# THE PRICE OF NATIONAL SECURITY

17 October 1955

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Publication No. L56-43

INDUSTRIAL COLLEGE OF THE ARMED FORCES

Washington, D. C.

Dr. W. Randolph Burgess, Under Secretary of the Treasury was born in Newport, R. I., on 7 May 1889. He took A.B. and M.A. degrees at Brown University in 1912 and the Ph.D. at Columbia in 1920. He holds an honorary LL.D. from Brown University awarded in 1937. Dr. Burgess was with the Federal Reserve Bank of New York from 1920 to 1938, serving as Vice President, 1936-38. He served as Vice Chairman of the National City Bank of New York, 1938-48, and became Chairman of the Executive Committee, 9 March 1948. Dr. Burgess was appointed Chairman of the Board of Directors of the City Bank Farmers Trust Company, 10 March 1948. He was appointed Deputy to the Secretary of the Treasury 21 January 1953 and Under Secretary in August 1954. He was President of the American Bankers Association in 1944-45. The publications of Dr. Burgess include "Trends of School Costs," 1920; "The Reserve Banks and the Money Market," 1927, revised 1936 and 1946; and Editor: "Interpretations of Federal Reserve Policy in the Speeches and Writings of Benjamin Strong," 1930. This is his first lecture at the Industrial College.

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GENERAL HOLLIS: Gentlemen: It is a privilege to present to you our speaker of this morning. The old cliche that the job should seek the man is well borne out by his life and his experience. He is professionally first in the money market of the United States. You have read in his bibliography of his long association with the Federal Reserve Bank of New York, with the National City Bank, that great financial institution of New York City, and with the City Bank Farmers Trust Company.

He has written widely on the subject of money management and lectures frequently, as he is in much demand as a speaker.

We are very fortunate to have as our speaker this morning the Under Secretary of the Treasury, Honorable W. Randolph Burgess.

SECRETARY BURGESS: General Hollis and Gentlemen: I am glad you did not all come in uniform. It would have been a little overpowering. I remember years ago speaking at Annapolis, and in looking out the window I saw the whole student body marching toward me--a very fear inspiring spectacle.

I am glad of this opportunity because it carries my memory back a bit. I am old enough to be justified in reminiscing, I guess. I remember very well when the Industrial College was founded in 1924. I was still a reserve officer from World War I and was doing tours of duty now and again in that general area.

This carries me back also to an experience in World War I, when I was associated with Leonard Ayres in the Statistics Branch of the General Staff of the Army; and of course there our business was to record particularly the industrial achievements of production and that sort of thing, and we ran over into the air pockets in the Armed Forces on matters of industrial and economic information. The officers, for example, who were assigned to us in the Statistics Branch of the General Staff, were completely bewildered with the kind of information they ran up against when they were faced with a war in which the industrial phase was so very much a part of the thing. Out of that

experience there was made perfectly clear the need for many officers in the Armed Forces who were informed on economic matters and on industrial trends, so that they would understand the language.

The progress that has been made since that time is enormous, and I think it clearly paid off in World War II and will pay off in the future, because it has to pay off; because the kind of war we would have to fight in the future, and the degree of preparation for war so that it would be a preventive one, certainly depends on economic and industrial information.

So, in preparation for this talk this morning, I have been reviewing in my mind some of these previous experiences on the price of war, thinking in terms of the money situation and the economic situation. When I was reviewing, for example, I pulled out a book that I helped to write, and I pulled out of that book a speech by Benjamin Strong, at that time the Governor of the Federal Reserve Bank of New York.

His speech was before the War College and may have been in this very room.

If you want to pick up a chapter which discusses that whole question of the financing of war and its economic effects, it is in that speech by Benjamin Strong. It is in a little book which I edited, called "Interpretations of Federal Reserve Policy in the Speeches and Writings of Benjamin Strong."

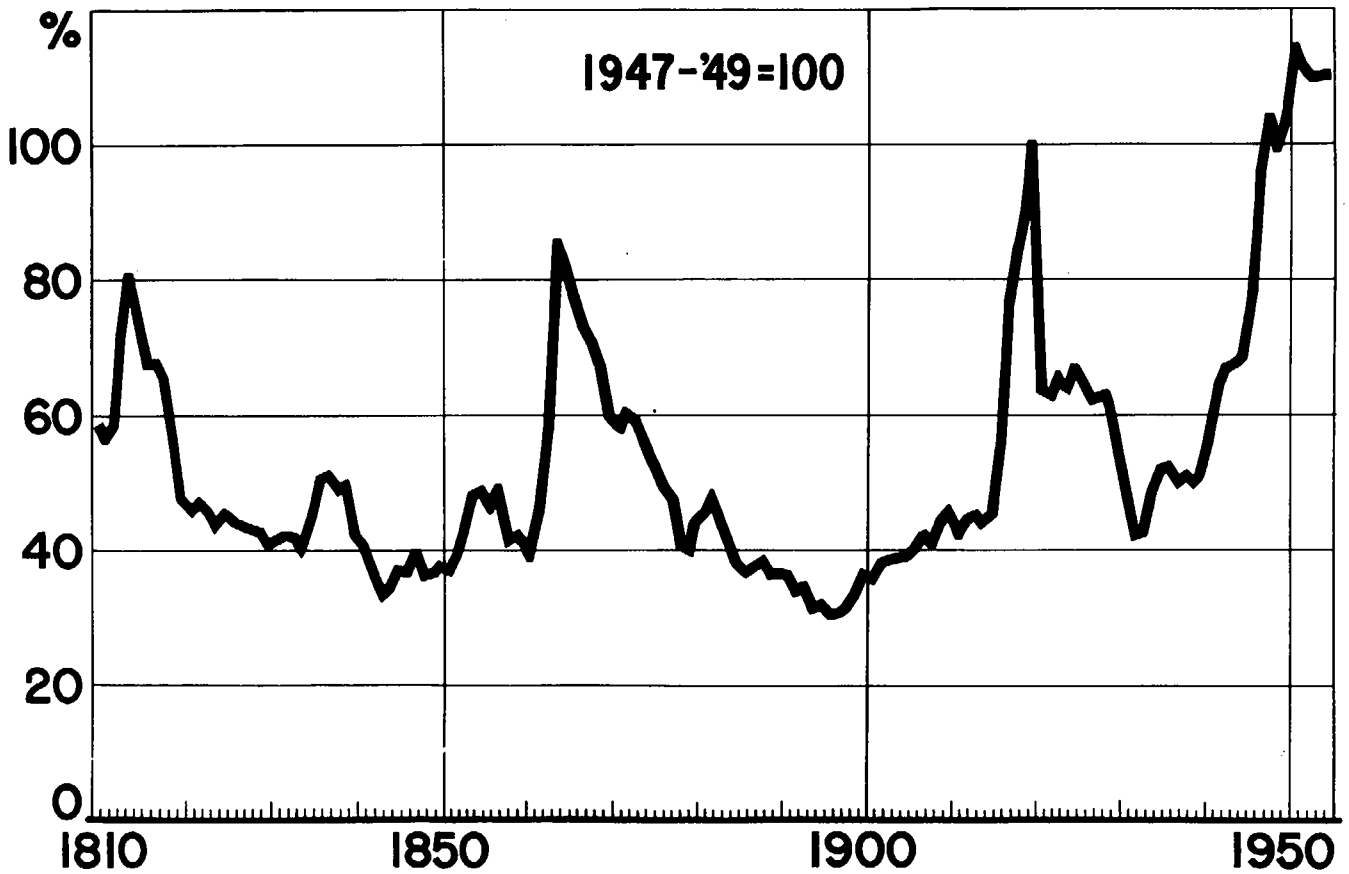
There is, of course, a wide literature on this subject of the economic and monetary effects of war and of the preparation for war, and the price of security. I thought this morning, as a way of boiling it down and getting a dramatic focus on it, I would bring here a few charts which deal with the subject, and which may stimulate your questions, because I do not hope that in the few minutes which I have that I can really cover it.

