The President and the Council of Economic Advisers

Interviews with CEA Chairmen

edited by Erwin C. Hargrove
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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 Ecnomic Advisers, Ph.D. thesis, 1978, University of Conn., pp. 168-69.

99. Arthur Burns, p. 121.

Participants in the Vanderbilt Faculty Seminars

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The Council of Economic Advisers Under Chairman Arthur Okun, 1968–1969

Summary History

The selection of CEA member Okun to succeed Ackley as chairman in January 1968 indicated a basic continuation of the policies associated with the Heller-Ackley Councils. At age thirty-nine, Okun was the youngest chairman in the Council's history. He was considered as articulate as his predecessors and as committed to the "New Economics." Basically a "numbers man," he had been responsible for the CEA's forecasts. James Duesenberry also remained on the Council and was joined by Merton Peck, one of Robert McNamara's "whiz kids" in the Defense Department in the early 1960s. With Duesenberry from Harvard and Okun and Peck from Yale, the CEA in the last year of LBJ's presidency had a distinctly Ivy League cast.

Okun had many of the same difficulties that Ackley experienced in dealing with Johnson. By early 1968, the problems in Southeast Asia were increasingly monopolizing the President's time. And when developments like the Pueblo incident, the siege of Khe Sanh, and the Tet offensive were not commanding LBJ's attention, his political problems engulfed him. The challenges from Eugene McCarthy and Robert F. Kennedy for the Democratic party nomination put LBJ in an increasingly vulnerable position. On March 31 that situation was eased, however, when Johnson publicly announced his decision not to seek renomination for the presidency. His plea to Congress at the same time to act on the surcharge proposal also raised hopes that the legislative stalemate might now be broken.

The 10 percent surcharge had never been popular with Congress or with the public. Rather than appealing for support on the basis of war needs, LBJ and his advisers had emphasized the importance of a tax increase to stem inflation, ease the credit situation, and avoid further balance of payments problems. The President's Economic Report and the CEA's Report in early 1968 had both been rather pessimistic about what would happen to the economy if Congress continued to delay action on the August 1967 proposal. Congress, however, was unmoved. Representative Wilbur Mills, Chairman of the House Ways and Means Committee that had bottled up the proposal, refused to consider a tax increase on the basis of forecasts of economic trouble, although he yielded on delaying cuts in automobile and telephone excises and speeding up corporate and personal tax collection.

The administration's predictions soon appeared to be coming true, however, as the GNP increased by $19 billion in the first quarter of 1968, inflation climbed to the 4 percent level, interest rates passed the 1966 peak, and the balance of payments problem worsened. Business leaders and the financial community joined the administration in pushing for the tax proposal. In particular, the failure to act on the surcharge was perceived by the international financial community as fiscally irresponsible and only served to further undermine confidence in the dollar. While the shift to the "two-tier" international gold system eased the situation, the threat of an international financial crisis increased support for the surcharge. What finally assured passage, however, was Johnson's concession to demands from Mills and others for a ceiling on federal expenditures. LBJ had resisted budget cuts because of his desire to maintain and expand his Great Society programs, but when it became evident that such cuts in domestic spending were the price that would have to be paid for passage of the surcharge, he yielded. The size of the budget cut was determined in negotiations between Congress and the administration, the House and the Senate, and Democrats and Republicans. As it was finally worked out, under the leadership of Treasury Secretary Henry Fowler, the surcharge and $6 billion expenditure reduction were added in the Senate to other tax legislation already approved by the House. Although this was an unorthodox approach, Mills yielded. Johnson signed the Revenue and Expenditure Control Act of 1968 on June 28, eighteen months after the surcharge had first been proposed in January 1967.

The surcharge was to be retroactive to April 1 on individual incomes and to January 1 on corporate incomes. Okun and other administration economists expected the surtax to slow down the economy and lead to a lower inflation rate. This would raise the unemployment rate temporarily about 4 percent. After the surcharge went into effect, there was some slowing of the economy, but the boom actually continued. The economists had apparently failed to clearly interpret the economic situation in the early months of 1968 and had underestimated the extent of the economic boom. Consumer spending did not moderate as expected, but actually increased by $5 billion in the third quarter of 1968. Home building had been in a slump early in the year, but the trend was reversed by late 1968. Plant and equipment spending also increased. The administration's fiscal policy appeared to have little effect on the economy. The tax hike had come too late and was too small to reverse the economic pressures that had been building since 1965.

Okun himself has suggested that such factors as expectations of long-term prosperity and the temporary nature of the surcharge probably moderated the impact of the tax increase. Perhaps more important was the Federal Reserve's easing of monetary policy. The CEA and most of the administration's other economists had approved of a more accommodative monetary policy because of their reading of construction industry trends and their fears of excessive fiscal restraint. But both their economic analysis and their

fears proved wrong, and the Fed's policy only served to offset efforts at fiscal restraint and feed inflation. When the Fed shifted to a tightened policy later, however, the economy proved no more responsive than it had been to the administration's fiscal policy. The shifts in the Federal Reserve's policies from 1966 through 1968 brought criticism from Congress and increased interest in a monetary rule and closer Congressional control, but the Council backed the Fed in insisting on the continued independence of the board.

