THE ABILITY OF THE UNITED STATES ECONOMY TO SUPPORT MILITARY PREPAREDNESS FOR WAR IN THE PERIOD 1956-1960

17 May 1956

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Publication No. L56-132

INDUSTRIAL COLLEGE OF THE ARMED FORCES

Washington, D. C.

Mr. Leon H. Keyserling, was born in Charleston, South Carolina, 22 January 1908. He graduated from Columbia University in 1928 with an A. B. degree, and from Harvard in 1931 with an LL. B. degree. During 1932-33 he was an assistant in the Department of Economics at Columbia. He became an attorney in the Agricultural Adjustment Administration in 1933, and from 1933 to 1937 served as Secretary and Legislative Assistant to the late Senator Robert F. Wagner. From 1938 to 1942 he served successively as General Counsel, Deputy Administrator and Acting Administrator, U. S. Housing Authority. During 1942 Mr. Keyserling served as Acting Commissioner, Federal Public Housing Authority, and from 1942 to 1946 he was General Counsel, National Housing Agency. In 1946 he was appointed Vice Chairman, Council of Economic Advisers under the Employment Act of 1946, and from 1950 to 1953 he was Chairman of the Council. He is the author of various monographs, articles and essays on full employment, economic stability, housing and related subjects and contributor to "Saving American Capitalism," 1948. He won second prize in the 1944 Pabst Postwar Employment Awards for his essay, "The American Economic Goal: A Practical Start Toward Postwar Full Employment."

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DR. HUNTER: General Calhoun, Admiral Deutermann, Gentlemen: As a preliminary to this morning's discussion, I want to throw out a brief historical note. Back in 1917 when Washington found a world war on its hands, the economists, I suppose, were the rarest of the bureaucratic species here in Washington. One of the most interesting features of our first formal resource mobilization was the movement to Washington of a small but capable group of economists and statisticians.

Now as our mobilization got under way back in 1917, it was quickly discovered that you can't mobilize your resources for war without a fairly detailed and fairly accurate knowledge of the kinds and the amounts of these resources. The indispensable contribution of these economists, who came to Washington, to the war effort consisted above all in providing what this country sadly lacked, statistical measures of our basic production resources, first and foremost of our production capabilities.

Now this job was done, of course, but the initial lack of such data and the time required to find out what data was needed and then to go out and get that data undoubtedly delayed our mobilization effort at least several months.

Well, a lot of water has gone over the dam since 1918, including especially a peacetime depression crisis and the second world war, each of which made heavy demands upon economists. Today, of course, economists are one of the major props of defense as well as of business enterprise.

One of the most vital questions, obviously, on which we require their advice is essentially the same as that first raised in World War I and that is the capacity of the economy to support war, any kind of a war. To discuss this question this morning, we are very fortunate in having Mr. Leon Keyserling, who is a distinguished member of his profession. During the years 1950-1953, he occupied what was, from the viewpoint of national policy, the top economist position in the United States, Chairman of the President's Council of Economic Advisers. With this

background of his experience especially, he is peculiarly well qualified to discuss the problem before us this morning: the ability of our economy to support military preparedness in the period, 1956-1960.

Mr. Keyserling.

MR. KEYSERLING: I certainly appreciate the opportunity to be here again. I have always enjoyed my visits here and know that I will again. I am also appreciative of the brevity of the introduction. I have been going around the country making some talks on various matters, and some of the agencies which arrange these talks send out a life history that is really something to hear. After sitting and listening to these three or four times a month, I am very glad when in such succinct form the truth about me is told.

However, I do want to take exception to a part of the introduction. I am not sure that I am an "economist." At least, I am not an economist as that term is frequently thought of, as one who deals primarily with statistics, and who insists that at the point where an individual attempts to interpret those statistics and to pass into the area of national policy, he stops being an economist and becomes a politician. If that be the definition of a politician, then I am a politician, because I do not believe that there was ever a time when it was more important that economists in the United States, particularly those who have the good fortune or have had the good fortune to occupy responsible official posts, should move out of their shells and become advocates of those conclusions which their analyses of the facts lead them to. It is just as necessary that responsible economists concerned with public service do this as that responsible people in other branches of public service at the policy level do this.

I am not, however, politically inclined in the sense that the critical things which I will say about our economic approaches to problems of national defense arise out of the fact that I am not a member of the current administration. I am critical of what is being done now. I was also critical of what was being done when I was in the Government. I expressed myself equally forcefully, even if equally wrongly, and I got into a certain amount of hot water by so doing, although I have survived.

There was a saying many, many years ago, "Oh, liberty, what sins are committed in thy name." I think the banner which we should

hoist now is, "Oh, economy, what sins are committed in thy name," because in the name of a false economy we have grossly neglected the problems confronting us in the world as it now exists, problems which seem to me to be accented by the headlines in the newspapers today. We hope we will come through to a peaceful solution; everybody does; but a rosy and easy complacency is certainly not justified at this stage.

I can best describe my approach to this problem by going into a little history. At the very beginning of the Korean war, in fact at the beginning of international tensions which preceded the Korean war, I took the view, as is well known, that we had not begun to realize the productive potentials of the American economy, that because we were not beginning to realize those potentials and were not bringing to bear upon them the policies needed to translate them into actuality, we were grossly underestimating what resources we had available and what part of our resources we had available for our major national priorities.

