GENERAL ECONOMIC CONCEPTS AND BACKGROUND

28 August 1953

CONTENTS

Publication No. L54-9

INDUSTRIAL COLLEGE OF THE ARMED FORCES

Washington, D. C.

Dr. Arthur Edward Burns, Dean of the School of Government, George Washington University, was born in Oakland, California, 3 September 1908. He received his A.B. degree from the University of California, Berkeley, California, in 1931, his M.A. degree from the same university in 1934, and his Ph.D. from George Washington University in 1935. Dr. Burns has taught economics at George Washington University beginning in the position of instructor in 1934 and advancing through several assignments to his present position of Dean of the School of Government and Professor of Economics. In 1952 he was visiting professor of economics at the University of Brazil. His service with the Federal Government includes: economist, Federal Emergency Relief Administration 1934-35; economist and assistant director of research 1935-40; adviser 1941-42, and special consultant to Office of Price Administration 1942-43; deputy director, Office of Materials and Facilities, War Food Administration 1943-45; consultant to the War Department, 1947; public member, Foreign Service Selection Board, State Department, 1951. He is the author of: "Modern Economics" (with Neal and Watson 1953); "Government Spending and Economic Expansion" (with D. S. Watson) in 1940; and "Federal Work, Security, and Relief Programs" (with E. A. Williams) in 1941.

GENERAL ECONOMIC CONCEPTS AND BACKGROUND

28 August 1953

DR. KRESS: Admiral Hague, General Greeley, gentlemen: Today we begin our economics refresher course in earnest. This afternoon the Brookings Institution will present its film "Big Business in the Competitive System." The narrator is Dr. A. D. H. Kaplan, their senior economist, who has kindly consented to attend and will answer your questions at the end of the presentation. It takes 38 minutes for the film.

Next week's movies, in contradistinction to this one, are voluntary, but they have been carefully selected and I am quite sure that attendance at them will save you time on your economics reading assignments.

Now, you have the biographies of the distinguished leaders who will help us during this course. Two of them are able to be with us this morning and I would like to introduce them to you: Dr. Allen G. Gruchy, of the University of Maryland, likes to be called "Al"; Dr. Melville J. Ulmer, American University, likes to be called "Mel." All of our discussion leaders have been chosen--if I might use the word--because they are outstanding teachers.

Now to those of you who have your M.A.'s and Ph.D.'s in economics along with you, in these next 10 days, I hope you will act as assistant instructors and help to inform your fellow students who are not so well educated in economics.

Our speaker this morning has a great deal of practical experience as well as an academic background. His textbook, revised edition, has been adopted for use at the Naval Academy next year as the prescribed course. As a teacher and discussion leader, his great experience has been channeled into a few years. He is still a young man and he looks even younger than he is. We are glad that he is to share his vigor and his enthusiasm for economics with us this morning and throughout the next 10 days. It is a great pleasure to introduce to you the Dean of the School of Government of George Washington University, Dr. Arthur E. Burns.

DR. BURNS: Good morning, gentlemen.

I have as my topic "General Economic Concepts and Background." This is a neat three- to four-hour lecture. I shall compress it into 50 minutes and I hope no more.

What I want to do this morning is to discuss some of the rather fundamental aspects of economics and then conclude on something that is of more current interest--the impact of the present military program on the American economy. But first let us get to the fundamentals.

The general subject of economics and all economic activity has its origin in one simple and sometimes distressing fact, and that is the fact of scarcity--the scarcity of things that satisfy wants and the scarcity beyond that of the resources that produce the things that satisfy wants.

Scarcity has to be considered in the special meaning or sense that economists use. It doesn't just mean the unavailability of things. Scarcity means that things are not available freely in the quantities that satisfy our wants for them. Quite obviously, a lot of things are available but not available freely. We have to work to get them or we have to pay for them. Actually we have to work to get the money to pay the prices for the things we want.

But for the fact of scarcity there wouldn't be any subject of economics and you gentlemen wouldn't be here for this particular lecture and the succeeding lectures on economics. The fact of scarcity of economic resources--labor, capital, and natural resources--has some consequences that are far-reaching.