I will just open it up (chart 1, page 3) and let your minds work at it, and see if I can help you think about it.

Now, I left that first chart open standing there so that it would hit you in the eyes when you arrived on the scene of action, because that is a graphic way of showing the price of war--the price of security.

CHART 1

# WHOLESALE PRICES

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You will see that the chart runs for something like 150 years and shows what happened to wholesale commodity prices in the United States over a period of four major wars.

This goes back to 1810, and the War of 1812 is clearly reflected in this rise of prices and in the drop after the war.

The Mexican War did not make much of a dent in it.

Then the Civil War came along, and there was a doubling of commodity prices, and again prices came back after the war to a lower figure.

The Spanish American War had very little effect. I suppose this little rise here (indicating) reflects that war--1898.

Then we had a gradual rise in prices during the early part of the century, until we hit World War I. Prices started up even before we entered the war. In fact, the bigger part of that rise was before we entered. There again prices doubled and then came back again in the period of the twenties, which, by way of passing, was one of the great prosperities the nation has ever seen. Prices were fairly stable for a while, and then dipped down in the depression almost to the level before World War I.

Then we hit partial recovery from the depression, and then World War II, which carried prices again to something like double their prewar figure.

Now, the interesting thing about this is that prices have not come down again. They have stayed up there. Now, you can speculate on that all you want. Of course one reason is that we were just starting to demobilize from World War II when we found we had another on our hands, the cold war, in here (indicating) which meant rearmament and very heavy military spending, and a continuation of budget deficits.

So, in terms of the economy of the country, that is a graphic way of showing the price of security. You all know, without my outlining it, what the effect of that sort of thing is on the economy. When you have price rises of that sort, people on fixed income--the pensioners, the school teachers, people whose income does not rise very fast--are all subjected to very serious troubles; whereas the speculator, the wage earner who can put pressures on, tends to benefit and push his income up even faster than the price level itself.

In fact, through these periods the farmers have done extremely well. These periods after the war are when the farmer does not do so well. When we think about the farmer today, we have to remember what he has had. His was an extremely prosperous position during the war, with a little decline after that.

So price changes affect an enormous number of people in many ways. I am interested in a couple of colleges, and you know what this does to them, because their endowed funds do not increase--the income from the endowed funds does not increase; the spending budget enlarges; their expenses go up; they have to pay teachers a little bit more to hold on to them.

In a thousand ways the cost of war is shown here. Of course in this country we have been mighty lucky. This performance of ours is far better than the performance in most other countries. You have, of course, the tremendous inflations in France, in Germany, and even in England, which did perhaps next as well as we did; but in most countries inflation was a great disorganizing factor, the thing that took the bottom out from the economy. Many of those countries have not recovered yet. However, in Europe they are now back well ahead of prewar and getting their feet pretty solidly under them.

Now, let us go back to this and analyze what you do about it. Of course in the midst of war you try to hold down these wholesale prices by price controls of one sort or another--price and wage controls--slap them on as fast as you can. Usually you are too slow. I think one thing this shows is that we never had much luck with that in our experience. That is the experience of most countries.

You can try to force, to compel, prices to stay put, but they don't, in one way or another. If you have pretty rigid price fixing, wage fixing, and rationing, it is a palliative, but it does not go to the root of the difficulty.

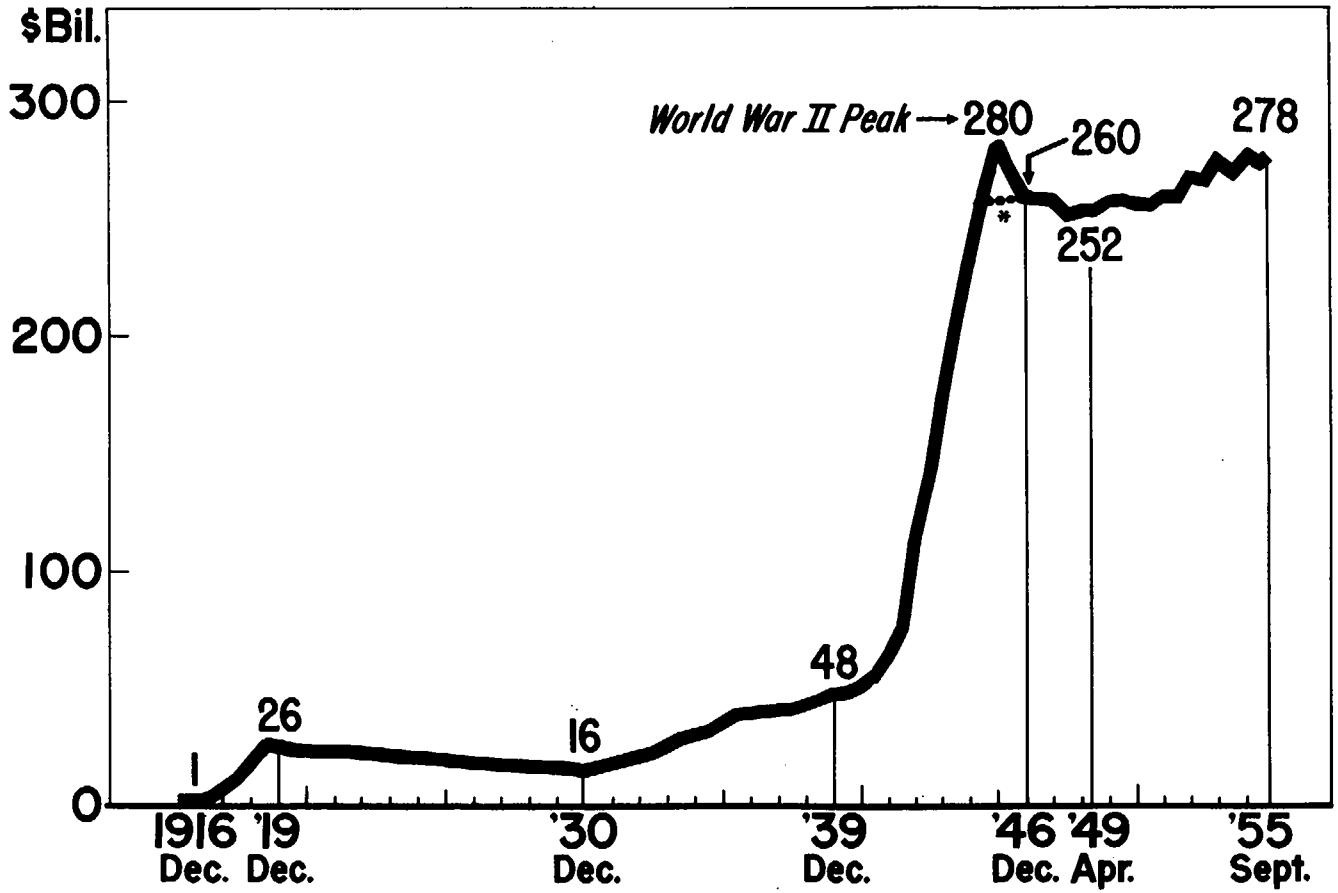
The real problem goes back to the basic economic conditions that press on these prices and move them.

Now, if we can have this first chart slipped down, we will go back into the causes of this thing and try to analyze them a little bit.

