

economy. Even a decision to “do nothing” implies a forecast that the fiscal policy which results from “doing nothing,” taken together with the expected behavior of the private sector in the economy, will bring the overall economic results we desire. And, in any event, it is literally impossible to “do nothing” in a fiscal policy framework. Expenditure decisions have to be made. Normal economic growth brings large annual increases in Federal revenues. If “doing nothing” means holding expenditures constant and keeping tax rates unchanged, then “doing nothing” will automatically result in a large change in the full employment surplus or deficit. We cannot, in other words, avoid forecasting, unless we wish to ignore the impact of fiscal policy decisions on employment, growth, and price levels.

Given the expenditures proposed in the President’s 1969 budget and in the absence of a tax increase, the Federal deficit, on a national income accounts basis, would range in the neighborhood of \$13 to \$14 billion for both fiscal 1968 and 1969. Will such deficits lead to excessive aggregate demand, an acceleration of the rate of price increase, and a significant tightening of credit conditions? The answer to this question depends upon a forecast of the strength of demands in non-Federal sectors of the economy. If it appears likely that there will be a significant shortfall of private spending relative to the income which would be generated by a stable path of economic growth, then an offsetting excess of Federal spending relative to income will be necessary to balance overall demand against potential output, and prevent rising unemployment. Conversely, if private spending appears likely to approximate the level of private income generated by stable growth, then a substantial Federal deficit will generate an overheated economy and demand-pull inflation.

The administration’s economic forecast foresees the latter situation. With the 10-percent surcharge, the extension of excise taxes, and the other proposed revenue measures—and a consequent NIA deficit for fiscal 1969 of about \$2½ billion—the Council of Economic Advisers forecasts a rise of almost 8 percent in GNP from 1967 to 1968. Roughly speaking, this would keep the rate of unemployment at about yearend 1967 levels, provide for economic growth about in line with the growth of economic potential, and offer a reasonable hope of some deceleration in the rate of price increase by yearend 1968.

This forecast, of course, implies that private demands relative to private income are strong enough to warrant a tax increase. Conversely, it implies that without a tax increase, and with a NIA deficit approaching \$15 billion, total demands for goods and services would substantially exceed economic potential, with consequent demand-pull inflationary pressures.

Instead of reviewing with the committee the specific components of the Council’s forecast, I should like to approach the question of its overall reasonableness from several different standpoints.

*1. Postwar surpluses or deficits in periods of full employment:*

Do periods of full employment, once attained, typically require the support of large Federal deficits? Or, put another way, once full employment is attained are private demands typically so weak relative to full employment levels of income as to require a large Federal deficit if full employment is to be maintained? The short answer is “No.”