

The President and the
Council of Economic Advisers
Interviews with CEA Chairmen

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88. Alan Greenspan, p. 447.
 89. Arthur Burns, p. 122.
 90. Arthur Okun, p. 304.
 91. *Ibid.*, p. 306.
 92. *Ibid.*, p. 308.
 93. Herbert Stein, pp. 395-96.
 94. *Ibid.*, p. 396.
 95. *Ibid.*, p. 402.
 96. Alan Greenspan, p. 442.
 97. *Ibid.*, pp. 441-42.
 98. George Jaszi, "The Role of the Economist in Government: An Economic Accountant's Audit," paper delivered at a conference on the role of the economist in government, Royamont, France, 1974. Quoted in David Naveh, The Political Role of Professionals in the Formation of National Policy: The Case of the President's Council of Economic Advisers, Ph.D. thesis, 1978, University of Conn., pp. 168-69.
 99. Arthur Burns, p. 121.

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4

The Council of Economic Advisers Under Chairman Walter W. Heller, 1961-1964

Summary History

President-elect John F. Kennedy's announcement of his appointment of Walter W. Heller, a Minnesota economist, as Chairman of the Council of Economic Advisers came in December 1960 as he was also announcing his Cabinet appointments. Heller was well-respected within the economics profession and could be expected to reflect the liberal economic views associated with the Kennedy candidacy. Heller then recommended for the other two positions James Tobin of Yale and Kermit Gordon of Williams. While Heller was an active chairman, there was a division of labor, with Tobin responsible for monetary policy and Gordon in charge of industrial organization and incomes policy.

Heller was basically an activist concerned more with policy application than with theory. He saw nothing wrong with the CEA publicly advocating the policies it felt to be economically wise and educating the public in the "New Economics" espoused by himself and his colleagues. If JFK was more cautious and perhaps conservative in his economics, he still encouraged Heller and his associates to take advanced positions on economic issues. Consistent with this desire for consensus and his sense of political vulnerability, Kennedy preferred that his advisers feel out and educate the public on more unorthodox policies such as a tax cut to stimulate growth even with the economy on the upswing. He was thus able to avoid risking his own position on less popular policies while still trying out new ideas and retaining the image of a liberal administration.

Kennedy supported open testimony by the Council before congressional committees. While there was at first much concern that the CEA be cautious and not violate its advisory role in testifying, Kennedy soon recognized the educative value of such testimony as well as the importance of cultivating a friendly Congress. Along this same line, Heller and his associates also made speeches around the country to mobilize popular support. For instance, in 1962, after the steel crisis, Heller's frequent speaking engagements were part of the administration's strategy to win business support. Interviews and articles that could build support for administration policy were also encouraged.

Heller and the Council helped prepare Kennedy for his public appearances. In addition to working on the President's major

economic messages, Heller was a member of the group of close advisers that routinely met with JFK to brief him prior to press conferences. The CEA prepared lists of possible questions and answers for Kennedy to study, and then Heller would follow up with an oral briefing at breakfast the day of the press conference. And of course, the Council's memos were not confined just to press conference briefings. Hundreds of often rather lengthy memos were sent regularly to the President on various issues. While Kennedy did not often specifically acknowledge the CEA's memos, he apparently did read them, for the Council was frequently pleased to find the President later using a particular concept developed in the memos.

Kennedy preferred to deal with small groups whenever possible and only with reluctance held large formal cabinet meetings. Believing in the value of expertise, he did not want advice from agency heads outside their own jurisdictions. He preferred instead to consult only with those directly involved in the issues. In economic policy, this meant meeting with what Heller termed the Quadriad. Set up at the request of the CEA, the Quadriad consisted of the heads of the CEA, the Treasury, the Bureau of the Budget, and the Federal Reserve. Its meetings were not regularly scheduled, and they usually met only when Heller suggested to the President that a particular problem needed to be discussed by the President's top economic advisers. Perhaps more important was the Troika, the same group but without representation from the Fed. The Troika did not meet with the President but rather reported to him confidentially on the state of the budget, revenue, and the economy. Although there was at times internal disagreement over such matters, the Troika attempted to reach a measure of agreement before reporting to the President. Functioning at three levels (staff, sub-cabinet, and cabinet), the Troika became an important mechanism for coordinating economic policy during the Kennedy years. One other group was set up at Heller's suggestion in August 1962 in order to work out inter-administration differences over the proposed tax cut. This Cabinet Committee on Economic Growth was made up of the CEA chairman, the BOB director, and the secretaries of Treasury, Commerce and Labor. Under the Johnson administration, this committee's duties were expanded to include consideration of wage-price policy. Johnson also continued the Troika and the Quadriad.

