

BALANCE OF PAYMENTS POLICY

The recent dramatic drop in our short-term interest rates and the narrowing of the differential vis-a-vis Europe has exposed us, in the opinion of many experts, to the danger of a larger balance-of-payments deficit this year. Yet, this and last year's report relegate the question of our continuing payments deficit to the last chapter, unlike the 1965 report which featured our payments problem. Recent developments have also presented the Federal Reserve once again with the dilemma whether to moderate its domestically oriented credit-easing policy for balance-of-payments reasons or to run the risk of worsening our payments position by easing credit further. But there is little if any discussion by the Council of the appropriate monetary-fiscal mix that it considers necessary to minimize both domestic recessionary tendencies and the payments deficit this year.

Instead, there is a less helpful discussion of the responsibilities of other nations (p. 189) to "adopt measures to neutralize their 'windfall' foreign exchange gains," measures to achieve consensus on balance-of-payments adjustment policies, and measures to achieve international monetary reform.

To be sure, efforts to enhance international monetary balance-of-payments cooperation deserve support. But by the same token, in appraising our payments problem and devising courses of action to right the payments balance, particular effort should be made to avoid ad hoc measures resulting in undesirable restraints or controls on the free flow of trade and credit.

There is little dispute that many elements enter into determining the international flow of capital; that the flow is affected by factors other than a shortage of real capital; and that the flow does not occur "always and automatically in just the economically 'correct' amount" (p. 189). In refuting such contentions, however, the Council may well be knocking down strawmen.

The unpleasant fact is that since 1961 the Government has advanced only ad hoc measures to cope with our payments problem; it has lacked a clear policy regarding the range of responsibilities which have come to the United States in its role of international banker; it has resolved the growing burden of defense responsibilities by measures perpetuating so-called temporary and voluntary restrictions on export-earning private investment, and it has relied far too heavily on monetary measures and too little on fiscal measures to offset overheating of the U.S. economy.

As a result, this year, when facing the danger of a larger deficit despite many ad hoc measures with adverse effects on long-run prospects for free flow of capital, the Council also faces at home declining productivity, rising unit labor costs, and labor unions bent on wage settlements beyond productivity gains.

The real issue is whether the Council gives full recognition to the dangers of unduly prolonging restraint upon the kind of investment, foreign or domestic, which is a major stimulus to exports. Guidelines, when perpetuated year by year, freeze old patterns of investment and export expansion that may be belied by dynamic growth patterns. Such guidelines likewise gain a status quo which it becomes easier to defend than to replace with long-term measures reflecting full recogni-