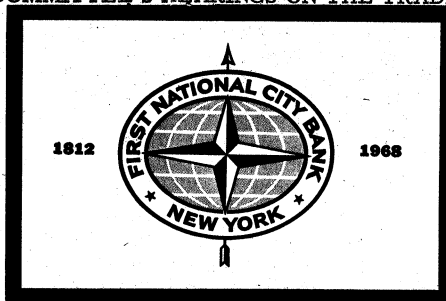


* ENCLOSURE TO LETTER FROM WALTER B. WRISTON FOR INCLUSION IN THE RECORD OF THE WAYS AND MEANS COMMITTEE'S HEARINGS ON THE TRADE EXPANSION ACT OF 1968, HRI 7551
June 1968

Monthly Economic Letter



General Business Conditions

The heated acceleration of economic activity that marked the first quarter shows little sign of slackening. Production, sales, and profits continue strong. Demands for labor, particularly skilled workers, continue to strengthen. The backlog of manufacturers' orders is again climbing.

The rate of economic growth in the second quarter gives every evidence of matching that of the booming first quarter. Yet this growth in gross national product—at an annual rate of roughly 10 per cent, of which 4 per cent represents inflation—is generally recognized as being unsustainable. Inflationary expectations are stronger and more pervasive than at any time since the Fifties. They show up in high wage settlements and rising prices, including interest rates—the price for borrowed money.

Consumer spending is still growing and is expected to grow further, though not at the unusually expansive rate of the first quarter. Incomes

are high and consumers are in a buying mood. Auto sales have been particularly brisk. During May, dealers' daily average sales of domestic cars were up 9 per cent from a year earlier.

Restraint Is Needed

The inflationary content in the economy shows no sign of abatement.

The Federal Reserve has been exercising monetary restraint since late last year without slamming on the brakes. Demands for borrowed money continue heavy, and interest rates have reached peaks which are among the highest in the past century. This has provoked renewed disintermediation—shifts of household funds from financial institutions to direct investment. In time, this could severely squeeze mortgage lenders and consequently weaken the housing market. Against this background, some reduction in Government demands on the economy would be welcome.

The proposal for a tax surcharge and expenditure restraint has become symbolic of a return to fiscal prudence. If Congress now rejects the tax surcharge and fiscal restraint, the reaction in financial communities here and abroad could be severe. So much publicity and discussion have attended the tax surcharge that high hopes are now riding on affirmative action by Congress. By itself, the fiscal restraint package will not overnight eliminate the inflationary imbalances in the economy. But failure to enact the program might overnight add fresh fuel to inflationary expectations and undermine the willingness of foreign governments to hold dollars.

Amidst economic growth and general prosperity, the world has witnessed widespread rioting and strikes, primarily by students, but spilling over dramatically to include organized labor in

CONTENTS

PAGE

General Business Conditions 61
Restraint Is Needed • The Economic Consequences of De-escalation • Wages, Prices, and Profits • A Nervous Money Market

Pitfalls of Fiscal Finesse 65
Anatomy of a Fiscal Squeeze • An Illusory Tax Reduction • Tightening the Fiscal Reins

Trade Policy at the Crossroads 67
The Trade Hearings • Residual Protectionism • Intensified Competition • The Cost of Protectionism • A Surcharge on U. S. Imports • Border Tax Adjustments • The U. S. Responsibility