The basic concern of economic policy in the early 1960s was the conflict between economic growth and stability that had dominated the Eisenhower years. While most Republicans and conservatives remained committed to the necessity of a balanced budget in order to maintain the price stability essential to economic growth and a favorable balance of payments, many liberals and Democrats felt that fiscal activism to achieve economic growth and lessen unemployment should take precedence over anti-inflation policy. When he entered office, Kennedy was forced to deal with this divergence of opinion. In addition to his own doubts about the validity of liberal economics, Kennedy realized the potential political problems of pursuing expansionist policies. His narrow victory in the presidential race had scarcely been a mandate for the "New Economics," and the control of Congress by conservatives

of both parties indicated that an orthodox approach to economic policy would be politically wise. The new President was also concerned that he not be branded fiscally irresponsible and that his policies be consistent with his campaign call for sacrifice by the people. Political considerations simply outweighed economic reasoning.

The clearest example of this acceptance of orthodox economics was Kennedy's anti-recession program in early 1961. Some sort of recovery program was essential, and his liberal advisers urged a tax cut or possible increased spending. They were not prepared for his commitment in his State of the Union Message to fighting the recession within the confines of a balanced budget. His advisers were not concerned so much that JFK's political concession to the budget balancers would prevent recovery but that it would mean a sluggish recovery short of the economic potential of the nation. Although the anti-recession program worked out by the CEA within Kennedy's guidelines was fairly conventional and stop-gap (centering on administrative acceleration of expenditures and legislative proposal to broaden government welfare transfers), the President's promise to re-evaluate his anti-recession program in mid-April held out the possibility of a more expansionist policy. But recovery by March 1961 made fiscal activism even less justifiable than before.

Kennedy continued to insist on the necessity of maintaining a fiscally responsible program throughout the first year of his administration. Despite the arguments of his advisers, he remained unconvinced of the wisdom of a deficit except during a severe economic downturn. A tax cut when the economy was on the upswing was not justifiable despite arguments about the need to move beyond sluggish recovery and the slack economic growth of the past decade. Accelerated defense spending did provide some stimulus to the economy, but Kennedy tried to offset such expenditures with drives for economy and efficiency. When the Berlin crisis of July 1961 threatened to increase the deficit, Kennedy considered even more drastic action. Concern over avoiding inflation, balancing the budget, and emphasizing the sacrifice expected of all Americans led to a move within the administration to seek a tax increase to finance the cost of U.S. involvement. Secretary of Health, Education and Welfare Abraham Ribicoff, Secretary of Labor Arthur Goldberg, Attorney General Robert Kennedy, Secretary of the Treasury Douglas Dillon, and Theodore Sorensen were some of the supporters of this action. Kennedy had apparently approved the proposal and was preparing to announce it, when the Council intervened with the assistance of Paul Samuelson and Kenneth O'Donnell to change the President's mind. Using national income accounts figures, the Council convinced JFK that a tax increase to cover the cost of the Berlin crisis would damage the already sluggish economy and that a small deficit would probably help the economy. But he was still not willing to abandon his emphasis on fiscal responsibility and made clear his commitment to a balanced budget in FY 1963.

In addition to his concern with his image of fiscal responsibility, Kennedy's budget balancing was rooted in a fear of inflation. While the Council and the other liberal advisers repeatedly