One of the large issues which arose at that time--I don't remember at the moment exactly when, in 1950 or thereabouts--was, first, what balance we should strike between reallocation or reassignment of our resources to defense purposes, and the building of our total resources, so that we would have more with which to carry the defense burden on a long-range basis.

I felt that mistakes were made in both areas. I felt, in the first place, that we were not building our total productive strength as rapidly as we well could under our free system, and I also felt that we were not identifying the priorities of our national needs and putting a large enough part of our resources into them.

Whether I was right on the second point, I cannot prove, although I do believe that I may have been right. The first point, however, I can prove, because the gross underestimates which were made of what the American economy could make and could do at that time, as a base for possible neglect of our national priorities, turned out to be very wrong. It is a matter of record by now that the various projections which I made as to changes in American productivity, as to changes in the productive power of the economy, all fell somewhat short of what we actually accomplished. Yet my projections were originally deemed to be outlandishly high.

I say this only because I want to give myself a clean bill of health, so that no one will suspect that the position which I am taking is new or governed at all by the fact that I am not now a member of the Government. However, I do say that it is more important to analyze what is happening now than what happened five or six, or eight, or ten years ago. Therefore, with this introduction, I will address myself to what is happening now, and what I think needs to be done now and in the future.

In the first place, to create some background for the situation, I want to say a few words about the potentials of the American economy. Let me say that, while what I say is critical, I will sound wrong if we are satisfied with comparisons with the long ago. Compared with what happened ten years ago or fifteen years ago or maybe even five years ago, the American economy is making a wonderful record. I am just as proud of that record as anybody who uses that record to evade rather than to face responsibility. I am proud of the fact that our country is growing as fast as it is. I am proud, as I travel around the country, to see the burgeoning enterprises, the growing plants, increasing industrialization, the high level of employment, the rising standards of living, the great increases in indexes of output. And yet I say to you in all sincerity that I don't think we now live in a world situation where we can be satisfied with much less than our best.

I don't think that the fact that we have a freer system than some other countries--which I value--should lead us to ignore the fact that there are some other countries, much as we dislike their systems, which, on the straight economic front, on the front of marshaling their resources and using them, are making very fast records of progress, are not being stopped by the economics of ten, fifteen, or twenty years ago, and are measuring their economic strength, not by the budgets of a government, but by the available resources and productive power of a people, which is what economics is really about.

I therefore believe that we, not by their methods, but under our methods, under the methods of freedom, must also move from a measurement of our economic potential in terms of dollars, in terms of budget balancing, in terms of financing, to a measurement of our economic potential in terms of our resources and what we can do with them, because it is a truism of economics too long forgotten by some economists that whatever--and I want to underscore this and say it again and again--whatever we have the economic strength to do, we have the financial strength to do.

The greatest misleading of the general and even of the informed public within the past years, I won't say just the past three or four years, but as long as I can remember, has been the spreading of the belief that we might not have the financial strength to do what we have the economic strength to do. Financial strength is merely an index measurement of resources. With good and prudent management, with intelligent policies, we can do financially whatever we can afford to do economically. And the fact that, when we get into a total war, we realize that principal and no one contests it, proves that when we get into a crisis we get back to reality.

Now it is much too dangerous to live in reality only in a period of ultimate crisis. It is much more important to follow reality even before you get into that ultimate crisis, because we cannot be sure that, with all of our resources, if we wait until we get into that ultimate crisis, we will always come through as fortunately as we have unless we build our strength as we go along.

It has always been a source of terrible concern to me that the only time we get realistic about our economic strength and economic policy is when we are in total war. When we are in a total war anybody who puts the budget ahead of our resources, anybody who puts financing ahead of economics, anybody who follows the classical textbooks of the 1900's instead of what we have learned during the 1950's, would not be tolerated for a moment. Yet in every period short of that, that kind of thinking seems to have supremacy, and I, for one, cannot understand it at all.

Let me say a few words about our economic strength as distinguished from our financial accounts, and then I will try to tie the two together; then I will try to indicate some of the policy changes that I think should be made, because my interest as an economist is from the viewpoint of economic policy as it relates to the well-being and security of our country.

Of course, the first source of our economic strength is the changes in productivity. Productivity means very simply how much more the average working person--by working person I mean everybody following economic pursuits, not just a worker in the traditional sense of an industrial labor person--can produce in one hour than he did a year ago, and, of course, that is the whole history of economic progress. That is,

the difference between an underdeveloped country and a developed country, and that is the supreme difference thus far between the American economy and even the other developed economies. We have increased productivity at a faster rate. And to indicate how fast that rate has been, during the period from 1920 to 1930, we increased productivity by 1.8 percent a year. During the period from 1930 to 1950, we increased it by 2.7 percent a year. During the period since World War II, we have increased it by 3.7 percent a year, or more than twice as fast during these last few years as during the period between 1920 and 1930, which we regarded as a high watermark of American prosperity and progress in that early era.