Okun had never claimed that the surcharge would end the nation's economic problems, but he had hoped that the government's fiscal restraint would set a good example for business and labor. Although LBJ had set up the new Cabinet Committee on Price Stability on February 23, 1968, little was actually accomplished in the wage-price field before passage of the surcharge simply because Okun and others were reluctant to push for business-labor restraint as long as the government did not itself follow such a policy. The CCPS did undertake studies of medical care prices, the construction industry, and regulated industries, but there was little in the way of specific wage-price action. Okun did manage to secure a CCPS statement critical of the construction industry settlement, but his efforts to stop a copper price hike were futile. No action was taken on the telephone settlement.

As inflation worsened and business-labor settlements continued to exceed administration guidelines, Johnson and others considered the possibility of direct wage and price controls, but Okun managed to convince the administration to continue its jawboning policy. On July 21, the CCPS released a statement, at the suggestion of the CEA, urging all major unions and companies to secure guidepost settlements. Before the November 1968 election the CEA managed to secure a price rescission on home heating oil, a cutback of a steel price hike, and a moderation of an automobile industry price rise (the latter two with the assistance of Defense Department pressure on the industries). After the Republican victory in the fall, the lame-duck Johnson administration was less active. In December, the Labor-Management Advisory Committee reaffirmed its endorsement of the guideposts, and the Cabinet Committee on Price Stability recommended new goals for wage and price negotiations, as well as a number of micro policies involving manpower development, trade, antitrust action, and the like. Okun for his part was less than enthusiastic about the administration's performance in this area. While he felt the guideposts performed an important service, he emphasized the need for specific numerical guidelines, consultation with business and labor, and separation of the responsibility for the guideposts from the CEA and the presidency.

In the last Economic Report of the Kennedy-Johnson years in January 1969, the Council noted the unprecedented economic growth that the nation had undergone since 1961. The Report acknowledged the inflation problem, but insisted that the failure to move to a policy of fiscal restraint soon enough indicated not the failure of the "New Economics" but the need for a more flexible policy that would give the president the authority to raise and lower taxes within prescribed limits without congressional approval. In calling for an extension of the surcharge with discretionary authority to his successor to eliminate it if the economic situation changed, Johnson himself affirmed the need for increased flexibility in fiscal matters. According to Okun, the inflationary problems of 1966-69 did not indicate the need to return to an inactive fiscal policy but rather the increased importance of acting to stabilize the impact of the government's fiscal policy in order to avoid a repetition of the same errors. Whether his successors would view the problem in the same light remained to be seen. What was clear was that the Kennedy-Johnson years had proved that prosperity was sustainable. What remained for the incoming Nixon administration was to deal with the continuing problem of inflation.

The President and Economic Policy

EH: Let us turn our attention first to President Johnson. When you became Chairman of the Council, you were dealing with him. Do you think he tried to structure advisory processes so that he would get the result he wanted?

AO: No. The focus of your question is, "Did he fix it so that he heard what he wanted to hear?"

EH: It's not really that; it's the sense that he really knew what he wanted to do right along.

AO: I believe he was more responsive to professional advice and judgment than that statement makes it sound. He listened. He did his homework. He didn't want to go through all the analytical reasoning. My perception is that Kennedy intellectualized problems much more than Johnson. That's partly based on Walter Heller's ability to make direct comparisons. Sounds similar to the analogy between the patient who wants to see the X-ray and the patient who wants to look hard in the physician's eyes when he renders the judgment. Johnson was the second type: he didn't ask to see the X-rays, but he did ask for the judgments and he was responsive to them. He did not play his own economist. He did call on people on the outside, by telephone largely, for reactions. I remember that he once explicitly cited something that Bob Anderson had told him. "I'm sure that's the way he sees it," I replied, "but Mr. President, he doesn't share your values on a lot of things." He said, "You're telling me he's a goddam reactionary, I know that. That's exactly why I called. I wanted to find out what the views of a sophisticated and thoughtful goddam reactionary are and that's what I use Bob Anderson for." He really did have a sense that everybody's advice was somewhat colored by an ideological position. He once chided me: "When you tell me that I ought to cut a Great Society program, I know you mean it because that's not where your natural inclinations are." He was asking what the doctor's bias was and how do you correct for it. But he really took economists and economics very seriously.

LS: If he wasn't interested in your analysis, did you stop giving him analysis?

AO: In the sense of giving him a less detailed presentation of how we arrived at a conclusion, yes. We did sketch roughly what a verdict depended on or why we thought something would be too stimulative. We also tried to give him a sense of the confidence with which we could say that something was dangerous or desirable, a sense also of why something might be controversial and why other people might come to different decisions on it.