

restraint was relaxed and policy turned promptly toward encouraging increased flows of money and credit.

The timing of changes in policy, as well as the degree to which policies of restraint or ease may be carried, are necessarily matters of judgment. There is still much to be learned about economic stabilization policies, both fiscal and monetary, in a high employment environment.

Nevertheless, the difficulties encountered should not be allowed to obscure the rapid and favorable response of the economy to changes in the direction of monetary policy. For example, since indications of abating inflationary pressures last fall made it possible for monetary policy to be redirected toward ease, interest rates have come down swiftly, with some rates already below their levels of a year ago; bank credit has expanded at a vigorous rate; inflows of savings to thrift institutions have picked up very substantially; the housing outlook has brightened considerably; and resumption of more orderly and balanced economic growth is in prospect. The experience of the past year and a half should serve as a warning against underestimating the resilience or responsiveness of the U.S. economy.

Nor should we overlook the substantial gains recorded by the economy last year, despite our valid concerns for those sectors of the economy that did not share fully in the advance. The year 1966 was one of considerable economic achievement. Our gross national product rose by 5½ percent in real terms, well above the long-term growth trend. More than 3 million workers were added to the Nation's payrolls, and the capacity of our factories grew by almost 7 percent. Moreover, for the first time in over a decade, the United States was able to achieve substantially full utilization of its growing resources. Unemployment fell below 4 percent, the lowest level since 1953. And unutilized industrial capacity declined to the lowest level since 1955. This was an impressive performance, one in which we all can take some satisfaction.

But the record was not unblemished. Indeed, in pushing forward under forced draft, some serious strains and distortions emerged in the structure of production, finance, and our balance of payments—flaws, which if not corrected, could seriously hamper our ability to sustain rapid economic progress. Let me touch on the most important of these, for there are lessons to be learned by policymakers in all branches of Government from the failures as well as the successes of economic policy.

First, as we approached full utilization of resources, demand pressures manifested themselves in a strong and pervasive rise in costs and prices. In an economy where many wage contracts are geared to cost-of-living changes, yesterday's price increases become tomorrow's cost pressures. It may prove difficult to avoid, in 1967, some reflection in costs and prices of the failure to restrain adequately the inflationary pressures of 1966.

Second, the excessively rapid pace at which domestic demands grew meant that they could not be satisfied from domestic sources alone. Our imports of materials and finished goods—particularly capital goods—surged. And although U.S. exports continued to rise somewhat faster than their long-term uptrend, our favorable net balance on international trade was seriously reduced—by almost one-fourth.