sort of price leadership. There are only a few services included in this procedure and there are no imported goods which are subject to these procedures.

Representative REUSS. Are there taxes on luxury imports?

Mr. SEIDEL. Yes. We have a value-added tax with three different rates. The highest rate is for so-called luxury goods, which is quite high.

Representative REUSS. What is that rate?

Mr. SEIDEL. Thirty percent, and the normal rate is 18 percent of the value added.

Representative REUSS. If you talked to an American economist about inflationary conditions in this country, he or she will say that inflationary expectations are, unfortunately, part of the process. For example, right now, the rate of inflation is about 10 percent, but the interest rate is still 20 percent. Well, that means that the real interest rate is 10 percent, which many of us regard as outrageously high.

My question is, does the fact that Austria has had for 23 years an incomes policy which is believed by many to moderate wage and price increases have an additional beneficial effect over and beyond that moderation of wage and price increases, in that it calms down inflationary expectations so they aren't as rabid as they otherwise would be?

Mr. SEIDEL. Yes, Mr. Chairman, we think that that is a very important element in our policy. We think that the price-wage process has some influence on expectations. And in that respect, as far as interest rates are concerned, up to 1975, we had practically stable nominal interest rates which didn't fluctuate at all. We think that interest rates primarily are a cost factor, increasing let's say the cost for houses, rents, and so on, and capital costs, and that interest rates only have a certain delay effect on demand and thereby act to mod-

erate inflation very slowly. So we think that the high interest rates which prevail in the Western countries magnify our inflationary problems. It doesn't help to solve them.

Representative REUSS. How are high interest rates in one large country, one located between the Pacific and the Atlantic Ocean, communicated to little Austria?

Mr. SEIDEL. Well, we maintain a constant relationship between the Austrian schilling and the German deutsche mark. Interest rates on money markets are the same in Austria as they are in Germany. Otherwise, there would be interest arbitrage between the two countries because banks are free to place their money wherever it gives the higher return. So practically, in order to keep the value of the Austrian schilling fixed to the deutsche mark, we use a monetary policy which results in interest rates which are similar to rates in Germany. So when interest rates in West Germany are influenced by interest rates in the United States, their link to the Austrian rates too are influenced.

Representative REUSS. What is the Austrian equivalent of the U.S. bank prime rate?

Mr. SEIDEL. Well, just now I would say 12.5 percent or 13 percent.

Representative REUSS. And that's up from how much over what period of time?

Mr. SEIDEL. Well, it used to be 8 percent.

Representative REUSS. Is there a feeling that higher interest rates within Austria that are necessary to contain domestic inflation are an unfortunate thing and that they make maintaining growth and employment more difficult?

Mr. SEIDEL. Yes. Allow me to put it in this way: we quite accept that the United States has to do something to fight inflation, that it's important for you to get more price stability. At the same time, we have to admit that the burden which your policy puts on the European countries is quite high, because it makes the dollar strong. It was easier for we European countries to overcome the first oil price shock because at that time the dollar was weak and oil was denominated in dollars. The second oil shock put more strain on the European economies, not only because of the rise in oil prices, but also because of the rise in the dollar against the European currencies. Now your high interest rates, according to our opinion, just add to the adjustment problems of the European countries.

Representative REUSS. Turning now to another subject which you touched on in your prepared statement. You had several things to say about income distribution. One was that you do not use your wage-price incomes policy as a method of changing the distribution of incomes. Do you use it as a method of preventing the deterioration of the distribution of incomes?

Mr. SEIDEL. As far as I understand it, social partnership means that we agree on keeping the share of capital and labor constant in national income. That doesn't mean there's not a lot of discussion of how fair the income distribution is and what other methods can be taken to change it. As a matter of fact, income distribution didn't change during the 1970's, neither the personal nor the functional distribution, if you allow for actions of the self-employed persons.

Representative REUSS. How do you keep your income distribution statistics? We do it in fifths of quintiles of the population here. Do you have something like ours?

Mr. SEIDEL. Yes. We have less reliable statistics than you have. Representative REUSS. It could hardly be less reliable.

Mr. SEIDEL. For instance, it's hard to get data on family incomes. We know the distribution of incomes for employees, but not for families.

Representative REUSS. You return to the subject of income distribution in the last of your prepared statement, as well, where you pointed out, as you have again just now, that interest rates which have been low and stable over a long period became high and volatile. You then go on to say that this and other factors leads to shifts in income distribution which seems to be hardly acceptable for some groups.

I take it that what happens in Austria, as in the rest of the world, is the following:

The families that borrow are, by and large, lower-middle-class families. They borrow particularly for their homes, for their consumer goods, their education and their health. On the other hand, those who lend tend to be in the upper income groups. Therefore, what happens is that the effect of high interest rates on the distribution of income in Austria would be distressing to lower-middle-class people. Is that a fair statement?

