

ECONOMIC FACTORS IN RECONVERSION
TO A PEACETIME ECONOMY

10 March 1950

	<u>Page</u>
INTRODUCTION--Dr. Marlin S. Reichley, Director of Instruction, ICAF.....	1
SPEAKER--Dr. Edwin G. Nourse, First Chairman of Council of Economic Advisers, Office of the President.....	1
GENERAL DISCUSSION.....	15

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DR. REICHLLEY: Gentlemen, the lecture this morning is entitled "Economic Factors in Reconversion to a Peacetime Economy." The problem of selecting a speaker for this subject was not a difficult one. Dr. Nourse is so well known as one of the Nation's leading economists that I am certain the only introduction necessary is to say it is indeed a privilege to welcome him back to the Industrial College. Dr. Nourse.

DR. NOURSE: Mr. Chairman, heads of both Colleges, and gentlemen: I assure you it is a very great pleasure for me to be back here. Although we had some difficulty in making arrangements as to time, I am glad that, in a rather busy life, it is possible to take off some time and talk to the home folks as well as to those out over the country.

The title of my remarks perhaps leads you to expect something of a more technical character than I am prepared to give you in line with the work you are doing in your regular courses. It is always a disadvantage for a speaker--at least one who is an old-time professor on the loose--to come in near the end of, or well along in, a series of carefully arranged discussions and try to fit in his remarks. If I had seen your prospectus and had been acquainted with the course all along, it might be that I could fit in my remarks more effectively.

However, I want to express at the outset my very high regard for the way in which the work of this organization is focused. I think it indicates a very clear perception of the fact that we have come to an entirely new, or very much modified, concept of the task to be done--regarding war not merely as a disruptive episode, something of short duration and from which, as was expressed by one of our Presidents, we go back to "normalcy" rather promptly. Under such a concept our economy would, in effect, "play it by ear." By contrast, the essential thing in your undertaking is that you start with a basic conception of the enormously complicated process by which 150 million people live together, try to meet emergencies when they come, and try to show that they do have the know-how needed for running a free-enterprise system within a system of free government, without being disrupted by even such events as a succession of two world wars, in the second of which we had to take the major responsibility. It seems to me highly important that the armed services in our country should have been organized as they are now organized to study that complex interrelation between military effort, if it has to come, and the continuing process of our civilian life. This links your undertaking with the National Security Resources Board, the Council of Economic Advisers, and other analytical and integrating agencies that are being fitted into our Federal Government.

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It is something which challenges every one of us. And I hope a great deal more emphasis will be placed, from here on out, on the role of the social sciences, in addition to the natural sciences, so that our thinking will be not merely in terms of industrial mobilization but in terms of a broad analysis of the economic problem in its social setting. This, beside economics and statistics, would bring in political science, history, and even basic anthropology. You know the extent to which the social sciences were called upon during the late war and did contribute from these several sources.

The subject I want to discuss with you in the somewhat limited time we have this morning stems from the remarks which I made--and which created a certain amount of disturbance--in the Pentagon a year ago last November. There, Secretary Forrestal set up, for citizens who could come in only for a few days, something which I think had the same general orientation purpose as your longer, more carefully organized studies for selected personnel. It was an attempt to bring together a group, or series of groups, of representative citizens from over the country to consider what the nature of the diplomatic strains was under various contingencies of cold wars or wars becoming actual, what the services' outlook was, and then raise the question of civilian mobilization, the industrial background of military effort, the budget problem, and so on.

I was called on at that time to discuss the economic implications of military preparedness. I want to read to you just a couple of paragraphs from my presentation. That will be the quickest way of showing what I conceive to be the common frontier across which you from your side and we from our side try to work effectively. It is not a fortified or hostile frontier, but a very friendly line of imaginary division between groups of people of different lines of specialization who feel a responsibility for this global problem in dealing with military preparedness. I said at that time:

"Members of the military profession are technicians in the science of warfare. Their major premise is that the economy and the social structure, hardly less than the political state, are lost if the system of military security should fail. Like the engineer, they feel the need to include a substantial margin for safety in their calculations, but, unlike the engineer, they have no means of knowing in advance the loads or strains that will have to be dealt with. Hence, the plan they offer must be one that provides every technically available safeguard against any and all foreseeable threats. In a word, they must think of the total resources of the country as potentially available for implementing the security effort.