In the first place, the fact that the things that satisfy wants--Cadillac convertibles, cameras, and things of that sort--are scarce requires that a great deal of effort be expended in any economic system and of course throughout the world. It is probably true, taking the 2 billion plus people in the world, that the greater part of their waking hours is spent in working, offsetting to some extent the basic scarcity of the things they need for survival and for convenience and comfort.

Work is one of the consequences of scarcity. Another is the necessity to economize, to organize the resources we have, to handle the funds in our possession so as to get the best results from the resources and to get the best results out of the money we individually spend.

This question of mobilizing, managing, or organizing resources is very evident to all of you who have worked on the problem of industrial mobilization. I think industrial mobilization highlights the main point I am discussing right now. There is a scarcity of money available to the armed forces but the scarcity of money is merely a reflection of the scarcity of the resources that produce the things that both the military and civilian sectors want. The problem, then, is to manage, to organize, to allocate, to distribute the resources in such a way as to get the most for the military budget and the proper balance of the things that fit into the procurement plans of the services.

Here we have in a nutshell really the underlying economic problem, scarcity, the need to work, the need to organize, to allocate, to distribute resources and money to get the best possible results. The things that economics is concerned with, the resources and goods that are scarce, are called economic goods in the textbooks. In economics the things that aren't scarce in terms of wants are called "free goods" and they are pretty much out of the realm of economics except as indirectly they might affect economic activity.

Scarcity must always be considered in terms of wants. Some things probably are very scarce but they may not be economically of any importance. We all know that a four-leafed clover is a very scarce item and I suppose some people occasionally spend some of their time idly looking for a specimen. But scarcity in that sense isn't of any significance because given the values of our civilization, a four-leafed clover is nothing more than a curiosity.

The fact of scarcity was mentioned in connection with the problem of economic mobilization and the need to organize resources to get the best possible results. Or look at it from the budget point of view. I am sure that no responsible officer in the armed services would say that the armed forces, or his particular branch, gets all the money it wants. I have never heard any such statement as that. The problem of scarcity in this case is not enough money to meet the goals that each service has in mind. Or if we want to get away from the large realm of military economics to the personal realm of each one of us, I am sure that, with the exception of a handful of people, hardly any of us has enough money to satisfy all the wants that we have.

Scarcity means that the economic processes have to be organized in some sensible fashion. There are all sorts of ways of organizing economic activities. There needs to be a system and guidance in production to assure that economic resources produce the commodities and services that the economy wants most.

The second basic process is the distribution of income in the system. Income arises out of the production of commodities or the performance of services, and if income in an economic system--either money income or the goods and services which comprise real income--is scarce, the system has to organize a distributive process to share out the scarce goods and the scarce money incomes in the system.

Then another process required by the scarcity of things is the need to develop a system of exchange and a means of evaluating goods. Evaluation is essential so that an economic system may select this over that kind of goods to be produced.

And, finally, the fourth main economic process that needs to be controlled or regulated because of scarcity is the process of consumption.

As I said a moment ago, the things we all want are usually more numerous than our means of purchasing them. Consumption has to be regulated, has to be limited to the volume of goods and services available for consumption. In this system, price is principally the means of limiting the consumption of anything by anyone.

This is a very effective system of control. There are other ways of controlling and limiting consumption. Goods could be rationed as so many of them were during World War II. Or possibly consumption could be regulated in accordance with social or political status. But in this system, consumption is very simply and very effectively limited. If some things are very scarce, the price is quite high. The higher the price, the fewer the buyers; the lower the price the more buyers there may be.

Thus we have four main processes in economics: The production of commodities and services; the distribution of income which is created in a process of producing commodities and services; the exchange of commodities and services and their evaluation; and, finally, the consumption of commodities and services.