Mr. SEIDEL. Yes. Of course, the share of interest income will increase because of the higher rates. That means we will have a shift of income out of labor and income out of capital and that's a functional problem. Then we have a personal problem of who really benefits from high interest rates; certainly the upper middle class enjoy a larger benefit from high interest rates than do, let's say, lower income families.

Representative REUSS. So I take it there is concern in some circles lest the rather even sharing of income in Austrian society becomes distorted by a regime of high interest rates if it continues for a long time.

Mr. SEIDEL. Yes. The point I was making in the last part of my statement simply was that this system of negotiation and compromise on wages and price setting can absorb some shocks coming from outside. But, these shocks cannot be too great. We will have to reconsider the whole process of negotiations if there are important external shocks which we cannot avoid that will change the income distribution.

You see, we originally thought what we had was just a problem of distributing the national product between labor and business. That was the type of situation when we started with the incomes policy. So the price of interest rates, raw materials, and energy were more or less stable. We had opportunities to sit together and say, "Well that is the cake we have and we'll discuss the distribution should it change very much. The price setting should be fair." While I wouldn't say that all negotiators were gentlemen, we did agree on certain relationships between profits and wages. We did not want to get into a price-wage spiral because we could not agree upon the

distribution of income. That continuing type of reasoning will not hold if external shocks are very great, and that's our problem now.

Representative REUSS. As I see your social contract process, there could be trouble in paradise if high interest rates continue, because unions would say, "Look, we have to pay higher interest rates and people in the upper income groups are, of course, getting the benefit of those higher interest rates. Therefore, we want higher wages." But if you say yes to higher wages, you have started to destroy the equilibrium by which the social contract was erected in the first place. Is that not so?

Mr. SEIDEL. Yes, sir, I think that is part of this line of argument. Another point is the terms of trade in our foreign trade have deteriorated very much in the last year. That means that real income is reduced. So we have a second factor. On top of that, our increase in productivity is less than it used to be. Import prices rising more than export prices alone reduced national income by 2 percent. That means that labor will probably have a decrease in real income and real wages this year. And this is not very easy to accept or to explain. In the beginning of the 1970's we had a rule saying that real wages should increase at least 3 percent a year, and in fact it did increase more than 3 percent generally. Now the Austrian workers are willing to accept a similar increase in the minimum wage, but it's hard to convince them that in certain periods reductions in real wages will be necessary.

Representative REUSS. Congressman Richmond.

Representative RICHMOND. Thank you, Mr. Chairman.

Professor Seidel, let's discuss Austria's incredible success in this last decade. I think you have been the most successful country in Europe during the 1970's in attaining high growth rates, right?

Mr. SEIDEL. Yes.

Representative RICHMOND. What has your commission done to modernize or rejuvenate industries? What are some of your explanations for the incredible success you have had in Austrian business this last 10 years? Is it because of Government controls? Is it because labor and Government and industry work together? What are you doing that we're not doing?

Mr. SEIDEL. I think the workers in Austria at the plant level are really interested in what happens to their firms and they are willing to cooperate in, let's say, discussing problems of labor relations. That's part of the explanation.

Representative RICHMOND. In other words, you have what the Japanese call productivity circles? The Japanese invented that phrase where little groups of workers in each factory get together and discuss how they can improve their own operation.

Mr. SEIDEL. In big firms we have labor representatives on boards; not in the management of the firm, but on the board of the companies. One reason for this cooperation was that our society was initially involved in a catching up process. The level of income in Austria was below that of much of the rest of the European countries although now it's a level above the others. It is always a little easier to catch up than to lead. To answer your earlier question, we have quite generous tax deductions for firms who invest to modernize or rejuvenate their plant.

Representative RICHMOND. How about your depreciation policy? Can any firm write off their entire capital investment in 1 year?

Mr. SEIDEL. Well, practically, yes.

Representative RICHMOND. I think we are the only modern industrialized country in the world which has depreciation schedules that ignore the impact of inflation.

Mr. SEIDEL. For some years now, 90 percent of the expenditures for investment in equipment can be written off in the first year.

Second, I think European integration helped us to rearrange or reorient our industry. You know, it was only in 1972 that we concluded a Free Trade Agreement with the European community. For reasons of neutrality, we were not able to join the Common Market in Europe, although our main trading partners were all members of the Common Market. So it was only in 1972 that we were able to get a free trade arrangement with the European community. Of course, competition was increased in the domestic market, but at the same time, we got free access to the market of Western Europe which was quite important for us.

Representative RICHMOND. One of our big problems in this country is teenage unemployment.

Mr. SEIDEL. We don't have teenage unemployment.

Representative RICHMOND. As an example, in my district which is predominantly black and Hispanic, 50 percent of my teenagers are unemployed. Now what do you do to make sure that your teenagers finish school? Do they go to vocational schools or what?