The rate of productivity increase more than doubled. Yet it is fantastic that not enough consideration to our economic potential, and therefore to our potential to bear a defense burden in the years ahead, has been given by those economists and financial analyzers and Government advisers, who, following their leanings, keep insisting, in estimating what our potential is and how it might be cultivated, on the use of the average of the last 50 years instead of the average since World War II, and say that, if the average during the past 50 years was two percent or 2-1/2 percent, that is a more conservative and a more reasonable base for estimating our potential than the records of the last seven or eight years.

I don't think this is conservative; I think it's utter nonsense. You don't have to be an economist; just ask any intelligent person: If you were going to estimate the rate of our technology change and our productivity change over the next five or six years, would you be guided mostly by what has been happening recently or by what has been happening in 1900? Any intelligent person would say, obviously, more by what has been happening recently.

If they went around the country and saw what is happening in American factories; what is happening with respect to automation; what is happening even in the application of new productivity techniques in areas of the economy where one thought they could never be applied; if they could see what is happening in agriculture where productivity is rising even faster than in industry--they would immediately conclude that we have crossed a new sound barrier of productivity and technological change quite as striking as that which has taken place in medicine, where, as we all know, the changes that have taken place in the last

few years have been greater than all the changes which took place between the battle of Yorktown and the battle of Belleau Wood. There has been an acceleration, a more rapid rate of increase in every phase of science and invention and the applied arts.

I say that, during the next few years, our average rate of productivity growth is going to be higher than the 3.7 rate since World War II. It's higher now. It's around four percent now, and I think it's going to be around 4-1/2 percent over the next few years. So we have to take that factor into account.

The second thing that affects our productivity, and affects our total output, and affects our economic capacity is the size of the growth and the character of our labor force. Our labor force by and large grows by about eight-tenths of a percent a year, and when we add that to the productivity factor and make proper adjustments, even if we only take the productivity rates since World War II, we have about a 4-1/2 percent annual growth capacity in our economy year by year.

Now we are underestimating and neglecting the labor force potential as well as the productivity potential because, while we have reasonably full employment, that is merely a count of numbers. That has nothing to do with how much attention we are directing to education, to effort, to training, to higher skills, to certain national policies toward dealing with the problem. Today, a very large part of our labor force, which is technically employed and counted in the statistics, is highly underemployed from the viewpoint of utilization.

Of course, the outstanding example of this is that we have a farm population of 22 million people, when we need considerably less to produce such farm products as could be used. It isn't enough just to inveigh and say that there are farm surpluses. We need at a time like this, when manpower is so important, if we need only X million instead of 22 million, to examine what are the areas of policy by which we can directly and properly under our free system and through appropriate inducements draw that underutilized labor force into effective and useful productive work. It can't be done just by income deflation, although I am not here to talk about the farm problem.

Let us translate this economic potential first into an examination of what has happened in recent years, and then into what the potential for the years ahead is.

We are told that during the last few years we have had a very high level of prosperity. To be sure we have, measured by the old times when we were affected seriously by the ravages of the business cycle and had large depressions which we haven't had recently. But measured in terms of the world conflict, measured in terms of the necessity to marshal our resources, measured in terms of the unthinkability to my mind of doing woefully less than our best at a time when, because we are doing less than our best, we say we cannot afford to do what we must do, the record has not been good at all.

The fallacy of the record comes from measuring what we are actually doing against a level line instead of against an upward inclined line. In other words, if you visualize a level line and ask yourself every year whether you are higher above that line than you were the year before, the answer over the past few years in the main would be yes. In other words, we had a little more employment than we had a year ago. We had a little more production than we had a year ago. We have a little more business than we had a year ago. But that is absolutely fallaceous, because the par for the course of the American economy or any vital economy is not a straight line but an upward inclined line, an inclined line that takes account of growing productivity and a rising labor force. Even if we could afford to neglect this domestically, we cannot afford it when there are these other crucial enemies of ours, at least as of now, who are not moving on a straight line and who are factoring--and it has nothing to do with whether or not we care for their systems--who are factoring in the growing labor force potential and the growing productivity potential and achieving, according to all informed American estimates, a very high rate of economic growth and also a very high allocation of their resources to aggressive defense purposes.

Now when you measure what we have done over the past few years--and I could just as well carry this back further; the same thing was true when I was in the Government--against this upward inclined line, which is the true measurement of the utilization of our resources, here is the way we are falling behind:

During the four years, 1953 through 1956, we had a total national product measured in uniform 1955 prices of 1,526 billion dollars, or an average of 381.5 billion dollars a year. The figures year by year, 374 in 1953; in 1954 we had an economic setback, 365; 1955, 387; 1956, it looks to me like about 400.

Now, if we had 374 in 1953 and we have 400 in 1956, 1956 could be called the highest year on record. We might say that we are doing better now than we were ever doing before, and what is there to get concerned about, and how foolish must be anybody who thinks that we are not realizing our potential or allocating our resources properly.

But the fallacies in this approach are apparent, when we consider what we would have done in each of these years if we had fully utilized our growing labor force and our growing productivity, instead of allowing a large slack in our economy at the same time that we said we didn't have the resources to do what we needed to do.

If we had grown, not at a fantastic rate, not at the rates reflected in what I think is our current productivity, but merely at a projection of the average rate of productivity growth, say, since World War II--which I think is very low for the current situation and for the future; I think it is extremely conservative for reasons I could demonstrate if I had the time--if we had done that, our progress over the four years, starting with 374 in 1953, would be 392, 408, and 426; or a total of 1,600 billion dollars as against the 1,526 billion dollars, and the differential in those four years alone comes to 74 billion dollars, or approximately 18.5 billion dollars a year.