"The economist's thinking is definitely cast in different mold. His basic problem is: How can scarce resources be most efficiently administered toward the attaining of specified objectives? These objectives are steps toward attaining higher standards of consumption

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and a freer and richer cultural life for the whole population. Ideally, the economist's field of work would concern the efficient administration of economic resources in peacetime, with security assumed or at least with military insecurity adequately guarded against by a relatively minor allocation of men and materials."

Those assumptions, of course, had to be revised when we had two world wars within a span of 25 years. But more particularly, I think we are challenged now to rethink our problems in terms of a continuing military strain or military threat, in other words, a cold war situation, which, we have to recognize now, may go on somewhat indefinitely. But to return to my Orientation Conference speech:

"There is, however, a common ground ~~on which the military man and the businessman, or economist, can and must meet.~~ This common ground is likewise the field of decision on which the President, the Congress, and the thoughtful citizen must take their stand during the next few months and over the ensuing years."

That was in November 1948. They had to take their stand in January and succeeding months, with the economic program and the budget program laid before the Congress and the country at the beginning of 1949, just as they are having to make decisions now, with an Economic Report of the President and a budget before them for public discussion and Congressional action. To resume:

"The common problem, in whose solution both points of view and both types of professional competence are required, is that of the needed balance between the military striking force and the civilian reservoir of men, morale, and machinery upon which the fighting force must depend in this day of industrialized war. The old adage that 'an army travels on its belly' has to be enlarged to the form-- 'travels on the economic machine that maintains the physical and psychological well-being of the soldier and keeps him supplied with efficient weapons.' In providing the means of modern war, the total structure of economic society is involved."

At a later time, I made a similar talk to another orientation group. In it I went somewhat beyond the first speech. I want to stress one point of that speech with you today because I think it is at the very crux of present difficulties and the still-unresolved problems that lie in this field.

I think it would be a mistake if you--or if Congress, the Executive Branch, or citizens in general--conceive the preparedness problem too narrowly as a merely military matter, as something outside the organization and operation of our whole politico-economic society in this country. A difference in point of view, as I said before, is impressed on us by the fact that we don't think any longer of war as an episode and reconversion.

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as something that brings us back to normalcy. Instead we think of preparedness and civilian business together as a continuing administration of our resources in such manner that we shall always be well protected against strains to our society coming as a result of military needs and that the economy shall be in good position to shift resources to make the needed adjustment of plan when, as, or if, unfortunately, the military item comes to be a larger factor in that total society. That, of course, is emphasized in the work of the National Security Resources Board. Likewise it is an indispensable part of the analyses of the Council of Economic Advisers and the revisions of those analyses by the Economic Joint Committee of the Congress. It is not merely a matter of plans of mobilization and then plans of demobilization and reconversion, but it is a question of the organization of our economic life for a continuous process of functioning.

We thought, after the late war, that we were going back to a peaceful condition in which the productive powers that had been revealed during the war were going to be very promptly available for the satisfaction of our people. If you think back to that time, you will remember the almost fantastic dreams there were of what a utopian condition of economic life, with high production and, hence, high consumption, was spread out before us. The Employment Act was passed early in 1946, expressing a purpose of organizing the several parts of our economic machinery so as to maintain maximum production and the incidental maximum employment and maximum purchasing power which would go along with maximum production if it was attained.

As I looked, from the standpoint of the Council of Economic Advisers, at this problem of reconversion to a high-level and stabilized economy, it seemed to me that the old problem was changed on 17 March 1948. On that day the President went to the Congress and said in substance, this idea of demobilization, of disarmament, of a peacetime economy, in which we can look forward to enjoying the fruits of our high production with a constantly diminishing amount of drain for military purposes, has changed. As I read his speech I felt that his remarks were quite momentous. That impression has been borne out by the facts since. We have had to revise our thinking with reference to the postwar economy, revising our thinking from the hopes of a peacetime economy to the realities of a cold war economy. I want to emphasize one point throughout my remarks this morning. We took the superficial numerical fact of that changed situation and forgot to take its implications, and we have not as yet faced the implications of that changed situation.

The military chiefs, a day or two after the President's address, spelled out one phase of the revision we had to make in our plans.

"In our judgment, the prospects are so serious that it would not be prudent to continue on the scale of military demobilization and disarmament on which we have been proceeding on a happier hypothesis.

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We must ask the country to divert an annual amount of 3 billions of dollars additional product out of this economy toward maintaining a proper military security for that economic and social system which we hope to continue on a basis of nonfighting. We must continue for an indefinite time on a basis of different military assumptions than we have had before."

