

There will, of course, be a large volume of security issues in the second half of this year as in the first, but the pressure from these issues should not be exaggerated. The volume of Treasury issues will increase; but the effect of those issues will be partially offset by a large reduction in corporate sales of Treasury securities to finance tax payments.

To keep security markets in balance commercial banks must, of course, have sufficient resources to purchase a substantial volume of securities as well as to accommodate loan demands. The needed resources should be available if the Federal Reserve continues to supply adequate reserves to the banking system. There will be no need for a turnaround in monetary policy if fiscal policy provides the restraint needed to prevent an excessively rapid growth of demand.

THE ROLE OF FISCAL POLICY

The state of economic activity reflects the interaction of private demand and public policy. Underlying the current strengthening of demand in the various sectors of the economy is the impact of the strongly expansionary fiscal monetary policy that has been pursued in the first half of 1967.

There has been a marked and appropriate shift toward stimulus in policy this year. In 1966, fiscal and monetary restraint helped to brake an economy that was going too fast. Much of the fiscal action of last year was temporary in its restraining character, and is no longer holding down the economy. An increase in payroll taxes of \$6 million a year preceded the initiation of medicare benefits and contributed a large restrictive fiscal impact, but medicare benefits have since risen to their full program level. The graduated withholding system for personal taxes drew off a substantial volume of consumer purchasing power in 1966, but this spring it was actually a significant expansionary force because of the lower tax liabilities left over on 1966 incomes. The suspension of the investment credit had an important shortrun impact on capital goods demand, which has now been removed by its restoration.

These changes were reinforced by a further large increase in defense outlays and by the automatic downward effects on revenues of the sluggish pace of the economy. Together, they have brought the Federal budget from its balance of 1966—national income accounts basis—into deficit at an annual rate over \$10 billion in the first half of 1967.

New restraining measures have not been called for now because the economy has been sluggish. The expansionary fiscal policy, reinforced by a stimulative monetary policy, fits the economy's needs while inventories are adjusting, while consumers are saving at an unusually high rate, and while the level of homebuilding is still abnormally low. But a large Federal deficit at high employment and an expansionary monetary policy would, in combination, become excessively stimulative as the temporary weakness in private demand gradually wears off. New policy restraints will be needed to take the place of those that operated last year. In terms of economic impact, fiscal restraint could, in principle, come from cutbacks of expenditures