

POTENTIALLY EXPLOSIVE ECONOMIC EXPANSION PRODUCTS

To explain the basis for the foregoing general propositions, let me depict briefly an alternative analysis of the outlook in contrast to the eight-point analysis previously outlined.

One.—During the first half of 1968, heavy inventory buying will accelerate as strike deadlines approach.

Two.—Plant and equipment spending plans were formulated when the outlook for 1968 continued to be relatively uncertain. The initial impact of rising sales with no real increase in capacity will be to reduce unused capacity.

Yet, there is little excess capacity outside of the manufacturing sector, which accounts for less than one-third of GNP generated. With greater capacity utilization, with a leveling in the rate of increase in unit costs, corporate profits during the first half of 1968 could continue their fourth-quarter recovery. It is easy to visualize, under such circumstances, a spurt in plant and equipment spending by business.

Three.—With an increase in plant and equipment outlays, with a Government deficit of some \$18 billion, without a surtax, and with a continued labor shortage, it is difficult to envisage the growth of aggregate demand not resulting in continued price increases.

With a continuation of price rises, consumer anticipatory buying of automobiles and other durables, could be triggered as price increases accelerate during the first half of 1968.

Four.—All of the above was within a domestic economy on the assumption of no change in required spending on international wars and domestic programs.

(A) But international security requirements could potentially cause increases in spending of \$4 to \$7 billion, as indicated above.

(B) In addition, additional financing for programs dealing effectively with urban unrest and related problems, may be viewed with increased urgency as time goes on.

(C) Furthermore, with tightening of the financial markets, the pressures to "do something" for sectors adversely affected.

If all three of the eventualities listed under (A), (B), and (C) occur, the forces on the economy may at that time be recognized as leading inexorably to price increases of a magnitude that cannot be countenanced. In such circumstances, a tax increase might then come, but it would clearly then be too late to undo the damage underway.

Even if points (B) and (C) are discounted and only point (A), the international aspect is considered, the consequences could be serious. General price increases in the magnitude of 5 to 6 percent annual rate would be inevitable. There would be a worsening in our balance-of-payments position, both in the short run by stimulating imports, and in the long run by worsening relative price trends in the United States versus the other developed nations in the world.

Recognition of these adverse developments would, because of the well-known lags, undoubtedly require an over-reaction to reverse the process. Another financial crunch would be unavoidable, its dimensions uncertain. The worsened balance-of-payments position would undoubtedly bring in its train a further quickening or rising protectionist sentiments.