Mr. SEIDEL. Well, a large part of the Austria people go to a vocational school.

Representative RICHMOND. At the high school level, a vocational high school?

Mr. SEIDEL. No. Most young people want to become skilled workers and they have to serve some years of apprenticeship. It is not very difficult for a young man or woman to get such training or an apprenticeship. So, although we have a lot of young people coming into the labor market because birth rates were very high early in this generation, we don't have a problem with unemployment among youths. As a practical matter, we do not have a youth unemployment problem.

Representative RICHMOND. What you are really saying is that companies themselves have training programs for young people. When a young person leaves high school, he or she goes into a training program in a company. I am sure that program is subsidized taxwise, something else we ought to have in this country.

Mr. SEIDEL. Yes, we do have that. On the other hand, we might have some unemployment among those people who stay in high school and out of apprentice programs. But, as a rule and on the whole, our youngsters leave school at the age of 15 and it's very easy for them to find work—there are sufficient places for them for training purposes.

Representative RICHMOND. That training is, by and large, carried on by the companies themselves?

Mr. SEIDEL. Yes.

Representative RICHMOND. I'm sure their taxes are adjusted accordingly.

Mr. SEIDEL. Yes; small business is employing a lot of these youngsters for training purposes.

Representative RICHMOND. What do you do with your foreign workers? I know that about 10 percent of your labor force in the past has been made up of foreign workers; is that correct?

Mr. SEIDEL. That's a little too high now, but I think approximately 7 percent of the labor force are foreign workers.

Representative RICHMOND. Can the foreign workers become members of unions and eventually citizens of Austria or are they on temporary arrangements?

Mr. SEIDEL. That depends. I would say part of them stay in Austria and obtain Austrian citizenship, but a large number of foreign workers do not want to stay in Austria. They generally just want to make money. When they have enough saving, they go back to Yugoslavia, for instance, where most of our foreign workers come from, and perhaps start a small business. So quite a lot of these workers want to get back to their native countries—and, of course, we did reduce the number of foreign workers temporarily, which helps keep unemployment low. We have some room for maneuvering in this case, although one has to mention that foreign workers will take jobs which many Austrians do not want to have.

Representative RICHMOND. The lower jobs?

Mr. SEIDEL. Yes.

Representative RICHMOND. Very similar to our country where many Hispanics take the lower jobs.

Thank you, Mr. Chairman.

Representative REUSS. You discussed, Professor Seidel, Austrian incomes policy and cultural policy. There's one additional area I would like to touch on briefly, and that is industry policy. Does Austria have an industrialization policy? What is it concentrated on? That is to say, is it import substitution? Is it export oriented? And what are some of the means, if you have such a policy, used to carry it out?

Mr. SEIDEL. Well, I would start by saying that industrialization is a very important aim of all groups of Austrian society. Whenever the GNP share represented by manufacturing is found to be declining, there is some rumor of de-industrialization and generally a reaction to that rumor. There is more or less a consensus that Austria can only raise its standard of living if we will have a competitive and efficient manufacturing industry.

Now what are the problems of our manufacturing industries? If you take the structure or the commodity breakdown of our production, you will find that goods of the basic industries, like steel, paper, and aluminum, play a large role. They are too big, in fact. We have to shift our production from basic products to finished products. That's one problem.

The second problem is with the light industries—clothing and textiles. The growth there is larger than in many other commodities. We think we need a shift within our manufacturing industries into what we call skill-intensive and research-intensive lines of production.

We want less production from basic industries and more finished products and we want to produce more complicated finished products

than we do now as well. We have had some success in shifting some of our production to finished goods, but there's a lot still to be done. The government can help this desirable restructuring of the Austrian industry by extending cheap credits to firms who are willing to produce new things. Of course, we have had wide success in attracting multinational firms. And, Austria has a really efficient system of export promotion, extending export credits in order to sell products to less-developed countries which are not able to pay cash.

Representative REUSS. We have ranged widely over a series of subjects, including, most important to us, your incomes policy. You have done an outstanding job of educating this committee, Professor Seidel, for which we are very grateful. I'm struck throughout the questioning at the interdependence of the modern world. What we do here in our economy transmits itself to Austria and, of course, what you do is of direct interest to ourselves, as is evident from the fact that we asked you to come here this morning. Nothing but good will come from your visit.

I am most grateful to you, Mr. Ambassador, and you, Professor Seidel, for the considerable effort that you have made to be here. You contributed greatly to the deliberations of the Joint Economic Committee and I would appreciate your expressing our gratitude to your Chancellor for permitting you and encouraging you to come. He has done a further nice thing for Austrian-American friendship, and so, with many thanks to both of you, we will stand in adjournment.

[Whereupon, at 11:30 a.m., the committee adjourned, subject to the call of the Chair.]