Chart 2, page 6.--Here is the really guilty party. It is the changes in the public debt that bring about the trouble. The public debt of course

CHART 2

# THE PUBLIC DEBT




*Excluding Victory Loan proceeds used to repay debt in 1946.

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is a shorthand term for what goes on. What happens in time of war is that a country spends more than it receives in taxes, and the result is that the balance has to be made up by one form or another of debt, which is apt to be the equivalent of printing money. When you don't collect enough taxes to pay your bills, what do you do?

The old sovereign used to clip the coin. A little later than that he used to print more paper money. They still do that in many countries. We have a modern and improved device for doing that. We do it by bank credit, by selling Government securities to the banks, and by backing them up with the central banking system, the Federal Reserve, putting out money to banks to enable them to buy Government securities.

Here is the guilty party--the debt. This is what you have to deal with fundamentally if you are going to face the situation. Of course, the first thing you try to do in time of war in this area is to tax more, to try to bring your taxes up to a point where they will carry the largest part of the war costs.

Now, that was not always the theory. Back in the War of 1812, Secretary Gallatin, one of our ablest Secretaries of the Treasury, whose statue sits in front of the Treasury Building on Pennsylvania Avenue, developed the theory that that war was going to be just a little war, one of those little jobs, and they could pay for it by borrowing money, which would not disturb the country's economy as much as levying taxes would. They pretty soon got into trouble in trying to sell bonds. It was difficult to do so; the people were skeptical of the credit of the country; and interest rates went up to 6, 7, or 8 percent.

In the Civil War we had a mixed up policy. The Secretary of the Treasury at that time did not like to put on the brakes very hard and they did not start collecting taxes soon enough. They did not get them rolling; not until they had been at war 2-1/2 or 3 years.

We learned something from that lesson and in World War I we did increase taxes with great rapidity. Fortunately, we had just introduced into the tax system the income tax, which has become a more and more progressive tax on incomes, as some of you gentlemen recognize, and a vehicle for raising a lot of money.

The income tax also was supplemented by various forms of excise taxes. Of course there are problems in getting the taxes up. You

don't want to destroy your economy in the process, because you depend on that economy to carry you along through the war, so you must not remove the incentive for working that extra hour or two on the part of the worker or the incentive for the buisnessman to put on full steam. He is moved deeply by patriotism and at the same time the prospect of a little additional profit if he works twice as hard is a factor in getting results.

I suppose the greatest difficulty in imposing taxes enough in time of war is the inequity of it; the difference between different kinds of taxpayers. Here is a wage earner, for example, whose wages are doubled. He can well afford a 25 percent increase in taxes; whereas let's say, an army officer whose wages don't get doubled quite in the first years of the war--Congress puts them up only 15 percent or something like that--cannot afford such a tax increase. To apply the same rates of taxation to those two people obviously is unjust. You tax one unreasonably while you are putting a reasonable tax on the other.

In the past war we tried various schemes to work out a tax that would be based on the increase in income. Congress, after surveying that carefully, decided that was not practicable. I suppose we will have greater wisdom with each new emergency as it comes along. The thing that appalls you, of course, is the political pressure.

Let me illustrate that. If you compare our tax system with the tax systems of most other countries, you find that we collect a much larger portion of our taxes directly from the individual in the form of the graduated income tax, whereas other countries collect a much larger part at the point where somebody spends some money--not where he receives it--through excise taxes of one sort or another.

The British have, as you know, a tremendous purchase tax which runs 20, 30, or even as much as 40 percent. They have nibbled it down a little bit. It hits the man at the point where he purchases something.

Now, in the past crisis, just recently, we have faced the question of the renewal of those excise taxes, and it becomes a battle royal. The automobile people and everybody who pays excise taxes come down and say that the greatest injustice would result, the greatest calamity to the country, if these excise taxes were continued or raised. The battle on that is much more political than on the income tax; whereas the income tax is the one where, in my judgment, there is much

more injustice. What that does, particularly to the middle ranges of incomes, is the most grossly unfair part of our system of taxation.

So that illustrates the problem of taxes in time of war. You can do a great many things you can't do in time of peace. We have been successful in mixing up the taxes and putting in the excise taxes. The best tax system is no single approach to the problem, but is in approaching the taxpayer on various different fronts--the graduated income tax, the corporation tax, the excise tax of one form or another, spread over the whole economy. By mixing it up you can make the rates higher and bring in more income than you can if you focus it all in one kind of tax, where the injustices to different groups of people are much more obvious.

But no matter what pious resolves you start out with at the beginning of a war, it becomes impossible to finance a war wholly from taxation. About the only real record we have of financing a war currently without accumulating debt was Napoleon's campaigns, and he broke the ground rules, because he collected so much from the nations he conquered. So it did not become a very typical performance, and we can't shape our own policies after that. But he, however, curiously enough, had a very sound theory about it, and fought desperately to avoid financing a war by borrowing. So it was not all good fortune, of having conquered every country he encountered; but it was partly a sound theory which he carried into effect, levying taxes and doing everything he could to avoid borrowing.

But aside from that example, most countries have failed dismally. I am not going to bore you by trying to give the percentages of war paid by taxes. They run less than 50 percent. Almost no civilized country succeeded in carrying it that high. Usually it is 25 or 30 percent.

In the last war we did much better than ever before. Increasing the percentage as we went on. The trouble was the cost kept rising on us until we got up to a hundred billion-dollar budget. We collected something approaching half of that in taxes.

Now, the net result of spending more than you take in is shown in this chart. The earlier figures are not included because they would not show on a chart of this size. Prior to World War I the debt stood at one billion. We had practically eliminated prior debts. That billion dollars was largely in bonds that bore circulation privileges, held by the national banks, that were kept out as a matter of policy.

Now, the debt went from one billion dollars in 1916 to a World War I high of 26 billion, which we thought at that time was a large debt. During the twenties that was paid down to 16 billion. That is an interesting period, because some of the modern economists say you must not ever pay off your debt, because it is deflationary. We were paying off the debt at the rate of a billion dollars a year in an economy a good deal smaller than the present one. We made a substantial payment. We had a roaring prosperity while we did it. Paying off a debt is not necessarily deflationary. It depends on what others are doing about their debts, and on the whole economy.

Then we ran into the depression of the early thirties, and began increasing the debt; so that by the time war came along in 1939 we had increased the national debt from 16 billion to 48 billion, all in time of peace.

That is a separate question. I won't try to discuss that--whether it was necessary or desirable or not, or how much of it was. It did not produce the kind of recovery that had been hoped for.

Then we ran into the very heavy war spending, resulting, as I said, in a budget, toward the end of the war, of almost 100 billion dollars for a single year, increasing the national debt to 280 billion dollars.

Now, there is a catch in that. That debt included about 20 billion dollars that was received in payment for the victory loan of December 1945, and that balance proved not to be necessary, because, as you know, war was terminated, and we were able to hold that balance for a while and then use it to retire the debt. So the real debt was more like 260 billion dollars. There was a 20-billion dollar balance which was never expended for war purposes.

Then, in the demobilization, the debt was reduced further by about eight billion dollars, and then, with some anticipations of Korea, and Korea, it began crawling up again; and it is now 278 billion dollars, and we are having plenty of trouble to keep inside the 281 billion debt limit that confronts us. We are going to bump up very close to it. It is, as you know, a temporary legal limit, and the debt limit goes back to 275 billion next June. We will have to deal with the Congress on that.

Our 278 billion dollar debt is, in a sense, a war debt. It includes a cold-war debt, too. It represents a volume of spending that is not

a peacetime volume. But all of you, I know, as you have been sitting there, have looked at that chart and said: "Here we are with this terrific debt. We have not retired it practically at all after World War II, whereas after every other war in the country's history we retired a substantial amount of debt." Well, that simple thought is worth grinding over in your mind, because debt is what causes this great price swing. That debt means an interest burden of around 6-1/2 billion dollars a year at the present time. Debt is a major factor in the operating of the economy. Operating with that debt, without making any dent in it, I know bothers anybody brought up in New England, and a good many people from other parts of the country as well.

