STATEMENT OF RAYMOND J. SAULNIER, PROFESSOR OF ECONOMICS, BARNARD COLLEGE, COLUMBIA UNIVERSITY

Mr. SAULNIER. It is a pleasure to be here, Mr. Chairman. I have a short statement which I will read—it will take only a few minutes.

I am sorry if there is alarm in what I have to say today, but the fact is, I am alarmed. And I feel sure I am not alone in this. It has been my observation in the past few weeks, both in the United States and in Europe, that thoughtful people are deeply concerned that, while the United States is caught in a kind of impasse between expenditure policy and tax policy, developments over which we have little control will precipitate a financial crisis with worldwide effects.

Trouble could come from either of two directions. It could be generated domestically, if failure to limit Federal spending and lift taxes were to invite an abrupt shift in monetary policy to a firmly anti-inflationary style. This happened in 1966 and it could happen again. With the help from fiscal policy a more gradual shift might be brought off successfully; but if it is done to offset a perverse and inflationary fiscal policy it will have to be severe and there is a risk—as we saw in 1966—of interest rate escalation, disintermediation, a drying up of the mortgage market, a sharp drop in stock prices, and general suppression of economic activity.

On the other hand, if monetary authorities try to work themselves out of the dilemma by continuing to expand the money supply at inflationary rates—hoping all the time that something will happen to permit a change in the script—the danger is that the contingencies, as the saying has it, will go against us and trouble will develop from the international side. The cutting edge would be a heavy drain on gold.

It is in this context that we must consider the economic outlook. The GNP numbers look reasonably good, but this is a year in which it will take a lot of doing from policy to make those numbers come true. Looking ahead, one gets the impression that, subject to certain reservations, everything will be all right in 1968 so long as the whole situation doesn't fall apart. What is needed is a formula for defusing what virtually everyone concedes is a highly explosive condition.

Basically, the risks are due to the impasse between expenditure policy and tax policy. The Joint Economic Committee would perform an enormous service if it could devise a formula for breaking this impasse. It might be done, it seems to me, if the committee were to propose a program along the following lines, especially if it made its proposals in a unanimous report:

(1) *Remove the gold reserve requirement against Federal Reserve notes*

Although this is only indirectly involved in the expenditure policy-tax policy question, I put it in first place because it is already at the top of the legislative agenda, and especially because it is urgently needed to avoid the gold drain which would otherwise be an immediate danger.

Failure to change the law would mean that, unless the requirement were suspended by the Federal Reserve authorities, the dollar, in all probability, would be inconvertible into gold within 2 years. But a suspension would not solve the problem. Unless the Federal Reserve