I call that our national economic deficit, and let me tell you that a national economic deficit of 74 billion dollars over four years is, if I may say, a lot more serious than what the books of the Federal Government show, because the books of the Federal Government merely show a decision on the part of those making public policy as to how they want to finance economic operations.

You can run the Post Office and charge three cents for sending a letter and run a deficit of 100 million dollars a year, or you can charge four cents for sending a letter and run a deficit of 50 billion dollars a year--I am just using arbitrary figures--or charge five cents for sending a letter and show a profit, but that doesn't in the slightest affect the economic strength or resources of the country. It takes the same amount of manpower to transport the letters. The letters perform the same economic function in helping our economy to run. That is simply a bookkeeping decision as to paying the real economic cost of carrying the mail in different ways. You may decide to do it in a way that relies more heavily on what the people pay directly through buying stamps, or

more heavily on what they pay indirectly through taxation to support the Government. But that isn't economics; that's financing. Therefore, I say, using that homely illustration, which applies to everything, when you run a 74 billion dollar economic deficit over four years, you are running a deficit in real production, in real output, which, incidentally, is also the base for tax collections.

When we say over these four years that we must cut back--I am not an expert on what we should spend for national defense in all its parts--but when we say that we should cut back, not because the informed judgment of experts is that this is not the best pattern of national defense, but that we should cut back because we can't afford it, that is perfectly preposterous when we are using our resources slackly to that extent.

Therefore, I say that national economic policy and the allocation of resources to various purposes should be guided by something which is not an invention of mine, should be guided by a policy which was adopted overwhelmingly by the American Congress and the American people in the Employment Act of 1946 and which has been more honored in the breach than in the observance.

Very simply stated, that policy was couched in terms of economics rather than in terms of financing. It didn't talk about budgets; it talked about needed levels of employment, production, and purchasing power, which are the essence of the economy in operation, and it said that, as a Nation, through our free methods, we can no longer afford to let these matters take a natural course but should start with projections of what we can do as a guide to policy and as a guide to the allocation of our resources among different purposes.

Incidentally, if you are interested in a balanced budget--which I am not particularly for the reasons I have given very frankly--but if you are interested in it, it is still true that at any given level of taxation, if you had had 74 billion dollars more of real output over the last four years, you could have cut our tax rates, Federal, State, and local, and still collected very nearly 15 billion dollars more in additional taxes, and still have had a budgetary surplus all along; just as we are getting a budgetary surplus even now, larger and larger, every month, above the computations of a month or two earlier, because the people estimating what the budgetary yield was going to be were guided by the

statisticians and account-keepers rather than looking at the real economy and seeing what would happen if our real economy operated at certain levels. So every month they have to revise and show that we have a bigger budgetary surplus, meanwhile predicating the servicing of our national priorities upon the estimates of the budget resulting from their failure to connect it with the real economy. So even if you are interested in budget balancing, the approach I favor brings you to a better result.

Now let us look at it over the few years ahead, to open up a few more vistas, and then I will get into the area of policy. I want to set the factual basis, first so that I will be accepted by the "economists."

Starting where we are now, let us take a little look at what our potential is over the next few years, and again I want to underscore, these are very conservative estimates because they are based upon average productivity growth during the years since World War II and not on what is happening now, which is much higher.

Take first 1965, which is ten years from now. We now have a total national product of 400 billion dollars in round figures. It was 398.5 billion dollars in the first quarter of 1956. By 1965, if we have reasonably full utilization of our productive resources, that 400, measured in uniform dollars, will rise to 600 billion dollars, and by 1960, four years from now, to around 490 or about 500 billion dollars by the end of the year.

If we break that down into parts a little bit, business investment, which provides the sinew, so to speak, for our economic strength, the plant, the equipment, the tools, the methods of increasing productivity and technology, would have room within that economic growth to rise from a current level of 62.4 billion dollars to 85 billion dollars by 1960, again measured in uniform dollars, and 100 billion dollars by 1965.

So I want you to understand that this so-called model that I have made does not neglect the very important factor of building the base of our economic strength, which is industrial advance. As a matter of fact, I have projected the industrial investment growth at a somewhat higher rate than the overall national economic growth. I have also projected a rising standard of living for consumers.

With our standard of living where it is, I might believe personally that maybe we ought even to cut back a little bit, and do some other things that are needed more, but I am practical and therefore I realize that so long as we are in a period short of total war, unless you have a little carrot, unless the people feel that, through hard work, they are making some gains from year to year in their living and opportunities, they will not continue to support the imposition of taxation and other burdens necessary to do the other things. That's what makes the economists call me a politician. I think that's just as much a part of the realities of American economic life as anything else.

So I have projected a considerable rise in standards of living and consumer outlays, running from 259 billion dollars now to about 325 billion dollars in 1960 and about 390 billion dollars in 1965, or an increase in the real standard of living, allowing for population change, of something like 40 percent, let us say, in ten years.

