headway can be made during that period in bringing down the present excessive rate of inventory accumulation. A postponed adjustment would have to be all the greater and longer lasting.

Inventory movements are large relative to other changes in spending outside the consumer area. Neither plant and equipment spending nor housing, nor even Federal spending, is likely to experience quarterly changes in annual rates exceeding $5 billion, but inventory spending may well do so. Resting as it does upon a questionable appraisal of the most volatile factor in the ceonomy, the Council's GNP estimate must be regarded with serious misgivings.

A further question relates to the recovery of housing. Substantial easing of monetary policy is required to get residential construction going again. Whether this ease will be forthcoming depends on capital flows in the balance of payments that are partly dependent on interest rates abroad. A question mark needs to be entered after the Council's housing forecast.

There remains the possibility that Vietnam expenditures will again be larger than anticipated. If indeed the pattern of 1966 should repeat itself, the Council's forecast will be valid at a minimum and a tax increase will be needed. There is no way, for an outsider, of appraising this prospect.

Adding up the components of the outlook, I am compelled to question the need for a tax increase even at midyear. Certainly it is wise to postpone its enactment until close to the beginning of the fiscal year. On present reading I would not believe that it should be enacted even then.

Spending Cuts

Even if inflationary pressures should mount sufficiently to require counteraction, expenditure cuts would present an alternative to a tax increase. Federal expenditures in the NIA budget, including for Vietnam, are scheduled to reach 21 percent of GNP, contrasted with 18 percent in recent years. After this as after any other war, expenditures are unlikely to return to their earlier GNP relationship. Hence the case for holding them down now is a good one if economic balance calls for restraint.

The quite unjustified view seems to have gained ground that cuts must necessarily and virtually exclusively fall upon the new programs in the areas of space, education, poverty, health, pollution, urban life, and the like. Clearly, almost all Federal expenditures are capable of being cut. The fact that a program has been going on without much change for many years seems more nearly a reason for examining it closely than for leaving it undisturbed. It may be more diffult to cut an old program than to block a new one, but it may not be better economics.

Tight Money in 1966

The Economic Report indicates, correctly in my view, that in 1966 monetary policy went about as far as it could. Interest rates reached levels not observed for 40 years. The housing industry was seriously injured. Some observations to qualify these facts nevertheless are needed. Interest rates must be viewed with respect to changes in the price level to obtain what economists call the real interest rate.