Fundamental to all of them is the process of production. I should like to define a point here slightly although it will be elaborated in another lecture. Production as it is measured results in what is called the gross national product (GNP). The GNP is the end product, the final output of the work of the economic resources of the country. It includes the market value of all the consumer goods on the retail shelves of the country, all the capital goods--machinery, equipment, and plant currently built--and the value, the procurement price, of all the goods that Government buys, military and nonmilitary. In addition, the GNP includes the services privately rendered or sold to consumers--the services of lawyers, physicians, dentists, entertainment people, and so on. Finally Government renders services which are measured by the civilian and military payroll of the Government.

Add these all together and they give us a total which is currently 367 billion dollars. That total represents the end product, the result of this year's work on the part of the resources of the country. The GNP is a highly important concept and I am defining it at this point because I shall have occasion to use it when I discuss the impact of rearmament following Korea on the American economic system.

The problem of organizing an economic system, as I said, goes back to the basic fact of scarcity, and this problem exists in all economic systems. One of the fallacies that reformers often make is that by changing things a little bit, by changing the form of government, by changing the ownership of economic resources, the economic problems somehow will be solved or greatly improved. Certainly, so far as solving the economic problem, a change in the ownership of property, or a change in the form of government would have no effect upon the underlying fact that wants exceed the capacity for their satisfaction. Resources are scarce, whether it be a socialist system, a communist system, or the capitalist system that we have here.

The economic problem is common to all economic systems and a change in the form of the system is not likely to change the underlying problem at all. It might affect some problems; it might alleviate some difficulties; probably it will create some others as well. All systems, then, have to go through the job of organizing a production program, a method of distribution, and a method of controlling consumption.

In general there are two ways of doing this job. One would be to organize the production, distribution, and consumption processes centrally, something like the Russians do in their system. In this case the main decisions respecting what shall be produced, how economic resources are to be managed, and what is available for consumption, would be centrally determined by some sort of planning organization. The GNP output would then reflect the judgment of the planners as to what ought to be produced and in what quantities. That would be a centralization of the decision-making powers in the economic system.

At the other extreme is a system where the power to make decisions to invest, to produce something, to employ people, to consume, to spend, to save, is decentralized. Each individual is perfectly free to consume and to save as he wished within his financial ability. Each firm produces what it thinks it can sell profitably. It can produce more or produce less, or shift over to something else. Those decisions are decentralized.

Roughly speaking, the American economy is one in which there is a great deal of decentralization of decision-making power. Even with the growth of governmental controls and governmental activity in this system, there still remains a vast amount of decentralization of decision-making power. Between 85 and 90 percent of the GNP is privately produced. There are very few, if any, important controls over consumption and no controls over what to do with one's income--after the tax collector has taken his share. Thus there is this decentralization of decision-making power with the 52 million households in the country mainly determining what is being produced in the country. Producers must satisfy them by giving them something of a quality and at a price that they will buy. The decentralization in decision-making power in this system is in contrast to the great concentration of power and decision in the other systems.

Probably no system ever achieves either extreme. We have a considerable amount of decision resting with Government as to economic activity, and probably in Russia the planners must at times bow to the preferences of the public at large. But the difference between both systems is vast.

The decentralization of decisions in the American economy means that the main control of our economic activity comes by way of a complicated system of prices. Another lecturer will discuss the price formation problem in considerable detail. All I wish to say here is that decisions to produce on the part of business firms and the decisions to buy and consume on the part of the household are basically governed by prices and price relationships.

I don't know how many different kinds of commodities are produced in this country. It depends upon how they are classified. But certainly there are hundreds of thousands of classes of commodities produced in this country and no one plan is set up to show how much of each type must be produced. The decisions along this line are made by some 10 to 11 million producers in this country, not conforming to a plan but conforming to what they regard to be their own best interest. They operate in terms of a price mechanism. They buy at prices and sell--they hope--at better prices. The system is by and large governed in this way in contrast to a more centralized system where these decisions are made centrally.

The importance of price in the study of economics rests upon the fact that the price system is the method of organizing the central economic processes of a free or market economy. Unfortunately, economists in their analysis of price determination often lose sight of the main point in a maze of technicalities. The real economic and political significance of price is that it is the chief method of running this economic system in accordance with producers' expectations of profitable sale to consumers who, in turn, act in accordance with their preferences, incomes, and the prices of goods.