What's the importance of this to what I am saying here? Within the compass of our economic potential, even with this increase in the standard of living, even with this tremendously rapid increase in business investment as the productive expansion base for our economy, we still have room to do as a people as a whole, which means to do through Government, an increase from the current level of outlays, Federal, State, and local, of 77.5 billion dollars now to about 90 billion dollars by 1960, and about 110 billion dollars by 1965, to do it without sacrificing the standard of living--in fact, in some respects improving it--to do it without sacrificing the enormous growth in private investment, to do it simply through allocating, not larger percentages of our total output, but larger real amounts as we go along toward expanding the things that we have to do as a Nation and therefore have to do through public outlays, one of the very most important of which, of course, is national defense.

It seems to me utterly unconscionable that, with this potential existing in the American economy, and with the alternate to total utilization of this potential being inescapably a rising level of unemployment and disuse of resources, which not only weakens us at home but blemishes us among all other free people who have not yet completely put aside the Marxist propaganda that the American economy cannot maintain full employment, it seems to me absolutely unconscionable in the face of these economic potentials to gear our national priorities to the

standards of the past or to gear them to the picture of the Federal budget rather than to the picture of the national economy.

Actually, to illustrate this, if I had the time to analyze over the past few years that I have reviewed what would have happened to the Federal budget if we had come closer to realizing our economic potential, even if the level of taxes were reduced, we would have had a substantial surplus in every year instead of having a deficit in three years and a surplus now. That shows what happens when pride in Federal budgetary performance takes precedence over looking at the national economy.

Let me tell you another fact about this, and again I want to emphasize that this is a position which I took all during my period in the Government. I took it not only privately, I took it in print; I took it in many ways; and I am going to use strong language: The Federal budget of today is misleading. Now this is serious, when the budget is used as a guide to policy for necessary priorities. And I want to try to explain very briefly why it is misleading.

Suppose that a responsible private business had to spend 100 dollars to put out a fire that broke out in the stockyard, and had to spend another 100 dollars to put a new machine into its plant to increase its productivity and its earning power. What would anybody think of the private business that classified those two expenditures in the same way? And yet under the conventional Federal budget, in the determination of whether we are running a deficit or a surplus, in the determination of what the true Federal budgetary position of the Government is, everything under the conventional budget is lumped and added together in one grand potpourri.

For example, if the Government makes a one million dollar outlay for current services through the employment of people, that is classified the same as if the Government guarantees a private FHA insured loan which the experience record over the years shows has yielded the Government a net profit on a 22-year experience record. Stated more simply, the Government classifies loans for which monies are initially appropriated exactly the same as current operating expenses, and uses those figures to tell us that the budget is in deficit when in fact it is in surplus. That's one example.

Another example is that the Government classifies expenditures, let us say, for building defense weapons, which are a great national

need but which are not economically productive, exactly the same as it classifies investment in plant which is economically productive, and which we know from the post-World War II experience became very profitable when disposed of to private industry.

The Government makes payments into a social security fund--I don't want to elaborate this too much but it is very important--to meet obligations which theoretically will arise 30 or 40 years from now, invests these in Government obligations, but treats them as current outlays for purposes of the conventional budget.

Now what am I getting at? What I am getting at in essence is that the budget has become an instrument to mislead and to divert from what the Nation can afford to do economically, and also beyond that to mislead and divert as to what the actual condition of the Federal budget is, not by radical criteria, by the criteria of any conservative American business or bank. If the Federal budget was set up in the conservative way that any prudent and conservative bank or financial institution or investment house or industrial concern would set up a budget, we are running large surpluses right now and have been for years.

I wouldn't care, except that this is a device to pander to the desires of certain classes of taxpayers and a certain class of economizers and completely to mislead the American people--and to a degree the Congress because many don't understand it--as to what this Nation can afford to do, and that is dangerous in these times. Therefore, it is extremely important that we start thinking of the Federal budget in terms of the national economy and realize that, after all, the operations of the Government, which the budget reflects, are merely one department in a vast enterprise.

You might take the analogy to a department store. No well-run department store measures the success of its activities by whether every department makes a profit. You look at the whole thing. You may decide, as a matter of management, that you want one department to run at a loss. Your advertising department always runs at a loss. Certain other departments always run at a loss. You look at the whole picture, and on the net balance decide what is the best composition of the forces to give you the greatest overall profit in the case of a private business, and overall economic strength and the meeting of national priorities in the case of the Nation.

Until we can force, through the process of education, until we can force the Government, the people, the Congress, economists and others to start looking at our economic potential realistically in terms of what it is rather than in terms of these shibboleths, and until we can start using the Federal budget as a tool of our people, of national security rather than as an engine merely to create a pretty picture for itself and to help those who can afford to but don't want to bear the costs of what we can afford to do and must do, then we are going to continue along the same course that we are now following.

It's perfectly obvious that, as a Nation which has a growth potential of 15 or 20 billion dollars a year, which is rising each year because you are starting from a higher base quite aside from a rapidly rising productivity and technology, that we are not--and I say this advisedly--beginning to adjust our outlays for high national priorities, including national defense, to the best judgments of those who are competent to pass judgment upon that question. I have never, either in public life or out of public life, assumed to be an expert on what we should spend on national defense or what the composition of the effort should be. I have certain ideas on it, but that is just as an amateur.

