security taxes were increased in January 1969 by $3 billion with no corresponding increase in benefits; (*b*) final payments required by April 15 to cover retroactivity of the surtax will take $1.5 billion more from taxpayers; and (*c*) increases in expenditures will be less than the $13 billion increase in tax revenues which is the trend figure at high employment growth rates. In consequence, by the spring of 1969 the Federal budget is expected to show a surplus, so that Federal Government operations will be taking purchasing power out of the economy rather than putting it in. Arthur Okun, Chairman of the Council of Economic Advisers under President Johnson, has said of this change: "Involved is a $20 billion swing in the budget [since the spring of 1968]—the biggest swing toward restraint we will have had in any year in the past 20." And he adds, "Nobody can be sure that the economy can take it."

We believe Mr. Okun has good reason to be apprehensive. The last time a comparable fiscal swing occurred was in the 15-month period between the fourth quarter of 1958 and the first quarter of 1960. During that period the budget situation changed from a $10 billion deficit to a more than $7 billion surplus on a national income and products account basis. This sharp swing to restraint was followed only a few months later by the recession of 1960–61, in which the unemployment rate rose to more than 7 percent. While attempting to balance the budget, the administration unbalanced the economy.

STATE AND LOCAL GOVERNMENT SPENDING

Looking at other sectors of the economy, demand for the services of State and local governments is perpetually on the increase, with the result that State and local government expenditures have been rising steadily at a rate of more than 10 percent per year in recent years. This pressure will continue as respects current expenditures, but, on the other hand, State and local capital expenditures are sensitive to the level of interest rates. If these remain at the current exorbitant level, or rise even higher, it is quite likely that some public fixed investment projects now planned for will have to be postponed.

CONSUMER SPENDING

As previously noted, real consumption expenditures increased by more than the normal rate in third quarter 1968, in spite of the income surtax, doing so at the cost of a sharp reduction in the savings rate. In the fourth quarter this trend was reversed and consumption expenditures, after adjustment for price changes, actually declined. It is expected that real consumption expenditures will continue to be weak in the first half of 1969 because of the factors already noted—the increase in social security contributions, payment of the retroactive portion of the surtax, and the relative inflexibility of contractual savings.

BUSINESS INVESTMENT

In the fourth quarter of 1968 private fixed investment expenditures for plant and equipment increased substantially over the previous quarter, and both the McGraw-Hill survey and the FTC–SEC survey predict further substantial increases in the first half of 1969. But these