So it is something. We have two problems. One is, we don't like the size of it, and the other is, it takes a lot of management; because it turns over completely about every four or five years now. We typically have an amount of new cash financing to do each year. More than that, we run into around 50 billion dollars of refinancing that has to be done in the course of a year, plus 20 billion dollars of Treasury bills that roll over four times a year. That is a disturbing factor in the money market.

I want you to think a little about that public debt. Let me pause a second. The three financial factors that handle the cost of the war are taxes, the management of the debt, and monetary policy. The second two relate to what you do when you find you can't tax enough to meet the costs of war.

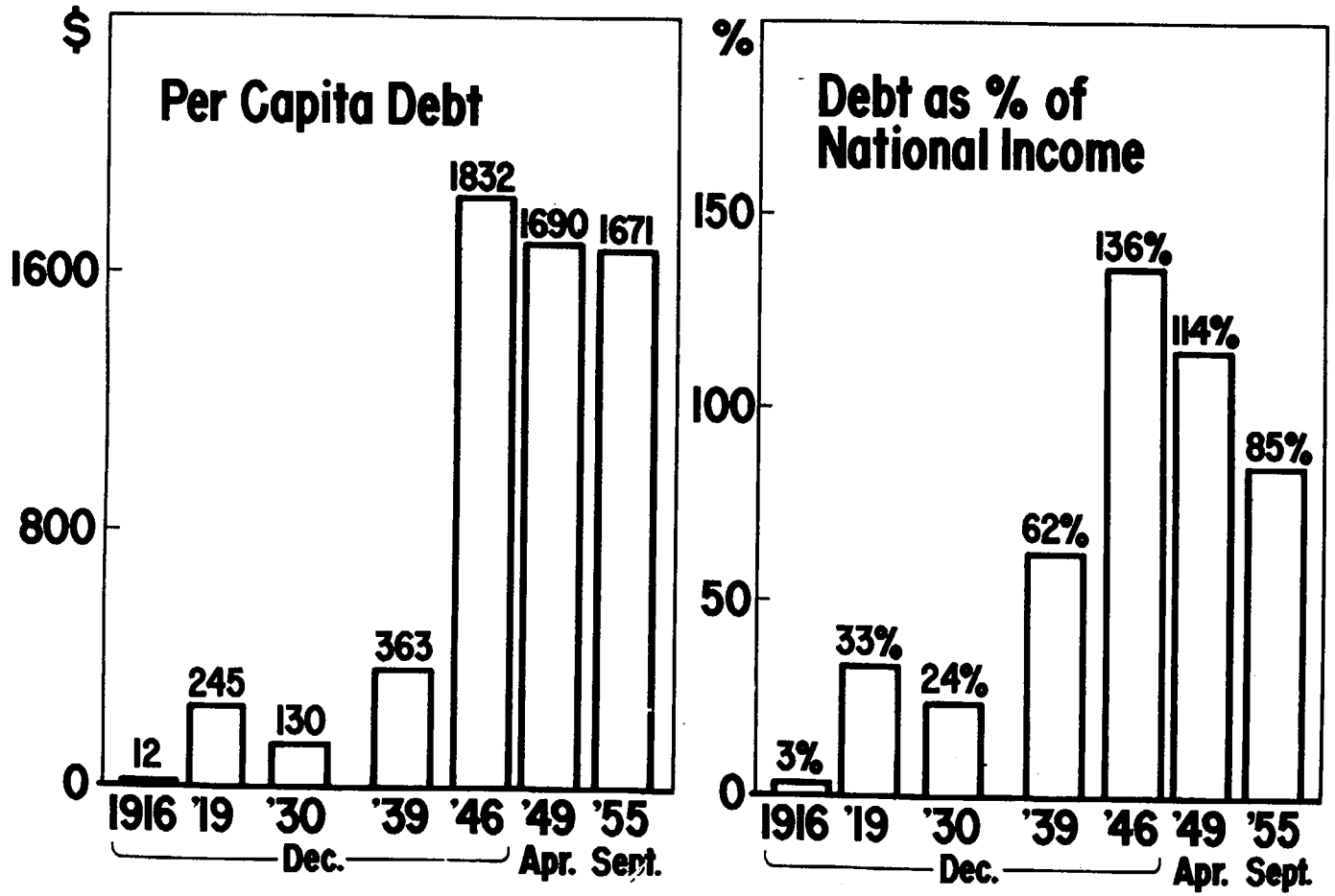
Now, I have been talking mostly about war, but exactly the same principles apply today when you are dealing with cold war. We are able to finance a much larger portion of it with taxes, but the same problems of the debt management and monetary policy appear today.

Chart 3, page 12. --The other charts will go fast. I wanted this one to sear itself into your souls a little bit. Lest it sear too deeply, I want to point to one factor that is just slightly cheering.

That is, while we have not made any dent at all in retiring the debt, we have done a little something about growing up to the debt. This tremendous debt is easier to handle today than it was, because the population increases, and because the national income increases. I think most of you read today in the daily paper the fact that the national income in the second quarter of 1955 is at a new high annual rate of 321 billion dollars. It is some 17 billion dollars higher than the record year of 1953.

CHART 3

# RELATIVE SIZE OF THE DEBT

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So if you look at the debt today as a per capita debt, divided by the number of people in the country, you get these figures over here (indicating). In 1916 it was 12 dollars per capita. In 1919, at the peak after World War I, it was 245 dollars. Then we reduced it to 130 dollars, partly by actual reduction of the debt, partly by the growth of the country. Then it increased in 1939, peacetime, to 363 dollars, and then jumped, in World War II to 1,832 dollars.

Now, since the end of the war, the per capita debt has been decreased by the growth of the population. As you know, the Army, the Navy, and the Air Force have done one very commendable job. The men who came out of there have done a great deal to increase the population--much more than anybody expected. Incidentally, that is one of the curious dilemmas of our age. Here we sit in the shadow of the atomic bomb ready to drop on us and destroy all of us and wipe us out, and yet our kids are producing more children than we did. In this dark world you can't figure out exactly what is going to happen to you, but you do know what some good things are in life. One good thing is the family.

Now, the national income has gone up even faster than the population--much faster than the population. We can't turn around and slap ourselves on the back for that, wholly. Part of it is due to inflation. Part of it is due to the prices I showed you in the first chart.

But here you have the debt as a percent of national income. It was three percent; rose to 33; went down to 24; and up to 62 percent. And 136 percent is the peak figure of the debt as a percent of national income. By the process of the increase in population and the increase in income, it is down now to 85 percent. Goodness knows, that is big enough.