I want to make that point as clear as I possibly can. The statement that we had a changed situation was basically true. The thing that this country, with every bit of its intelligent and fearless economic, political, and social thinking, should have faced from that time forward was that we had a changed situation, and that it meant not merely a question of 3 billion dollars of additional expenditure. We needed to see and accept the implications of having to look at the preparedness problem in that different focus.

The outstanding thing which should have been added to the country's thinking was that we would have to face the fiscal problem involved in this level of expenditures; that we should consider how to avoid an insecure fiscal and inflationary situation, which would put us in a poorer position to carry these responsibilities from year to year, and in a still poorer position to meet a new strain if it came upon us.

Let us put it quite concretely. We had to recognize that we had come out of the war with a debt six times what we thought at the beginning of the war was about all we could prudently carry. In other words, you will remember that we were very much disturbed at the increase of public debt which accompanied the recovery efforts of the New Deal period. That effort brought us from 24 billion dollars of national debt up to 43 billion. Then during the war, we multiplied that new figure just about six and came out of the war with a debt of 278 billion, which, however, was partly fictitious because it included a large Treasury balance that grew out of the overpayment of the last war loan. So we were approximately on a 252 billion dollar basis. And our philosophy prior to 17 March 1948 was that we would be developing a high level of productivity which would enable us to meet the problems of debt management, to handle that gigantic national debt, and to move ourselves back into a strong position. Not merely the strong underpinning of a continuing high-production civilian economy, but in a position where, if war came again, we would have financial reserves; we would be able to make an expansion somewhat comparable to what had taken place in the previous war.

I have become somewhat notorious for talking about these old-fashioned ideas on national solvency. I don't mind being called a "fuddy-duddy." From my point of view, a great many people are overlooking the real problem of fiscal security, as related to our general economic security but also as related, in turn, to our problem of military security. We do have a problem there which I think the country will have to face.

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There is a second phase of the problem of maintaining the strength of the financial and economic underpinning of our society to meet whatever strains may come upon us as the leading nation within the society of free governments that we are trying to build up. This calls for maintaining a set of human attitudes with reference to the economic relationships which will prove workable and reasonably satisfying. The financial position of the United States may be undermined not merely by lines of action which stem from Federal spending and Federal tax policy, but also by relations which develop from the commercial or market side of our total economy.

I have been in some groups recently that were discussing this whole question of monetary stability. I kept emphasizing that there are two approaches to it. There has been, to my mind, an exaggeration in recent economic thinking on fiscal policy or on monetary controls which might be exercised through our system of Federal Reserve controls and money management. Those are tremendously important because what we do in this very complex set of money relationships is, of course, affected by the level of expenditure through which the Government pours money back into that great spending stream and, at the same, draws out an equal amount, a lesser amount, or a larger amount, or a larger amount from that spending stream to put through the public treasury. But don't forget that those relationships, whether we have inflation or don't have inflation, are influenced, also, very strongly by the voluntary, private, wage-making, price-making, agricultural, and all other policies which make up our whole set of market arrangements.

There are in fact two streams that run along side by side. One comprises these bargaining, price-administering, income-administering relationships which have an affect on whether we get a workable set of price relations and the level at which we get that set of workable relations more or less stabilized after the profound disturbances of the war. The other stream is the public side of the monetary and fiscal process, which is determined primarily by the actions of the Treasury, under the wing of the Congress and its spending and taxing legislation, and through the Federal Reserve System, Deposit Insurance Corporation, and the like.

The point that I want to make in that second area is that, since the seventeenth of March, there has been no adequate revision on the part of managerial thinking, or on the part of labor thinking, or on the part of agricultural thinking to the changed facts there announced. Did that history-making speech of the President on 17 March 1948 mean that we would have to work out a different set of price and income relationships and that we would have to adjust our thinking to somewhat different forthcoming conditions from what we had assumed up to that time? I suspect, frankly, that that is true; that the rosy bloom of the picture after the war--"two chickens in every pot and two cars in every garage"--had to undergo some revision, and that an unwillingness to accept that view has resulted in the development of a continuing set of strains within our economic system, strains that are there--and perhaps increasing--today.

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These were manifest at the beginning of this very week when, at one extremely important strategic spot--the coal industry--a certain kind of answer was given. Just because it is written on paper and just because it nominally settles the coal controversy for a year or two does not mean we really have a workable answer to that economic problem.