I have protested because I have seen that the judgments have not been based on that at all, changed in the light of experience. They have been based upon pseudo economists and tax savers and financial manipulators misleading the sincere people who have to make the decisions into believing that our economy could not do what it can do. And I have seen that at the top. I haven't read it in the newspapers. It is still going on, and it is probably getting worse.

Now that is the essence of the problem. I think that I would like to say a few words about a few more specifics. One of the things that we have to do is to recognize that abundant productive capacity can be translated into effective use. Let us take a few areas of our economy and see what is happening, and let us try to connect it up with our security problems, because they all interconnect.

I want to say parenthetically here, you know it's almost hard to know what words to use. We have become so afraid of words that almost any word you use has an unpleasant connotation, and in the tyranny of words which is taking place on the American scene, we are sacrificing a lot of people who have ideas that are very important to the security and strength of the American economy and the American people.

Take this word "planning." What does planning mean? Planning is the difference between the civilized man and the savage. The savage doesn't look a day ahead and he doesn't plan. The civilized man tries to figure out what is going to happen in the future and to mesh his activities so that they have some consistency, and that is planning.

But now we have gotten to think that only the totalitarians can plan, and that anybody who stresses planning is totalitarian. Let me tell you here and now that if we adhere to that idea, if we don't recognize that a free and democratic people, with a small "d," can plan more effectively and more intelligently and more farsightedly, than the totalitarians, I think we are sunk. We are not adequately planning our defense effort, and we are not now adequately planning the meshing of our defense effort with our national economy. We are not planning because we do not start even with the objective of wresting from our economy what it can yield productively and then making realistic appraisals of how we want to quantify and translate those into the service of our great national priorities.

I have sat in at all the levels of Government where these things are supposed to be done and where, if one read the press, one would think we have a great array of instrumentalities for meeting these problems. Well, they are being met better than they were five years ago, or ten years ago, or twenty years ago. It is not good enough for me, and it is not up to our capabilities because the overall top judgments are stultifying the effort by the very kind of nonsense that I have been talking about for much too long now.

You can't plan the highest use of your resources for the security and growth of the country if you start with fundamentally wrong assumptions as to what is the source of economic strength. If you start with an effort to balance the budget rather than an effort to balance the national economy, if you start by confusing financial strength with economic strength, and if you impose that as an ultimate plan by which all those who are trying to work out the details must be guided, no matter how smart, no matter how devoted they are--and most of them are--they can't possibly get the right results, because they are forced into a framework that puts them on the wrong field and sets the wrong conditions for their operations.

That's what's happening, and therefore, as the more minute decisions are made as to what to spend for national defense, as to how to

set up the budget, as to what to put into other elements of our national productive strength, they are all guided by the wrong criteria.

Let me give some specific examples after that generality, to show how it works out. Take the farm problem. We hear about farm surpluses. Now here we are in the United States blessed as no other country in the world with ability to produce a lot. If economists had any sense, if we were guided by our resource possibilities, we wouldn't regard the fact that one farmer now can do the work that one and a half could do a few years ago as a curse. We wouldn't say, "We're sunk because farm productivity is going up so rapidly."

Quite apart from the question of whether some of that food can be used elsewhere in the world--and I don't want to get into that because that is a little off my subject here; I think we could and I think it would have a defense value along with weapons--what do you think the Soviets would give if they could have our agricultural productivity and if therefore they had the release of that amount of manpower to put into the vital things that they want to do?

We need a program which accentuates the fact that, if we speed up our industrial development, if we provide some kind of guidelines to it, if we use the power that we have as a people to redirect these resources, we will fortify our freedom by becoming more productive and more secure. There's no use talking about freedom in the 19th century sense. We can't compete in the world on that basis, but we can yet do it on a free basis as we really understand freedom in the 20th century, just as we operate our military establishment under freedom as against the totalitarians.

Why can't we redirect these resources into the production of things that we need? That is what real economic strength is. In other words, there's a potential within these wasted agricultural resources to be translated into national defense, to be translated into the industrial complement underlying national defense, to be translated into anything we want to have it translated into.

It is not an easy job, but it is not a job beyond our capacity. We did it when we were in total war. That is the fantastic part about it. When we were in total war, we didn't hesitate to take people off the farm. I am not suggesting a draft for everybody. But we didn't then say that slack resources were something that we couldn't do anything about.

We have that wasted productive potential now. I don't attempt to project at this moment an exact plan as to how it should be done, and how it can be reconciled with a peacetime economy, and how it can be reconciled with liberty and freedom of choice. I just state categorically that it can be so reconciled. All I have time to do here is to state categorically, which nobody will deny, that nobody is talking about the fact that farmers have become more productive as a potential national asset. All anybody is talking about is that grain stored in warehouses is a great detriment to our economy.

Then, again, they are getting into the financing rather than into the economics of it. How is grain stored in warehouses--I wish there were less of it--but how is it an economic liability? It's there. It has already been produced, so economic resources are not currently being consumed in producing it. Why is it such a great economic liability, as against the fact that millions of farmers are being underemployed and are not being turned to productive purposes? We are worried more about the bills of lading and about the transfer charges than we are about how our economy is functioning.

