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1st Session } { No. 94-425

THE 1975 MIDYEAR REVIEW OF THE ECONOMY

REPORT

OF THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

TOGETHER WITH

SUPPLEMENTAL AND MINORITY VIEWS

OCTOBER 9 (legislative day, SEPTEMBER 11), 1975

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OCTOBER 9 (Legislative Day, SEPTEMBER 11), 1975.—Ordered to be printed with illustrations

Mr. HUMPHREY, from the Joint Economic Committee, submitted the following

REPORT

together with

SUPPLEMENTAL AND MINORITY VIEWS

[Pursuant to Sec. 5(b) of Public Law 304, 79th Cong.]

This Report is submitted in accordance with the continuing responsibility of the Joint Economic Committee to apprise the Congress of economic circumstances and make such recommendations as it deems advisable.

The Joint Economic Committee's Midyear Report is presented at a time when the United States stands at the crossroads of its national economic policy. In the last few months, the nascent economic recovery from the worst recession since the Great Depression has begun. This recovery, however vigorous it may appear to be in the last months of 1975, remains very tenuous. If it proceeds according to current forecasts, the Nation is faced with excessively high unemployment and unused productive capacity for the rest of this decade.

The Congress is confronted with the choice of accepting a sluggish recovery, with lower income, production, and employment, or acting decisively to produce a healthy, sustainable recovery which increases production, creates new jobs, increases income, and produces higher tax receipts. Some would accept the risk of a sluggish recovery out of fear that stimulative fiscal policies will increase the Federal deficit and intensify the threat of inflation.

It is important to remember that the currently high deficit we are now experiencing results not from excessive Federal Government spending, but from an enormous shortfall in revenues—an inevitable consequence of high unemployment, sluggish sales, lower income, and lower profits. The only effective way to return the Federal budget to balance is by putting the American economy back on a strong, sustained growth path. It is only then that higher tax revenues resulting from higher personal incomes and higher profits will offset necessary government expenditures for providing public goods and services.

The Congress and the President must work together to eliminate any unnecessary or wasteful government spending which contributes to larger deficits. But we would be shortsighted indeed if the short-run goal of reducing the Federal deficit were allowed to thwart our longer run and more vital goal of a healthy economy at full employment. A tax reduction over and above the continuation of the 1975 tax cuts and a substantial emergency jobs program to get the unemployed back to work are the means for achieving economic growth and a balanced budget. If Congress fails to enact a program to restore high employment and to utilize our productive capacity, it will have abdicated its responsibility to the American people.

It is within this context that the Joint Economic Committee presents its Midyear Economic Report.

I. INTRODUCTION AND SUMMARY

Although it now seems clear that the U.S. economy has passed the turning point of its most severe recession since the 1930s, the present outlook is far from satisfactory. Many urgent questions of economic policy require prompt resolution. The economy stands at a crossroads. Policy decisions to be made in the next few months will determine whether it proceeds steadily along the road to full recovery and high employment or whether it is deflected onto a path of stagnation, inflation, and a possible new recession.

After falling for five consecutive quarters, real output stabilized in the second quarter and will probably rise fairly strongly in the second half of this year. If current policies are followed, however, there is little prospect that this strong recovery path will be sustained in 1976. Typical forecasts indicate a sharp reduction in the rate of output growth as 1976 proceeds, and there are ominous signs on the horizon that a new recession could be in the making for late next year or early in 1977. Swift and decisive actions are required both to sustain the recovery through 1976 and to cope with continuing inflationary pressures. If these policy needs are neglected, 1976—our bicentennial year—may be a year in which output grows very little, the unemployment rate remains above 8 percent, and excessive price increases plant the seeds of a new recession.

The specific foundations for our concern and our sense of urgency include the following:

> Even with a strong recovery, unemployment will remain far above normal levels for several years. Already approximately 1.5 million persons have been unemployed six months or longer. At present there is no program to preserve the skills, work habits, and personal dignity of this growing number of individuals.
>
> Exceptions of a strong economy in the second half of this year are based on the stimulus provided by last spring's tax rebate and on the expected strength of the inventory swing. Both of these are temporary factors.
>
> Forecasts of even a moderately strong economy in 1976 assume extension of the 1975 tax reductions. This action has not yet been taken.
>
> These same forecasts also assume a monetary policy which is more expansive than the announced intentions of the Federal Reserve.
>
> Recent progress in reducing inflation now threatens to be reversed. Fuel prices have been increasing steadily and, if controls over domestic petroleum prices are not reimposed, the increase will accelerate. Danger also exists of a new round of consumer food price increases. The reductions in consumer purchasing power resulting from food and fuel price increases and the automatic restrictive effect which inflation had on the Federal budget produced a recession in 1974. They could do so again in 1976. A new recession, coming at a time when un-

adopted. It should be of a size sufficient to employ one-half of the unemployed in excess of a 4½ percent unemployment rate, that is, an estimated 1.6 million persons in calendar 1976 and about 1.3 million in 1977. If activated in January, the fiscal year 1976 cost would be slightly over $3 billion, after allowing for offsetting savings on tax receipts and income support programs.[5] [6]

Taxes.—The major provisions of the Tax Reduction Act of 1975 should be extended through 1976. An additional $8 to $10 billion tax reduction for calendar 1976 should be enacted, preferably in the form of an "earned income" credit on both employer and employee income tax returns, which would offset some of the burden of the social security tax. The fiscal year 1976 impact of this additional tax cut would be $4 to $5 billion. This tax change would be accomplished through the income tax system and would in no way affect social security trust fund revenues.[7]

Aid to State and Local Governments.—Pending legislation which provides for antirecession grants to State and local governments and for emergency public works should be enacted.

The Budget.—Higher than expected rates of inflation are having an unintended restrictive effect on the budget. The tax and spending programs recommended above are needed simply to restore to the budget the degree of economic stimulus which was intended at the time Congress enacted the First Concurrent Resolution on the Budget. With our recommendations, outlays in fiscal 1976 are estmiated at approximately $370 billion and receipts in the neighborhood of $300 billion, leaving a deficit of roughly $70 billion. This deficit slightly exceeds the $68.8 billion target set in the First Concurrent Resolution, but the gains promised against both unemployment and inflation thoroughly justify this small increase in the deficit.

Monetary Policy.—Over the months ahead, monetary policy should be designed to hold interest rates below the levels which will interrupt the economic recovery by diverting funds from housing and other crucial sectors. It appears likely that this will require growth of the monetary aggregates somewhat in excess of the range proposed by the Federal Reserve authorities.

Price-Incomes Policy.—An active voluntary price-incomes policy should be initiated and maintained through the direct leadership of the President himself and of his highest level economic policy advisers. This policy should include voluntarily negotiated price restraint on the part of major companies, voluntary cooperation in holding major wage settlements to trend productivity gains plus a partial cost-of-living adjustment, and tax reductions sufficient to restore purchasing power losses not covered by wage settlements.

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[5] Senator Proxmire states: "Rather than this emergency jobs program, I favor the government as employer of last resort provision which is described in my footnote on page 39."

[6] See Supplemental Views of Senator Bentsen.

[7] See Supplemental Views of Representative Reuss.

II. THE ECONOMIC OUTLOOK

Most indicators of economic activity signaled an upturn at the beginning of the third quarter. Industrial production increased in May after declining for 10 months. Several developments in the second quarter set the stage for significant growth in sales and output in the last half of the year. First, inventory liquidation proceeded much more rapidly than had been anticipated in the first half of 1975, necessitating some increases in production to meet current demand. Second, the tax rebates paid out in the second quarter have provided some temporary stimulus to retail sales and will probably continue to have some impact through the end of this year. Even so, the growth rates which now appear most likely for the second half are below the historical pattern which has followed the trough of past recessions.

THE CURRENT OUTLOOK

Given recent impetus to production, real output can be expected to grow as much as 7 to 9 percent, at an annual rate, during the last half of 1975. This rate of growth, while below historical post-recession experience in the United States, would nonetheless be encouraging if it could be sustained through 1976 and 1977. However, typical forecasts indicate growth rates of only 4 to 6 percent during 1976, and a further slowdown in the rate of growth in early 1977. These forecasts generally assume extension of the 1975 tax cut and the maintenance of some degree of control over oil prices.

These projected rates of growth will reduce only gradually the extremely high rates of unemployment. Given the recent drop in unemployment to 8.4 percent of the labor force, much more improvement is unlikely through the end of 1975. Since the economy must normally grow at a 4 percent rate simply to maintain the current unemployment rate, and since every percentage point reduction in unemployment requires 3 additional percentage points of real growth, expected output growth rates of only 4 to 6 percent in 1976 and 1977 imply only very limited reduction in unemployment in the next two years.

In its Annual Report, the Joint Economic Committee established output goals for the end of 1975 and the end of 1976 and the respective unemployment rates which would accompany those output targets. Current forecasts indicate that the economy is falling far short of these targets. Even assuming that the 1975 tax cuts are extended, that growth of the money supply is at the upper end of the Federal Reserve's target range, and that there is no sudden decontrol of oil prices, it appears that the economy will fall some 5 percent short of the Committee's output target for the end of next year and that the number of persons at work will be more than one million below the suggested employment target. Table 1 compares the Committee's targets with the real gross national product (GNP) and unemployment trends contained in typical recent forecasts.

The Committee emphasized in its annual report that its output and unemployment targets were ambitious by historical standards. But the U.S. economy faces a longer and more severe period of unused productive resources—both labor and capital—than at any other time since the Great Depression. If our goals are not met, the United States will not approach its potential output and employment by even the end of this decade. As illustrated in Chart I, even assuming quite rapid output growth later in this decade, a projection which takes as its starting point the current outlook for 1976 and 1977 would imply GNP still 7 percent below its potential in 1980 and an unemployment rate of above 6 percent in that year. The line labeled "Preferred Growth Path" in Chart I illustrates the better performance which can be achieved if the Committee's targets are met. It is already clear that our growth and unemployment targets for the end of 1975 are most unlikely to be met. Achieving the 1976 and 1977 targets is still possible, but it will require quick and decisive policy action.

TABLE 1.—OUTPUT TARGETS AND CURRENT OUTLOOK

	JEC targets		Current outlook	
	GNP (billions of 1958 dollars)	Unemployment rate [1] (percent)	GNP (billions of 1958 dollars)	Unemployment rate (percent)
1975: IV	825	7.9	810	8.4
1976: IV	895	6.6	850	7.9
1977: IV	960	5.4	890	7.8

[1] Trend unemployment rate based on the assumption, generally known as Okun's law, that each 3-percent shortfall of GNP below its potential increases the unemployment rate by 1-percentage point.

Source: Joint Economic Committee.

employment is already at almost unprecedented levels, would bring with it extremely serious social and economic consequences.

The importance of firm action to avert these threats to our economic health is all the greater because of weakness elsewhere in the world economy. Other major nations have also experienced severe recessions, with unemployment rates exceeding anything in post World War II experience. Evidence of an upturn in the major European countries has yet to emerge. Revival of the world economy is thus heavily dependent on the strength of the U.S. recovery. The Managing Director of the International Monetary Fund (IMF) stressed the international nature of the recession in his recent address to the IMF annual meeting in which he stated:

> It is reasonable—indeed, necessary—to ask these three countries (the United States, Germany, and Japan) to conduct their demand policies so as to take particular account of the international recession.

As a responsible member of the world community as well as from a responsibility to its own citizens, the United States must act to keep its economy on a strong and steady growth path not just for the rest of 1975 but throughout 1976 and beyond. The specific policy actions which are needed at this time are summarized below and are discussed in greater detail in the remainder of this report.

These actions are not designed to promote faster growth of employment at the expense of more inflation. Nor are they designed to restrain prices by keeping unemployment high. Progress toward price stability and toward full employment are not alternatives. Each is essential to the other, and our recommendations are designed to promote both.

The combined effect of these recommendations by the second half of 1976 would be to increase employment by an estimated 1 to 1½ million persons while at the same time lowering the inflation rate by roughly 0.6 of a percentage point, as compared to the situation which might exist if these recommendations are ignored. Even more important, if our recommendations are followed, unemployment should continue to fall steadily. If our recommendations are ignored, it is our best judgment that unemployment will remain near its present levels or even begin rising again at the end of next year, because output will not be growing fast enough to keep pace with labor force growth and productivity gains.

Summary of Recommendations [1] [2] [3] [4]

Job Creation.—A new emerging job creation program which will put the unemployed to work on special temporary projects should be

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[1] Representative Long states: "While I concur with the recommendations in this Report, I am concerned that the combination of the jobs program and the tax cut in addition to extending the Tax Reduction Act of 1975 will be inflationary for the economy. This takes on an added significance in view of anticipated OPEC oil price increases, which will supply additional inflationary pressures to the economy."

[2] Representative Hamilton states: "While I favor most of the Committee's recomemndations contained in this Report, I will reserve judgment on the recommendation for additional $8 to $10 billion tax reduction for 1976 and on antirecession grants to State and local governments."

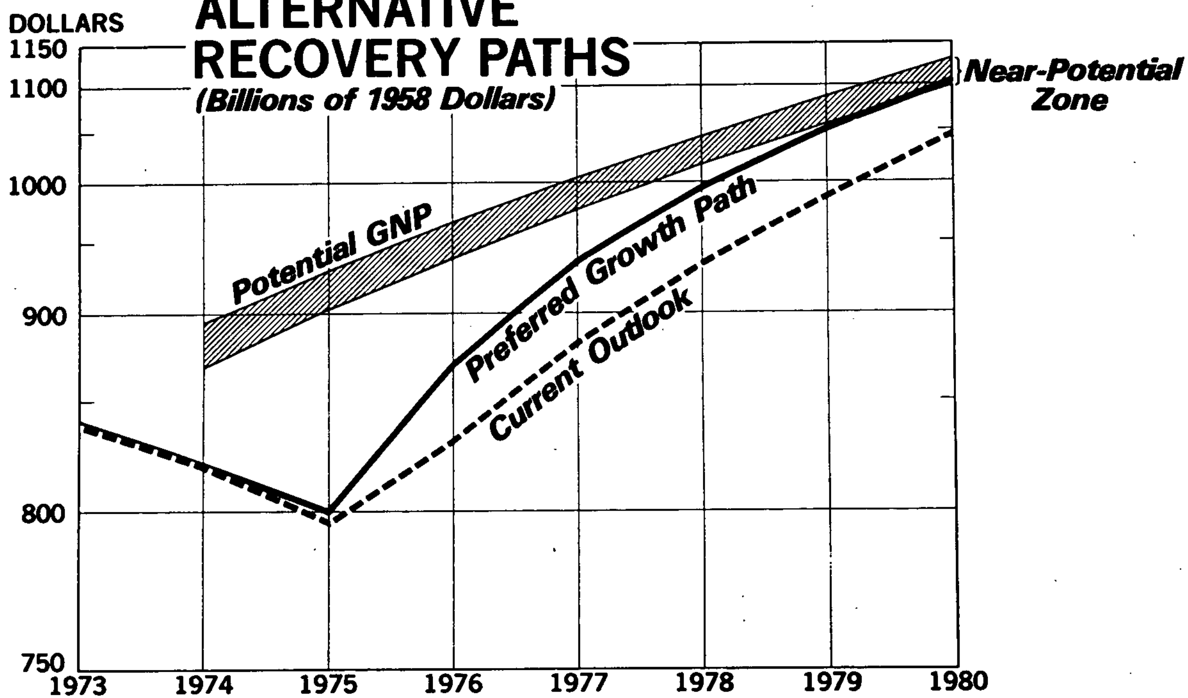
[3] See Supplemental Views of Vice Chairman Patman.

