assets—will have the effect of reducing the deficit, especially in fiscal 1967.

Budget Policy in Calendar 1966: Economic Effects

The above facts and figures on the Federal budget have important implications for economic stability in coming months. To assist in the understanding of these implications, some basic principles of economic analysis are reviewed. This framework is then used to analyze the administration's fiscal plans within the economic setting expected in calendar 1966.

The following section presents a theoretical framework for analyzing the effects of the Federal budget on the level of economic activity. Also, the terminology used in later sections of this article is introduced here. The reader who is not interested in the analytical framework may proceed directly to the next section, "Economic Setting."

ANALYTICAL FRAMEWORK [6]

The level of economic activity is determined by the saving and spending propensities of households, businesses, governments, and foreigners.[7] The most comprehensive measure of economic activity is gross national product (GNP)—the total value of final goods and services produced in a given time period. GNP can be measured by summing all expenditures or by summing all incomes. All production can be thought of as being bought; thus, the total product can be measured by gross national expenditure (*GNE*) on this product. Similarly, all production has income charges against it equal in value to what is produced; thus, the total product can be measured by gross national income (*GNY*). This definitional relationship between total product, total expenditure, and total income can be expressed as follows (where triple bar, $\equiv$, means "identically equals"):

$$(1)\quad GNP \equiv GNE \equiv GNY$$

Gross national expenditure (*GNE*) can be divided into its major components—consumption (C), investment (I), and government purchases (G). Gross national income (*GNY*) must be allocated to consumption (C), savings (S), and taxes (T). Equation (1) can be rewritten, expressing *GNE* and *GNY* as the sum of their components:

$$(2)\quad C+I+G \equiv C+S+T$$

where:

- C=personal consumption expenditures;
- I=gross private investment;
- G=government purchases of goods and services;
- S=gross private saving;
- T=net government receipts.

Both *GNE* and *GNY* contain consumption (C). As a part of *GNE*, consumption is spending on consumer goods and services. As an allocation of *GNY*, consumption is that portion of income spent on

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[6] This section draws heavily from Robert Solomon, "A Note on the Full Employment Budget Surplus," *The Review of Economics and Statistics*, XLVI (February 1964), 105-108.

[7] All terms are defined so as to be consistent with the national income accounts framework. Investment is defined to include gross private domestic investment and net foreign investment; private saving includes both personal and business saving; government purchases are for Federal, State, and local governments; and net government receipts are essentially taxes net of transfer payments.