insisted that other problems were more pressing, the new President remained concerned with the inflation problem much as his predecessors had been. The most pressing reason for pursuing an anti-inflation program was the balance of payments problem that had been the focus of concern within the Eisenhower administration since 1958. According to more orthodox economists like Federal Reserve Chairman William McChesney Martin, the deficit in the international balance of payments and the subsequent gold drain required government action in the form of tight money policy and a balanced budget that would insure confidence in the dollar abroad. Expansionist policies were deemed irresponsible and inflationary. Although the Democratic platform in 1960 had called for monetary ease and the Heller Council had subsequently urged that policy, Kennedy feared the international repercussions of easing credit and was reluctant then to use monetary policy as an anti-recession device. This concern also restricted fiscal policy and was particularly responsible for his commitment to a balanced budget. A number of actions were taken to reduce government expenditures abroad, restrict civilian spending, and expand export trade (the Trade Expansion Act of 1962), but the major innovation was the monetary "twist" that provided high short-term interest rates and low long-term rates in order to encourage domestic investment and reduce the outflow of gold. Although Martin, Dillon, and others emphasized such policies to stabilize the dollar, the Council eventually gained support for its own proposals for reforming the international monetary system in order to lessen pressure on domestic policy. Although the balance of payments problems continued to trouble the Kennedy and Johnson administrations, efforts to ease monetary policy were sufficiently successful due to Dillon's influence with Martin, and the traditional conservatism of the Fed did not hamper domestic programs.

Even the CEA, however, came to accept the necessity of an anti-inflation program. Although Democrats had long criticized Republicans for their preoccupation with inflation and failure to focus on the need for growth, the Kennedy administration appeared to be doing the same thing in late 1961 and 1962. Although the CEA pushed for fiscal activism, it soon realized that some program to insure price stability was politically necessary before any plans for expansion could be realized. The CEA became active in the development of wage-price stabilization policy in 1961. In June it convened an "Economic Consultants' Meeting" under Kermit Gordon's direction to consider the problem. The division of opinion over the scope of government intervention was made clear in the meeting, and Heller, in a private memo to Kennedy, made clear the conflict over the proper policy and suggested his own framework involving productivity guidelines for price and wage changes.

Guidelines had not yet been established, however, in the fall of 1961 when contract negotiations in the automobile industry and the possibility of a steel price rise arising from earlier contract negotiations required administrative action. The administration intervened publicly in the latter case to influence public opinion against action by the steel industry. The CEA took a particularly active role, encouraging Senate debate on the issue

and pushing Kennedy to issue public statements critical of a price rise. There was no price increase, but it was not entirely clear how much credit could be given to administrative actions.

The administration's labor advisers and specialists could not reach agreement on proper wage-price stabilization guidelines because of internal conflicting interests, but the Council of Economic Advisers with Kennedy's support went ahead anyway and published the "Guidelines for Non-inflationary Wage and Price Behavior" in the 1962 Economic Report. Calling for non-inflationary price and wage actions within the limits of changes in productivity, both within the industry and within the economy as a whole, the guidelines (written by Kermit Gordon) were non-binding and dependent upon administration persuasiveness and public opinion for enforcement. Kennedy did not even specifically endorse the guidelines. As expected, the reaction was not favorable. Labor considered the guidelines too restrictive and questioned the assumption that income distribution would remain constant; management insisted compliance would cut severely into their profits and restrict expansion; critics on all sides questioned the practicality of the rather vague criteria and doubted that the guidelines would be applied consistently; and even the Council's own staff feared the new policy would result in direct controls and an end to collective bargaining.

Despite such criticisms, however, the administration was determined to enforce the policy and set about applying it to contract negotiations in the steel industry in 1962. Heller assured Labor Secretary Goldberg in late December 1961 that a non-inflationary wage settlement within productivity gains could be negotiated, satisfactory to both labor and management. With CEA support, then, Goldberg and Kennedy successfully pushed a settlement that met labor demands without necessitating an inflationary price increase. Both labor and management seemed willing to follow the guidelines. Then on April 10, U.S. Steel announced there would be an across-the-board price rise. Seven other major steel companies followed suit. Kennedy was incensed by U.S. Steel's actions and insisted that the company had committed itself to holding prices down. Having gone out on a limb to convince labor to accept a modest settlement, Kennedy was determined not to allow steel's actions to jeopardize his labor support. Beginning with an April 11 press conference in which JFK bitterly criticized the price rise, the administration undertook to force a roll back. The FTC and the Justice Department began pricing investigations, the Defense Department shifted contracts to smaller companies that had not raised prices, administration advisers telephoned everyone they knew in a position to influence the decision, sympathetic congressional leaders prepared to begin their own investigation, and the Heller CEA worked around the clock to prepare a "White Paper" denying steel's insistence of a cost-price squeeze as the basis for the price increase. When Bethlehem Steel yielded to administration action and rolled back prices, all others, including U.S. Steel, followed suit within 72 hours. The administration had enforced its wage-price policy, but only by using strong-arm tactics that further alienated already suspicious business interests.

