

Past experience has shown that unexpected developments in military requirements, budgetary trends, or economic conditions sometimes call for rapid adjustments in Federal tax policies. But prompt changes in tax rates, either up or down, are typically difficult to obtain under present procedures. In order to permit more rapid adjustments in tax levels, we would urge that consideration be given to some flexible mechanism to permit removal of the renewed 10 percent surcharge by the President before the end of the 1970 fiscal year, if changing circumstances warrant such action. The precise form of such a mechanism would be a question for discussion between the Congress and the new administration. While we do not presently visualize the emergence of conditions that would call for early removal of the surcharge, we feel that this type of flexibility would represent a potential improvement in our fiscal controls.

3. *Monetary restraint* is vitally needed to hold down the growth rate of money and credit, perhaps for a considerable period ahead. Beginning last December with an increase in the discount rate, the Federal Reserve authorities have moved in the direction of more restrictive monetary policy which has slowed the growth rate of money supply and brought greater pressure on member bank reserve positions in recent weeks. We believe that monetary restraint should be applied in a gradual fashion, in order to avoid the violent disruptions of a "credit crunch" but should be persistently maintained for a sufficient period to break the inflationary psychology which has gripped the financial markets in recent months.

As noted earlier, the upsurge of inflation during 1968 has quickened the desires of consumers, homebuyers and corporations to purchase goods in anticipation of rising prices, and to borrow to finance such purchases. The rise in interest costs of recent months has been outweighed in the minds of many borrowers by the expectation of higher prices for goods if the purchase were delayed. At the same time, lenders have become increasingly aware that they must obtain a higher return on fixed-debt obligations if they are to be repaid in dollars that have been cheapened by inflation. While precise measurement is difficult, it appears that these attitudes have produced an "inflation premium" on fixed-dollar investment, which has been an important force working toward higher interest rates in recent months.

The Annual Report of the CEA expresses the hope that as fiscal restraint is continued through fiscal 1970, monetary policy may gradually be able to shift to a less restrictive stance and that a decline in interest rates may take place. In our opinion there is a grave danger that premature easing of monetary policy, at the first signs of economic slowdown or rising unemployment, would revive inflationary expectations among savers and lenders and lead to higher interest rates rather than lower rates. The prospect of continuing inflation under these circumstances would impel the public to borrow more, while lenders would shun fixed-dollar investments or build in an "inflation premium" in their fixed-debt lending rates. For these reasons, we believe it is imperative to maintain a restraining monetary policy until present inflationary psychology has disappeared from the financial markets. This may require a considerable period to accomplish against the background of recent developments.