Take as another example small business. Even now small business is being forced off the periphery of the economy. It is moving downward while others are moving upward. Now I am not going to make a traditional talk about bigness and smallness and monopoly. I think we need bigness and smallness in our economy. But the real reason why small business is being forced downward is not because of big business. The real reason is because, unless you have a philosophy and program of full utilization of your resources, the smaller ones are not going to be used, not because crimes are being committed against them, not because they are less efficient or more efficient, but because they merely get forced out of use when everybody isn't being used.

In other words, when you have a full production program, when you are really using your resources, you feel that you have to use the small components and the big components. It is not a matter of one against the other. When you are operating under economic slack, and when you are not worrying about this problem of full resources use, you don't worry about using these small components, and you say they are inefficient.

Well, the fact that Unit A is more efficient than Unit B doesn't mean that using Unit A and Unit B isn't more efficient than using only Unit A.

Do I make myself clear? Yet a lot of our economists and a lot of our public figures seem to think that because A is more efficient than B, then there is more national efficiency in using A and letting B lie idle.

That's silly. If you follow that to its logical conclusion, you would ultimately get to the point where you would only have one person in the labor force, the most efficient person, and you would have only one person in the Army, the best fighter. That's an exaggeration, but it illustrates my point. Overall national efficiency has nothing to do with these efficiency tests of the classical economists that are being used as guides to our national policy.

I could give other examples, but I have about run out of my time, and maybe we can do better with the question period. The point I am making is that this is not a question that can be solved or approached by any one detail or any one panacea, or any one gadget, or any one political slogan. We need a fundamentally different approach, and the fundamentally different approach is simply to get down to the realities of economics rather than flying around in the meaningless stratosphere of financial measurements.

We have in this country an economic strength, an economic potential, that just defies description. I am ashamed to use these productivity figures of four percent and 4-1/2 percent, but I have to use something that somebody will accept. If I told you what I really think, we have a productivity growth potential in this country of eight percent a year easily. We just haven't begun to realize it.

We saw it to a degree during the war, when we drew so many people out of the labor force and yet accomplished fantastic results. One motor company in this country, without changing its plant or equipment, can produce more cars than the Big Three are producing. That's just one example of what our productive potential is. Of course, you can't produce fully if you are guided by the laws of the classical economists who say, "What's the use of producing more when there's no need for more, when people can't buy more, and when there are too many goods glutting the market now?"

My answer to that is very simply, if we have the productive capacity to produce more cars than can be used, for goodness sake, what is the purpose of national policy but to get us into the production of something we need more of and that we are not getting because we are told that we can't afford it.

Therefore, I end on my original note, that we can afford financially anything that we can afford economically. If we have economic strength to support an adequate level of national security, then we must find the financial ways to do it. If we have the plant and the resources and skilled manpower to fulfill our obligations and meet our needs, then we are absolutely corrupt in our thinking if we get drawn away from that by the idea that some budget or some method of financial accounting shall take the place of true economic analysis in our approach to these problems.

QUESTION: On our field trip just recently concluded, we had a concept offered that I would like your opinion on, to the effect that it is an established fact now that industry investment in research and development has a direct relationship to its expansion potential, and I think the figure cited was that four percent in research and development would insure a ten percent annual growth. Do you have any thoughts on that?

MR. KEYSERLING: No, I don't think that is correct. First, research and development is very important to investment growth and to industrial expansion, but I think that the business people who say it is the sole factor or the main factor are putting it on too narrow a base, because another factor that has a very important effect upon investment growth is demand; in other words, what the business investor thinks the market for his product is going to be, both at home and overseas, both through private buying and through public orders.

In other words, if the Government of the United States said that we are committed to a policy of the full utilization of our resources, and that insofar as we have slack resources they would be applied to some of these priority purposes, whether they be national security, or whether they be roads, which are another element of national security, or whether they be resources development in education, then I think that would be a great inducement to industry's reaching out toward optimum plant expansion, quite as much as research. I think that is important. Although I do think research is important, I think it is too astigmatic a base, just to say that if we devote enough to research we will expand enough.

I want to say something else about that. I have been talking mostly about overall figures, a national product of 400 billion dollars, a national product of 500 billion dollars, a national product of 600 billion dollars.

There is another very important consideration. In one sense, those figures are misleading as an indication of national strength, because the national strength depends very much upon the composition of that 400 billion dollars of output. Let me illustrate it very simply, and I will take an arbitrary illustration as to the figures.

Let us just suppose, by way of arbitrary illustration, that our national economic growth is five percent a year and that of the Russians is five percent a year. Those aren't the actual figures, but they will do. Now, suppose that figure which makes up our five percent figure includes a lot of gadgets that have nothing to do with national economic strength, Cadillacs as distinguished from Oldsmobiles. I realize that automobiles are an element of economic strength, but nonetheless the difference between the chrome that goes on a Cadillac and the chrome that goes on an Oldsmobile has to be produced and it enters into this 400 billion dollar figure, but it has nothing to do with real strength. If the Russians are putting that five percent not into the chrome that goes on the Cadillac rather than on the Oldsmobile but into planes--see what I mean?