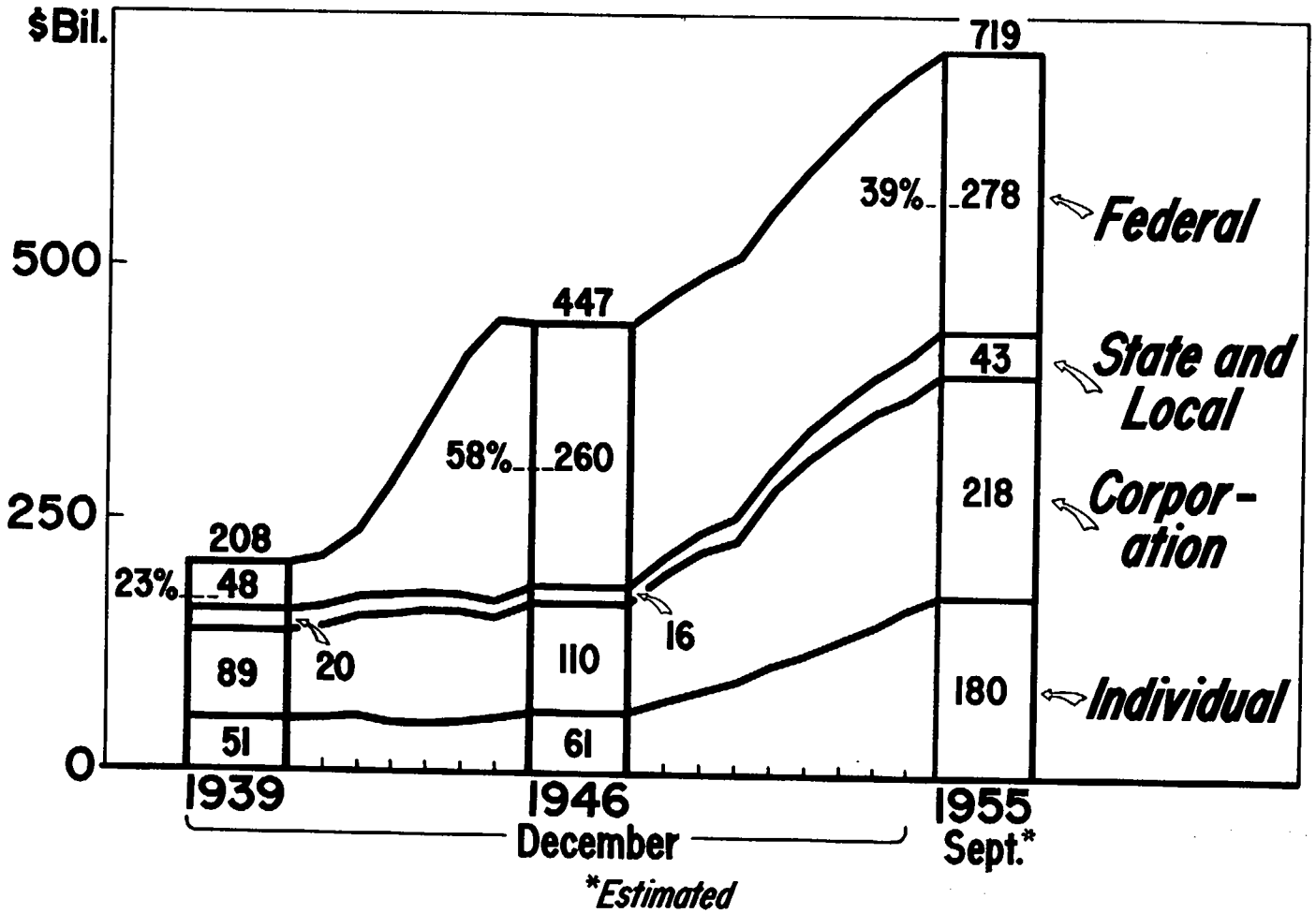
In the interpretation of this chart, you must remember that every little baby that is born into this world today has hung around his neck his share of the national debt, and it is 1,671 dollars.

Take that chart away; they can't bear it.

Chart 4, page 14.--Now, about managing this debt, which is the job we have at the Treasury, an important consideration is who else is borrowing money, and how much, and what happens when you go through a war period, such as 1939 to December 1946. During that period the national debt, which is here in the blue section, went up

CHART 4

# PUBLIC AND PRIVATE DEBT

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tremendously. It was 58 percent of the total debt in the country. The state and local debt did not go up at all. We just suspended public works, except for emergency work in connection with war housing and that sort of thing. The corporate debt went up hardly at all--89 to 110 billion; it was about 40 percent of the total in 1939. In 1946 it was only about 25 percent of the total. The individual debt went up relatively little during the war period.

When you go into the time of peace you exactly reverse this.

When you go into the time of peace, like this, you get a tremendous increase in the state and local debt, a tremendous increase in the corporate debt, and a tremendous increase in the individual debt. Under these conditions the Treasury has to take what is left over. We pay lower rates of interest because we are as good a risk as you can get and our problem of financing is in competition with all the other borrowers.

We have to handle this debt without going to the banks too heavily, which creates bank credit, and we try to appeal to the savers, but try to do it in a way which won't make it too difficult for the other borrowers. The borrowing of these people is essential to have a vigorous and going economy, the kind of economy where you can finance these gigantic war budgets that we have to finance today.

That illustrates one thing. It illustrates why we have a savings-bond program; why we make such a business of trying to get everybody we can in the country to put a part of his income into savings bonds regularly. In that way we take something of our share of the mass of accumulated savings and keep our debt from being too much in the hands of the bankers.

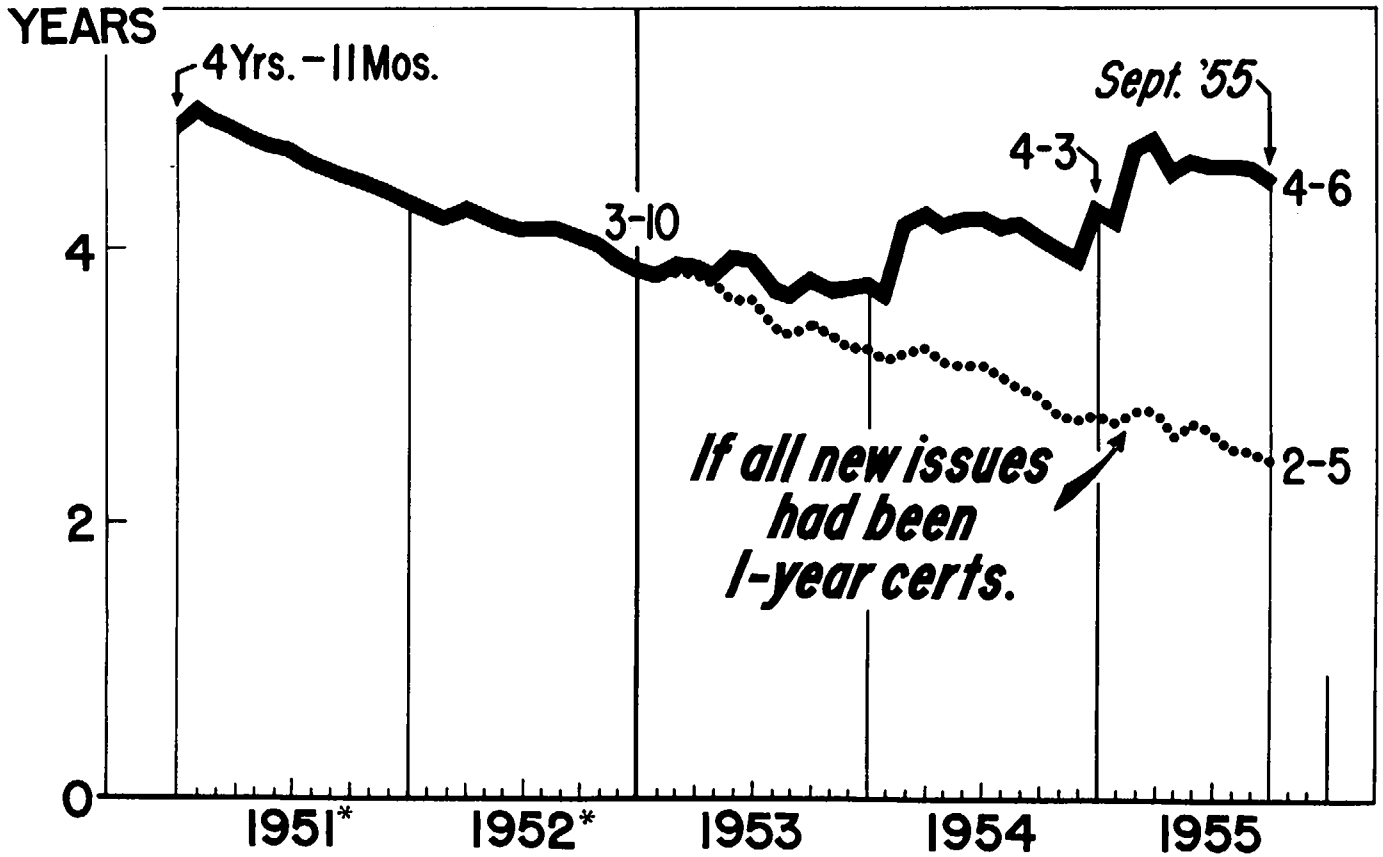
Similarly, we have to work out various other devices to appeal to particular types of investors. We put out a long bond when we think the market will take it. We don't try to force it on the market when it won't be taken. That is a matter of judgment. You have to judge the condition of the market, to see if what you have to offer is desirable in relation to it.