Those strains were there last fall when, in another basic industry, steel, another strike (which certainly put us in a poor position to meet an early military strain) was solved in a certain way. It was not solved on the basis of the kind of careful economic analysis which you are attempting to give to these problems in your school organization here. It was settled on the basis of some very partisan, very opinionated thinking, in terms of economic cliches or interest pressures from both sides. It was not a process of collective bargaining in an economic sense, but a settlement on a power basis.

The point I want to make there is that if we are going really to settle down and work out relationships under which we can continue to have this society organized on a voluntary basis and go along with a high sustained use of our resources--so that we have the biggest possible pie to divide--we cannot have the parties at interest struggling and fighting and grabbing for the controls and making forced kinds of settlements.

"Collective bargaining"--and I am one of the strongest advocates of collective bargaining as the major apparatus for making free enterprise work within a system of free government--does not mean collective contract-writing on a power basis. It means collective bargaining in good faith, by both sides, and on the basis of an honest and completely frank undertaking. It means trying honestly and with technical competence to see what there is in the productive potentialities of our system and to make arrangements which will keep us using those productive resources at high efficiency. This requires that we distribute the fruits of this efficient production not in a way which satisfies some abstract concept of so-called equity or particular lusts for political power, or the rivalry between the heads of the organizations on both sides. We would not think of organizing a military system on that basis or, in a mechanical sense, of having a machine run on that basis, where the predilections of the cylinders, the crankshafts, the flywheel, or something else would have to be considered distinct from the technical requirements for having a total machine work together.

Of course, I don't think for a minute that we are going to have an economic god with omniscience and power to answer those questions. What I am saying is that, over at the other extreme, if we throw away all consideration of economic workability, we are asking for trouble. We cannot safely ignore the implications of trying to have 375,000 men retained in an industry and of getting a standard of wages in that industry as high as or, through shortened work time, much higher than that of other heavy industries regardless of the market. If we use strategic pressures to get a settlement of that character, then we are not getting a working set of

arrangements and we are not getting our economy organized on a continuing peacetime basis which will keep our production machine purring along at maximum power and ready to take the heaviest load which may be put upon it.

I don't want you to get the impression that I am saying that the effort to get a peacetime organization of our society which will give the safest background against which to consider military problems is a responsibility of labor alone, or that shortcomings in that system and a failure on our part to develop the very greatest industrial-economic strength in this society as a whole come from labor alone. There is just as great a responsibility on the part of management. In fact, last fall, while talking with the top executive of the leadership company in one of the basic industries, I expressed very great concern as to a business policy in his area which would, even in a pretty satisfactory profit situation, allow the struggle over a wage contract there go to the point where we actually had a strike, with all the wastes, losses, and dangers that it involves. It seems to me that management tends just as much as labor to cling to certain absolutes, to say, from its managerial point of view, "We must have that," just as the labor people say, "We must have this." One side is ready to fight for the proposition that the economy can afford to meet the demand; the other will fight for the proposition that it can't. But they act on assertion, not proof. We need to use the best technical resources that we have to find out just what is involved in that "ability to pay" and in the relationship of the distribution of the several income shares to the continuing of the process.

From the standpoint of management, a very important question is raised, which management naturally considers its prime responsibility. It says, "We are the custodians of a capitalistic, that is to say, a mechanized, a very highly capitalized plant. People are not working just with their bare hands. It is our responsibility to provide jobs, properly equipped jobs, and to develop the resources and the flow of resources through which production, at this high level, can be maintained for 10 years, 50 years, or whatever the time perspective properly is. We cannot make this provision for the capitalistic part of this productive process if we grant the demands which are made for immediate consumptive sharing in the products."

Here are two perfectly clean-cut questions. What is the best evidence that our economic analysts and statistical technicians can in good faith lay on the bargaining table, not to get a power settlement, but to get what I am pleased to call an "engineering" settlement? What will the intelligent, patriotic, and deeply concerned citizens of this country, through their technical experts on both sides, say is an economically workable arrangement, not an arrangement which will satisfy certain crotchets of the management group or certain ambitions of the labor group to bring home the bacon in their politically powerful organizations?

