

even though the relation between monetary policy and such prices is indirect. Assuring owners of these resources that, in the aggregate, they were free to press for whatever rates of remuneration they might choose, without fear of the discipline of restraining stabilization policies, would open the door to a never-ending round of cost-price increases.

Even if the establishment of this principle were desirable, however, it could not be made operational. Rates of price advance cannot be decomposed into cost-push and demand-pull elements, except arbitrarily. Businesses do not alter prices in response to cost changes, irrespective of the state of current demand. Neither do pricing policies respond to changes in demand, irrespective of costs.

The performance of prices during 1967 attests to the intermingling of demand and supply effects in price behavior. Unit costs in manufacturing were rising quite early in the year. But with aggregate demands sluggish in the first half, these cost pressures did not result in a significant advance in industrial commodity prices until after midyear. It was not until demands for goods and services picked up in the second half of 1967 that increases in unit costs that businesses had incurred earlier—and were still incurring—began to be passed through to higher prices. The experience of 1967 indicates that cost-push pressures can be contained by limitations on aggregate demands, and conversely that over-exuberant demand facilitates transmission of cost pressures into rising prices.

Mr. Reuss' guidelines suggest also that temporary deviations in the target growth rate of money should be permitted to accommodate large Treasury borrowings. Since this is the only explicit recognition in his proposal of the relation between fiscal policy and monetary policy, the impression might be gained that monetary and fiscal policies should be determined largely independently of one another. Such a view would depend on an extreme position with regard to the determinants of money income and the causes of economic instability. A small group of monetary economists does, in fact, argue that the effect of fiscal policy on money incomes and prices is insignificant—that "money only" matters. In our view, fiscal policy plays a critical role in the determination of incomes, spending, and financial flows, and must, therefore, be an important consideration in deciding what rate of monetary expansion should be permitted by monetary policy over both the long and short run. Fiscal decisions must be taken into account in monetary policy in a more significant manner than merely by providing temporary accommodation for unusually large Treasury financing needs.

Mr. Reuss' guidelines suggest, in addition, that short-run deviations in the growth rate of the money supply may be appropriate when they reflect variations in the public's demand for money. Thus, his proposals allow for changes in the target rate of monetary expansion to the extent that growth in time and savings deposits and shares substitutes for growth in money holdings, and to the degree that business liquidity requirements rise in periods of resource slack for reasons not associated with current expenditure plans.

It may be useful to state the general principle that underlies these two qualifications. It is that the growth rate of the money stock should be altered in response to changes in the demand for money that are not associated with changes in the public's plans to spend