In the general field of economics, it is possible to divide most problems into two general categories. One set of problems has to do with what might be called the composition of the gross national output. Hundreds of thousands of different things make up this total. Behind the end product there is a great variety of raw materials and semifinished materials in the industrial pipelines which will end up in the course of time as finished products.

The problem of explaining how much of each thing is produced is one of the central problems of economics. This is largely a matter of the price mechanism and the demand of buyers reflected through the purchase of goods at prices.

The composition of output is one main problem. The other one has to do with the level of output or the size of the GNP. How big was it 10, 15, 20, or 50 years ago? How big is it likely to be in 10, 15, or 20 years from now? And what are the influences that determine the size of the GNP?

In connection with the GNP, there are two things that interest economists and I suppose they should interest everyone else. One is the prospects of long-term growth in the GNP; and, second, the problem of short-run instability in the production of the GNP.

When we look at the American economy as it developed out of the early commercial and industrial capitalism of Western Europe, one of the striking things is its enormous growth over a long period of time. Over the last 50 to 60 years the GNP in this country has grown at an average rate of about 2.5 percent per year. If we look at the last 8 or 10 years, the rate of increase has been 3.5 percent per annum. Long-term growth is one of the striking features of the American economic system, and this long-term rate seems to be greater than that of almost any other economic system in the world.

This long-term growth in production in the United States has its origins, first, in the developments generally known as the industrial revolution—the application of mechanical power to the productive process. That has been a central factor in the growth of the economy. There are many other things that can be specifically mentioned. The labor supply in the United States has grown greatly over the period of the country's growth. At the present time the labor force is about 67.5 million persons, nearly 64 million of whom are in the civilian labor force; of these over 62 million are currently at work. The increase in the labor force has come about because of immigration, high birth rates, the shift of women into paid employment, and because more and more of the population is in the working-age groups.

A second and vital reason for economic growth is the accumulation of capital, mainly in the form of fixes instruments of production such as plant, equipment, and machines. But to build these capital facilities requires annually that this country save a portion of its income and output. Saving technically means not spending for current consumption; in real terms it means setting aside some of the output for capital purposes rather than for current consumption.

Over a period of time this country has accumulated a vast amount of capital. One reason for the emphasis on capital accumulation is that the country started with a relatively small population and labor force but with enormous natural resources. The scarcity of labor in relation to natural resources meant that output per man in this country right from the beginning was very high. It is out of this high output per man that the country accumulated capital. Moreover there was a strong incentive to accumulate capital because labor being scarce it was relatively expensive. American capitalism has always stressed labor-saving innovations which further increased output per man.

In countries where there is a very large supply of labor, labor is cheap; in such cases there is much less incentive and ability to accumulate capital. In this country the accumulation of capital has been spurred on by the shortage and therefore the high price of labor, and capital accumulation has been readily possible because of the abundance of natural resources.

Innovation has been a third factor in the country's growth. Technical inventions comprise only one type of innovation; perhaps equally important are innovations of other forms—in the organization of markets, in business organization, and so on. Such innovations have stimulated growth and have at the same time contributed to the instability and change in the system.

The fourth factor in the growth of the economy has been the presence of a big country, a big frontier, and the stimulus to the economic system of filling out the country. Finally, another point that accounts for the growth of the country was the shift in production from relatively low- to relatively high-product industries. As an example, this country was overwhelmingly agricultural 125 years ago. It is now overwhelmingly nonagricultural. There are just about 6.5 or 7 million people on the farms feeding themselves and the rest of the 155 million in the country. At the same time they pile up considerable farm surpluses in warehouses, some of which we give away to foreigners.

The shift in employment has been to industry and to the service industries. This shift has meant a larger product per man. Today, even with highly efficient agriculture, per man output in industry is greater than in agriculture. But the growth in the American economy has never been very steady. We have had periodic booms followed by depressions. The economy has grown by fits and starts for many complicated reasons.

Much can be said on the problem of instability and the possibilities of stabilization, but time does not permit extended discussion. Growth is a long-term trend in America but, in a short run, there is and always has been a considerable amount of instability.