[4] See Supplemental Views of Senator Proxmire.

Chart I

ALTERNATIVE RECOVERY PATHS

(Billions of 1958 Dollars)



Sources: Department of Commerce and the Joint Economic Committee.

A look at the expected performance of the various components of total output explains the current outlook for a sluggish recovery. For illustrative purposes, Table 2 summarizes one recent econometric forecast. It can be seen that the only sectors which are expected to show strong growth in 1976 are consumer durables, where the gain is heavily concentrated in automobiles, and residential construction. It is noteworthy that in both cases the expected increases in 1976 will barely be sufficient to restore these sectors to the levels of mid-1974. In effect the expected growth of consumer purchases of automobiles and housing in 1976 largely represents a replacement of existing stock which was postponed during 1974 and 1975 and may not foreshadow a sustained period of growth in these bellweather sectors.

In addition, the expected growth in real GNP is quite a bit stronger than the rate of growth in final sales.[1] The difference between the two is explained by the inventory cycle. As Table 2 illustrates, total GNP will drop about 3.6 percent this year. However, much of this drop is in inventories. Final sales will drop only 1.5 percent. Conversely, in 1976 businesses will be rebuilding a sharply reduced level of inventories and this will cause total real GNP to show a growth of perhaps 5 percent. Final sales, however, may grow only about 2.5 percent.

The swing in business inventories is a temporary phenomenon. It is final sales which must sustain the growth in GNP. The inventory cycle has a one-time, short-lived impact on the economy in each business cycle. Once inventories have been rebuilt to a reasonable level, consumer demand, business investment, and government expenditures must provide the stimulus to growth. As Table 2 suggests, business fixed investment, personal consumption other than durables, and government expenditures could grow by less than 2.5 percent in 1976.

TABLE 2.—ILLUSTRATIVE FORECAST: GROSS NATIONAL PRODUCT AND SELECTED COMPONENTS [1]

[Percent change from previous year]

	1975	1976
GNP total	−3.6	4.8
Final sales	−1.5	2.5
Personal consumption	0	2.9
Durable goods	−4.2	7.1
Nondurable goods	.5	1.3
Services	1.6	2.8
Nonresidential fixed investment	−13.6	2.3
Residential construction	−23.2	25.6
Government purchase of goods and services	2.3	2.0

[1] Simulation using Wharton Econometric model. Assumes fiscal 1976 unified Federal outlays of $367,000,000,000, extension through 1976 of the 1975 tax reductions, only moderate rise in energy prices, money supply growth of 8 percent during 1976.

Source: Joint Economic Committee.

THREATS TO THE RECOVERY

The current outlook for production and unemployment, summarized in Tables 1 and 2, while by no means desirable, does not represent the

[1] Final sales includes all the components of GNP except the change in business inventories.

most pessimistic forecast. It assumes certain policy actions not yet taken, including extension of the 1975 tax reductions and maintenance of some degree of control over domestic oil prices. A number of factors, some of which have become quite probable, could abort the projected recovery. Among the most serious would be failure to control the price of "old" domestic oil with resultant rapid increases in industrial and personal energy costs. In fact, recent events suggest that gasoline and fuel oil prices will continue to rise somewhat even with controls as the prices of imported and "new" domestic oil rise.

The combination of energy and food price increases threatens to repeat 1973–74 experience, which resulted in large income transfers to the domestic agriculture and energy sectors and to foreign energy producers. The resulting erosion in consumer purchasing power was a major cause of the 1974 recessionary spiral, and the present situation contains disturbing overtones of a similar progression of events.

The current outlook projections assume that the 1975 tax cuts, which expire at the end of this year, will be extended. Failure to continue these tax cuts would increase tax withholding on January 1, 1976, and would reduce consumer purchasing power some $12 to $13 billion during 1976. The forecasts further assume that Federal expenditures for fiscal 1976 are at the level recommended in the First Concurrent Resolution on the Budget rather than at the lower level recommended by the President.

The forecasts also assume a rate of monetary growth in excess of the range proposed by the Federal Reserve; in typical forecasts for a moderate recovery in 1975 and 1976, the money supply (demand deposits and currency) is assumed to grow 8 percent or more through the end of 1976. The impact of alternative monetary policies on the recovery is discussed in more detail in Chapter V.

A significant change in any of these key assumptions—that is, sharply higher food and fuel prices, failure to extend the 1975 tax cuts, more restrictive monetary or fiscal policy—could easily throw an already modest recovery off the track.

The Committee has had its staff analyze the probable impact of a set of policies which includes sudden decontrol of oil prices, monetary growth near the center of the Federal Reserve's announced target range, and an expiration of the Tax Reduction Act of 1975 as scheduled. The estimated impact of these policies would be real economic growth in 1976 of only 2.0 percent; that is, growth so low that unemployment would again begin to rise. Even this is not a "worst case" scenario.

The policy recommendations presented in the remainder of this Report are designed first, to avert the threat of an aborted recovery due to any of the above factors and second, to put the economy on a strong growth path with improved prospects for meeting the 1976 and 1977 output and employment targets we have advocated and to do so while at the same time lowering the rate of inflation.

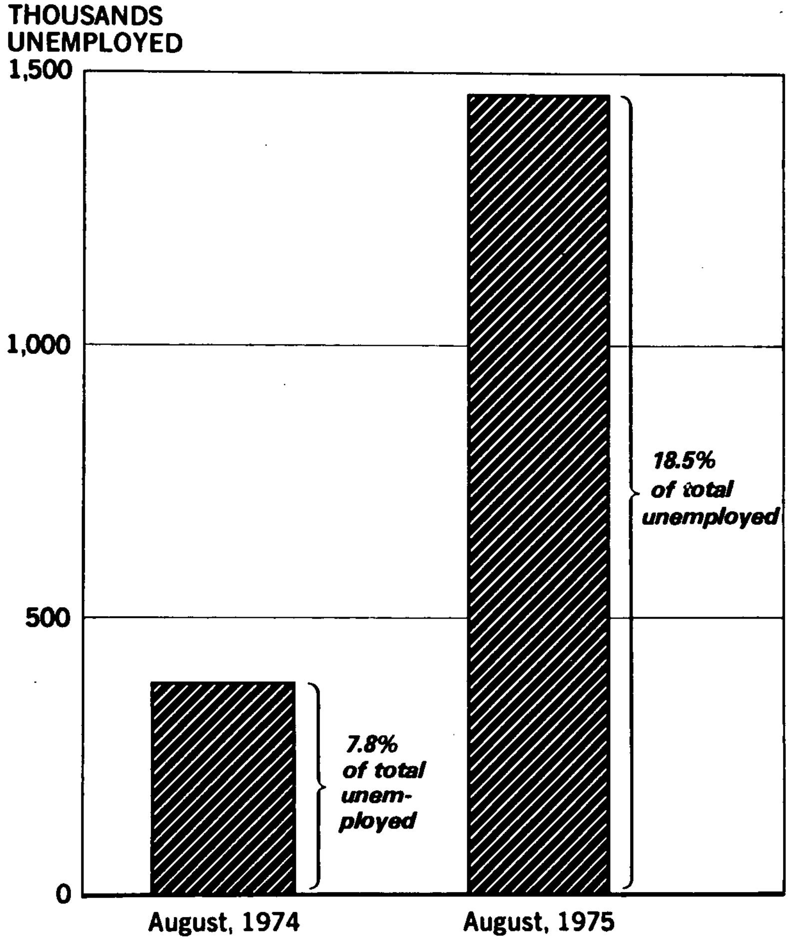
III. EMPLOYMENT POLICY

The expected growth path of the economy in the next two years could still leave unemployment as high as 7.5 to 8 percent by the end of 1976. If output increases between 4 and 5 percent in 1977, there will be only a very limited further reduction in the unemployment rate during 1977. Continued levels of high aggregate unemployment not only carry serious implications for several labor force groups but will do serious long-run damage to the efficient working of the economy.

The duration of unemployment has risen sharply in the past year and will continue to increase further. Almost 3 million of the 8 million workers unemployed in August 1975 had been out of work for at least 15 weeks. Thirty-six percent of the jobless had been unemployed for 15 weeks or more, compared to 19 percent a year ago. As shown in Chart 2 the number of workers unemployed more than six months has also increased sharply in the past year, rising from 7.8 percent of total unemployed in August 1974 to 18.5 percent in August 1975. The actual number of persons unemployed six months or more (1.5 million in August) is nearly four times the level of one year earlier.

The United States is faced with a minimum of three or four years of unemployment far in excess of that which is due to frictional or structural reasons, years during which many unemployed, experienced workers will lose valuable skills. Many younger workers entering the labor force for their first full-time job will lose the opportunity to gain both skills and work experience. The first three or four years of full-time employment have traditionally been used in the United States to experiment with different kinds of jobs and to adjust to the demands of the labor market. Because of the expected high unemployment rates of the next several years, many young people may reach age 24 or 25 before they even hold a full-time job.

Chart II
LONG TERM UNEMPLOYED
(unemployed 27 weeks or more, seasonally adjusted data)



Source: Bureau of Labor Statistics, Department of Labor

The employment policy implicitly being followed by the Administration is to extend unemployment compensation benefits as long as necessary to cushion the individual financial hardship of high unemployment and to allow the private economy to return very gradually to higher levels of employment. Only a limited number of public employment jobs, 300,000 in fiscal 1976, is to be funded under the Comprehensive Employment and Training Act (CETA).

when the economy appears to be reviving. As stated in earlier chapters of this report, this and other policy changes are needed to keep the recovery from faltering. Continuing inflation is having the effects both of eroding consumer purchasing power and of automatically making the Federal budget more restrictive. Individuals are being pushed into higher tax rate brackets purely as a result of inflation. The tax cut recommended may be thought of as a necessary compensation for inflation. Unless this compensatory tax action is taken, the United States may find itself in the grips of a new recession in late 1976 or in 1977.

Primary reliance on unemployment compensation is an expensive and inefficient way to deal with high unemployment. First, the costs of unemployment insurance benefits are running close to $20 billion annually; in addition food stamp and Aid to Families with Dependent Children (AFDC) costs are substantially higher than they would be at 4 or 4.5 percent unemployment. The Federal Government in effect is substituting welfare for an employment strategy. Furthermore, many of the unemployed—especially those with little or no work experience—are not covered by unemployment insurance.

A second reason why exclusive reliance on unemployment compensation is an inefficient way to combat high unemployment is that there are a great number of unmet needs in our cities and rural areas—neglected public buildings, inadequate transportation, underdeveloped parklands, inadequate water and sewer facilities. The opportunity to put the unemployed to work meeting these needs should be seized.

Third, by simply paying the unemployed their weekly unemployment insurance benefits, we are doing them a great disservice. While unemployment compensation can be extended for a considerable period, the loss of skills and work experience which accompanies prolonged unemployment is a tragic waste of our productive resources.

Given the high rates of unemployment the country faces for the next three or four years, a broad antirecession employment policy should be structured to maintain job skills and to complete relatively short-term projects in cities and rural areas. In the past, Congress has pursued an antirecession employment policy of simply expanding existing job training programs in addition to extending unemployment compensation.

This past approach has several disadvantages. First, it thwarts the original intent of jobs training legislation, which was to provide jobs and training to those who because of poor education or other handicaps would be unable to find jobs even in a period of high employment. After training, these structurally unemployed are sometimes moved into permanent or semipermanent Federal, State or local government jobs. Using these existing CETA programs for a large-scale antirecession employment effort will divert funds and program resources from the structurally unemployed and their particular problems. Some State and local administrators feel that this has already happened by the extension of Titles II and VI of CETA to create 300,000 public service jobs.

Second, large expansion of existing programs would strain the capacity of State and local governments to deal both physically and administratively with a large influx of temporary workers.

Finally the existing program creates expectations of permanent government employment among those hired for clearly antirecession, countercyclical purposes. Since some CETA jobs do lead to regular government employment, and since many CETA employees are placed in permanent job slots which involve a continuing governmental responsibility, both employer and employee come to expect that public service jobs will continue indefinitely.

An emergency employment program should be adopted which is targeted on those unemployed who would normally be able to find jobs in an economy operating near capacity.

The antirecession jobs program should be clearly temporary in nature. The jobs created under this program should be in special projects of one or, at most, two years' duration. The projects should have a highly useful and identifiable output. This emergency program should be in addition to the existing CETA programs, which will then be left free to deal with the structural problems—poor skills, geographic immobility or discrimination—for which they were designed. The antirecession jobs program should employ at least one-half of the unemployed in excess of 4.5 percent unemployment.[1, 2]

Structure of Emergency Jobs Program

In order to make clear the type of program which is needed and to expedite consideration and adoption, a fairly detailed description of a possible program is presented below.

Work projects would be proposed by State and local or Federal Government units, by nonprofit organizations, and (under specified conditions) by private businesses. A special Federal administrative board would be established to make final determination of which projects to fund and to provide guidance to the Labor Department in administration of the program. The work projects would be activities which would not otherwise be undertaken and which could be completed in less than two years. Funds would be allocated in accordance with the geographic distribution of unemployment.

There would be a clear understanding from the beginning that employment would terminate with the completion of the project. No individual would be employed under this program for more than two years. Financial and other incentives would be provided to encourage individuals to find regular private or public employment whenever jobs became available.

The administrative board would have four full-time members, appointed by the President and confirmed by Congress. They would be persons whose past experience demonstrates both a dedication to full employment and a familiarity with the design and execution of labor market policies. The Secretary of Labor would also be a board member. While the board would have final say on which projects to fund, to the extent reasonably possible, it would concur in recommendations from the local level.

Local or State governments, nonprofit organizations, Federal agencies, and private businesses could apply for project funds. Private businesses would, of course, be expected to undertake nonprofit projects. The projects would be of limited duration and would provide socially valuable goods or services to the community. For example, these

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[1] Chairman Humphrey states: "I will introduce legislation immediately to carry out this recommendation. This jobs program is not only an emergency response to the present situation, it can also be the first step in a longer term effort to guarantee jobs for all Americans. The concept of a job guarantee is embodied in the Equal Opportunity and Full Employment Act of 1975 which I have introduced in the Senate. I plan to introduce a revised version of this bill shortly and to do all I can to secure its early enactment."

