

In a study for the CED¹⁷ Professor Eckstein noted that the effect of inflation is likely to be a reduction in the real value of Government budgets. For as inflation proceeds, it would take some time before the Government would appropriate sums or spend sums that would reflect the inflation. There are certain institutional delays involved here, even if the Government wants to achieve a stable level of real governmental expenditures. Because of the money illusion, of course, there might well be a tendency for the Government to cut real expenditures more or increase items less rapidly than otherwise would be the case just because of inflation. Contending that the response of taxes to inflation would be more prompt and effective than the rise of expenditure, Professor Eckstein concludes that, on the whole, inflation tends to improve the state of the budget rather than the reverse. This generalization, however, does not apply to State and local budgets.

Dean Bach contends that the major gains of inflation are obtained by the Government and the large losses by the public. Over a period of about 20 years he calculates "that * * * over \$500 million inflationary erosion of real purchasing power of creditors over the period" has occurred. Since—

householders have consistently been heavy net creditors and governments (especially the Federal Government) consistently net debtors, inflation has caused a huge transfer of purchasing power from households primarily to the Federal Government.

Since the Government debt is not likely to be repaid in the foreseeable future, Dean Bach argues that the real gainers of the reduced real cost of financing the debt are not the taxpayers but the nonbondholders, who are therefore able to increase their share of total output as their incomes increase with inflation. Government bondholders and money holders are partially expropriated by inflation, and the benefit is distributed over the whole population, with the biggest benefit for those who buy the most. All households, according to Bach, hold about 30 percent of their total wealth in the form of fixed dollar value assets, but they are in debt up to only a little over 10 percent of their total wealth.¹⁸

We should note, however, the distribution of Government securities. At the end of 1958, of the \$283 billion outstanding, commercial banks inclusive of the Federal Reserve banks held 33 percent, U.S. Government investment accounts held 19 percent, and other investors held 48 percent. In the last category individuals held 23 percent, State and local governments, miscellaneous investors, and corporations 6 percent each, insurance companies 4½ percent, and mutual savings banks 2½ percent. Obviously, individuals experienced the largest losses from inflation, particularly if we assume that the holdings of the banks really belong to the depositors. Of course, to some extent the holders of equities in banks would suffer, though insofar as their profits responded to inflation or gained from it this would not be true. Government itself was also a very important loser, especially in view of the fact that the excess profits of the Federal Reserve belong to the Gov-

¹⁷ CED, "Trends in Public Expenditures in the Next Decade," April 1959, pp. 8, 9.

¹⁸ Joint Economic Committee, "The Relationship of Prices to Economic Stability and Growth," compendium of papers submitted by the panelists appearing before the Joint Economic Committee, 1958, pp. 41-42.