In one sense, the problem of periodic depression is really a part of the problem of growth itself. The economic system spurts forward on some new development. Spirits run high, speculative activity is strong, and business tends to overreach itself. It is a psychological requirement that a business man be an optimist. This fact cannot be ignored in a discussion of the related problems of growth and instability.

This is no explanation of the complicated problem of business cycles. What I wish to stress is that equal rates of growth in all parts of the economic system are simply improbable and perhaps impossible. The system gets out of gear from time to time. In fact it is partly out of gear all the time. Some things are always going faster than others and the problem of depression comes about periodically. There will be another one, and one after that, and one after that, even though attempts will be made—and they will probably be somewhat successful--to stabilize the economic system. But such attempts to stabilize must take care not to impede long-term growth.

One small point on this matter of the depression--the depression of the 1930's had a tremendous effect upon the economic system and upon the people in the system. Everyone fears depressions because they always think of the one of the 1930's. I am quite prepared categorically to say that we will never again have a depression of the magnitude of the 1930's. That was more than a depression; it was something of a partial collapse; it was not the normal type of depression. We will never have a repetition of it partly because institutional changes have strengthened the system and because political sentiment will not allow for a policy of wait and drift.

This brings me to the final point in my lecture. The fear of a depression at the present time is partly occasioned by fear of the rearmament program. What will happen after the rearmament program tapers off, if it ever does? This raises the question of the impact of the military program on the American economic system.

The way that economists chiefly measure the impact of the rearmament program is to see what has happened to the GNP since 1950. Before the Korean outbreak, the GNP, measured in prices of 1952 to avoid any influence of price changes, was running at a rate of 302 billion dollars a year. At the present time it is 367 billion dollars a year, a 65-billion-dollar increase in the GNP in three years. This is about a 20-percent increase and all in all a remarkable production performance.

In 1950 the services and the Atomic Energy Commission were spending a total of 19 billion dollars out of the 302 billion dollar gross national product. That was about 6 percent of the GNP. At the present time such expenditures are running around 51 billion dollars, an increase of 32 billion dollars in the military program. This represents about 14 percent of the GNP. But meanwhile the GNP has increased 65 billion dollars. The military has taken 32 billion of that and the civilian economy has taken the remaining 33 billion.

So often we hear it said these days that this military program and the tax program that goes with it are a danger to the economic system, that we are in some sense on the verge of bankruptcy. I think such pessimistic statements are completely uncalled for. The facts show a 65-billion-dollar increase in goods and services in three years; a little over half of this went into the civilian economy; a little less than half went into the military program. Consumption on the part of individual consumers has increased, figured on an aggregate and a per capita basis. Savings on a per capita basis have increased, and the military program has increased a great deal.

To be sure, there has been a big increase in taxes. The tax bill for the economy as a whole since 1950 has gone up over 30 billion dollars above the 35 billion dollars of revenue in 1950. The tax bill, in fact, has gone up just about as much as has the military procurement from the GNP.

From a money point of view the rearmament program has been a self-supporting program. It has been covered by increased tax money. The increase in tax money has just kept step with the increase in the amount of money spent for the military program over the three-year period.

Now, to be sure, the increase in taxes means that individuals have less to spend and less to save by virtue of those higher taxes. However I am prepared to argue that the sum of 30 billion dollars of extra taxes is income the public would not have had were it not for the rearmament program. That is to say, the civilian economy, from the standpoint of disposable income, consumption, saving, and investment is fully as well off as it would have been in the absence of this big military program.

In one sense the program has been a self-financing project, in real terms as well as in financial terms. The 32-billion-dollar increase in the military program over 1950 is hardly at the expense of the civilian economy. You might say that people have to work a good deal harder to produce this larger amount for the military program. Well, let us take a look at the figures.

There are 3 million more people at work today than in 1950. That is about a 5-percent increase in total employment. There has been about a 2-percent increase in the average hours worked on the part of the public since 1950--5 percent more people and everyone working on the average 2 percent more time.