[2] Senator Proxmire states: "Rather than the program described here, I favor a government as employer of last resort program with the Government providing jobs to all laid-off workers with compensation at the unemployment compensation level plus job-related expenses. I also favor employing new job seekers at the minimum wage. The cost of such a program, while it would be difficult to determine, would cost only marginally more than the costs of a good unemployment compensation program, but it would provide an opportunity to work for all of the nearly 8 million unemployed."

projects might include restoration of public buildings; rehabilitation of housing occupied by low-income or elderly persons; small-scale improvements in transportation, such as construction of bikeways and improvements of rural roads and bridges; improvements of parklands and public spaces in urban areas; and work on sewer and water facilities. In most cases, these projects would be completed in one year and could be operational in a short period of time, greatly enhancing the program's value as a countercyclical measure.

Scope and Costs.—To adequately deal with the expected unemployment problems of the next three or four years, the program should employ one-half of the unemployed above 4½ percent unemployment. Based on current forecasts, in calendar year 1976 this would mean about 1.6 million jobs, in calendar 1977 about 1.3 million, and in calendar 1978, assuming a continuing economic recovery, a much smaller number.

The distribution of funds should be based on area unemployment rates, as is currently done under CETA. However, once a particular project is approved, its funding should not be interrupted regardless of movements in local unemployment rates. Flexibility would be preserved by the relatively short duration of each project—preferably one year—although some projects could be extended to two years.

The wages paid under this program would be equivalent to the average local wage for similar work, up to a maximum of perhaps $3.50 an hour. The annual costs per person employed, including about 15 percent for overhead and equipment costs, would be about $7,500 to $8,300. Although 15 percent overhead may seem somewhat high, one of the major shortcomings of past employment programs is that they have literally failed to allocate workers any tools to work with.

The per-employee cost estimates above represent gross rather than net costs. An average of $2,600 of this per-employee cost would be offset by savings in the unemployment insurance program. In addition, tax receipts would be increased and transfer program costs—AFDC and food stamps—would be reduced.[3] Estimated net cost per-employee after allowing for these offsetting savings would be about $3,800 annually. These estimates do not include the multiplier effects on consumption and output which would result from employment increases. Taking these multiplier effects into account would reduce per-employee costs even further.

Assuming that the program were fully operational on January 1, 1976,—that is, halfway through the fiscal year—the fiscal 1976 costs are estimated at slightly more than $3 billion. Full-year costs for the succeeding 12 months would be about $5.5 billion.

A number of studies, including one issued recently by the Congressional Budget Office, have concluded that direct creation of jobs is the most efficient form of fiscal stimulus which the Federal Government can use in a slack economy. An antirecession jobs program, according to these studies, reduces the level of unemployment more sharply per dollar of expenditure than any other change in fiscal policy.

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3 Exact savings on AFDC and food stamps are difficult to estimate, but the Agriculture Department has recently estimated that the number of participants in the food stamp program under today's conditions of extremely high unemployment is roughly twice what it would be under more normal conditions.

Without an innovative and substantial (in number of jobs) program similar to the one described above, the United States will suffer extremely high rates of unemployment until the end of this decade. Aside from the loss in income, purchasing power, and human dignity, the failure to enact such a program would permanently erode the productive capacity of our labor force.

IV. FISCAL POLICY

Two important fiscal policy decisions face Congress at this time. The first of these decisions relates to the Tax Reduction Act of 1975. This Act expires on the 31st of December, and Congress must decide whether to allow it to expire or to extend it into 1976. At the present time the Administration has made no recommendations with respect to extension of the Tax Reduction Act, saying that this decision could be postponed until the end of the year. The First Concurrent Resolution on the Budget assumes these tax cuts are extended.

The second major decision Congress must shortly make is whether to amend the First Concurrent Resolution in other respects and, if so, by what amounts, and whether these changes should be on the tax or the spending side.

Energy Policy and the Budget

In considering tax and spending actions for the remainder of the fiscal year, energy policy must be explicitly considered. As this Report is written, price controls on domestic petroleum have been allowed to expire, but legislation providing for their temporary reimposition has been passed in both Houses. The recent pricing decisions of the Organization of Petroleum Exporting Countries (OPEC) will add further to energy prices. The analysis and recommendations in this Report assume some form of control over domestic petroleum prices and no further large OPEC price increases.

Actual developments which departed significantly from these assumptions, such as the failure to control the price of domestically produced petroeum, would have a significant impact on the economy. Any oil policy which allows a large price increase would shift purchasing power from consumers to petroleum companies. While these funds might be reinvested over a period of time, the immediate impact on the economy would be negative. To the extent that price increase come from foreign sources and cause funds to be shifted out of this country, there is no assurance even in the long run that increased investment expenditures would offset the loss in consumer purchasing power.

Although the Government's energy policies have not been fully decided at the present time, there are some statements which can be made with a reasonable amount of assurance about energy prices for the near future. First, energy prices have gone up substantially in the past few months. Since the beginning of this year, the fuels component of the Consumer Price Index has risen at a 16 percent annual rate and the Wholesale Price Index for petroleum products at an 18 percent rate. Furthermore, the energy-producing companies have had substantial cost increases which they have not yet translated into product price increases. This means that some fuel price increases during the remainder of 1975 must be expected.

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If price controls are not maintained, large price increases must be expected over the next six to nine months as domestic prices rise to the world level. Removal of import fees of $2 per barrel will by no means fully offset these increases. At September 1975 world price levels, decontrol, even with removal of import fees, would cost U.S. consumers approximately $11.5 billion during 1976. However, if world oil prices rise by $1.00 per barrel, as recent OPEC discussions indicate will happen, the consumer cost of decontrol will rise to roughly $20 billion if import fees are removed, or $35 billion if they are not. A $1.50 world price increase, coupled with decontrol, would impose a consumer cost of about $24 billion (or $39 billion if import fees are not removed). World prices will continue for some time to be subject to sudden large changes. The absence of any controls over the price of domestically produced petroleum would make the stability of the U.S. economy extremely vulnerable to these uncertain world price movements.

Each energy policy suggested by the Administration this year has been accompanied by the recommendation that fiscal policy actions be taken to offset any loss in consumer purchasing power that results. In testimony before this Committee on July 23, the Chairman of the Council of Economic Advisers stated:

> The President's energy program specifies a full rebate to consumers of the induced loss in purchasing power from the energy price increase. It would eliminate the loss in purchasing power and, at the risk of oversimplifying expectational and other factors, certainly dampen if not completely short-circuit any wage-price spiral pressures.

However, while the Administration has been resolute in its support for decontrolling the price of oil, the accompanying fiscal policy offsets have been discussed only vaguely. There is substantial risk that if decontrol issues are considered alone, the fiscal policy actions required to offset the negative economic impact of such decontrol will be inadequate.

Under the provisions of legislation developed earlier this year by the Senate Finance Committee, the windfall profits realized by petroleum companies would be taxed and the taxes rebated to consumers. Consumer rebates in 1976 would be about $12 billion. However, as discussed above, purchasing power lost by consumers would vary with the world price of oil and could be as much as $35 billion if a $1.00 per barrel world price increase is imposed, price controls are removed, and the tariff is maintained. To minimize the economic impact of oil price increases, the dollar amounts of tax rebates should be based on estimates of consumer purchasing power lost rather than on the amount which may be collected through taxes on oil company profits.

Removing all price control makes the United States vulnerable to large income shifts within the domestic economy caused by arbitrary pricing decisions of foreign oil producers. To try to compensate for these income shifts through fiscal and monetary policy changes would be extremely difficult if not impossible. Thus, the reimposition of controls in some form is a necessary economic buffer against possible OPEC price actions.

> In order to avoid large shifts in income within the United States caused by changes in oil prices abroad, the price of

domestically produced petroleum must be controlled at some appropriate level.

The energy price increases of the past nine months and any expected rise during the remainder of this year should be offset by tax reductions related to the loss of consumer purchasing power rather than to the size of the increase in oil industry profits.

Budget Policy for Fical 1976

In formulating our fiscal policy recommendations, we have assumed that the price of domestically produced petroleum continues to rise steadily but not dramatically throughout this year and the first part of next year. Barring a price rollback mandated by Congress or complete decontrol followed by a substantial OPEC price increase, this appears to be a reasonable assumption. Should oil prices rise significantly more than is here assumed, then the offsetting personal tax reductions should be correspondingly larger.

An appraisal of fiscal policy as it is currently projected either by the Administration or by the First Concurrent Resolution on the Budget shows a continuing movement toward restraint in the coming year. The impact of the Tax Reduction Act of 1975 was concentrated primarily in the second quarter of this year when tax rebates and other payments associated with that legislation were paid out. Although this stimulus is still in the process of filtering through the economy, there is little net additional stimulus to be gained from that action. Even if the Tax Reduction Act is extended through 1976, there will be some increase effective January 1, 1976, in the amount of income tax withheld from workers paychecks.[1] Failure to extend the Tax Reduction Act would result in further fiscal restraint of approximately $12½ to $13 billion during calendar 1976.

The United States economy can in no way afford what amounts to a tax increase in early 1976. Extension of the tax reductions was assumed in the First Concurrent Resolution on the Budget. We can foresee no prospect of a recovery so strong that the Tax Reduction Act should be allowed to expire at the end of this year. Extending it at the earliest possible date would contribute to improved business and consumer confidence.

Another program for which provision was made in the First Budget Resolution is the combined program of emergency public works and antirecession aid to State and local governments. This has now been passed by the Senate and is pending in the House. Fiscal 1976 outlays under this bill are estimated at approximately $2 billion.

It is not possible to determine at this time how close fiscal 1976 outlay totals will be to the $367 billion target set in the First Concurrent Resolution. Legislative consideration of a number of appropriation measures, including defense appropriations, is still under way. If defense appropriations are held to the level proposed in the Budget Resolution, total appropriations actions on controllable pro-

[1] The 1975 adjustment to tax withholding was designed to incorporate the entire year's tax cut into withholding in the last eight months of the year. If the cut is extended into 1976, the withholding reduction can be spread over the full 12 months. Hence, the amount of tax withheld in each individual month would be greater.

grams should be well within the target figure, even allowing for the antirecession aid to State and local governments. However, it presently appears that some uncontrollable categories of spending, such as unemployment compensation and veterans' benefits, could exceed earlier estimates by some $2 to $3 billion. Thus total outlays may turn out to be a little above the target figure.

Even so, fiscal policy will be moving in a restrictive direction throughout fiscal 1976. This move toward restriction was not intended by Congress at the time the First Concurrent Resolution was adopted, but is resulting from the impact of inflation on budget receipts. The Congressional Budget Office has recently estimated that, even with the removal of oil import fees—which will reduce receipts by $2.7 billion, actual fiscal 1976 receipts will be about $303.8 billion, or $5.6 billion higher than the First Concurrent Resolution target. According to estimates made by the staff of the Joint Economic Committee, if outlays are approximately at the $367 billion target, the surplus in the full employment budget will rise by roughly $9 billion (annual rate) from the first half of fiscal 1976 to the second half and a further $9 billion in the succeeding half year.[2] Given the fragile state of the economy, discussed in the Economic Outlook Chapter, fiscal policy should, at the very least, be neutral in the coming year. The tax changes recommended below combined with the expenditure increases necessary to implement the job creation program discussed in Chapter IV would achieve this objective.

> Actions provided for in the First Concurrent Resolution on the Budget should be carried through by:
>
> Prompt extension of the Tax Reduction Act of 1975.
>
> Adoption of presently pending legislation providing for antirecession aid to State and local governments and for emergency public works.[3]
>
> In addition, because higher than expected rates of inflation are having an unintended restrictive effect on the budget, new initiatives are needed simply to restore to the budget the degree of economic stimulus which was intended at the time Congress enacted the First Concurrent Resolution on the Budget. The fiscal 1976 outlay target should be raised $3 billion to cover the cost of the emergency jobs program described in Chapter III. Tax reductions with a fiscal 1976 impact of approximately $4 to $5 billion beyond the simple extension of the 1975 tax cut are also needed.

Although the combined fiscal 1976 cost of the emergency jobs program and the additional tax cut is $7 to $8 billion, this does not mean enlarging the deficit by this amount. The improved level of economic activity which would result from the additional stimulus would produce higher personal and corporate incomes and hence, higher Federal tax collections. In addition, as discussed above, it now appears that tax receipts are running ahead of the estimates made at the time Congress

[2] The full-employment budget is a calculation to determine what tax receipts and Federal expenditures would be if the economy were operating at a constant rate of resource utilization. The above calculations make the standard assumption of a utilization rate consistent with an unemployment rate of 4 percent of the civilian labor force.

[3] Senator Proxmire states: "This special antirecession aid would not be necessary if the Federal Government adopted a policy of employer of last resort. See my footnote on page 39."

considered the First Concurrent Resolution last May. Our recommendations imply a total outlay level in fiscal 1976 of roughly $370 billion (as compared to $367 billion in the First Concurrent Resolution). With adoption of our recommendations, receipts are estimated in the neighborhood of $300 billion, leaving a deficit of around $70 billion. It should be stressed, however, that tax receipt estimates are highly sensitive to changes in both inflation and employment. Even a relatively small change in our assumptions about price behavior would produce a significant change in our estimate of the deficit. Likewise, a faster than expected recovery of production and employment would act to reduce the estimated deficit.

The additional tax reduction we are recommending should take effect January 1, 1976. Its total size should be about $8 to $10 billion for the calendar year. One half of this, or $4 to $5 billion, would take place within fiscal 1976. The tax reduction could be accomplished in any of several ways. One way to achieve part of it would be to continue the withholding rates in effect in 1975. Because these withholding rates would be in effect for 12 months rather than eight, this would enlarge the total size of the tax cut by about $4 billion, or about one-half of the additional tax relief which is needed.