Chart 5, page 16.--Another way of looking at this debt business is the average maturity. The average maturity today of our Federal Debt, 278 billion dollars, is four years and six months. That is a little better than it was when we came in back here (indicating) two

CHART 5

# AVERAGE LENGTH OF THE MARKETABLE DEBT

## (Callable Bonds to Earliest Call Date)




*Adjusted to exclude 2½'s exchanged for nonmarketable 2¾'s.

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years and 10 months ago. It is quite a job to keep the maturity of the debt at some reasonable level, because time keeps catching up with you all the time. Bonds are constantly moving toward their maturity.

This simply illustrates our fight to try to keep our securities long, in the hands of non-bank investors, rather than short, in the hands of the bankers, where it is more inflationary.

Chart 6, page 18.--Now, I am not going to spend much time on this. This relates to monetary policy. You already had Win Riefler talk to you about that. This is an attempt to illustrate graphically what the monetary policy tries to do to keep things on an even keel. Of course the kind of economy that can finance a war or cold war needs to be fairly stable, an economy that does not run to booms or busts.

I spent part of the summer abroad in Spain, Italy, and Turkey this year. The thing you always notice when you go over there is the way they watch this country, because their own welfare depends so greatly on the continued relatively stable prosperity of this country. So, whether we look domestically on our ability to produce for the cold war, or among our allies, in either case the necessity for trying to avoid booms and busts is very apparent.

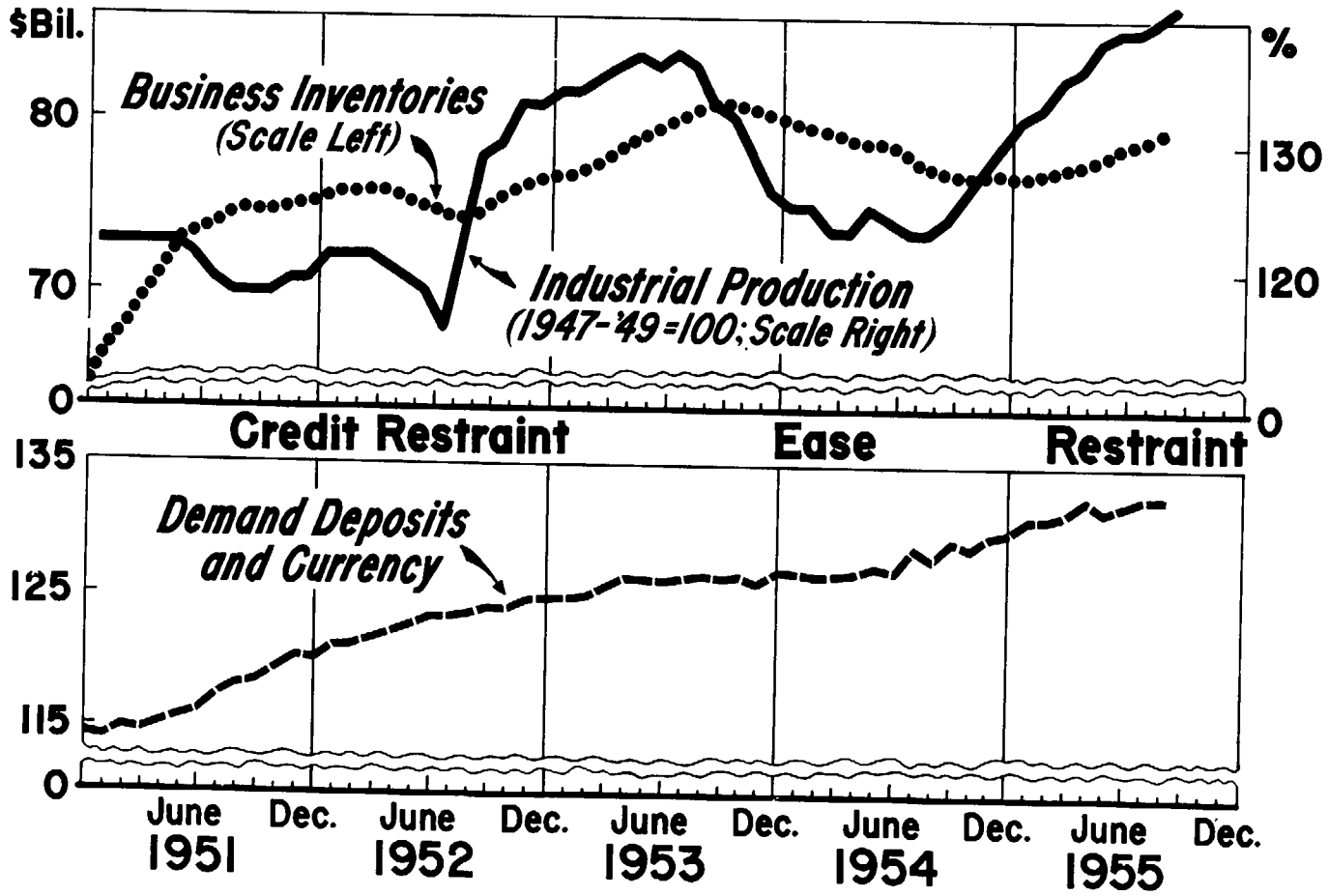
This is not as difficult as it looks. This figure here (indicating) is industrial production. This is the Federal Reserve Board index, which had a great boom in the second half of 1952. Whether that was due to the Eisenhower election or what it was I won't try to convince you. It went on up to the high point in the middle of 1953, and then eased off again, fortunately, because it was going too fast, and is back again to a pretty high point.

Now, whether it is going too fast or too slow is partly shown by this figure for business inventories (indicating). If you are producing simply for inventories, you do not have a healthy economy. Sometime you have to stop doing that. Then you have a slump. Here we were producing too heavily for inventory. For that reason, the policy of the Federal Reserve Board and the Treasury was one of credit restraint, which we have shown in pink. That is the area of credit restraint. When things start to go down again you add an area of credit ease. We are always trying to lean against the wind. At the moment we are leaning against the wind of boom, and trying to keep the thing from going too fast.

Now, that illustrates in a very quick way the three factors that you play with to try to keep the forces of war or cold war from destroying your economy.

CHART 6

# ECONOMIC INDICATORS AND MONETARY ACTION




*Note: Seasonally adjusted data.*

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Just in conclusion I want to read you a couple of quotes, one from this article by Benjamin Strong, where he says, "The true war reserve of the present day is a high, well-balanced productive capacity, and a people's willingness to consume less than is produced."