The wage-price guideposts remained in effect after Lyndon Johnson came to office. Although there was debate within the CEA and the Cabinet Committee on Economic Growth about how actively to apply the policy, Johnson specifically endorsed the guideposts in the 1964 Report, an action the politically cautious Kennedy had always managed to avoid. Under Heller's guidance, machinery was set up to identify major problem areas. An inter-agency watchdog committee, headed by CEA member John P. Lewis, focused on automobile industry negotiations as the major target. The basic problem was that United Auto Workers would accept the wage guideposts only if the price guideposts were also enforced, an action that would mean price cuts in line with increased productivity. Despite administration reluctance, Heller and others tried unsuccessfully to get the industry to accept the price cut, but in the end their major accomplishment was simply preventing further price increases. Although the wage-price guideposts proved less effective than planned, the Kennedy-Johnson administration could at least point to a period of relatively stable prices, with inflation less than 2 percent through 1965.

Persistent unemployment (8.1 percent in February 1961) was recognized from the beginning of the Kennedy administration as perhaps the major economic problem, but the President's concern with maintaining an image of fiscal responsibility had limited his ability to act. Yet even if Kennedy had been willing to move beyond his concern with the budget, there was no clear consensus about just what was the nature of the unemployment problem and how it should be dealt with. The more conservative view (held by Arthur Burns and Federal Reserve Chairman William McChesney Martin) was that an increasing proportion of the unemployment was due to structural factors. This view rested on the assumption that at least 4 percent, and probably more, of those unemployed could not find jobs because of lack of training or obsolete skills, and that efforts to stimulate the economy and create more jobs would only aggravate inflation and not deal with the bottleneck of the structurally unemployed. What was needed to lessen unemployment was vocational education, manpower retraining, and other programs, but within the confines of a balanced budget. The opposing view held by most liberals was that some sort of fiscal stimulus to encourage economic growth was needed to combat the problem.

The problem of the past decade, according to these economists, was that the economy had simply not been operating at its full productive potential. While not opposed to structural programs or meeting social needs, these economists insisted that the focus of economic policy should be on stimulating aggregate demand in order to close the gap between real and potential output. Increased production would then mean more jobs and less unemployment. Tax reduction in order to eliminate fiscal drag on the economy was the main tool. Countering the criticism of conservatives and structuralists, these liberal economists insisted that the resultant budget deficit would not be inflationary, for there was so much slack in the economy. And in any case, existing high rates of unemployment were more dangerous than potential inflationary pressures. The aggregate demand theorists insisted that the addi-

tional economic output would lead in the long run to even greater revenue for important public needs.

From the first Cabinet meeting, Heller pressed his argument that recovery alone would not eliminate excess unemployment. In his March 6, 1961 statement to the Joint Economic Committee, Heller insisted that the economy was operating at least 8 percent under capacity and at a growth rate of only 3.5 percent. An expansionary fiscal policy was needed in order to stimulate growth sufficiently to bring unemployment down to the target of 4 percent. To deal with the sluggish recovery, Heller advocated in the spring of 1961 both a stand-by public works program and a \$10 billion tax cut, but recovery and political considerations eliminated them from JFK's program. Kennedy was more concerned that spring and summer with his commitment to the American space program and growing defense needs. While such spending undoubtedly helped the economy, it satisfied neither the advocates of spending for public needs nor the proponents of the aggregate demand theorists. The two groups actually came into direct conflict over the Berlin crisis, for one feared a cut in domestic programs if there were not a tax increase, while the other feared the damaging effects of a tax increase on the already sluggish economy.

A more politically acceptable aspect of the growth thesis was an emphasis on encouraging industrial modernization and expansion. The Treasury's proposals in 1961 for tax incentives to investment included liberalized depreciation and a 7 percent investment credit. Even these measures met resistance and were not passed until 1962. Although these tax policies were directed at long-term growth, they reflected more conservative concern with the investment rather than the consumer side of the economy.