Another possibility which has special merit in terms of its favorable effect on both prices and employment would be to allow both employers and employees a credit on their income tax returns equivalent to an appropriate fraction of the social security taxes they have paid. Workers who have paid social security taxes but whose incomes are too low to take full advantage of the tax credit would be given an equivalent offsetting payment. Such an "earned income" tax credit offers the following advantages:

> It would be of benefit to all who work and pay social security taxes, including those with earnings so low that they do not pay income taxes.
>
> By providing credits to employers as well as to employees, it would reduce employment costs, thus stimulating employment and helping restrain price increases.
>
> Incorporation of this tax change into tax withholding would mean higher after-tax take-home pay for workers. This would help reduce pressure for large wage increases. The fact that 1976 is a year in which many major union contracts must be negotiated makes this an especially important advantage.
>
> While this tax change would help offset the burden of high social security tax rates, it would be accomplished through the income tax system. It would not in any way affect social security trust fund revenues.
>
> *Accompanying the extension of the Tax Reduction Act should be the adoption of an "earned income" credit on the income tax returns of both employers and employees in an amount adequate to reduce total income tax collections in Calendar 1976 by $8 to $10 billion (fiscal 1976 impact of $4 to $5 billion).*

Some may find it surprising that the Committee is recommending additional tax cuts at a time when the deficit is already very large and

V. MONETARY POLICY

One point which has been stressed by virtually all witnesses before the Committee is the crucial importance of an appropriate monetary policy in achieving a strong economic recovery while simultaneously coping with inflation. Failure to provide sufficient money and credit would drive up interest rates, thereby aborting any recovery of residential construction and discouraging a revival of business investment. Excessive expansion of the money supply, however, would make no contribution to the further rise of real output but would generate additional inflation. The difficulty arises not with reaching agreement on these principles but in applying them to determine the precise dimensions for monetary policy.

CURRENT MONETARY POLICY

After remaining unchanged in the first quarter of this year, the money supply (demand deposits and currency) grew 9 percent in the second quarter. Much of the increase was concentrated in the month of June and was to some extent associated with the payment of income tax rebates and special social security payments. Despite this special factor, the Federal Reserve authorities felt monetary expansion in the second quarter was excessive and should be reduced quickly even though this meant increases in short-term interest rates. Thus in July the Federal Open Market Committee raised its target for the Federal Funds rate to a 5 to 6 percent range (from a June target range of 4.5 to 5.5 percent).[1]

In fact, the Federal funds rate was permitted to average 6.1 percent in July and 6.2 percent in August and early September. The money supply grew at an annual rate of only 3 percent in July and August. Treasury bill rates and other short-term interest rates rose steadily throughout July and August.

The Chairman of the Federal Reserve testified to this Committee during our Midyear Review that:

> The growth of monetary aggregates in recent months has been well above the longer run rates of expansion that we have been seeking. The Federal Reserve has no intention of permitting rates of increase as high as those in the second quarter to continue. The special Treasury disbursements have come to an end, and we have already set in motion forces that should return the growth of the monetary aggregates to the moderate path desired. These recent actions have left their mark, if only temporarily, on short-term market rates of interest.

[1] The Federal Funds rate is the interest rate charged in the New York market for the overnight loan of funds. It is through its impact on this overnight rate that the Federal Reserve measures the short run effects of its open market operations.

Several private witnesses sharply criticized this policy, however, feeling that to permit interest rates to rise at a time when recovery is barely under way is a serious mistake. This Committee shares the view of these witnesses that the Federal Reserve has moved prematurely to tighten monetary policy in the past few months. When the special circumstances of the tax rebates are taken into account, monetary growth in the second quarter was not excessive. While some reduction in the rate of monetary expansion in the third quarter may have been desirable, the change has been too abrupt.

> Monetary policy in the past three months has been too restrictive. Over the months ahead policy should be designed to hold interest rates below the levels which will interrupt the economic recovery by diverting funds from housing and other crucial sectors.

In particular, this means that short-term rates must not rise to levels which cause depositors to withdraw funds from savings institutions in order to invest in higher yielding market instruments. The exact rate of monetary growth which will be required to achieve this objective is difficult to specify. In establishing monetary targets for the year ahead, the Federal Reserve has quite properly stressed that these targets are subject to revision as circumstances warrant. The particular targets announced by the Federal Reserve in May and reiterated in July included an intended growth of the money supply of between 5 and 7½ percent from the second quarter of this year to the second quarter of 1976. It is conceivable that the rise in interest rates can be contained with an expansion of the money supply toward the upper end of this proposed range. However, most witnesses before this Committee have felt that a somewhat greater expansion of the money supply was both likely and desirable.

Typical current forecasts project an increase in the money supply at or somewhat above the upper end of the Federal Reserve's target range. What is disturbing is that these forecasts also predict a steady rise in short-term interest rates, perhaps to a level of 8 or 8½ percent for the three months' Treasury Bill rate in the second half of next year. These expectations of very high short-term interest rates are a serious concern. In the six months from April through September 1974 the bill rate averaged 8.3 percent, and growth of deposits at savings institutions was cut in half as funds were diverted to higher yielding market instruments. This in turn meant mortgage credit availability was severely restricted and housing starts plummeted.

The 1976 interest rate outlook implies similar disastrous consequences for the housing industry and a serious threat to recovery throughout the economy. Based on information and forecasts presently available, a growth of the money supply within the range of 8 to 10 percent during the period from second quarter 1975 to second quarter 1976 would appear to be required if short-term interest rates are to be held below a level which would seriously interfere with continued recovery of the economy.[2, 3]

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[2] Chairman Humphrey states: "In addition to conducting a general monetary policy which will support recovery of the housing industry, we must also make mortgage money available to middle and low-income families at interest rates they can afford. The Federal Housing Bank Act (S.1122) which I have introduced in the Senate would accomplish this."

[3] See Senator Proxmire's Supplemental View on the need for additional measures to help the housing industry.

The Committee, of course, would not wish to see such an expansive monetary policy continued indefinitely. At present, when so much plant capacity and so many workers are idle, the additional growth of money GNP which a larger growth of the money supply would support can be expected to translate into additional real output and employment. If the economy were at, or near, full resource utilization, such rapid growth of money could only translate into higher prices. As output returns closer to its potential, growth of the money supply should be brought into line with the potential growth rate of the economy. For the period immediately ahead, however, it can only be concluded that the announced policy targets of the Federal Reserve are not fully consistent with the strong growth of output and employment which the Committee feels to be required.

Thus, a situation exists in which a highly independent monetary authority is pursuing a course not fully satisfactory to the Members of this Committee nor, perhaps, to the majority of Members of Congress. This situation of institutional conflict could have very damaging consequences for the economy.

Congressional Supervision of Monetary Policy

Earlier this year the Congress acted to require Federal Reserve authorities to appear periodically before the Banking Committees and to discuss their monetary growth targets for the year ahead. The Chairman of the Federal Reserve has complied with this requirement through appearances before the Senate Banking Committee in May and the House Banking Committee in July. These appearances have been very useful in informing the Congress of the intentions of the Federal Reserve and providing opportunity for discussion. The question of what further action to take if the Federal Reserve's proposed policies are unsatisfactory remains unresolved, however.

> The following steps should be taken to help establish the proper degree of congressional control over monetary policy:
>
> Congress should adopt systematic procedures for establishing output, employment, and purchasing power targets.
>
> The Administration should be required to present specific monetary policy recommendations to the Congress.
>
> The Federal Reserve should be required to present targets for the monetary aggregates which are consistent with congressionally determined output, employment, and purchasing power targets.

The Employment Act of 1946 requires the President to recommend to the Congress the policies necessary to "promote maximum employment, production, and purchasing power." It requires the Joint Economic Committee to report to the Congress on the adequacy of these recommendations. In its Annual Reports, the Joint Economic Committee has typically presented the output and employment targets which it concludes to be realistic and desirable. In this year's Annual Report, for example, the Committee recommended output targets of $820–830 billion (1958 dollars) for the fourth quarter of 1975 and $890–900 billion for the fourth quarter of 1976. The unemployment rates which would normally be associated with these output levels would be 7.8

to 8.1 percent at the end of this year and 6.5 to 6.8 percent at the end of 1976.

The Employment Act does not require Congress to take any specific formal action on the Joint Economic Committee's Annual Report. Hence, these output and employment targets, while they may have the support of many individual Members of Congress, do not have the formal endorsement of the Congress as a whole.

The fiscal policy adopted by Congress in the First Concurrent Resolution on the Budget in May was estimated by the Budget Committees at the time to imply an unemployment rate of about 7½ percent at the end of next year, and this might be regarded as at least an indirect endorsement by the Congress of an employment target. It could surely be argued, however, that it would be preferable to agree upon the output, employment, and purchasing power targets first and then to adopt a budget policy—and also monetary and price-incomes policies—designed to reach the agreed-upon objectives. Establishment of these basic economic policy targets could be achieved through congressional debate on the adoption of the Joint Economic Committee's Annual Report, through a planning process such as that provided for in S. 1795, The Balanced Growth and Economic Planning Act of 1975, or through other mechanisms. Whatever the procedure adopted, proper congressional supervision of economic policy must begin with a clear enunciation of specific short-run targets for the economy.

Another obstacle to proper supervision of monetary policy is the veil of silence maintained by the Administration in this area. As was emphasized by a former Member of the Federal Reserve Board of Governors who testified during the Midyear Hearings, the original intention of the Employment Act was that the President would incorporate monetary policy recommendations into his annual Economic Report. In practice, these recommendations have been either extremely vague or missing entirely. Furthermore, the Chairman of the Council of Economic Advisers and other Administration officials have refused on a number of recent occasions to make any specific or detailed recommendations on monetary policy, arguing that this should be left to the Federal Reserve.

Congress has the responsibility to make sure that monetary policy as conducted by the Federal Reserve is designed to achieve the economic objectives established by the Congress. In carrying out this oversight responsibility, Congress should have the benefit of a detailed presentation of the Administration's analysis and conclusions regarding the most desirable path for monetary policy. The secrecy which presently surrounds Administration views on monetary policy should be lifted. The President's Economic Report should contain recommendations on monetary policy, and these should be couched in terms of specific rates of growth of the monetary aggregates, specific interest rate targets, and/or such other specific dimensions of policy as the Administration judges to be appropriate. The Administration should forward additional or amended monetary policy recommendations to Congress throughout the year as necessary.[4]

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[4] Senator Proxmire states: "I do not agree. It is the constitutional responsibility of the Congress, and the Congress alone, to control monetary policy. To rely on the Administration for recommendations would, in effect, shift the responsibility which should be borne by the Congress. It would be a congressional cop-out."

The responsibility for the detailed design and execution of monetary policy has wisely been entrusted to the Federal Reserve. The Committee would oppose any effort by the Congress to legislate or otherwise impose specific targets for growth of the money supply or any other monetary variable. Congress should, however, insist that the Federal Reserve periodically present a "plan of action" which is consistent with congressionally enunciated targets for output, employment, and purchasing power.

These "action plans" should be accompanied by documentation demonstrating why and how, based on the best available information, these monetary policies will contribute to the basic objectives sought by Congress. At present Congress is considerably handicapped in evaluating monetary policy by the refusal of the Federal Reserve Board to make staff economic forecasts and other similar material available to Congress. The Chairman of the Federal Reserve has testified that he believes the employment targets suggested by the Joint Economic Committee for this year and next are "reasonable" and that current monetary policies will contribute to their achievement. He admitted, however that he was "more optimistic" than his own staff with regard to the speed with which unemployment is likely to decline. Private witnesses before the Committee also presented unemployment forecasts sharply at variance with that of the Federal Reserve Chairman. The Federal Reserve has declined to make staff forecasts available on the grounds that they are continually subject to revision. However, the Congress regularly receives Administration and private forecasts of which this is equally true. It is difficult for the Congress to evaluate conflicting testimony when that testimony is not supported by any detailed evidence or analysis.

Congress is also handicapped in its oversight of monetary policy by lack of sufficient professional staff with expertise in this area. Another former Member of the Federal Reserve Board who testified before the Joint Economic Committee last spring urged that Congress establish its own independent professional unit to analyze monetary policy. Such a staff should be completely nonpartisan and professional in nature. It could be either an expansion of the staff of the appropriate existing committees or it could be a separate unit.[5]

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[5] Senator Proxmire states: "There is no reason to set up an indepnendent Congressional Monetary Office. While a case might be made that existing staff should be strengthened, this function is performed and should continue to be performed by the Congressional Banking Committees which properly have jurisdiction over the Federal Reserve Board. To remove this proper function fom them and put it in chage of an independent office is unnecessary."

VI. PRICE-INCOMES POLICY

At the beginning of 1975 most forecasters expected the rate of increase in consumer prices to slow to 4–6 percent by the end of this year. Recent sharp increases in both food and fuel prices at the wholesale and retail level, however, have caused most estimates of the rate of price increase in the second half of 1975 and 1976 to be revised upward.

FOOD AND FUEL PRICES

In the the second quarter of 1975, wholesale farm product prices rose at a 17 percent rate and retail food prices at a 10 percent rate. The most recent Department of Agriculture forecast predicts that the increase in consumer food prices during 1975 as a whole will reach 9 or 10 percent. Fuel prices also rose sharply in the second quarter, at both the wholesale and retail level. Consumer prices of gasoline, motor, and fuel oil, and gas and electricity rose at a rate of more than 18 percent in the second quarter. As Table 3 indicates, prices of consumer goods other than food and fuel showed a considerable moderation in the rate of increase, rising at only a 4.2 percent rate in the second quarter.

Because of the uncertainty that surrounds energy policy and domestic grain supplies at present, the outlook for prices in 1976 remains clouded. Assuming a gradual decontrol of "old" oil, a good harvest, and only moderately increased grain sales abroad, consumer prices may rise as much as 6–8 percent in 1976. If any of these key variables is substantially different, that is, energy prices rise rapidly after immediate decontrol, or farm prices rise more sharply because of poor harvest or higher exports, inflation could become a serious impediment to the recovery. Failure to establish the domestic food reserves which the JEC has repeatedly recommended in past reports makes consumer food prices highly sensitive to changes in crop conditions.[1] It would be especially harmful if this inflation, caused primarily by external, relatively uncontrolable forces and not by excess demand, were used as a rationale for pursuing restrictive fiscal and monetary policies, as was done in 1974.

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[1] Chairman Humphrey states: "Enactment of S. 513, The National Food and Agricultural Stabilization Act of 1975, would give us the national food policy, including food reserves, which we must have in order to stabilize both farm incomes and consumer food prices."

for eight months after the February 1961 turning point of that recession. Industrial prices then remained essentially stable for the next three years. During the current recession, we have experienced not even a single month in which industrial prices held steady or declined. Furthermore, date for the most recent three months suggest that the rate of price increase has begun to accelerate again; from February to May the annual rate of increase was only 1.5 percent, but from May to August it rose to 6.0 percent.

A large part of this renewed rise in industrial prices can be attributed to the fuels component. However, as shown in Table 4, there are several other major components of the Wholesale Industrial Price Index which have also shown persistent increases. Chemicals, machinery and equipment, transportation equipment, and miscellaneous industrial products have shown rates of increase between 3 and 5 percent in the most recent six months. In each case, these figures are dramatic improvements from the year-earlier situation, but in no case do they represent the kind of aggressive price-cutting behavior which traditional economic theory would lead one to expect at a time when there is such enormous idle capacity. Concern must also be expressed about the important metals category, in which prices began to rise again in August after a year of relative stability. The major steel companies have announced further significant steel price increases to take effect October 1.

