

One current cost in 1966 is the inequity of inflation, with its especially severe impact on those with fixed or lagging incomes. Another current cost resulted from the effect of tight money on State and local governments, which found their borrowing activities seriously curtailed, and on those industries which rely heavily on credit to finance their operations and/or sale. Homebuilding is an important, although not the sole, example of this latter group. Still another current cost is the \$3 billion increase in Federal spending in fiscal 1967 which, according to Government officials, was a result of stringent monetary conditions in 1966.

It is clear in retrospect that the period beginning in mid-1965, when the war in Vietnam began to escalate sharply, and extending well into 1966 involved a variation of "forced saving" in the classical inflationary sense. Federal tax revenues were not large enough to command the transfer of real resources necessary for the war effort. Deficit financing had to be used and, with near-full employment, price inflation was the result. This inflation, coupled with the impact of tight money on groups vulnerable to tightening credit conditions, "forced" the real saving necessary to release resources sought by the Federal Government.

These can be viewed as the current costs of inappropriate policies in 1966. The future costs, although less easy to identify, may be even more significant for the performance of the economy. They stem directly from the imbalances generated by the demand-pull inflation of an overheated economy.

OUTLOOK FOR 1967

These imbalances have led to more than the usual disagreement among economists concerning the outlook for 1967. Although a "standard forecast" of "weak first half, strong second half" appears to be developing, there is still a significant minority of observers who expect, if not recession, at least a distinct pause in the pace of economic growth this year. This view, bolstered by the clear diminution in the strength of private demand in recent months, calls for caution in carrying out economic policies in the months ahead.

The American Bankers Association believes 1967 will be a year of rising economic activity, but with perhaps much greater strength of private demand in the final 6 months than in the first half. Still, the arguments of those who foresee the end of the long economic advance should not be ignored. In part, their position reflects concern with the most significant short-run imbalance of 1966; namely, the high rate of inventory accumulation, which reached its peak in the final quarter. If the inventory situation were the only factor, the continued strong uptrend in Government spending (barring an end to the Vietnam conflict) could be expected to soften and shorten any adjustment. This view supports the standard forecast.

But there are in addition deep-seated imbalances which, if not corrected, will continue to threaten the longrun sustainability of the economic advance. The most important of these imbalances is reflected in the tendency for total labor compensation to rise much faster than output per man-hour. Stability in unit labor costs of production—the mathematical result of equal percentage increases in total labor compensation and output per man-hour—has been a major factor account-