More liberal growth measures were ruled out until mid-1962 when fears of a "Kennedy recession" finally convinced all but the most conservative within the Kennedy administration of the necessity for action. John Kenneth Galbraith still emphasized the importance of spending, but Kennedy considered such a policy politically impossible. The Heller Council had been pushing for a tax cut since the spring of 1961, and their arguments were increasingly convincing. Although Treasury Secretary Dillon had been an opponent of a tax cut and an advocate of a more fiscally responsible program, even he became convinced that a tax cut would be beneficial, especially when accompanied by the tax reform proposals he had long been advocating. After the May 28 stock market crisis, Kennedy also became convinced and on June 7 finally announced his commitment to tax reduction in 1963. He followed this up with his June 11 speech at Yale in which he attempted to lay bare the myths and illusions that had limited economic policy decisions. If Kennedy had disappointed the liberals in 1961, he no longer did so by mid-1962.

Heller and the Council wanted a "quickie" temporary cut as soon as possible in 1962, but Kennedy was not convinced to go that far. He realized that congressional conservatives such as Wilbur Mills would simply not accept a temporary cut in less than an emergency situation and that an attempt to secure such action might in the long run damage the structural reform. But it was not until Kennedy read Michael Harrington's The Other America in

1962 that he began to realize that the problem was more than just individual or area poverty but was widespread and not diminishing. Beginning in 1963, Kennedy began to reconsider the administration's efforts in this regard. In the spring of 1963, a CEA analysis by Robert Lampman confirmed Harrington's findings on the persistence of hard-core poverty. In June of that same year, the Council, with BOB assistance, began planning a comprehensive poverty program. In November 1963, shortly before his death, Kennedy told Heller to continue work on the program for inclusion in the 1964 legislative package.

When Heller told Johnson about the anti-poverty proposals on November 23, just after JFK's assassination, Johnson was enthusiastic and adopted the program as his own. In contrast to the tax cut and civil rights legislation, the other two priorities of the Johnson administration in 1964, the poverty program was to be Johnson's own program. With CEA facts and figures backing him up, Johnson then declared in early 1964 his "War on Poverty." Although the resulting program was hampered by bureaucratic infighting, limited funding, too many slogans, and not enough planning, it became central to Johnson's goal of a Great Society and the development of a national consensus as the 1964 election approached.

Walter Heller resigned from the Council soon after the 1964 election. In the four years of his tenure on the CEA, Keynesian fiscal activism had achieved a new level of acceptance in the making of American economic policy. In 1961, a balanced budget and price stability had been the goals under the prevailing orthodoxy, but under CEA guidance standard administration policy was refocused by 1964 on the problems of unemployment and balanced economic growth.

Oral History Interview

The Selection of the Chairman

EH: Would you like to comment briefly on how you came to be appointed Chairman of the Council?

MHH: I've been told by people that I went down to Washington-- somebody wrote something on this--knowing that I was going to be asked to be Chairman of the Council, but I had no idea. Well, excuse me, that's not quite right. For all I knew, I was going down there for a consultation about positions. Sarge Shriver, Kennedy's brother-in-law and chief recruiter, called me. He came into the Dupont Plaza to meet me and he got a call the moment he got there. I heard him say, "Yeah, yeah, I know we need a woman. Yes, yes, I know we need a black." So as I met him for the first time, I said, "I have my burnt cork and a wig and I'm ready to go." But I really didn't know. Somebody from a Chicago paper had called me and said, "Do you know that you're going to be offered the chairmanship of the Council?" My reaction was, "G'mon, you have to be kidding." My assumption had always been that if Paul Samuelson--wanted to be Chairman of the Council, he could have been. He is and always has been one of my heroes. But I think the role he played as outside adviser may have been an even more effective one than he would have played as chairman, just in terms of the range of his interests and his desire or lack of it on the administrative side.

EH: Do you think it was his recommendation to Kennedy on your behalf that led to your appointment?

MHH: It was one of them, I'm sure. It was Samuelson, Galbraith, Orville Freeman, Hubert Humphrey--a combination, of economic and political backing. But it was, as I say, a surprise to me. I did not know that that was the job he was going to offer me....

Hubert Humphrey recalled that he talked with me about the Council and that I said that I would not take a position interested in the chairmanship. It's a conversation that I shouldn't have thought I would have forgotten, but apparently there is a strong belief in the Humphrey camp that that's the way it came about. All I can tell you is that I recall vividly that I ran into the Dean of our Graduate School on the plane on the way back to Minnesota and told him of the surprising offer I'd just had and added, "I don't know whether I'm going to do it or not." He said, "You're going to stew, and you're going to weigh all the pros and cons and then you're going to say yes." He was right, of course. I just cite that as an indication that I was not at all privy to the fact that I was going to be offered the chairmanship of the Council.