

The only thing the United States can do now is to use every possible measure it can to maintain its own domestic stability. It will simply have to ignore the balance of payments if we get into a serious depression, and it will have to pay attention to it if we undergo serious inflation, in the interests of world stability and preserving the system.

The problem now is that in this transitional period, with respect to current measures to stop the inflation, we run a great risk. The risk comes from the fact that in the past 2 months monetary policy has slammed on its brakes, and there has been a great squeeze in American capital markets. Credit is extremely tight, and this has already begun to have some effects in toning down the expectations about proper spending for 1967 of big business companies.

The results of this tight-money policy in July and August 1966 are going to be felt in 1967, and they are going to be substantial. They can hardly fail to be felt.

There has been no monetary contraction in the past 15 years that corresponds to what has gone on in the past 2 months. First we went too fast, then we went too slow. That was a mistake, because you shouldn't make abrupt changes in monetary variables. Policy has to move slowly.

Now if, on top of this, the authorities panic by looking at a continuing rapid rate of inflation in the United States, they may end up fighting the wrong danger. The tight-money policy may have already been enough to jerk the economy onto a stable growth rate again. Additional fiscal measures at this time, while they were completely appropriate 6 months ago may be quite inappropriate now.

I believe that strongly restrictive fiscal or monetary measures pose a real danger to the economy at this time. Great uncertainty has been created by the about-turn in monetary policy, there is uncertainty about what is going to happen to fiscal policy, and there is also the enormous burden that is on the British balance of payments this autumn. And next year, these problems, on top of the gold problem and increased gold hoarding, pose serious danger for the whole world economy.

Chairman REUSS. Mr. Salant?

Mr. SALANT. Mr. Chairman, I didn't have the impression that Professor Despres was as complacent about the situation as Professor Mundell indicated, and I would like to see that cleared up. I also didn't have the impression that his view of what was required was simply a change in the U.S. attitude without any corresponding action resulting from that change. I hope he will be given an opportunity to answer that question.

I think what Professor Mundell has just said about the dangers of fiscal restriction, as I understand it at least, is based on the assumption that we are in for the effects of monetary restriction, that these will be felt in the future, and that as a result of adding fiscal restrictions to it, we will have too much restriction.

I would assume that some of this fiscal restriction that is intended as a result of the President's announcement yesterday, his recommendation specifically that the investment credit be suspended, and his statement that he will try to reduce Government expenditures, is intended to replace some of the present monetary stringency, and so I think Professor Mundell's view would be justified only if it were clear, which it is not to me, that it is too late to undo some of the effects of what may have been excessive monetary restrictions.