The total amount of additional effort if measured simply in terms of more time, comes to around 8 percent, but the total amount of goods and services available to the civilian economy at the same time is about 11 percent. That is to say, the amount of additional time worked has been more than covered by additional goods and services available to the civilian population. The whole 32 billion dollars of additional goods and services for the military program is over and above. How did we get it? Mainly from three different sources.

First, there has been an enormous accumulation of capital going on ever since the Korean War started. Right now investments are higher than at any time in the history of this country.

In the second place, technical innovations have taken place which make capital and labor a good deal more efficient.

In the third place, the increase in employment has been in the direction of more expensive and higher valued goods.

If we look at the figures, our increased production of ordnance is up about six times. The whole range of electrical industries is up about two or three times. The increase in employment and somewhat longer hours of work have been in the direction of higher-valued products. At the same time, fewer people are working in agriculture, which is a lower-product industry. Without necessarily working very much more in terms of time, the shift into higher product-value industries has increased GNP percentagewise twice as much as the increase in time worked for military and civilian purposes.

But now you might say, What about the money? Taxes have increased over 30 billion dollars, and that is about what the increase in the military program has been over the three years. There are two ways of looking at the budget and looking at public finance. One is to count all the cash that comes into the Treasury and all the cash that goes out the cash budget. On the basis of cash collected in taxes and cash spent, for the three fiscal years 1951, 1952, and 1953, the United States budget shows a surplus of over 2 billion dollars. In terms of cash, the defense program has been covered.

There are of course, expenditures which are not cash outlays but show up in the administrative budget. This budget includes many intra-government expenditures, by one Federal agency to another. Such payments are also Federal agency receipts, but they show on agency budgets only as expenditures.

The sum of about 50 billion dollars of the national debt is owned by Federal Government agencies, mainly trust funds. This involves probably 1.5 billion in interest that the United States Treasury pays to other agencies of the Government. The payment appears as a Federal expenditure, which is a bookkeeping transaction in reality. It is not a cash expenditure. The public debt has gone up 10 billion dollars since 1950 but on a cash basis the Treasury has a 2-billion-dollar surplus. The cash budget in 1951 showed a surplus of 7 billion dollars. This past fiscal year it showed a deficit of over 5 billion dollars.

The financing of the present military program then has been remarkably sound compared with the financing of World War II or the financing of World War I. On a cash basis over 100 percent of the expenditures for the present program have been covered by taxes. From a physical production point of view, the goods taken out of the system by the program has been matched by the added taxes taken out of the increased income. And the civilian economy is left with more goods and services and with more income and more savings than it has ever had before. The system has adjusted remarkably well to high taxes and high military expenditures.

When necessary the system probably can adjust back without much trouble--by cutting taxes quickly so that the public can spend more of its income as the Government spends less. The system has grown to a point where it can adjust to a big military procurement program. At the same time, taxes have grown to a point that a skillful and prompt reduction holds promise of cushioning, possibly of offsetting, a reduction in military outlays. In any case, a reduction in military outlays would cause only a temporary pause, if that. The basic toughness of the American economic system can take a military program either way, and grow.

Thank you.

QUESTION: I am not a student of economics. But in this national growth, the 3.5-percent increase, and so forth, it is not clear to me whether you have taken into consideration the reduced value of the dollar?

DR. BURNS: The 3.5 percent represents, since the war, real output increases, discounting the influence of price. It is much higher if we take the cheapened dollar over that period of time, but all the figures I gave here were in constant dollar terms so that inflation does not affect what I said.

QUESTION: You mentioned that our gross national product today was 367 billion dollars. Is that at the present value of the dollar?

DR. BURNS: It is in terms of the 1952 dollar. The contrasts of 1950 to 1953 were in terms of translating everything into the 1952 dollar so that the inflation of the last several years does not affect my comparisons. Also when I spoke of the 2.5- or 3-percent increase over a long period of time, that is in commodities and services without the influence of inflation distorting the figures at all. Statisticians make corrections for price increases and the figures measure a real increase in GNP.