Then the question is raised as to whether management, on its side, was really trying to protect certain other interests. There were questions raised in the recent steel settlement as to the advance of executive salaries just at that time, whether it was necessary to the working of the system, and what the implications of that action were. There are questions of the difference in attitude toward executive pensions on a noncontributory basis and whether the steel industry should be thrown into the costs and confusions of a strike on the basis of insisting that the union should recognize the contributory principle; a principle which management did not recognize. But we come at the end to the part where the irresistible force of labor--that is, income and current consumption demands--meets the immovable body of resistance on the part of management. Then we face the question of whether that resistance is on the ground of protecting a more favored distributive position for themselves, which is a lower sort of motive, or of really exercising a managerial responsibility to conserve prudently the resources or technologically advancing equipment for a growing population.

We have seen in the newspapers since the strike settlement that this very same company had back of its position the justification of important research and exploratory work which has resulted in locating an ore body of extreme richness and very large volume within a fairly well-protected military position in the case of future war; in fact, two--one in Canada and one in Venezuela. So a part of their case would be: "The costs incident to that development and the costs incident to the building of railroads, the putting in of plants, the establishing of steamship lines, and the relocation of smelting and rolling facilities in this country all have to be provided for on a 10-, 15-, or 25-year basis, and we will show figures that we have made only reasonable provision for them."

I am not trying to give personal answers to that problem or type of problem. I have no answer. But one thing I feel as an economist and I perhaps have a right to dogmatize on, is this--it is on analytical pressures that we must rely if we are going to get our business adjusted on a continuing basis of efficiency.

What I have said has perhaps linked up sufficiently in your minds the general point of view that I wanted to present--that security is a global concept; that we must have a fighting edge, a cutting edge, let us say, of military effort available at the times when it may be called upon, and a reasonable judgment as to where and in what way it will be called upon; that we must have just back of that military edge a plan of civilian and industrial mobilization; ~~that~~ the focus must be not merely on quick conversion of industrial and civilian peacetime arrangements, but on the much broader concept of organizing that industrial system over a long-time period so that in the unpredictable future, whenever strains may come, we will always be in a position to improvise plans, to modify arrangements for the particular strain.

I want to go one step further in connection with this. If you are going to have the kind of industrial system that will provide an always dependable basis for possible use in war it cannot be one which relies on mere mechanics or the mere technical managerial assignment of people to the various areas. A good deal of pressure, incentive, and inducement will be developed toward getting people to the various positions in the system, but there is also a psychological factor which is involved. This cannot be figured out purely as coldly correct or logical answers. You cannot go to John Lewis and his followers, or to Mr. Murray and his followers, or to the building trades, or the railroad brothers, or any of the rest of them, and say, "We wise men, we competent technicians, have worked this plan out, and you have to accept it." If we recognize that ours is a system of free enterprise within the structure of free government, we must constantly accept it as a limiting factor that individuals can talk back, that they have the last word, that we must persuade their minds or "condition" their behavior. Perhaps they think with their elbows. All right; if so, we must address our educational campaign and our incentive program to the level at which they think or according to which they act.

American industry in peace or in "preparedness" is a system of voluntary participation. That is what the boys in the late war thought they were fighting for. They were inclined to feel, "Once we get this thing cleaned up, we will go back to normalcy. There is going to be a nice opportunity for everybody, and this high productivity shown during the war is going to make favorable conditions for everyone." But they come back and find that they have to work within a set of limiting circumstances. That is the meaning of the strikes and industrial unrest we have had and are still having. There lies the great psychological problem we have to work out. We have to get some sort of interpretation that is both workable and satisfying of the freedom of people to organize, the freedom of people to conduct those organizations, the freedom of people in those organizations to strike to force a settlement, and yet not demoralize our productive machinery.

On the managerial side, too, we have to recognize that there is just as much intellectual arrogance as on the labor side. Management does not propose to be forced into what it regards as an unwarranted sharing of increased productivity. One case in point is the whole profit-sharing idea, where the management point of view is often reflected in this remark, "Why, when we raise the productivity of labor by putting our capital, our managerial skill, and our know-how into securing added productivity, should we give it to the workers, who are not working any harder, and probably not so hard as, they were working before?" This is a psychological bent on their part which we have to meet.