TABLE 4.—WHOLESALE INDUSTRIAL PRICES

[Percent change, seasonally adjusted [1] annual rates]

	February-August 1974	August 1974, February 1975	February-August 1975
All industrials	[2] 35.6	9.5	3.7
By stage of processing:			
Crude materials, excluding foods and feeds	31.6	−9.7	7.2
Intermediate materials, excluding foods and feeds	44.4	8.5	3.1
Producer finished goods	26.1	18.7	6.0
Consumer nonfood finished goods	23.5	10.2	5.7
Textile products and apparel	10.0	−7.3	0.9
Fuels, related products and power	62.7	5.4	18.3
Chemicals and allied products	71.6	27.8	3.4
Lumber and wood products	−2.5	−13.4	10.5
Pulp, paper and allied products	49.2	9.3	−.4
Machinery and equipment	28.4	20.2	5.1
Metals and metal products	56.1	1.6	−3.0
Transportation equipment (NSA) [3]	13.6	19.0	3.4
Other industrial products [4] (NSA) [3]	21.6	12.6	3.4

[1] Except where otherwise noted.
[2] Calculations utilize seasonal factors based on data through March 1975.
[3] NSA—Not seasonally adjusted.
[4] Includes: Hides, skins, leather, rubber, and plastic products, furniture and household durables, nonmatallic mineral products, and miscellaneous.

Source: Department of Labor, Bureau of Labor Statistics.

Why price increases continue in the depths of such a serious recession? Certainly it cannot be attributed to any excess demand for the products involved. Manufacturing firms were utilizing only 66.5 percent of their plant capacity in the second quarter of this year. In some part, continuing price increases are due to rising costs, fuel costs in particular. The remainder of the explanation may lie in changes in the fundamental pattern of price behavior in concentrated industries, changes which have not yet been fully analyzed but which make prices

TABLE 3.—SELECTED MEASURES OF PRICE CHANGES 1974-75

[Percent changes during quarter, seasonally adjusted annual rates]

	1973				1974				1975	
	1st quarter	2d quarter	3d quarter	4th quarter	1st quarter	2d quarter	3d quarter	4th quarter	1st quarter	2d quarter
WHOLESALE PRICE INDEX										
All commodities	19.8	19.8	13.0	9.4	24.8	11.0	34.9	14.2	−6.3	7.2
Farm products, processed foods and feeds	48.7	44.9	33.2	−10.4	12.6	−29.6	60.5	18.8	−27.6	17.0
Industrials	9.3	9.4	6.3	18.8	31.3	33.2	28.4	11.1	4.2	2.6
Fuels, related products and power	13.6	17.7	15.6	55.3	127.9	50.8	35.5	12.6	.3	16.0
CONSUMER PRICE INDEX										
All items	8.0	7.9	9.6	9.8	13.7	10.9	13.4	11.0	6.0	7.1
Food	25.9	18.5	25.6	11.6	17.0	5.4	11.7	14.3	−.2	10.0
Fuel (gasoline, motor oil, fuel oil, gas and electricity)	7.0	14.2	.7	51.2	65.9	20.8	5.5	3.9	5.9	18.2
All items less food	3.8	4.7	4.7	9.4	12.4	12.7	14.1	9.5	8.5	5.8
All items less food and fuel	3.8	3.8	5.3	5.9	8.9	11.5	14.9	9.9	9.4	4.2

Source: Department of Labor, Bureau of Labor Statistics.

INDUSTRIAL PRICES

While continued substantial increases in prices of food and fuels have been the major sources of recent persistent inflation, these are not the *only* sources. Prices of many industrial products have also continued to rise, and unless this rise can be contained, industrial price behavior could constitute a serious impediment to the strength and duration of an economic recovery.

The Director of the Council on Wage and Price Stability warned at our Midyear Hearings:

> It used to be that prices fell during recessions as severe as this one. The prices of many industrial raw materials have declined, but the list prices of most finished industrial goods have not declined, and they are beginning to rise very early in the recovery. What concerns me deeply is, if these price increases become widespread this recovery will be less vigorous than it should be. The Congress has passed, and the President has signed into law, a substantial tax cut designed to stimulate the economy. This will help to produce a rise in GNP, measured current dollars, but if that stimulus is dissipated in price increases, the rise in real output and in employment could be disappointingly small.

As shown in Table 4, the annual rate of increase of wholesale industrial prices has fallen dramatically during the past 18 months, from 36 percent in the February-August 1974 period to less than 10 percent in the subsequent six months and to less than 4 percent in the most recent six months for which date are available. Even so, this is not good enough. In light of the severity of the recession and the very low operating rate in most industries, wholesale prices should by this time have actually been falling. In the 1960–61 recession, wholesale industrial prices fell steadily during the nine month period from January to October, 1961; that is to say, the fall in prices continued in these industries even less sensitive to demand conditions than they have been in the past.

In sum, it must be concluded that the current problem of rising industrial prices is not one which is susceptible to demand management. That is, these price rises cannot be contained by allowing unemployment to persist at very high levels. Indeed, as this Committee has repeatedly stressed, a more rapid recovery will bring with it important gains in productivity which will help contain inflation by holding down unit costs.

Need for a Price—Incomes Policy

A crucial tool in containing the rise in industrial prices must be an active price-incomes policy. This is especially true because most of the industries exhibiting continuing price increases are highly concentrated industries which typically employ administered pricing techniques. These are the very industries for which a voluntary program of price restraint should be a feasible and workable approach to inflation control. Businessmen in these industries, which have been so hard hit by the recession, certainly have no wish to see the economic recovery weakened or interrupted by a new burst of inflation. With firm initiative and strong leadership on the part of the Administration, it should be possible to achieve business cooperation in a voluntary price restraint effort.

TABLE 5.—MANUFACTURING WAGES AND CONSUMER PRICES: MAJOR INDUSTRIAL COUNTRIES

[Percent change from previous year]

	1974		1975 [1]	
	Hourly earnings [2]	Consumer prices [3]	Hourly earnings [2]	Consumer prices [3]
United States	8.4	11.4	8	8
Canada	13.4	10.6	15	10½
Japan	26.3	24.4	15	12½
France	18.6	13.7	16	11¾
Germany	10.6	7.3	7	6
Italy	22.4	19.1	26	18¼
United Kingdom	17.0	14.5	28	22½

[1] Estimate and forecast by the OECD, July 1975.

[2] In manufacturing (for Japan, earnings are monthly earnings; for France and Italy earnings are hourly rates).

[3] For the United States, Canada, Germany, and the United Kingdom, the national accounts implicit consumption deflator is used.

Source: Organization for Economic Cooperation and Development.

The pattern of wage settlements during the months ahead will also require careful monitoring. The inflation of the past two years has in no way been a wage-induced inflation. Wage increases have persistently lagged behind price increases. In August, real average hourly earnings were 2 percent lower than they were two years earlier. However, wage restraint in 1975 has been aided by the fact that a relatively small number of workers have been involved in collective bargaining negotiations. In contrast, 1976 will be the heavy year of the collective bargaining cycle, with important negotiations in the trucking, rubber, automotive, and electrical equipment industries. Workers in these and other industries have quite legitimate needs to recover some of the purchasing power lost to past price increases, and growth of real disposable personal incomes is essential to sustaining an economic recovery.

At the same time, it is vital to the future stability of the economy that wage settlements reached over the months ahead do not in themselves constitute a new spur to further inflation. Table 5 shows that in contrast to most other major industrial countries, workers in the United States on the average during the past two years have not demanded wage gains that outstripped price gains. The United States is the only one of seven major industrial countries in which hourly earnings rose less than consumer prices in 1974, and the only one in which, according to the Organization for Economic Cooperation and Development (OECD) forecast, hourly earnings gains are not expected to exceed price gains in 1975. As of this moment, it is not too late for the United States to formulate and put in place an incomes policy which will both support real spendable incomes and prevent excessive wage settlements from provoking a continuing spiral of price-wage-price increases.

An adequate incomes policy should have two basic elements. First, major unions should be asked to join in a voluntary policy which limits wage settlements to trend productivity gains plus some reasonable catch-up factor for part of any real income losses which have been experienced due to inflation. Second, tax reductions should be enacted to help sustain real after-tax disposable incomes. A useful guideline for determining which price increases should be offset by wage increases and which by tax reductions might be the following: wage increases should be sufficient to compensate for the underlying rate of inflation in the nonfood, nonfuel component of the index and tax cuts should be used to compensate for the extra amount by which fuel and food prices have risen. The economic logic behind this division is that food and fuel price increases to a large degree represent transfers outside the nonfarm domestic sector of the U.S. economy.[2] These are real income losses to the nonfarm economy as a whole and an attempt to compensate for them through wage increases could only lead to further inflation. In view of the need to support real individual incomes if the private sector is to continue on a recovery path, however, it is especially important at this time that tax policy be used to offset these income losses.

In the Fiscal Policy Chapter of this report, we have recommended tax reductions which should be adequate for the above purpose, given our present expectations about inflation. Should inflation prove more serious than we have estimated (due, for example, to larger world oil price increases) then the size of the needed tax cuts will have to be correspondingly increased.

> Prospects for success in dealing simultaneously with high unemployment and re-emerging inflationary pressures would be greatly increased by the adoption of an active voluntary price-incomes policy initiated and maintained through the direct leadership of the President himself and of his highest level economic policy advisers. This policy should have the following elements:

[2] Or in the case of windfall profits to domestic oil producers, price increases represent net withdrawals from the spending stream since these profits are unlikely to be immediately respent.

Voluntary negotiated price restraint on the part of big businesses, especially in the highly concentrated industrial sectors of the economy.

Voluntary cooperation in holding major wage settlements to trend productivity gains plus a reasonable adjustment for some part of cost-of-living increases.

Tax reductions (as discussed in Chapter IV) sufficient to restore the purchasing power losses not covered by wage settlements.[3]

The above recommendation is not meant to imply that this is all that needs to be done about inflation. Responsible monetary and fiscal policy are fundamental. The maintenance of some form of control over oil prices is crucial. Many structural improvements in the economy, such as antitrust actions to breakup the monopoly power, are needed. Our foreign trade policy, especially with respect to grain exports, is of key importance. The price-incomes policy we have described above is far from the only action that is needed, but it is one vital and necessary element.[4]

Fortunately, the existence of the Council on Wage and Price Stability provides a start on the kind of price-incomes policy that is needed. The professional staff and the administrative mechanism for monitoring such a program are available. Congress has recently acted to extend the life of the Council and to provide it with subpoena power. The Council has already undertaken studies of price behavior in several key industries and of some particularly troublesome wage situations. It has held useful public hearings and has had some modest success in persuading a few industries to scale back planned price increases. It cannot be expected, however, that the Director of the Council, with his limited statutory authority, can himself negotiate and carry out the policies which are needed at this time.

The economy is at a turning point. With proper policies, reduction in both inflation and unemployment can continue; without those policies a renewal of inflation will in turn sow the seeds of further recession. Crucial among the initiatives which are needed is a voluntary price-incomes policy conducted vigorously and with full commitment by those at the center of Federal economic policymaking—the President and his closest advisers. Some of those advisers have indicated that they regard price-incomes policy as a highly distasteful policy instrument. This Committee, however, sees no other way in which we can reasonably expect to succeed in coping with emerging price and wage problems.

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[3] See Supplemental Views of Representative Reuss.

[4] Chairman Humphrey states: "An adequate policy to cope with inflation in the longer run, as well as to achivee full employment and equitable income distribution, requires a far more comprehensive and coordinated approach to economic policy than we have at present. I believe that the Balanced Growth and Economic Planning Act (S. 1795) which, I have introduced in the Senate, would provide for this more comprehensive approach."

bined with that phased decontrol would be a new system of natural gas price regulation, offering incentives to producers sufficient to attract the needed capital but preventing consumer prices from rising to the Organization of Petroleum Exporting Countries (OPEC) oil price equivalent.

Additionally, I stand totally committed to the need for increased energy conservation, both by mandatory measures to reduce waste and by incentives to consumers, homeowners, business and industry to use energy more efficiently and to produce goods that consume less energy.

The final principal component of an energy policy that I believe will be effective and fair is a crash effort on the part of the Federal Government, together with industry, to develop our domestic resources and alternative fuels as quickly as possible. I do not believe that the Energy Research and Development Administration (ERDA) is funded sufficiently or equipped with the power to meet the challenge of energy independence in the near future. What is needed, as pointed out by the Minority views, is Federal assistance on a massive scale to speed development of environmentally beneficial energy sources.

I agree with the Majority that the time has not arrived for the decontrol of oil and gas prices, but I do not believe that controlled prices are an inherent condition for a stable economy. After a reasonable period of time the issue should be reconsidered thoroughly with a view to decontrolling those aspects of energy that are subject to competitive conditions.

Finally, it is imperative that all sides moderate their positions with a view toward compromise. The American people are in a sea of uncertainty with regard to Congress and the President on energy issues; and only when the Federal Government produces a coherent policy can we expect that the people, who ultimately must carry out any policy enacted, will act decisively and responsibly to effectuate energy independence, which is our goal.

JACOB K. JAVITS.

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Appendix. IMPACT OF JOINT ECONOMIC COMMITTEE PROPOSALS

No one can say with certainty where the economy will be a year from now. Nor can the impact of the policy changes we recommend in this report be stated precisely. We are confident, however, that the policies we have recommended will have a significant favorable impact on employment, prices, and financial markets.

In order to provide as complete information as possible regarding the impact of our proposals, the Committee instructed its staff to prepare quantitative estimates of major economic variables as they might be in the second half of next year with and without the Committee's recommendations. These estimates, which were made with the aid of an econometric model, are shown in Table A–1 below. Other models would produce somewhat different results, and these estimates should not be interpreted as predictions of what will happen either with or without the adoption of our recommendations, but as an aid to understanding the general magnitude of the difference which our recommendations might make.

Table A–1 contains three sets of estimates. The first assumes the adoption of the jobs program, the $8 to $10 billion "earned income" tax credit, and the easier monetary policy which we have recommended. The second column presents estimates which assume that the jobs program and the tax credit are rejected, but that the 1975 tax cuts are extended, and that the money supply grows at or slightly above the upper end of the Federal Reserve's target range. The third column presents a more pessimistic alternative in which it is assumed that the 1975 tax cuts are not extended, that oil prices are completely decontrolled, and that the money supply is held to a 6 to 6½ percent rate of growth.