I will read one other quote, just by way of conclusion. The other day Bobby Cutler gave a speech out at the American Bankers' Association meeting in Chicago, and he gave a quotation which shows Jim Forrestal's philosophy. He said he was putting Forrestal's thought into his own words. (Incidentally, I noticed a good picture of Jim Forrestal out in the hall.) I quote:

> "The productivity of the United States, as developed by our industrial and scientific initiative and genius, is our greatest asset and our greatest power. Here is an unparalleled event in world history: the culminating productivity of America.
>
> "Our resources, such as coal, steel, wheat, cotton, and so on; our ability to produce and fabricate in mass quantities, because of the capacity of our managements and the skills of our laboring men and women; the inventive genius of our scientists; our vast transportation system--all these, taken together make up a potential that overshadows the capabilities of the Communist regime. More than the atom bomb, this preeminent industrial productive ability of the United States is the bulwark of peace in the world.
>
> "To the extent that we weaken or dissipate the enormous potential of industrial power that inheres in our American system, we invite despotic rulers to take the despot's last long chance and again plunge the world into war."

I think that is a good conclusion. I will be glad at the appropriate time to try to answer your questions.

DR. KRESS: Secretary Burgess is ready for your questions.

SECRETARY BURGESS: Let them fly, gentlemen.

QUESTION: In the event that compulsory savings during a war were found desirable, what would be the recommended manner of releasing this spending power after a war?

SECRETARY BURGESS: That is a subject that was thought about a great deal during the latter stages of World War II, to see what could

be done about it. It never got to the point where it was very definitive. Of course you can see what you can do. You can say we have to preserve incentives, say we are going to tax a worker, let us say, up to 30 percent of his income, but we will say that 10 percent of that will be refundable to him after the war; so, instead of a complete loss of those earnings, some of it becomes returnable. The difficulty with compulsory savings is that in one way you seem to preserve the incentive of the worker and it looks very fair in the picture up there, but imagine the rate you start at. Gelett Burgess refers to that as elliptical wheels on a car. You never work out anything satisfying. You don't preserve the incentive by saying you will give it back to the worker in X number of years. If you try to specify when you will return it, you are putting a load on your budget. If you don't, and then wait for Congress to make it a genuine obligation and decide when you can return it, that is really tough. When you consider the fact that we have not been able to retire any of our wartime debts, you can see if we had that additional debt of returning to our people some of these accumulated obligations, it would change the situation tremendously. I don't say that sometime, in cases of emergency, that might not work out. When they talk about it seriously they run into all those practical hurdles that seem so difficult.

QUESTION: Sir, I gather from your opening remarks that price controls weren't too effective in holding the price line. Would you be in favor of not using price controls, or do you think they do some good?

SECRETARY BURGESS: I think they did some good. You have to use them. I perhaps gave the wrong impression. One should not say they did no good. They did hold the line, at least in part. But there are serious difficulties which arise. You put a price ceiling on. Pretty soon you find the cost of production of this or that commodity has gone to a point where you can produce it only at a loss. At that moment you remove the incentive for production. So you have to adjust the prices.

It is all right to put in control right across the board at the first declaration of war. That's probably a good idea. Then your troubles for war only just begin. Then you have to get a group of people who will come in and make the adjustments that obviously become necessary as the war goes forward. Then you have to get another gang to enforce the levels arrived at; and the ingenuity of the great American public for finding ways around the price levels and ration books and so on is very great. We are a very ingenious people.

What I am saying really is that you have to do it, but that it does not go to the root of the difficulty, if you are spending such a lot more than you take in in taxes.

It is something you have to wrestle with and, at the best, you can't and don't expect too much from it.

QUESTION: Mr. Secretary, I wonder if you would discuss the reason for short-term financing of the public debt as opposed to long-term financing.

SECRETARY BURGESS: Well, the reasons are mostly the other way. When you finance in short term it usually means you are financing through the banks. When a bank buys government securities, new ones, it adds to the volume of bank credit. That increases the pressure on prices. I won't try to explain that. You all know that. Whereas long-term securities appeal to the insurance companies, savings banks, and individual investors, and get out of the bank-credit stream.

Now, you can't finance altogether at long term. The debt is too big; and the short-term debt is becoming a very convenient instrument for banks to do business. They use it to go to the Federal Reserve to borrow on it. They use it for adjusting their position when they get short of money. Thay sell some Treasury bills on the market, and so on.

It is also true now that a sizeable portion of the short-term debt is held outside the banks. Right at the moment, the amount of Treasury bills held by the corporations is very large. There is about 20 billion dollars worth of Treasury bills outstanding, or something like that. Most of that is held by business corporations and other short-term users other than the banks.

Now, if you wanted to stimulate the economy and wanted more bank credit to be created, you might deliberately finance at short term, so you would increase the volume of credit.

On that last chart I showed, there are times when you want to stimulate and times when you want to hold back. You try to adjust the borrowing schedule somewhat to those requirements. I say somewhat, because the requirements of actually turning the debt over are so great, it doesn't give you too much leeway.

QUESTION: Would you care to comment on expenditure rationing as a means of direct control and a cause of savings?

SECRETARY BURGESS: You mean expenditures of the individual. Of course we did that in effect during the war, when we practically told the automobile people to stop making automobiles; we removed one possible source of expenditure. Now, the prorationing of materials has that same effect. If you tried to tell the individuals how much they could or could not spend, then you would run into real trouble.

You do it really by allocating materials and by dealing directly with certain industries. You just stop making a lot of the things that people ordinarily would spend money for. By taxes you take away a lot of the income, so they can't spend it.

Those in effect are the ways you do it.

QUESTION: Mr. Secretary, I am delighted to find one humble economist who is disturbed by the size of the public debt. We noted in wartime that it increased taxation quite heavily, and we do it in a cold-war situation. Yet, because of the elections forthcoming, we talk about cutting taxes. What are we going to do? Never come to grips with it? Or let the growth of the economy minimize it?

SECRETARY BURGESS: Well, our Treasury policy is perfectly clear. You saw in the papers yesterday that George Humphrey was out talking to the President, and after he got through he made a statement that we do not advocate any cuts in taxes until we can see a budget surplus--until we see the budget in balance. He qualified that by saying it does not mean until we actually have balanced it, but when you are making an estimate for the fiscal year, you have the thing so that it is clearly in the bag.

I deprecate a great deal the news items that say both parties will push for tax cuts because it is election year. Politics are always in the picture, it is true. I think, though, that there are many responsible people in both parties who share our point of view.

Now, I will say that we have to get many stout fellows in the Congress who will stand up to be counted. The real problem comes in voting against a tax cut, which is very hard for a person to do.

That question calls for a prediction. I am afraid it is hard to make. I hope there are enough people like the Colonel and me who believe it is well to nibble down the debt, but over a period.

QUESTION: Sir, you seem to have indicated a preference for higher sales taxes and perhaps lower income taxes. Would you care to elaborate on that part?

SECRETARY BURGESS: Yes, that is my own predisposition. If you look at our tax system and compare it with the systems of other countries, you will find we have heavier income taxes and lighter excise taxes. I think the logic of it is that you do less damage by taxing the fellow who spends his money that you do taxing the fellow at the point where he earns it. His incentive is greater for earning if you don't tax his earnings.

I am all for the graduated income tax. I think it was a good law. It was particularly good when we made it pay-as-you-go, but I think we are making it carry too heavy a share of the load. I think it is a disincentive. I think it removes the incentive of the people who pay it.

We could collect with less pain and with better results, and get a larger share of our taxes at the point where the people spend the money, rather than where they earn it.

