proposed by the Administration. Their error is not by a wide margin, but by one sufficient to make their recommendations in the fiscal area inappropriate for dealing with the economic problems of 1967.

It will be recalled that the forecast of 1966 gross national product set forth in the Economic Reports of a year ago fell about $10 billion short of what actually occurred. This does not seem a very large error in a $740 billion economy. Yet it made an important difference in the tone and character of the economy in 1966, and in the fiscal policies appropriate for it. Instead of the anticipated stable non-inflationary growth, we had a sharp spurt of unsustainably rapid growth through most of the year followed by a noticeable slow-down toward the end. The Administration's failure to perceive the need at an early stage for a posture of greater fiscal restraint contributed to making 1966 an inflationary year.

This is mentioned only because we fear that the Administration's expectations for 1967 may be similarly in error, *but in the opposite direction.* Our reasons for this conclusion will be presented in greater detail later. It does carry the implication that a year in which the economy will have to adjust to a slower rate of growth is not the year in which it is wise to impose a general increase in income tax burdens.

But there is a larger question to be raised in regard to fiscal policy. It is not merely a device for making short-term adjustments in the economy. It is the means through which fundamental choices are expressed—choices as to how much government, and what kind of government programs, the nation will have. It is a matter of establishing priorities, both as between the government and the private sector and as between various government activities.

The Council of Economic Advisers discusses this matter of priorities, but without ever quite bringing their analysis to a head. And none of us should approach this subject in a doctrinaire way, since value judgments are involved that only the American people as a whole are entitled to make.

Nevertheless, we find it hard to believe, in examining the fiscal record of recent years, that it can possibly represent the true priorities of the American people. We do not believe that the large expansion of federal nondefense programs is in line with the deliberate choices the population would make in allocating the productive resources of the nation to government purposes. We fear that a tax increase in 1967 would validate and confirm this past trend and encourage its continuance in the future. Our specific reasons for this conclusion will be explained later.

In the area of wage-price developments the Council points out that, in 1965 and 1966, inflation resulted from the adjustment to a rapid increase in demand. It goes on to say that, although this is over, ". . . forces were set in motion which will continue to push up prices for a time." In other words, the inflationary problem in 1967 will be of the cost-push variety.

In this we believe that they are right. But it raises the question of whether a tax increase is the proper means of checking such an inflation. Tax increases seem more likely to strengthen the cost-push factors than to weaken them or offset them.

It might be thought that this would be the year, above all others, in which the "guidepost" approach would be most necessary. The Council has chosen this year to make a partial retreat from its former position. It reiterates its view that productivity growth still establishes the non-inflationary limits on the upward trend in wages, but in a context that suggests that it cannot be taken too seriously in 1967.

The NAM has viewed a setting-forth of the wage-productivity relationship as a helpful educational tool in promoting public understanding of the effects of wage settlements. We have always had reservations as to the desirability of using wage and price "guideposts" as a basis for various forms of government intervention. We hope that the retreat of the Council in this field will not too seriously impair the educational value of the productivity criterion. We also hope that it signals an intention to use whatever remains of the "guidepost" approach in an advisory rather than a coercive manner.

Additionally, the Council's urging that industry reduce its profit margins on a wide scale seems to us unrealistic and uncalled for. It is an arbitrary judgment rather than a conclusion drawn from any basic principle.

One economic objective of the Administration, which is emphasized more than any other in its economic reports, is the further reduction of interest rates. This is an aim with which we can sympathize—manufacturers do not like to pay high interest costs any more than anyone else. But it is an objective that must be considered from all sides.