We cannot press our institutional development--through the Wagner Act first and the Taft-Hartley Act afterwards, or through pension legislation, and so on--beyond the point at which, under a system of free

enterprise within free government, we can get a social assimilation of the institutional adjustments that we make and the procedures that we either legislate or, by practice, attempt to establish in the system. If we are going to have maximum strength and maximum security in the global or integrated sense, we must have not merely a well-equipped, well-organized, well-planned military effort. We must have not merely the industrial plant and the arrangements of technical efficiency back of that. We must have also what the Germans call "der Zeitgeist"--the whole spirit of the times and of the scheme of organization which gives a sense of satisfaction, which makes our whole population in time of war--the civilians as well as the military--definitely a positive, not a negative, force to be organized for the military effort. We must set that up as an ideal, and we must go as far as we humanly can toward getting that sense of satisfaction, of enthusiasm, if you please, a sense of righteousness, justice, and participation. We must see to it that there is a responsiveness in this system; that in collective bargaining the responsibilities and aspirations on both sides have been adequately recognized and effectively presented.

Then the final point, which at the present time I think we have not accepted and which is the greatest danger to the whole concept of having an effective peacetime system, is that there must be a willingness to accept limitations and go ahead with what you have. It is the playing-field attitude that, once the umpire has given his decision, everybody takes it in a spirit of good sportsmanship. I question somewhat whether that is the situation at the present time. It remains to be seen how much non-cooperation is developed by some of these settlements which have to be worked out under stress of fact-finding boards and the like.

We have a reasonably good level of performance in our industry today. I think, however, that we have not done our best toward improving that level of performance, toward strengthening the economic and, if you will permit the phrase, spiritual basis of organization of security in the global sense. Not of the three parties, labor, management, or agriculture, has really accepted the limitations which, in my judgment, means accepting in our present situation a less satisfactory consumer position than we had assumed would be available to us after the war.

The farmer had an extremely favorable situation during the war. He had to be given, just as industrial labor had, a pretty attractive break in order to stimulate the production of those things that were necessary. After the war, he tried to perpetuate that rather artificially favorable situation in spite of the fact that the ratio between agricultural productive resources and our consuming capacities at the time was one which, clearly, or in the analysis of all the experts, would put us back into a buyer's market. He wanted to perpetuate a seller's market by continuing to make Uncle Sam the buyer. And so we have had what you read about in the newspapers all the time--the keeping of agriculture on stilts by the continuation of agricultural supports at a level which results in the accumulation of very large, whole-season supplies, plus compounded and

built-up carrying charges. Doing that on a deficit basis, as we are, creates an inflationary system; this tends to rob even the farmers of the benefits of the direct support which prices get through that machinery.

Industrial people, as well as the farmers, are concerned in protecting agriculture against disaster. But that is something very different from trying to have a high and rigid set of prices which maintain the stimulative conditions appropriate in wartime but which now simply pile up additional surpluses to be held under very expensive conditions. Such surpluses become a disruptive factor in settling down to stable market price relationships.

I shall give time for you to ask questions where you think I am off the beam, or where I have not made the point clear, or on things I have omitted. But I want to make just one point as to how much of an inflationary danger there is, or what is the danger to the whole price-income-market system at the present time under these attempts to perpetuate artificial conditions rather than to face the basic elements of true economic adjustment.

Two rather different philosophies are presently being expressed by legislators, by the Executive Branch, by economists, and by businessmen. One group would try to solve these problems by retaining the particular advantage that one group gets, or by adding to the advantage that one group has by allowing wages to go up, letting prices go up, and then letting our one-way elastic monetary system respond. That is the inflationary solution to the problem. The other one is the deflationary answer--the knocking off those things which are above a good structural relationship to the others, moving in the direction of, or approximating so far as we can, a stable rather than a rising price level--even a price level declining moderately and slowly as we make technological progress. That is, in my book of economic mechanics, the kind of adjustment which I think would be the better economic "engineering."

The inflationary answer may seem more realistic, and certainly easier at the present time. We are upping wages and then upping prices, we are upping spending, and we are moving in a generally inflationary direction. Defenders of this course say, in essence, that it is a stimulative process; that we don't have to make people face the grim realities involved in the other kind of adjustment. Laboring men always want a few more dollars in the pay envelope and the labor union wants to bring that return back to them as a basis of strengthening their position. We have the same incentive argument on the capital side; that it is a continual stimulative process.

That raises the very nice question as to whether we can operate on that easier sort of economic philosophy and inject those stimuli into the situation and still keep the process in hand. That is the basic issue.