QUESTION: Mr. Secretary, I note the plateau on the wholesale price index for the last four or five years. Do you have a prediction on the turn this will take?

SECRETARY BURGESS: All I can say is that we are working very hard to continue that plateau. We think stable prices are good for a country, and that unstable prices are not. We have had the good fortune to be able to report practical stability in the cost of living, which does not fluctuate as much as wholesale prices, since we came in. I realize you can't control all the factors.

We are working very hard on it. The main thing is these basic factors of fiscal and monetary policy. Of course this has been an uneasy stability, in the sense that agricultural prices have tended to be weak and the prices of manufactured products, under the impetus of upward wage pressures, have tended to go up.

I do think, however, that the index of your nonagricultural prices may not be entirely exact; they may not take account fully of the discount house around the corner where you buy that refrigerator.

QUESTION: Sir, do you have any thoughts on the practicability or the desirability of imposing a tax for the specific purpose of retiring the debt--separate and distinct from all other present forms of government income?

SECRETARY BURGESS: It is a psychological question, really, a political or a psychological question whether that would be effective. Of course there have been various proposals for having specific taxes to meet specific needs. Somebody had a bright idea that we ought to have a specific tax to cover the cost of defense, so that we could locate that.

Of course it would not do any good to have a specific tax to retire the debt and have the rest of the budget unbalanced, so that you had to go into debt for the rest of the budget.

That is a psychological, political question.

QUESTION: Sir, I was curious about a particular tax we had for a very short period in the early part of the war, the automobile use tax. The Federal Government issued a five-dollar tax stamp which you bought at the Post Office. That would seem to be a fairly painless way to get 250 million dollars a year, with the automobiles running around.

I wonder why it was abandoned with such a short period of use.

SECRETARY BURGESS: I don't remember. I think it was the size of the squawk. It is the kind of tax that sounds very reasonable. You can't tell from that what the size of the squawk will be.

QUESTION: To go back to the question, which I think was a question on the retirement of the debt--I gather from your remarks that any reduction in the national debt will be as the result of more or less an accident. It just so happens that we end up having a surplus in one year; therefore we can retire a portion of the debt. Is there any move on hand or any plan to make a planned reduction of the debt?

SECRETARY BURGESS: Of course what happens, as you know, is that each year about this time the different departments go to work on the budget for the fiscal year 1956-1957. Then you have to decide the relative importance of aircraft, the carriers for the Army, the Navy, and so on, and each fellow puts in what he wants, and the civilian

agencies have road programs, and the educators say they must have a program for school houses. You try to add it all up and see where you come out.

Of course every secretary of the Treasury wants to budget for debt retirement. The thing you can't predict, of course, is what emergencies may arise for spending. You can't predict your tax receipts wholly, because the swing of the business pendulum may affect that a great deal. For example, this change in the stock market no doubt will enable a lot of people to take some losses. They will be glad to take some losses to reduce their income taxes. That may reduce income tax receipts somewhat compared with the estimate of three weeks ago. There are certain intangible factors

What we would like to do is make up our budget now for the statement of the President to Congress in January providing for a certain amount of debt retirement. I think we must not despair about this whole thing. As you gentlemen know from all your experience, we are having a cold war, which is just as much war as the war we were fighting before this, a different character of war. And if the Armed Forces are spending 34-1/2 billion dollars a year, or whatever the last figures are, that is a terrific handicap to retiring the debt.

We hope the time will come when we can do that; but, frankly, it has not come yet, and while that great block of expenditures is there it is going to be very hard to retire the debt. I hope even with that, assuming that it continues at that level, which it may, that we can retire some of the debt. But again, it will be very difficult, while that lasts.

QUESTION: Sir, several of our previous speakers have pointed out the importance of the agreement between the Federal Reserve Bank and the Treasury, I believe in 1951, that it caused the benefits that have been derived from that agreement. Is it possible that the lack of agreement during World War II contributed to the runaway debt?

SECRETARY BURGESS: Yes. I think it was not only the lack of agreement--I think they agreed on some of the wrong things at the beginning of the war. I think the fact that they fixed a ceiling on interest rates of 2-1/2 percent was a major blunder; because 2-1/2 percent is too low to attract savings over a period. It meant that the savings institutions that purchased those long-term bonds at 2-1/2 percent did so reluctantly, and they have been selling those bonds whenever there was an opportunity. It was a disturbing factor in the

market; a major factor in creating inflation. Banks had to take the allotted rate; it was not attractive to other people. They bought the bonds out of patriotism; bought them in large amounts, when there was nothing else to buy.

Then essentially interest rates are not an arbitarary thing. Life insurance companies write contracts for insurance with you and me and the others and they involve a guarantee, in many cases, of 2-3/4 and 3 percent. It is actually the obligation of the insurance company to earn on your money 2-3/4 or 3 percent. If you stick him with a 2-1/2 percent obligation he is going to dispose of it as fast as he can, as fast as there is an opportunity.

That was a major blunder. That was not a blunder of lack of agreement; they had agreed on the wrong thing at that time, in my judgment. As you got out of the war period, the Federal Reserve began trying to make its decisions somewhat in the light of the economic situation, whereas the Treasury stuck to the old war ideas that you take rates and stick to them.

I think the inflation after the war that kept wholesale prices up was partly due to the lack of Federal Reserve-Treasury agreement on a sound policy.

QUESTION: In our various duties, we often find ourselves in the position of having to promote a savings-bond payroll-deduction plan. Oftentimes it is difficult to counter the question: Is this a good investment? Is any thing being done, or are there being things done, to make savings bonds more attractive--a higher interest rate, or perhaps some guarantee as to the future value, and so forth?

SECRETARY BURGESS: We have given a great deal of thought to that. The fact is that the three percent that you earn on Series E and H savings bonds is the best rate of interest there is in the market; for a 9-2/3 year obligation. A 3 percent rate of return is an extremely favorable rate. In addition, savings-bond holders take no risk of market fluctuations since the bonds may be redeemed any time after short holding periods at fixed redemption values. They are very good investments.

We have considered all kinds of ways for improving it. We have not been able to find any such way. Somebody proposed tax exemption. We explored that. That would make them too attractive compared to other forms of savings. It would draw money out of savings banks, and so on.

It is presently attractive and fairly competitive with other forms of saving. The great drawback up to recent years was the general notion that we were in an inflationary period, so we had better buy common stocks.

One answer to that is we try to conduct the affairs of the Government in such a way that prices stay relatively stable. We are working, I think, as hard as we can. We don't have to have rising prices to assure prosperity.

We don't think inflationary policy is necessary or desirable. Looking back over history--this chart wanted to call itself to our attention--you will see that the price increase has not been, in the history of this country, the dominating factor. Those prices have tended to come back to the old level after the war passes. This idea that they have to keep on going up is rather a new idea. We don't think it is going to stick.

QUESTION: Mr. Secretary, in the event that you have just described, it seems that this planning that we have now for balancing the budget as we go into a period of prosperity has not worked very well. Do you have any plans for cutting off income sufficiently if we have a slight recession, or will the same thing happen as in the depression that you showed us in the thirties, where our budget went in the hole about 10 billion dollars in a period of recession?

SECRETARY BURGESS: Well, we haven't got any gadget. We don't believe you can do it with gadgets. Our notion is that, if you follow persistently a sound fiscal and monetary policy, you can avoid many of your problems.

Of course you gentlemen, as you go back into your services, are going to gradually find out how to give us the same amount of security, or more security, for less money. That is going to be a great help.

DR. KRESS: Mr. Secretary, you have exhausted their questions. On behalf of the College, we thank you very kindly.

(6 Dec 1955--250)O/ljt



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