TABLE A-1.—SIMULATION OF ALTERNATIVE ECONOMIC POLICIES [1] 1976—2D HALF

	Full adoption of JEC recommendations [2]	Partial adoption of JEC recommendations [3]	Rejection of JEC recommendations [4]
Real GNP (billions of 1958 dollars)	$850	$838	$819
Percent change during half, annual rate	5.5	3.9	2.1
Inflation rate (percent change GNP deflator, annual rate)	5.9	6.3	6.5
Unemployment rate	7.3	8.0	8.4
3 mo Treasury bill rate	6.6	8.6	10.9
Housing starts (millions)	2.0	1.7	1.3
Federal deficit (annual rate, dollars in billions, national income account basis)	$66	$56	$49

[1] These simulations were made using the Wharton Econometric Model.

[2] Assumes unified budget outlays in fiscal year 1976 of $379,000,000,000, including outlays for the emergency jobs program, extension of 1975 tax cuts, adoption of $9,000,000,000 earned income tax credit, money supply growth of about 9 percent, moderate increase in energy prices.

[3] Assumes unified budget outlays in fiscal year 1976 of $367,000,000,000, extension of 1975 tax cuts, money supply growth or about 8 percent, moderate increase in energy prices.

[4] Assumes unified budget outlays in fiscal year 1976 of $367,000,000,000, no extension of tax cuts, money supply growth of between 6 and 6½ percent, full decontrol of domestic petroleum prices.

It can be seen that the additional tax cut, the jobs program, and the more expansive monetary policy we have recommended have a significant favorable effect on the economy even as compared to the partial adoption of our recommendations which is assumed in Column 2. The difference between Column 1 and Column 3 is, of course, much more dramatic. Even as compared to Column 2, the full adoption of our recommendations would:

> Raise the output growth rate in the second half of next year to a level sufficient to achieve fairly steady reduction in unemployment. Unemployment is still very high in the second half of next year under any of the three assumptions, but only under the assumptions in Column 1 is it in the process of coming down at anything approaching a satisfactory rate.
>
> Significantly reduce the rate of inflation. Only under the assumptions in Column 1 is the inflation rate (as measured by the GNP deflator) brought below 6 percent. The improvement in the inflation rate can be explained by the higher productivity which would accompany faster output growth and by the antiinflationary features of the "earned income" tax credit. The econometric model provides no way of incorporating the impact of a price-incomes policy. Any success which such a policy had in reducing the rate of inflation below what it would otherwise be—and we believe its success could be substantial—would be in addition to the reduction in inflation shown in the model as a result of our fiscal policy recommendations.
>
> Markedly lower the three month Treasury bill rate and raise housing starts to a 2.0 million annual rate. Even a 6.6 percent bill rate is quite high, but it is probably below the crucial point at which high market rates lead to large outflows from savings institutions and thereby undermine residential construction.

The Federal deficit in the second half of calendar 1976 is estimated at about $66 billion (annual rate) if the Joint Economic Committee's recommendations are adopted. This is, of course, larger than it would be without the tax cuts and emergency jobs program which we have recommended. However, if our proposals are adopted, the estimated deficit narrows steadily with each half year, due to the higher tax receipts which accompany rising prosperity. By contrast, if the Committee's recommendations are rejected (Column 3) the deficit increases with each half year, because taxable incomes are not rising fast enough to keep pace with Federal spending increases.

SUPPLEMENTAL VIEWS OF VICE CHAIRMAN WRIGHT PATMAN

Generally, I am in accord with the findings and recommendations of this report.

However, I feel that the issues enumerated in these pages should include recognition of the serious problem confronting State and local governments regarding their ability to market long-term instruments at reasonable cost. It goes without saying that this is a perennial problem which neither the Administration nor the Federal Reserve have ever adequately addressed.

It has become a matter of painful routine for the tight money, high interest rate policies of the Federal Reserve to create the conditions under which State and local governments find it virtually impossible to sell bonds on reasonable terms to finance the construction of urgently needed public works and facilities. These range from pollution control investments to public schools and health clinics. The fiscal crisis of New York City and the uncertainty with which it has clouded the entire municipal bond market has made a dire situation even worse and underlines in a new and alarming way the need to come to grips with this situation in a positive and ongoing fashion.

If nothing else recent history should teach us that it is not enough to simply attempt to prod the Federal Reserve to establish and maintain policies which will provide the nation with a stable economy. That agency has demonstrated in the most convincing way that it will continue to swing the economy from one extreme to the other. For example, there is nothing on the horizon that can be taken as convincing proof that the money supply will not continue to be bounced from levels near zero to highly inflationary peaks with disasterous effects along the way.

Clearly, the time has come for establishment of a vehicle which will dampen the effects of these destabilizing policies and serve as a buffer for priority areas of the nation's economy such as State and local government financing.

In my judgment, one of the best approaches to this problem is the establishment of a National Development Bank which would be authorized and directed to purchase and to guarantee the obligations of State and local governments as well as provide direct loans on reasonable terms for low and moderate income family housing and small and medium sized businesses—the three areas of the economy which gyrating Federal Reserve monetary policies strike first and longest.

It goes without saying that a National Development Bank must be designed to restrict the assistance it would provide only to those who are creditworthy but cannot obtain needed funds on reasonable terms in any other way. Under these conditions, New York City would not qualify unless specific conditions were met to place its fiscal house in order.

But aside from that important point, the existence of a National Development Bank would mean that creditworthy State and local government borrowers, plagued by the uncertainties instilled in the municipal bond market from any source could turn to a lender of last resort.

A National Development Bank would provide a beneficial influence far beyond its ability to make direct loans through the purchase of State and local government debt obligations and to guarantee those obligations issued for sale in the open market. The mere fact that a National Development Bank could stand ready to help creditworthy State and local government borrowers would tend to create acceptance of their debt obligations on the most reasonable of terms even without direct intervention by such a bank.

The National Development Bank I am advocating could be patterned after the Reconstruction Finance Corporation which played a major role in restoring the nation's economy during the Great Depression and marshalling the economic tools necessary to gear the nation's industry for the all out effort required by World War II. The Bank should be capitalized at a level which would give it the stature needed to be effective. For example, it should be authorized to issue a total of $2 billion worth of stock subscribed to by the Treasury and purchased in amounts and at times the Bank considers necessary to fulfill its purpose. Maximum indebtedness of the Bank would be 20 times the amount of its paid in capital. The Bank would also be empowered to issue federally guaranteed obligations for sale in the open market so that it would not have to rely exclusively on tax funds. It could establish offices on a regional basis throughout the nation and fully promote awareness of it government and other priority area borrowers.

In this way, the nation could construct an economic guardian against the vagaries of the Federal Reserve's monetary policies. I urge the Members of Congress to seriously consider this proposal and to act on it in the immediate future.

SUPPLEMENTAL VIEWS OF SENATOR WILLIAM PROXMIRE

The report neglects housing, which, along with a revival in automobile production, is the key to economic recovery. For relatively small government outlays tremendous outlays can be induced from the private sector and millions of men and women put to work.

An interest rate subsidy of one to two percent on the average priced house would cost about $600 per house. As each new housing start produces about two man years' of employment, an outlay of $300 million could induce 500,000 housing starts and produce about one million jobs.

This is such a sensible method of proceeding that it is incredible that the Administration has resisted it so long. Here are its advantages:

1. It is noninflationary. It would put idle men and women to work (now almost 20 percent in the construction industry) on materials (brick, wood, mortar) now in surplus supply to produce needed and useful commodities; namely, a house to live in.
2. Compared with outlays for highways, public service jobs, and public works projects, its budget impact is exceedingly small.
3. It does not require a huge government bureaucracy and produces activity almost exclusively in the private sector.
4. It produces more jobs for the dollars spent than any other program.
5. By increasing the supply of housing it should bring rents down and, in fact, have a deflationary effect.
6. Because of the increased employment and economic activity, it would in fact more than pay for itself through increased government collection of taxes, and decreases in unemployment compensation and welfare payments.

By reducing unemployment through housing construction, the cost of my proposed government as an employer of last resort program would also be greatly reduced because of the relatively few who would then need help.

William Proxmire.

SUPPLEMENTAL VIEWS OF REPRESENTATIVE HENRY S. REUSS

While I am in full agreement with most of the recommendations contained in this report, I believe that the size of the proposed tax cut exceeds prudent limits. I also believe that we must have a stronger price-wage policy than is called for in this report.

In considering the need to extend tax cuts into 1976, we should not forget that the primary purpose of the Federal budget is to provide goods and services to the public. Tax reductions reduce the revenues available for these goods and services at any level of output, and they are an inefficient way of fostering State and local governments.

I therefore oppose the tax reduction provisions of the JEC report. In order to avoid a sharp drop in purchasing power at the end of this year, I would endorse an extension of the following provisions of the 1976 tax reduction only:

1. Increase in standard deduction—$1.2 billion.
2. $30 tax credit per exemption—$2.5 billion.
3. 10 percent earned income credit—$700 million.
4. household and dependent care credit—$10 million.

Total: $4.4 billion to June 30, 1976.

The additional investment credit and other tax reductions of 1975 should be dropped. In lieu of any additional tax cuts, such as the $8 to $10 billion recommended in this report, we should face plainly the fact that the emergency public employment program which we need will cost money. The proposed emergency jobs program, together with its multiplier effects, would provide much of the stimulus necessary to bring the economy to full employment without a further erosion of the Federal tax base. This stimulus would be targeted directly at those whom we are trying to help—the unemployed. If further efforts are necessary beyond the emergency jobs program proposed in this report, then they too should be in the form of expenditures targeted directly at the problem of unemployment.

The report, in its brief mention of prices and incomes policies, relies heavily on the dubious notion of voluntary restraint. Under voluntary restraint, the good and patriotic obey and bear the burden, while the others reap the benefits of "voluntarism." We should recognize that as employment and operating rates rise, statutory measures will be required in order to achieve the overriding priority of full employment without inflation. Such measures include a negotiated social contract or national wage bargain and selective price controls in administered price areas and in sectors especially subject to the pressures of excess demand.

HENRY S. REUSS.

SUPPLEMENTAL VIEWS OF SENATOR LLOYD BENTSEN

Despite the fact that the American economy has apparently passed the bottom of the recession, a steady and lasting recovery is by no means assured, as this report so well demonstrates. The prospect of continuing current unemployment rates if we fail to take the proper economic measures is chilling. Right now, unemployment among youths is over 13 percent, for teenagers it is over 21 percent, and for minority teenagers is over 37 percent nationwide and above 50 percent in many cities. If this continues much longer, we will have seen a whole generation of young men and women told that they must wait for years before having a decent job, years spent growing accustomed to life on welfare or unemployment compensation with no productive role or attachment to American society. We can't afford to waste a generation of young Americans and we can't afford to wait another 18 months for a new President to help them fulfill their job needs.

A strong recovery is needed, and I agree with the basic thrust of the recommendations in this report.

However, I would like to offer an additional recommendation with regard to Employment Policy.

We should concentrate on providing more incentives for the creation of new jobs in the private sector. Private jobs do not have to be phased out during a recovery; the Treasury cost is much less than comparable public service jobs; and by expanding the supply of goods and services, they help dampen inflationary pressures.

An employment tax credit, allowed to any firm which increases its employment in 1976 over its 1975 or 1974 peak, would be a very effective incentive for firms to accelerate their hiring plans, especially during a recovery. A credit equal to 10 percent of the wages of each new position, up to a maximum of $800 per year, could create up to 400,000 more jobs in 1976 than we would otherwise have, at a cost to the Treasury of less than $600 million.

To reduce the likelihood of firms receiving windfall tax credits for hiring workers that would have been hired anyway, an employment tax credit bill should also specify that firms must hire the long-term unemployed to quality for the credit, and that firms must plow the credit back into new capital investment.

Even with the possibility of some people being hired who would have been hired in the absence of the credit the average Treasury cost per job through an employment tax credit is $1,400, compared with perhaps $8,000 for public service jobs. I favor a continuation and improvement of the public service job program. However, we should not neglect opportunities to move the unemployed back into permanent private employment and to do so as quickly as possible.

While I favor extension of the 1975 tax reductions I will reserve judgment on the Committee's other tax reduction recommendations pending hearings by the Senate Finance Committee.

LLOYD BENTSEN.

Minority Views on The 1975 Midyear Review of the Economy

I. THE ECONOMIC OUTLOOK

After a year of sluggish performance, the economy definitely turned up in the second quarter. The issue now confronting us therefore has shifted to the strength of the recovery and whether any additional stimulus is needed. While the economic indicators still show a mixed picture, with both favorable and unfavorable movements, the lack of certainty is typical of the initial stages of a recovery and is not a clear sign of a weak recovery. On the contrary, the latter part of 1975 is expected to show further significant improvement—improvement that will set the stage for continued recovery in 1976.

Several factors suggest increased economic activity during the latter half of 1975. Consumer and business confidence have been boosted by the fact that the current growth rate of the Consumer Price Index has fallen from the double-digit levels of 1974 to 6 to 7 percent in the last several months. Real disposable personal income has risen strongly during the second quarter of 1975, following five consecutive quarterly decreases. Inventory liquidation has proceeded at a faster rate than expected, and stock building in the third and fourth quarters should stimulate additional production gains. As this inventory liquidation cleaned out unwanted stocks, new orders have turned up and industrial production has surged forward. Housing starts and corporate profits are up. Consumer spending has been quite buoyant in the past few months and the slight decline in preliminary August retail sales does not eliminate the strong gains marked since February. Employment has increased (1.5 million over the last five months) and other unemployment indicators have started to improve much earlier than is usually the case in business cycles. The layoff rate fell in the first half of 1975, and the average number of hours worked has increased, as well as the amount of overtime.

Whether the quickening recovery will falter in midstream is a legitimate concern, but the danger of excessive stimulation and the consequent boom-and-bust cycle is grim enough to warrant extreme caution in considering supplementary economic programs. Present Administration policies were based on the belief that the turning point was reached at midyear. The policies were designed to be sufficiently stimulative assuming that 1) liquidation of unwanted stocks occurred; 2) real personal disposable income recovered; and 3) the unemployment situation stabilized and consumer confidence returned. Since these events have materialized to a large extent, additional observations and analysis of the emerging recovery are necessary before any new programs should be undertaken.

One decision that must be made within the remaining months of 1975, however, concerns the extension of the Tax Reduction Act of 1975. While a reasonable case can be made for a simple extension of the Act in order to spare consumers increased withholding rates (an effective tax increase) at the end of the year, much less justification exists for a deepening of the tax cut to produce additional stimulation.

An extension would encourage consumers to maintain or surpass present spending levels, while the anticipation of what amounts to a tax increase could well serve as an untimely damper. The tax credit given to businesses should also be continued. Even so, the possibility of the necessity for a curb on spending if the economy's pace quickens dramatically should be kept in mind. We should remain sensitive to the strength of economic recovery as we approach "decision time" on the tax bill.

