

FLEXIBILITY AND POLICYMAKING IN 1968

The Council's report states that "the limitations of the economists' ability to predict the future argue for *prudence* in policy decisions, *flexibility* in the use of instruments, and continuing efforts to improve the reliability of forecasting techniques" (*italic added*). The efforts to improve the quality and quantity of economic information will no doubt bear fruit. But any benefits to be derived therefrom will appear with a long lag. For the present the courses of action open to us are only those of prudence and flexibility in stabilization policy.

As CED has said many times, a stabilizing budget policy is achieved when the Government sets its expenditure programs and tax rates so they would yield a surplus under conditions of high employment and price stability. Since the Federal budget is now in deficit, the present budget policy of the Government falls short of the stabilizing budget rule. It is our view that a policy designed to provide a budget surplus best deals with the dangers of continued inflation without foreclosing our ability to handle a lapse from high employment. If the deficit at high employment is allowed to continue and if total public and private demand rises more than anticipated, we face the danger in the present overheated state of the economy of a still higher rate of inflation. If total demand should rise less than is now widely anticipated, the depressing effects of the surplus can be offset by prompt actions to reduce taxes, to move toward greater monetary ease, and to restore currently deferred but desirable public expenditures.

Several major uncertainties complicate economic policymaking in 1968 and argue for prudence and flexibility; these are the Vietnam situation and the strength of consumer demand. Almost all forecasts, including that of the Council, anticipate a continued acceleration of economic activity throughout the first and second quarters of 1968. There are a few signs, however, which lead some forecasters to anticipate that, even without a tax increase, private demand will moderate in the second half of 1968. Others see little reason to believe that with or without a tax increase economic activity will moderate at all in the last half of the year. This uncertainty about the future course of economic activity clearly is finding its reflection in the failure of Congress to come to grips with current fiscal and monetary requirements.

With the economy currently operating at or very near its potential, with wages and prices rapidly rising, with interest rates at historic highs, and with demand expanding more rapidly than our capacity to produce, the evidence strongly indicates the need for a program of fiscal restraint imposed in part by the proposed tax surcharge. If the surcharge is not enacted the country will suffer serious setbacks.

—Prices and wages will continue to rise at unacceptable rates. To paraphrase the Council, another ominous turn will have been given to the wage-price spiral, postponing still further into the future a return to price stability.

Our international competitive position will be weakened and the deterioration in our balance of trade will be accentuated. The effects of continued price inflation in the United States along with rapidly accelerating incomes will increase our demand for imports and reduce our ability to export.