Mr. MARTIN. I would think that if it is possible to reduce expenditures, it would be equally satisfactory. I do think there is the psychological point of paying for the war in Vietnam, which at some time ought to be considered. It seems to me that we have to pay for those expenditures in one way or another.

Chairman PROXMIRE. Of course, we can pay for those expenditures by making sacrifices in other programs.

Mr. MARTIN. In other programs, and if that can be done, that would be equally satisfactory. You either have to reduce expenditures or increase taxes to deal with the problems that, seem to me, confront us.

Chairman PROXMIRE. Now we are moving into a different kind of an economic situation in 1967 than we had in 1966 in economy. The indicators, which were very expansive in early 1966, seem to have leveled off a great deal. This is true of automobiles. It is true in many other areas of industry. Inventories are high in relation to sales and so forth.

Under these circumstances, I wondered what emphasis you would put on the fact that the monetary policy is a mixed tool. It is more subtle and sophisticated than many of us realize. I know you understand that fully.

What I have in mind especially, is the impact of tight money in pushing up some aspects of cost last year. The report of the Council of Economic Advisers says the following:

> Mortgage interest rates, which had remained quite stable in preceding years, rose by 12.4 percent in 1966 alone. As shown in table 4, these higher financial costs accounted for were one-third of the total advance in the prices of services during 1966.

Now in view of the fact that services was the biggest element along with food increases, in prices in 1966, in view of the fact that it is clear that monetary policy cannot restrain demand in food, we don't eat less because interest rates are higher, doesn't it seem that even in 1966 that the impact of tight money in keeping prices down, which I agree the net overall was positive, may not have been as clearly deflationary as has been argued by some?

Mr. MARTIN. Well, it was not as satisfactory as we would have liked it to be, of course, but I think it is important for us to concentrate on the future rather than the past.

Chairman PROXMIRE. Yes. Go ahead.

Mr. MARTIN. But I would just like to put this in the perspective as I see it, which is that it seems to be that we would have been wiser if we had been following a more restrictive monetary policy from mid-1965 on. Also, if we had reduced expenditures and increased taxes, we would have had a better and smoother flow of funds through the economy than we have had.

Chairman PROXMIRE. But the fact is, when your Board does tighten credit, it does have the effect of pushing up the cost of borrowing money, pushes up the cost of mortgage interest and other borrowing costs which are an element in cost. At the same time it does restrain demand and lessen pressure elewhere. The reason I have asked this is because it has a great deal of pertinence for the future.

It is my understanding that in the present economy we have pressures on demand, and in the coming year more likely cost pressure on