The danger of excessive stimulation is clearly indicated by the revival of the inflationary fires that have just recently died down. At the present time, we are experiencing unpleasant repeats of yesterday's price rises with the recent price increases in food and energy. While the movements of these important components of the cost of living are expected to dissipate shortly—the rate of growth in the Consumer Price Index slowed sharply in August—they represent a large and visible portion of the average consumer's budget. Moreover, energy price increases could filter through the cost structure to influence the prices of other basic commodities.

Because the strength of the recovery in consumer spending will affect the magnitude of expected business investment, it is crucial that a renewal of inflationary pressures does not curtail plans for personal and business spending, thus aborting a sustained recovery. Therefore, care must be taken not to disrupt the stability of the expansion with excessive monetary and fiscal stimulus.

It is apparent that many companies have neither lowered prices nor even moderated their price increases. At first glance, this behavior is surprising, because these same industries are still averaging fairly low capacity utilization rates and overall demand is weak. Most of these price increases, however, are due to costs that have risen steadily over the past year. These higher costs have produced a smaller than usual cushion of "softer" prices that would remain stable with the return to normal business activity. Unwarranted stimulation, at the same time capacity constraints are beginning to be felt, could easily bring back double-digit inflation.

II. MONETARY POLICY

The Minority supports the present Federal Reserve System target for growth of the money supply of 5 to 7½ percent.[1] This target seems reasonable in light of the expected real growth in economic activity in the third quarter. We fully expect that continued growth in the money supply in this range can be pursued without fueling inflation or hindering the recovery.

As always, intense debate is focused on the specific monetary growth targets of the Federal Reserve System and the Chairman is now providing the Committee with extremely helpful information on the future direction of monetary policy. However, we would greatly deplore congressional abuse of this newly acquired openness on the part of the Federal Reserve System. Politicizing the Federal Reserve System can only endanger the professional and impartial nature of its independent actions. While the exchange of information has been extremely beneficial to this Committee, we are against what appear to be congressional moves to dictate necessary, vital, and flexible actions of the Federal Reserve System, and subject it to political control.[2]

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[1] Representative Heckler reserves judgment on this statement of the Minority concerning the target growth of the money supply.

[2] Representative Rousselot favors legislation which would provide for an audit of the Federal Reserve System by the General Accounting Office, and he has introduced H.R. 3056 calling for such an audit.

Representative Rousselot states: "It is my opinion that the Federal Reserve System must be held accountable for its use of what are essentially taxpayers' funds. Although the System does not operate on appropriated funds, nearly all of the System's earnings are derived from interests on government securities, and the net earnings (i.e., the total earnings minus the expenses of the System and the Federal Reserve banks) are transferred to the U.S. Treasury.

"There are several areas of the System's current operations where meaningful congressional oversight has not been established. A thorough Government Accounting Office (GAO) audit of the System would assist Congress in determining the following: (1) Why the Federal Reserve System has moved to assume control of the check-clearing functions of the American banking industry; (2) whether the establishment by the Federal Reserve System of 'Regional Check Processing Centers,' at a substantial annual cost for capital investment and operations, is justified; (3) whether Congresss should examine more closely the role of the Federal Reserve banks in the loan guarantee programs for defense production; and (4) whether Congress should take a closer look at the Federal Reserve bank premises which, according to the System's 1973 Annual Report, exceeded $221 million (net book value) in that year.

"Nothing less than a thorough, independent assessment of the efficiency and economy with which the System's functions are performed will suffice to enable Congress to fulfill its oversight responsibilities with respect to the Federal Reserve System." (A more detailed explanation of Representative Rousselot's views on this issue can be found on page fifteen of H. Rept. 94-20 on H. Con. Res. 133, and on page seventeen of H. Rept. 94-345 on H.R. 7590.

III. FISCAL POLICY

The size of the present Federal deficit is truly awesome. While "Federal belttightening" may sound like an oft-repeated refrain, calling attention to the burgeoning deficit is becoming more and more urgent. The original Fiscal 1976 Budget submitted by the President was $349.4 billion, with a deficit of $51.9 billion. The subsequent mid-session review increased outlays to $358.9 billion, with a deficit of $59.9 billion. At the present time, the First Concurrent Resolution on the Budget by Congress recommended outlays of $367.0 billion with a deficit of $68.8 billion.

As is well known, deficit spending has not been an uncommon phenomenon. Past programs funded by such spending have continued with little re-examination and/or elimination of inappropriate programs. Because many of these program expenditures are openended and increase automatically with the cost of living, much of the budget outlays have been termed "uncontrollable." Since congressional action could bring an effective reshaping of the budgetary items, the term "uncontrollable" is highly misleading. We have experienced at a time of economic slack the creation of new programs that do not take full effect until a time of increased economic activity and thus go far beyond the original intent.

The new Congressional Budget Office has established a unique scorekeeping ability and well-publicized budgetary goals. However, it would be ironical if the measures introduced by Congress to assure sound budgetary practices only serve to reveal insufficient congressional fiscal discipline.

Financing a sizeable deficit might produce two damaging side effects. First, the Federal Reserve System, which normally accommodates Department of the Treasury financing to minimize money market disturbances, might be forced to increase the money supply at a greater rate than prudent economic policy would dictate. Such excessive increases in the money supply could well prove so inflationary as to discourage rather than to stimulate real business growth.

Secondly, the continuous drain of funds into government issues could cause confusion in the money markets and displace private investment precisely at a time when increasing investment is needed to expand the supply of energy, housing, the capacity of American industry, and to create additional jobs. Additional private investment is also needed to meet the mandated requirements for health, safety, and pollution control equipment, all of which demand additional capital without increasing output.

IV. EMPLOYMENT POLICY

Like the search for a perpetual motion machine, the prospect of sustained full employment in a non-inflationary environment has eluded economists and policymakers for centuries. Whether the dominant problem of the moment was inflation or unemployment, government leaders have achieved a relatively favorable mix of unemployment and inflation for only brief periods of time. The Emperor Diocletian made violations of his wage and price guidelines a capital offense, but his controls program ended in dismal failure. More recently, this Government has expended billions for income maintenance and Federal employment programs; however, the problems these programs were supposed to solve seem as intractable as ever.

While the Minority does not profess to have magic solutions for our economic problems, we do believe it is necessary to call attention to some of the ironies of current economic policy and to emphasize the need for a reordering of economic priorities. We find it distressing, for example, to find the critics of large corporations urging legislation (e.g., expensive pollution control devices) which only large corporations can afford. We also find it ironical that the Federal Government should go into the marketplace to borrow billions for unemployment programs, when this very activity forces many would-be employers out of the market.

These and other ironies would be amusing if they were not so serious, and if they did not go to the heart of our economic system and our system of government. The record shows that massive deficit spending by our Government has failed to bring us closer to the economic goals which all of us, regardless of political persuasion, earnestly seek. Something must be wrong with a system which professes to support full employment and yet predicts five million unemployed Americans by 1980; which espouses fiscal responsibility and yet is compelled to run a budget deficit which will be almost 20 percent of total outlays.

We believe that the time has come to examine seriously the basis upon which our national economic policy functions. This effort should be made not simply as an idle exercise in report drafting, but as a conscious legislative statement of policy. It is our belief, for example, that the policies of the last ten years, and many of the policies being urged on our Government at the present time, will actually inhibit employment rather than help.

In our view, the economic conditions over which the Government has some control, and which should form the basis for our policies of full employment, are as follows:

> First, business responds adversely to uncertainty, whether the uncertainty be over future goverment actions or trends in the economy. In some cases, major investment decisions can be affected. Mobile Oil Company's decision to purchase Marcor is an example of one company's response to the uncertainty of

steady, long-term profits in the oil industry. Most of the time, however, uncertainty works in smaller ways. To a businessman deciding whether to take on one or two additional employees, the uncertain course of the economy over the next two years must be some cause for restraint. For a major mining firm to decide to embark on a large-scale project involving hundreds of new employees, the uncertainty of national energy policy, and such legislative efforts as strip mining regulation, all contribute to the making of basically conservative decisions regarding employment.

Second, inflation has direct effects on employment because of shifts in income, distortions in corporate balance sheets, and subsequent deflationary policies. Rapid price increases of some products cause shifts in income, and when such shifts are not matched by shifts in spending, as in the case of the crude oil price increases, employment suffers. Corporate balance sheets get distorted by inflation figures because depreciation allowances for capital equipment do not reflect the inflated replacement costs which the corporation must incur, and because inflation unrealistically values the book value of inventories under some accounting systems. These phenomena together tend to undermine the quality of corporate profits and, according to a recent study, have an adverse effect on the level of employment of nonproduction workers. Levels of employment are also clearly affected by the restrictive policies which need to be put into effect when inflationary pressures endanger the basic health of the economy.

Third, employment suffers at a time of swiftly changing competitive conditions. When these conditions cause severe, usually regional, unemployment, we believe there is a Federal responsibility for adjustment assistance which is not yet fully met under present legislation.

Fourth, sluggish markets are synonymous with sluggish employment conditions. In this regard, the Federal Government has a responsibility for reviewing regulatory procedures which inhibit the development of new markets and for maintaining macroeconomic policies which ensure the continued growth of existing markets.

Fifth, new, sudden, major costs disrupt business planning and often constrict new employment by such businesses. To the extent that such costs shift demand to new industries, which may not be able to supply a sudden increase in demand for their products or services, inflation is exacerbated in a fashion that can only have detrimental effects on employment. The introduction of Medicare and Medicaid, and the resulting explosive increases in medical costs in this country, are prime examples of new costs being suddenly imposed upon our society. Although these costs are for goods and services which we all desire (e.g., improved pension systems, better safety conditions at work, etc.), the truth is that the trade-off between sudden costs and benefits is not fully appreciated by the American consumer. These costs, as explained above, introduced market distortions and inflationary pressures which affect employment conditions.

Sixth, an inadequate supply of capital is perhaps the single most pervasive constraint on long-term employment growth. This issue is discussed elsewhere in this Report.

With the foregoing analysis in mind, we make the following recommendations for restoring full employment. Perhaps the major contribution made by Congress in the administration of fiscal and monetary policy has been the passage of the Congressional Budget Act, and of H. Con. Res. 133, which directs the Federal Reserve System to announced target money supply growth rates each year.

Recommendation I

We urge Members of Congress to observe the limits on outlays set forth in the First Concurrent Resolution on the Fiscal Year 1976 Budget, and to limit upward changes in the Second Concurrent Resolution. A demonstration of congressional seriousness and responsibility in this regard could contribute significantly to restoring public confidence in the management of fiscal policy.

Similarly, we urge that the Congress cooperate with the Federal Reserve System in maintaining the money supply growth targets announced earlier this year. As we have stated above, we believe these targets to be reasonable under the circumstances and consistent with a scenario of steady growth and higher employment.

Recommendation II

We strongly recommend the continuation and congressional support of the Council on Wage and Price Stability.[3] [4]

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[3] Representative Rousselot opposed the establishment of the Council on Wage and Price Stability, and has opposed any extension on the life of the Council.

He states: "The very existence of the Council on Wage and Price Stability is in itself creating an atmosphere of uncertainty in the business community, and as has been pointed out previously in these Minority views, 'business responds adversely to uncertainty, whether the uncertainty be over future government actions or trends in the economy.' "

"The Council on Wage and Price Stability could provide the mechanism for a reimposition of wage and price controls, and the threat of reimposing these controls is doing immeasurable harm to the economy. This principle was labeled 'Rukeyser's Aphorism,' after the noted financial commentator, in an editorial which appeared in the December 23, 1974, edition of Barron's. It is that, 'imposing wage and price controls is one of the few vices in life that is nearly as damaging when you talk about it as when you actually do it.' The same editorial also cited an account provided by the Wall Street Journal of the steel industry's price increase: 'Many steel observers said the timing . . . may have reflected a fear that wage and price controls would be imposed next year, retroactive to January 1.' The overriding concern is controls.

"Another example of this phenomenon was provided by an article published in the December 30, 1974, issue of Barron's entitled, 'Chilled or Frozen?'. Although the article dealt primarily with the relative prospects of chilled and frozen orange juice, the article quoted one observer concerning the possibility of reducing frozen orange juice prices: 'Growers and processors are so afraid price controls will be reinstated that they'll drink the juice themselves before cutting the price.' Yet another example is the recent flood of rebates, most notably in the automobile industry, under which reductions were granted to consumers while posted prices were maintained.

"To whatever extent the existence of the Council may have a chilling effect upon the tendency of businesses to reduce prices in response to the workings of supply and demand in the marketplace, the existence of the Council must be recognized to be counterproductive." (A more detailed explanation of Representative Rousselot's views on this issue can be found on page seventeen of H. Rept. 94–389 on H.R. 8731.)

[4] Senator Taft states: "I wish to emphasize that I do not view the Council on Wage and Price Stability as a substitute for prudent fiscal and monetary policy. These are the basics of the problem. If the Federal Government is fanning the fires of inflation with one hand, it will do little good to throw a cup of water on the pyre with the other."

> While we are strongly opposed to wage and price controls, we do believe an active policy of promoting public discussion of major price and wage increases is the responsibility of the Federal Government. We believe the problem of inflation to be serious enough to require an active Federal role that falls short of controls. At the present time, the appropriation for the Council on Wage and Price Stability is $200,000 short of the full authorization, and we urge that Congress give sympathetic consideration to restoring the full authorization. We would also urge the adoption of the provision passed by the Senate which would establish three new supergrades in the Council on Wage and Price Stability, and upgrade the position of Director.

In general, we are satisfied with the provisions which exist for protecting workers from the employment effects of sudden changes in import competition. However, we believe that considerably more work needs to be done to analyze and develop policy tools for minimizing the effects on workers of sudden changes in domestic competitive conditions. Several decades ago, such tools would not have been needed, but in a quickly changing economic environment we cannot rely simply on unemployment compensation and welfare provisions as our only means of helping the unemployed who are hurt by sudden changes in markets, products, etc.

RECOMMENDATION III

> We urge the appointment of a study commission to analyze the nature of economic change in this country and to recommend new institutions and policies which can assist workers in obsolescent jobs to achieve job mobility and new skills necessary to maintain an adequate level of employment income.

We are especially shocked at the ways in which heavy-handed Federal regulation can stifle economic growth and thus damage employment. Therefore, we heartily concur with the efforts being made by the President to reform substantially the regulatory agencies such as the Interstate Commerce Commission, Civil Aeronautics Board, Federal Power Commission, etc. Our industrial history is also replete with examples of products which have been destroyed by the vacillating opinions of Federal bureaucrats. Specifically, we point to the Zerex case, the Unburn case, and the 1973–74 ban on spray adhesives. In each case, products which were initially restricted or withdrawn from the market by government rulings are now legal. Due to such blunders, products which were developed at the cost of many millions of dollars have been kept off the market for years. We urge that the current debate over Federal Government regulation take a deep look into the barriers to produce innovation currently faced by business today. These barriers, if allowed to persist, will allow only the largest firms in this country to introduce new product lines.

