

and on the policy of the Fed. And there is an obvious need to help finance the Federal debt. When they do that, they do increase the monetary supply, and they do create additional inflationary pressure.

Now, this is where you get into an immediate economic justification for a tax increase. But we do not talk about that.

Mr. O'LEARY. If I did not emphasize it, I would like to do so. One of my reasons for wanting the surcharge, or fiscal restraint, is to take some of the pressure off the Fed, and to permit the Fed, in a more orderly way, to facilitate Treasury financing. That is one of the big objectives. I would agree 100 percent with you there. And I think this would be healthy.

Another thing I think is true. I think if we got the surcharge, you would see long-term interest rates come down fairly markedly. I think psychologically it would have that effect.

Some people would quarrel with me—but this is my judgment.

Representative BROCK. You mentioned earlier you had a very deep concern that the Fed might step on the credit too hard.

Mr. O'LEARY. Yes.

Representative BROCK. It would be almost impossible for them to step on the credit too hard at this particular juncture with the quantity of the deficit that we have projected for this year and next year. Very difficult for them to step down too hard.

Mr. O'LEARY. What you are saying is the same thing I was saying. Namely, that the Fed is in a box in the sense that, since most of the Treasury financing is going to have to be done with the commercial banks, the monetary authorities are going to have to permit an expansion of the money supply to accommodate that, so that they are restricted in what they can do. I would say they are also restricted, because if they step on the credit brakes very much, they will tip off the disintermediation process and hurt the housing industry pretty badly.

Representative BROCK. We went through that in 1966. I do not think there is a member of this panel that would disagree with you, that we would very much wish we imposed a tax increase in 1966. My question is today, with the different qualities involved.

Mr. OLSEN. I differ a little bit. I do not believe that the Federal Reserve would necessarily create disintermediation if it were to pursue a cautious slowing down of greater monetary expansion, such as it has demonstrated in the last few months. To a great extent the market is becoming more sophisticated, and they are aware that a slowdown in monetary expansion leads to a slowdown in economic activity, and this brings interest rates down. It is the way in which monetary policy is executed that is important.

Mr. O'LEARY. I don't disagree with that. You notice I said if they step on the brakes too hard. If they pursue a cautious moderate reduction in availability, I would agree.

Representative BROCK. Mr. Hart, would you want to comment?

Mr. HART. Yes.

It seems to me that as to whether there is a substantive necessity of coming in with a tax increase, there are two or three points to be made. One is the interrelation with this cost-push process.

If we want the trade union people to be reasonable about their wage demands, and if we want the employers to feel they should show resist-