QUESTION: You spoke of the effects of this increased military budget on spending since 1950. I think you mentioned, we will say, roughly 30 billion dollars for us, 30 billion dollars taxes, 30 billion dollars increase in consumer products for the civilian economy. We know that if we went into all-out production for the military in the event of a major war, the military budget might go out of sight, to 100 billion or more--

DR. BURNS: You are being conservative.

QUESTION: Yes, sir. Somewhere, we will say, the 100 billion, which is conservative, the civilian economy must be disturbed, at least we had that experience in the last war. But I would like to know what your views are on the principle. I don't think you mean to say that 30 billion is the optimum point. You could go to 40. Then what would happen to the GNP as a result? Would you comment on that?

DR. BURNS: One way to look at it is this way: If we should in this country get hours of work up to the point where they were in 1944 at the peak of industrial mobilization during the war, this increase of hours of work over the present level would increase the GNP from the present 367 billion to approximately 440 billion dollars.

Now that is a 70-billion-dollar increase of GNP in real terms. We could maintain our present consumption standards, our present levels of investment, and, by working a bit longer, add 70 billion dollars to the GNP. Of course, there would be the problem of getting the 70 billion dollars in taxes, but out of the increased output, there would be increased income, and out of the increased income, there would be more taxes.

COLONEL BARNES: Is that with the current labor force?

DR. BURNS: Current labor force.

QUESTION: Do you have any accurate figures on Russia's economy, of what its increase over the last 50 years has been?

DR. BURNS: No, Russia doesn't publish figures as comprehensively as we do. There have been some estimates made of its rate of growth. How reliable they are, I don't know. They have grown. But there is this rather interesting point, it seems to me, that one set of figures on the growth of the Russian economy, going back to the 1870's up to the revolution and from then on, indicate that the rate of growth has been just about in line with the rate of growth of the Russian economy before the revolution. I mean the extrapolation of the earlier figures would come just about where they are at the present time. I wouldn't put confidence in those figures because the Russians don't publish reliable data. They have expanded but not as much as the United States, I am sure.

QUESTION: Doctor Burns, I have gathered from what you have said that the top political economists and the administration have gotten the solution of the problems of the economy by the well-known you know what. In other words with more butter, you can get more guns. You mentioned further that we may hope to have a sloughing off in taxes, but we have a resurvey of military requirements coming up now. Suppose we require much more? You have based your statement on the status quo, the military effort at present. Suppose we had much greater emphasis on the military, I think it has a bearing on the question of just what is that optimum? How far can we go? Can we use more butter and still get more guns? Can we still increase the GNP to a point?

DR. BURNS: To a point, yes. Probably we could maintain the same level of consumption and investment that we now have and with an increased GNP. Because of improved technology and the accumulation of capital and some additions to the labor force, we could probably increase the military budget about 12 billion dollars a year over the next few years, without cutting into civilian consumption and investment at present levels.

QUESTION: Would inflationary prices be in that picture?

DR. BURNS: No, I am excluding the inflation in the 10- or 12-billion-dollar figure in expectation that, should the military budget actually be increased, steps will be taken to get additional revenue in to cover the increase. If the revenue isn't brought in, then the increase in the military program could be inflationary, depending on where the money comes from.

QUESTION: I would like to restate about the last three questions, sir, in a little different way. Our course is directed at a study of economic mobilization, and we hear a great deal during wartime of all-out effort. I am speaking of full mobilization in which you would want so-called all-out effort. You have developed the GNP and stated that it could be increased a certain amount. How much of that GNP percentagewise could be diverted to the military prosecution of a war without the civilian economy suffering unduly, collapsing, or failing to support a major effort?

DR. BURNS: As I said a moment ago, by holding the civilian economy at present levels and increasing the hours worked per week to what they were in World War II, in 1944, we could squeeze out about 70 billion dollars more of GNP which would be added then to the present 51 billion dollars to make 121 billion dollars, potential, at current consumption and investment levels.