We are not paying enough attention to these priorities, as to whether we are getting a balanced development which gives us the kind of strength we need. That is why I am terribly concerned about this rosy glow of contentment with high-level employment and high-level production--although not high enough--without more concern about what it is going into, which is another function of Government, if I may say so. The primary function of Government is to see whether our basic national priorities are being met. The only justification of any Government program in the final analysis under our system is that it marshal resources to do the things which are more necessary than other uses of those resources through private spending.

In other words, private people can spend a thousand dollars in Macy's; private people can't spend a thousand dollars for roads or for national defense, obviously.

Again this brings me back to the question of the Federal budget, in which you may by now assume I have some interest. Another trouble with our approach to the Federal budget is not only our foolish attitude toward its economic functions, but also our preconception with the idea that the dollar of private spending is by definition infinitely to be preferred to a dollar of public spending.

Now, other things being equal, I agree. Other things being equal, I would always rather see a dollar of private spending than a dollar of public spending. But we don't live in a world where other things are equal, and therefore it is rediculous to take pride in the fact that the Federal budget was slashed by 12 or 15 billion dollars over the last few years, and that this was "made up for" by more private spending. That's not the question. The question is: What value has the private spending to meet these essential national purposes, compared with how well they could be met with 12 billion dollars of public outlays?

To take it very simply, national defense is the easiest example. You can't say that you took three billion dollars out of the budget for national defense, and it doesn't make any difference because people spent three billion dollars more for cosmetics. Well, I would rather have them spend three billion dollars more for cosmetics if you don't need national defense, but you can't measure the relative value of cosmetics and national defense. And it is not only defense in that narrow sense; roads are a part of national defense. Roads are terribly run down. Everybody knows that. Certain other elements of resource development are a part of national defense. The restoration of farm producers to a state of mind, as well as a state of production, where they are not gradually becoming disheartened is a part of national defense potential.

Another example is education. All the reliable reports--I don't get any reports from behind the Iron Curtain, I don't know how to get them, and I don't know how reliable they are--but I read the reliable experts in the New York Times, American experts. Everybody knows that the Soviets are training scientists and engineers and technicians three or four times as fast as we are. Well, that is an allocation of resources. They don't have more resources to devote to the training of scientists, engineers, and technicians than we have. Evidently they give that a higher priority than having as many people engaged in the entertainment field as we have. So you can't meet any of these problems just by talking about private spending against public spending or the Federal budget against the national economy.

Now, we are deliberately neglecting our national priorities, not only national defense, which I am not an expert on, but other things that I think I know something about--education, technical training, primary and secondary education. We are not building these services at

the pace that is consistent with our national priority needs, and we are not building even at the pace that is consistent with advancing our productivity because we are moving technologically into an era--we are there already, but moving faster--where the level of skills required and the level of education required for effective performance is entirely different from what it was 30, 40, or 50 years ago. Yet, we have terrific school shortages at all levels. That is one of the things that you hear some general talk about, but you don't see it translated into a vital important national issue and a concern of national policy, and I would say in the modern world that is a part of national defense just as much as other things, just as much as highways or just as much as full production.

Then you have the question of research for what, which was brought to my attention by the question you asked, and which is a part of this same question. I think industrial research is wonderful, but suppose, for example, it is research into what shape bumper consumers like best on an automobile. What is the change in automobiles every year? That's what it is. It's research into how we can put out a new kind of bumper, or a new kind of headlight, or a new kind of snapper, that will make somebody buy a car who already has a perfectly good car, almost a brand new car. That's research. I am serious about this. This is no laughing matter.

That is research, and it is important research. If we didn't have any other great world problems, it would be very desirable research to use our labor force in giving everybody the kind of bumper he feels he likes better than the one he had the year before. But I think you need to run a different kind of bumper into a few people, under current conditions, to wake them up. What we need is more research into the basic problems, and to say that we can't afford, let us say, to put enough into research with respect to defense, but can afford to put billions and billions and billions every year into research on more desirable colors for lipsticks, more desirable shapes for bumpers on cars. Some people say, "Well, that's private." Well, it's taken out of the country. The real economic costs of any kind of research is the manpower that goes into it and the resources consumed in producing it. Whether or not you can afford it depends on just that. So if you make the sole criterion, who is doing the spending, this is the foolish result that you get.

QUESTION: I wish you would talk a little more about the planning that you have decried the lack of. Who is going to do it? How do we

come by the people with this talent? Does it mean the Government? And finally, what is the nature of the followup to insure that planning is implemented?

MR. KEYSERLING: I can't make any contribution to that, except by agitating the way I am now. That's quite serious. You have advanced a very pertinent question, but I can't advance any pat formula to say this is the way you are going to get the people in all these jobs who will do it right or do it the way I think it ought to be done. All I can do is to talk around the country, and bring the tiny little bit of pressure that one person can bring to bear, upon this reorientation of approach. That's all we can do with any of our great national problems, everyone trying in his own way to square it off a little better. It is not a matter for one person or of an election. It's just a matter of getting enough people convinced of this, and talking about it, and gradually produce a slight veering of the needle so that it comes a little closer to pointing toward the truth.

That's not a very good answer, but frankly I can't suggest any perfect solution to a question as broad as that one is.

DR. HUNTER: Mr. Keyserling, I don't intend to take issue with you on the question of your occupational status, but as a politician you have given us a lot of strong beef to chew on. Thank you very much.

(19 June 1956--450)K/ijk