I am reminded of the story of Professor Hugo Munsterberg. You older men probably remember this. Professor Munsterberg, a distinguished professor at Harvard, of foreign extraction and having some continental ideas, shocked the Puritan conscience of the United States by speaking in favor of moderate drinking. Because of its stimulative, comfortable, and relaxing character, he made a defense of it and ended up with the aphorism: "Better an America inspired than an America sober." I think we have just about the same thing in the advocacy of inflationary solutions to economic problems. They say, "Better an America constantly living in a process of always yielding in terms of price and income relationships on the upside than an America trying to have a stern gospel of limitation--of "disinflation," to use an expression you may have heard.

There is no absolute answer to this controversy. Personally, I am very much afraid of the ability to keep a process of creeping, organized, and rationalized inflation within bounds. I see real danger in accepting that philosophy and saying that a debt of a trillion dollars is one that an economy of this size could handle or soon grow into. I think that it exposes us to dangers and, to go back to what I said before, would put us in a very much more difficult situation to meet the financial strains which inevitably would come if the military situation markedly worsened.

It seems to me that this is not a calculated risk but a "miscalculated" risk. It is accepting an easy inflationary short cut, whereas we ought to be accepting sternly the consumption limitations of our economy and adjust our several relationships and our several shares in the product of that economy to those realities.

People may ask, "How could the inflationary danger become effective?" I think there are two answers to that question. I will just give you the alternative sequences because we are right in that position at the present time.

We came out of the war with a very large debt. Modern theories of fiscal policy require that we should accumulate a surplus in periods of high prosperity. We had an extended period of high prosperity, inflationary prosperity. The accumulation of a surplus at such a time not merely brings the debt down to manageable proportions, but it tends to have a dampening force in the market, so that inflation does not get out of bounds. Well, our inflation did not get actually out of bounds--it could have been dampened more--but what we ended with was a deficit of almost 2 billion dollars in the culminating year of the postwar inflationary prosperity. And on the assumption, or prediction, or forecast that 1950 is going to be a very prosperous year, we are promised, with such strain as there is in the military situation, a deficit of about 5.5 billion dollars. I think it will be higher. There is quite a considerable possibility that it might be 6 or 7 billion. That, by the thirtieth of June, less than four months from now, would, with the deficit that was reported last year on the thirtieth of June, extinguish all the saving that we made, all the accumulation toward handling that gigantic debt,

and put us in the way of raising the national debt, still further. That is what I meant in a certain speech that became somewhat notorious when I said I am concerned about a policy which seems to mean "slipping into deficits as a way of life."

Now, there are two possibilities as to what might happen from here on out. No one can tell you certainly. I disavow any intention of saying more than that the situation is vulnerable.

One possibility is that the process of moderate inflation could take on an accelerating turn and could get into something that would be runaway inflation. I don't think it would be the kind that Europe has experienced. I was over there and had the thrill of tipping a bellboy with a two million mark note and that sort of thing. I don't expect to see that in this country. But short of that, we could have an acceleration of price increases which would cause inflationary dangers and a flight from the dollar.

And there is the point. If this is dangerous, it is dangerous because of creating uncertainty in the character of our basic monetary unit. There is the danger. And if we get uncertain about it, what do we do? On several recent trips, people have come to me every once in a while and asked, "Well, Doctor, do you think that real estate is a good hedge against inflation?" When people begin to talk about hedges against inflation, we have something which is in the small incipient stages of a flight from the dollar.

Our answer cannot be in terms of a flight from the dollar to the pound or the franc or anything else. There is nothing to flee to, in monetary terms, but that does not mean that you cannot flee to goods. The flight to real estate might start a Florida land boom, a farm land boom, or a general land boom. I heard a very good economic analyst a short time back suggesting an inventory boom as one of the dangers in the last half of this year. What is an inventory boom except a thought that the slow, creeping trend of price advances is getting to the point where we had better stock ahead, accumulate more inventory with the artificial stimulus that gives the market a shot in the arm. Or we can flee to securities. The stock market is down. Everybody says, "Sure, there are great equity values there. We are smart. We can get in, clean up, and get out." We might repeat what we had in 1929. God bless the market every time it turns down after a little advance! But if it should not, if it should really get momentum, particularly if it were accompanied by an inventory boom and a considerable land boom based on hedging against inflation, I would say there we have our system of "healthy," "stimulative," "moderate" inflation getting out of hand.