Suppose we change the illustration a little bit. Suppose that the economy went back on a per capita basis to the consumption level of World War II, which was pretty high, and investment was cut back to something like 15 billion dollars for the maintenance of civilian facilities. Consumption and investments under those circumstances would come to about 200 billion dollars, out of a potential GNP of 440 billion dollars roughly. That is a lot of GNP that potentially could be diverted to the military program without cutting civilian standards below the level of World War II.

QUESTION: Dr. Burns, you have described to us a sort of ideal balance which is effective at the present tempo. However, from recent reports there is apparently considerable agitation for us to deal with our allies in terms of raw materials and manufactured goods. Now, if we adopt that policy and allow England, France, Germany, and Japan to ship in sizable quantities of goods and place those goods in our markets, would not that, to a considerable extent, upset this ideal balance which we have to date?

DR. BURNS: The balance I would not describe as ideal in terms of our international economic relationships because we have been exporting several billion dollars a year more than we have imported; by and large the deficit, so far as the foreigners are concerned, has been made up by grants on our part. If we allowed larger imports to come into the country, the effect would probably be rather hard on some industries. We would have less then, of course, to give away in terms of grants to foreigners, but the amount that could be brought into the country, even if we liberalized our tariffs and customs regulations, would not be of very great proportions. After all 60 percent of the merchandise that comes into this country comes in duty free and 40 percent is subject to tariff. It has been recently estimated that if tariffs were removed from the 40 percent, we might buy 2 billion dollars worth more from abroad than we now buy; 2 billion dollars, I submit, out of a GNP of 367 billion dollars is pretty small. It would hurt some industries, but it would have, in my opinion, no important consequence from the standpoint of the economy as a whole.

QUESTION: You talked about instability in our economic system. Did I understand you correctly that, in your opinion, if this amount of 30 billion dollars in taxes were left with the consumer rather than Government taking it, it would offset the production and keep the present high standard of employment that we now are enjoying with the sum of 30 billion dollars that is going into military production?

DR. BURNS: It might not be quite as smooth an adjustment as you suggest, but if there is to be a substantial reduction in military procurement, let us say in the neighborhood of 20 billion or 25 billion, taking that amount of demand out of the market in and of itself would be a pretty serious thing. I suggest that one way to offset it would be to cut taxes, let us say, around 20 or 30 billion dollars immediately, very quickly; just as the procurement programs drop off, cut taxes. And I am sure most of us would spend some of the tax rebates that we received, and it would either wholly or partially or largely offset, in my opinion, the drop in military expenditures.

The fact that taxes are very high gives Government a powerful instrument for stabilization control if it wishes to use it and if it uses it quickly enough. It is a lot easier to cut taxes theoretically and get that money spent than to appropriate additional money for public works which are difficult to get underway quickly.

QUESTION: We hear a lot of discussion that some sort of Government spending is necessary to maintain our high standard. Do you think that is true or can we maintain it without Government spending?

DR. BURNS: We cut total Government expenditures from 100 billion to 35 billion dollars almost at the same time the civilian economy expanded tremendously. Of course, there were deferred demands as a result of the war, but we had very high production and employment in the late 1940's and up until the Korean War broke out without really extraordinarily high levels of Government expenditures. My own belief is that the system is a good deal less dependent upon public expenditures to support the total amount of production and employment than a lot of people believe.

COLONEL BARNES: I would like to clarify one point I raised about current manpower before we leave. I am not quite sure you understood me or I understood you. You said we could, with the same hours of work that we had in 1944, up our 367-billion-dollar GNP to 440 billion dollars with the current manpower. Do you mean to say that we would not have to put on any extra workers or extra shifts, but just by additional hours of the present labor force we could jump to 440 billion?

DR. BURNS: Yes. This is just an arithmetical calculation. On the average nonagricultural workers of the country are working about 40.5 hours per week. During 1944 the hours worked were something like 46 on the average. What I say is, by increasing the average hours worked from the present level, with the present labor force, to the average hours worked in 1944, you would add approximately 70 billion dollars to the GNP, with the present 62 million people at work.

DR. KRESS: Dr. Burns, on behalf of the Commandant and the students, I thank you. This discussion with you will be continued at 10:30 Monday morning. Thank you.

(29 Dec 1953--250)S/ijk