Finally, we believe that the time has come to face realistically the costs which we incur with the passage of the kinds of socially desirable and even socially necessary legislation which we have mentioned above. As much as this legislation is needed, its true costs have been hidden from the American public on the rather naive assumption that because no direct Federal outlays are involved, that somehow these improvements can be had free of charge.

RECOMMENDATION IV

> We believe that Congress should utilize the services of the Congressional Budget Office to require a detailed economic impact statement with regard to each piece of major legislation. In this way the American people could weigh the need for such legislation with the costs they will be required to incur.

In this chapter of the Minority views, we have shied away from some of the traditional policies being advanced to deal with the unemployment problem. Various of our Members support increased appropriations for public sector employment and a strengthening of the Unemployment Insurance Program. The purpose of this chapter, however, is to emphasize that full employment depends on a great deal more than direct Federal subsidies for putting the unemployed back on job rolls, even though the short-term problem of enabling the unemployed to feed, clothe, and shelter themselves is a clear government responsibility.

> We urge that during the current controversy over economic policy, the Congress take a responsible approach and begin to attack the long-term causes of unemployment, as well as deal with the short-term symptoms. Only in this way can we help move toward the goal which up until now has proved so elusive.

V. ENERGY

A national energy policy remains the overriding issue before Congress and the President. Despite months of discussion, Congress has failed to reach any basic agreement with the President in the broad field of energy. The President has offered both a comprehensive energy package to the Congress and a desire to compromise on a number of vital issues, including oil decontrol. Yet, the Majority Members of Congress continue to refuse to reach any agreement on more than the most minor of energy issues.

An adequate energy supply is the key to the future prosperity of the United States. Sufficient supplies of both oil and natural gas are essential, as is the expeditious development of alternative sources such as coal gasification and liquefaction, solar, geothermal, and nuclear energy sources. Government policy must provide a conducive atmosphere within which these resources can be developed.

Decontrol of oil and natural gas is fundamental to an energy policy. In particular, planned decontrol along the lines suggested by the President is preferable to the harsh economic shock of immediate decontrol.

The Emergency Petroleum Allocation Act was inadequate to curtail foreign crude oil imports and provide sufficient incentives for increased domestic production. Last year the United States consumed approximately 18 million barrels of petroleum per day, of which declining domestic production accounted for only 11 million barrels. Petroleum use represented about one-half of our total energy consumption.

It is clear that the world's oil and natural gas supplies are limited. This reality combined with our need to develop energy independence requires us to promote the development of alternative energy sources. According to the Energy Research and Development Administration (ERDA), 75 percent of the United States energy consumption is based on petroleum and natural gas, with coal providing less than 20 percent of current needs although it represents about 80 percent of the Nation's present energy resources. Enhanced recovery technology and alternative sources must be more fully developed and utilized as quickly as possible.

Recommendation V

> It is recommended that tax incentives, additional research and development programs and loan guarantee programs should be enacted in order to promote the development of more sophisticated recovery technology of present resources and to develop alternative sources.

Congress should be careful in adopting tax reform measures in order to ensure that these reforms do not discourage energy production. Tax incentives for home and business use of solar and geothermal energy would assist in making these energy alternatives price competitive. In addition, Congress should take steps to clarify the issue of whether depletion allowances and the write-off of intangible drilling costs apply to geothermal energy, so the way can be cleared for further utilization of this source.

To enhance the ability of the private sector to engage in synthetic fuels and renewable resources utilization, a broad loan guarantee program should be established for the construction and operation of commercial facilities. Special efforts should be taken to assure the involvement of small businesses in the expanding energy field. Voluntary programs to enhance industrial energy efficiency should remain a high priority, as should the education of the general public on conservation methods in all forms of energy utilization.

As they have for the past two years, utilities will continue to suffer from high fuel cost increases and difficulty in financing new construction for additional generating capacity. Consumers will be faced with higher rates, even as coal conversion takes place, due to continuing high cost of emission controls and the high cost of maintaining peak-load capacity. To make power users more aware of actual service costs, strong consideration should be given to the encouragement of various pricing methods to even out power damands during the course of the day. Hopefully, both industrial and residential users will adjust their demands accordingly, resulting in a significant reduction in peak period damands.

The capital requirement for energy resources during the next several years is enormous. The Administration has estimated that capital requirements for energy over the next decade will total about $1 trillian. While other studies vary somewhat from this figure, each one proclaims similar investment needs. Because the pressure for capital investment in other sectors is equally as great, determination of priorities should be recognized by Congress and appropriate policies decided.

In conclusion, we again stress the need for immediate action by the Federal Government to develop a comprehensive energy policy. The President has offered proposals and demonstrated a willingness to cooperate with Congress in constructing a energy program. If we are serious about gaining energy self-sufficient, difficult decisions must be made concerning deregulation of oil and natural gas as well as incentives for massive investment of new capital into the energy industry.

VI. CAPITAL FORMATION

While short-term economic issues are predominately under consideration, one long-term issue—inadequate capital formation—is garnering an increased amount of attention. It has been asserted that the rate of capital formation in the United States compares unfavorably with that in other countries. If this is an accurate estimate of the situation. the consequences may mean a less productive United States economy with low job expansion and gradual loss of technological leadership.

The use of various statistics, the amount of investment relative to GNP, the pattern of retirements and replacements, etc., have been utilized to show a low rate of capital formation relative to historical levels and current levels abroad. Since this area potentially represents a large claim on United States resources, it is imperative that this matter be carefully studied. It is becoming increasingly apparent that our resources are limited, whereas the many claims from various economic sectors, including energy, seem to be inexhaustible. As it will take time to formulate and adopt policies which will encourage additional investment, it is not too early to determine whether or not this use of funds should receive priority over other pressing claims.

SUPPLEMENTAL VIEWS OF SENATOR JACOB K. JAVITS

I find myself unable to reach substantial agreement with the views of either the Majority or the Minority. Therefore, rather than sign either report, I present my own views on these most important economic matters of concern to our Nation.

I must state at the outset that I cannot view with complacency the prospects for economic recovery. Beginning in the last half of 1975, the "wait and see" approach has been closely linked to those attitudes primarily responsible for the sluggish nature of the recovery. I agree that we must be vigilant lest a new round of inflation defeat our hard-won efforts to restore some measure of economic growth, but the constant brandishing of the inflation specter at the least hint of additional efforts to stimulate the economy makes one ask whether the inflation threat is now being used as a means of defeating social measures badly needed to reduce unemployment and provide aid to many nearly bankrupt cities.

Although the Minority mentions the role of food and fuel price increases in its discussion of renewed inflation, it wants to deal with this problem through restrictive fiscal and monetary policies. The lessons of the last few years make it clear to me that such a course of action will only choke off economic recovery. Without legislative actions to substantially moderate food and fuel price rises, we shall continue to hold back economic recovery even while inflation may increase.

It is also time to recognize, as I discuss in geater detail later in my views, that the size of the current Federal budget deficit is the result of economic recession, not the cause of it. The best way to reduce the budget deficit is to restore "full" employment and greater utilization of our industrial capacity. This policy would result in lower welfare and unemployment compensation payments and increased tax revenues.

Both the Majority and the Minority members of the Committee agree that the present recovery is a fragile one. However, there is legitimate disagreement as to whether any further policy actions are needed to support the buildup and continuance of this recovery. In this respect, I do not believe that the Minority position goes far enough to assure that we will reduce the unacceptably high rate of unemployment. I cannot believe that we must accept unemployment of 7.9 percent by the end of 1976 and 7.8 percent by the end of 1977.

As a part of the program to provide anti-recessionary manpower measures, I have studied the Local Initiative Program (LIP) sponsored by the Canadian Government, which the Majority also have viewed favorably. A great many of the features of this program are deserving of further consideration, and consequently I am preparing legislative proposals along these lines.

A new manpower initiative to create more jobs must be undertaken. In reviewing various anti-recession alternatives, the Congressional

Budget Office evaluated public service employment as the most effective measure to deal with the problem of unemployment, with the least risk of adding to inflation. Where the present manpower programs have emphasized the traditional targets of the long-term unemployed and economically disadvantaged, these should be continued and expanded. But the need for a job creation program for all those without work through no fault of their own, including those with employable skills, must be underscored; and I recommend funding for 1,000,000 public service jobs. The idea of projects limited in time and objectives that provide new jobs without becoming a permanent feature of regular job training programs is an innovative approach that merits support. This approach is preferred to a deeper tax cut—I want the present one continued for a year—as the impact of a tax cut on job creation is peripheral, and the effect on employment can only be indirectly felt. To ask for an expanded manpower program and also an additional tax cut at this time would perhaps add unnecessary fiscal strain on the Federal budget, and I shall pursue the former—plus continuing the 1975 tax cut—as the more effective approach at this time.

An incomes policy can play a substantial and beneficial role in the present economic environment. While the advice offered by the Majority seems strong medicine, there is a necessity for voluntarily negotiated price restraint on the part of big business as well as cooperation in limiting the demands of major wage settlements. It would be helpful in this connection if Congress would renounce clearly any intention to return to mandatory controls so that business and trade unions will know that the proposed policy is truly voluntary and that no further action is contemplated. In such an atmosphere the Council on Wage and Price Stability should be strongly encouraged to increase their efforts in trying to stem any inflationary pressures which may emerge from the heavy calendar of wage negotiations in 1976.

As for the views of the part that monetary and fiscal policy play at the present time, I diverge in several important respects from both the Majority and Minority positions. I fully concur with the Minority members that the extension of the Tax Reduction Act of 1975 should be enacted. Enactment of the extension will ensure the continuation of individual purchasing power at its current level. Rising prices and the possibility of the deflation of consumer confidence offer persuasive arguments against the occurrence of what would in effect be a tax increase at this time.

However, the course of the recovery at the present time would seem to rule out the necessity for an additional tax cut of the size proposed by the Majority. This does not mean that a further tax reduction is to be ruled out completely. If the recovery weakens in early 1976, I hope that Congress would remain flexible enough to reconsider this possibility. At the present time, I believe that the expanded job creation program discussed above and countercyclical grants to State and local governments now presently proposed will be of sufficient stimulus. We should also be prepared to counteract the loss in disposable income as a result of policies that produce higher energy prices.

It is important, too, to have a clear understanding of the role monetary policy plays in the current economic situation. A resumption of restrictive monetary policy has the potential to stop the recovery in its tracks. The decision of the Federal Reserve System in June to raise target rates on Federal funds had the effect of halting the growth of member bank reserves and directly contributed to the run-up in short-term interest rates throughout the summer and fall. Such a restrictive monetary policy coming while the recovery is still in its infancy is unjustified. The Federal Reserve System must be concerned about output and employment targets as well as interest rate and monetary aggregate targets. (However, I cannot agree with the Majority proposition that the Federal Reserve System should be required to present monetary targets that are consistent with congressionally determined targets of output, employment, and purchasing power.) The Federal Reserve System must follow more expansionary monetary policies than it has heretofore indicated in terms of its goals for the monetary aggregates. I recommend a policy stance that guarantees growth of the real money supply, i.e., the money supply adjusted for price changes, consistent with vigorous economic growth and a return to full employment. In this vein, it is important to point out that the size of the Federal budget deficit is not the primary cause of rising interest rates. Overly restrictive monetary policy has slowed the growth of bank reserves, driven up interest rates, and jeopardized economic recovery. The current budget dificit is a result of the underlying economic recession, not a cause. The Federal deficit will not be reduced until economic recovery restores full employment and full utilization of our economic potential. To the extent that tight monetary policies continue in 1975 and 1976, economic recovery will be painfully slow and the Federal budget deficit will persist. For these reasons, monetary policy must be made more expansionary so that economic prosperity can bring both full employment and higher tax revenues from increased business activity.

No discussion of the economy can be complete at this time without a discussion of the problem facing America's cities. America's cities—and New York City is simply the tip of the iceberg—are in a precarious financial condition today because of population trends, the effects of recession, and the crippling effect of sharp cost increases which are not matched by increases in tax revenues.

The financial and economic aspects of the urban problem have become important enough to warrant Federal action. At the present time, for example, the effective interest rate on municipal bonds is at an all-time high, even though similar, taxable issues have backed off from historical highs. While some of the reasons for high interest rates can be traced to general economic conditions, evidence exists that a substantial factor in the tax-exempt market is the reluctance of investors to commit themselves under the uncertain conditions imposed by the New York City situation. These uncertain conditions affect even cities in relatively sound condition, so that they are forced to incur considerably higher debt service cost than under normal conditions.

With regard to New York City itself, the consequences of Federal inaction could be a major deterioration in the City's ability to provide basic services. Already, the City has been forced to make substantial cutbacks in employees, and to reduce drastically the operating hours of certain City facilities. A further cutback in City services can only exacerbate the major unemployment situation which exists in the City and accelerate the social and economic trends which have brought the City to its present position.

I recommend the following Federal initiatives in order to restore a proper fiscal balance to New York City and other cities which qualify across the country:

RECOMMENDATION I

The Federal Government must institute an effective program of countercyclical grants based on unemployment to State and local governments. This recommendation, which is embodied in S. 1359, currently in Conference, will help reverse the roller coaster effect on local government revenues from changes in the business cycle.

RECOMMENDATION II

The Federal Government must establish a loan guarantee facility for cities *in extremis*, and to State-chartered corporations whose purpose is to provide access to financial markets by such cities. Such a loan guarantee program should be available only as a last resort, and only if the loan guarantee facility finds that proper safeguards have been instituted to ensure the seasonable repayment of the loan and the financial integrity of the city.

RECOMMENDATION III

The Federal Government should establish an Insurance facility with a suitable premium so that investors in tax-exempt government securities will have protection similar to the protection afforded depositors by the Federal Deposit Insurance Corporation (FDIC) or brokerage customers by the Securities Investor Protection Corporation (SIPC). Such a facility would widen considerably the market for municipal securities, and thus compensate for the mismatch of supply and demand in the tax-exempt market which has taken place in recent years.

Legislation which I introduced last May (S. 1833), and which I have amended recently, follows through on the last two recommendations. In my view, this is the minimum which the Federal Government must do as a means of ensuring the continuing viability of our Federal system of government, a continuing market for municipal securities and the integrity of our economic system.

Nine months after the crystallization of the energy issues facing us in the President's State of the Union message, we are still unable to agree on the basics of a permanent energy policy, even though there is a consensus that the status quo is intolerable.

I set out a detailed itemized program for Federal action on energy in the last Annual Report. I stand by those concepts, and believe they continue to provide us with a program acceptable to a majority in the Congress as well as the Administration.

Chief among those concepts was the idea of a five-year phase out of oil price controls—something that is beginning to win support. Com-