

concept upon which this rate is premised. Is it the concept of opportunity cost in the private sector? Do you agree with Mr. Hoffman's conclusions on the rate concept?

Mr. CAULFIELD. The Water Resources Council, in developing this proposal, did not adopt any particular theory of the rate of return. Instead, it was reflecting what it believed to be the intent of the President, the intent of the President's words in the budget message, which did not in itself reflect a particular theory, either social time preference or opportunity cost concept, of the proper discount rate.

Chairman PROXMIRE. If you follow the current cost theory, obviously it would have to be higher than 4½%, would it not?

Mr. CAULFIELD. No, not necessarily, in terms of the testimony that you had from Professor Baumol and in connection with the testimony you had from Mr. Hoffman, the point was made that it would be at least the yield rate.

Chairman PROXMIRE. Professor Baumol indicated that it was not his preference, but you could not find any lower rate than that.

Mr. CAULFIELD. You are right, pardon me. He said he thought no economists would be in favor of using less than the yield rate. This is the yield rate, in my judgment, corrected for inflation.

Chairman PROXMIRE. Corrected for inflation?

Mr. CAULFIELD. Yes. Since 1966, there has been a substantial expectation of inflation.

Chairman PROXMIRE. Would there be inflation in one area and not in others?

Mr. CAULFIELD. We have used benefit-cost analysis in terms of constant prices. Therefore, we need a discount rate that does not excessively reflect expectations of inflation, such as the interest rates that have been occurring in the last year or so. As evidence, for example, sir, is the fact that 4 weeks ago, the yield rate was about 5½ percent and now it is just possibly a shade over 5 percent, since the tax bill became law.

Chairman PROXMIRE. Well, on the assumption that your costs do take into account inflation, I can certainly speak on that. Congress estimated it would cost \$65 million to build the new House Office Building and it cost them \$160 million. They estimated \$20 million for this building and it cost \$26 million. They are always underestimating the costs by an enormous margin.

It seems very unusual to assume that they have corrected for inflation in their estimate of costs.

Mr. CAULFIELD. The point is, they have not corrected for inflation. They have used the prices at the time of the estimate. Those estimates proved wrong because there was inflation between the time when they made the estimates and subsequently. There may also have been mistakes in the estimate.

Chairman PROXMIRE. I understood you to say that the reason for this 4½% instead of perhaps a higher rate is because inflationary factors were eliminated in its application to water projects. Am I wrong?

Mr. CAULFIELD. Pardon me. I shall go back now. One could have taken the view, for example, in June, as my testimony indicated, one could have said that the discount rate for 1969 should be based on the average of June prices. That would have turned out at 5.5 percent. We found this not to be appropriate, because, in our judgment, 5.5 percent