But events might not go that way. Before that happened, right in this year, we might have had businessmen feeling so much uncertainty on this score that they began to say, "I don't know. I am worried about

this situation. I guess we had better hold up this plan for expansion"; or consumers saying, in the same way, "I don't know. Maybe we are going to have a depression. After all, we are pretty well stocked up." The farmer has made large additions to his farm machinery, and city people have their cars and television sets. They might say, "Well, I guess we had better postpone our further buying of consumer durables." So we might have a withdrawal from the market because of the uncertainty, rather than a piling into the market. Either one is possible in the psychology of 150 million individuals not fully literate economic matters.

Those are the possibilities. That is the one word I want to leave with you. In my judgment, those things can happen. And for people to walk blandly into the development of that sort of vulnerability, unwilling to face the realities of the consequences flowing from the President's speech of the seventeenth of March, that is something which really causes me some concern.

I am sorry I have gone over into the discussion time.

QUESTION: Dr. Nourse, you have made it seem rather easy for a creeping inflation to get out of hand. I wonder if you could outline some of the steps we might have to take in disinflation.

DR. NOURSE: That is a more difficult course. I have been saying and shall, next Wednesday, at another place, say to an agricultural group, "I think you ought to face reality and recognize that, if you are going to have, under the present income structure, full current absorption of the product you are able to produce, it must be on the basis of lower prices and of holding that lower price line. Instead of thinking of agricultural supports as a means of advance to higher prices, think of it as an orderly line of price minima consistent with unit costs. Full-volume operation is the thing you should look to."

Because that is a managerial approach, it is essentially the same thing in industry. I would ask, "Is an increase in the price of steel because of the recent advance in coal really necessary?" I was reading "Iron Age" last night, and it flatly stated there is no need of an increase, because costs have been sufficiently low in terms of the present price structure and have been based on some extraordinary costs of preparing for a shutdown and the costs of shutdown. They argued that actual costs will not be higher under the new coal price than under recent operating conditions, therefore, there is no justification for an increase in price. If it becomes an excuse for a price increase, I would say that is a discouragement to our whole steel-using economy. If prices are held now, my judgment is--and it is a rather arbitrary one--that if we settle down to continued operation, prices of steel could be somewhat reduced from here on out. They don't have to cut now. They are in a seller's market temporarily. But they should follow the philosophy, not of saying that everything that causes a nominal increase

of cost has to be reflected in a proportionate or larger increase in prices, but of moving prices down gladly where possible, because that begins a process which means lower material costs for a lot of steel-using industries; and if they follow through, the benefits will be passed on to the consumer, and the market will keep moving with vigorous response to the production situation.

QUESTIONER: Sir, you have suggested placing great dependence on free collective bargaining in good faith as a solution for industrial tensions, and you gave an example of the inconsistency that management displayed in exhibiting good faith in the pension case. But I don't understand that any criteria have emerged for deciding whether labor is acting in good faith, and I don't see how you can judge that.

DR. NOURSE: That is a very technical thing and something on which, of course, NLRB has to give an answer in the particular instance. We have seen cases in which, sometimes, it was obvious that the union was not willing to bargain in good faith and, sometimes, that management was not willing to bargain in good faith. That will be a perennial issue. If they get a little stronger, they are not likely to abide very much by the economic issues.

I don't know that there is any formal criterion that can be set up, but I think it is important to have some agency which can say, reading the evidence and knowing the techniques involved, "You have not bargained in good faith and you are not living up to the obligations of the law."

COLONEL MCKENZIE: Dr. Nourse, I should like to ask a question about our reconversion planning after the last war, or during the last war. As I recall it, about the first announcement that was made had to do with the GI benefits that were to be expected or planned for. Then came along the Baruch-Hancock Report, with its termination features of contracts. It seems to me nowhere along the line did people anticipate expenditures which, I have understood, have run upwards of 70 billion dollars in rehabilitation, reconstruction, and direct aid to various countries of the world since then. Will you give us some pointers on how we can anticipate, in reconversion planning, some of these things that come about?

DR. NOURSE: I don't believe I can, because it seems to me that that is the very essence of the situation; that, with the best of our forecasting, we cannot predict some of those things. They are random, unpredictable elements. They play the joker wild on you. For instance, we had the assumption that we Allies, after we won the war and beat our enemies, were going to work together in double harness. When we found that basic assumption was wrong, then all the calculations based on it were thrown into the discard. And that is epitomized by the President's speech of the seventeenth of March about as well as anything.

COLONEL MCKENZIE: Dr. Nourse, we are thoroughly appreciative of the many demands made on your time. We are more than ever grateful to you for having come to us this morning with a stimulating talk. Thank you very much, sir.

(20 Apr 1950--650)S.