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THE U.S. ECONOMY IN MID-1970

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How serious is the US recession?

THE AMERICAN ECONOMY is now in a recession—the first in a decade. The longest sustained expansion in American history which began in the first quarter of 1961, when Kennedy was inaugurated, ended in the third quarter of 1969, some months after Nixon became President.

"If America catches a cold, the rest of the world will have pneumonia" was a common cliche in the years following the Second World War. This is no longer, if it ever was, true. However as the world's stock exchanges have shown in recent months, if America has pneumonia the rest of the world will well nigh certainly have at least a cold. Therefore the length and depth of the current recession as well as what is likely to follow is of interest in cabinet and board rooms around the world.

The recession to date can be imputed to policy actions taken to constrain inflation. As Nixon took office the Federal Reserve embarked upon a policy of constraining the growth of the money supply and bank credit. Virtually simultaneously, the rate of increase of Federal Government expenditures slowed and the Federal Budget moved from deficit to surplus. Whereas both monetary and fiscal policy actions were expansionary in 1968, during 1969 they both became constraining. In spite of this the rate of increase of nominal Gross National Product did not slacken until the fourth quarter of 1969, and was still rising in 1970.

To the middle of 1970, the downturn as measured by indices such as Gross National Product in constant dollars, industrial production, employment and unemployment is milder than the short and shallow recession of 1960-61. As measured by common stock prices and the public financial difficulties of major corporations the current decline is much more serious than any of the three recessions of the Eisenhower years.

The latest data continues to present a confusing picture. The decline in real Gross National Product apparently halted in the second quarter of 1970 and the seasonally adjusted unemployment rate in June was lower than in May. On the other hand the impact of the failure of the Penn Central Transportation Company in late June still has to work its way through the economy. The run on Chrysler Corporation commercial paper has shown that it has triggered a sizeable shift away from the commercial paper of some finance companies and non-financial corporations.

In spite of the down turn and threatening financial developments the rise in prices which began to accelerate in 1965 was unabated through the first half of 1970. The comprehensive price deflator for Gross National Product rose at an annual rate of 6 per cent in the first quarter of 1970, an increase from the 4.7 per cent rise during 1969. Similarly the annual rate of increase of consumer prices accelerated during the spring of 1970.

Wage settlements in early 1970 have been very generous. Many labour contracts provide for substantial wage increases immediately and further large increases during 1971 and 1972. Some agreements provide for increases over a three year period totalling around 40 per cent of the current hourly rate. Such contracts well might guarantee that cost pressures on prices will continue.

Thus the current situation is a policy maker's nightmare—an inflationary recession accompanied by financial disturbances. The rise in prices suggests a continuation of monetary and fiscal constraint, the recession signals a need to relax the constraint, and the financial disturbances indicate that the Federal Reserve System, as the lender of last resort, should be liberal in acquiring assets from financial markets and the banking system.

The spectrum of forecasts for the next two to three years runs all the way from those who see a replication of 1929-33 as being well nigh inevitable to those who fear an imminent rerun of the inflationary expansion of 1967-68. Each of these extreme positions is based upon too simple a view of the American economy and neither is likely to be borne out by events.

The evidence that the decline in activity has slowed can be interpreted as indicating that the economy is belatedly following the first part of the Administration's "game plan". The second part of this scenario, now revised to allow for recent developments holds that non-inflationary growth will be achieved by the end of 1970 if modest monetary expansion (say at the annual rate of 4 per cent) is combined with the present planned level of government spending. This too is most unlikely to happen.

The financial position of non-financial corporations, households and various classes of financial institutions changed quite radically over the post-war period and some changes were accelerated during the latter part of the expansion of the 1960's. The current financial structures are such that a decline in income or financial market disturbances may lead to a general movement to improve balance sheets. If this happens investment and consumption demand will be depressed.

Financial influences point to a second wave contraction being added to the present mild decline. If this happens the current recession will be the most serious of the post-war period. It is likely to be followed by a weak recovery and an extended period of sluggish economic growth as households, firms and financial institutions improve their balance sheet structures. As the second wave will be in response to a widespread preference for greater liquidity, monetary policy can facilitate the adjustment but will be unable to offset the contraction. Because of the involved budget-making legislative process, fiscal policy will not be available to offset the further decline but it could be used later to offset the tendencies towards persistant sluggishness. If income is sustained at close to full employment levels by positive fiscal action it will expedite the fulfilment of the

Changes in Selected Economic Measures
Current Recession and the Three "Eisenhower" Recessions
Per Cent Annual Rates of Change

Recessions	G.N.P. in current dollars	G.N.P. in constant dollars	G.N.P. implicit price deflator	Industrial production	Employment payroll	Personal income	Construction expenditures
	FROM PEAK TO TWO QUARTER AFTER			FROM PEAK TO EIGHT MONTHS AFTER			
1970	+3.6	−1.7	5.5	−3.3	+1.0	6.3	−1.3
1960	− 6	−2.4	1.8	−8.5	−2.3	1.2	1.8
1957	−5.1	−7.6	2.7	−19.4	−5.2	.6	−2.0
1952	−2.8	−5.2	2.5	−14.6	−3.9	−1.1	1.7

Source: Federal Reserve Bank of St. Louis

desires for restructured balance sheets, but such policies will be favourable to a continuation of inflationary pressures. Given the Nixon Administration's strong views that inflation must be contained, active fiscal policy will not be used at the first signs of substantial slack.

Thus what is most likely to occur is almost certainly not disastrous, perhaps serious but in large measure avoidable. This view depends upon three major considerations:

(1) The size of the government sector sets a high floor to income,

(2) The financial structure as it relates to corporations, households and financial institutions now tends to constrain private demand, and

(3) The Administration's tastes are such that they will be reluctant to use an active fiscal policy.

The prognosis that the most serious recession since the Second World War may have started is not a prophecy of doom. The recessions of this period have been mild and short (The most severe saw a 3.4 per cent decline in constant dollar Gross National Product and the longest lasted only 13 months.) In comparison the contraction phase of the great depression of the 1930s lasted 43 months and the constant dollar Gross National Product fell by some 30 per cent.

The high ratio of total government (state, local and federal) expenditures to capacity Gross National Product makes it virtually certain that a really deep depression cannot occur. In 1929 total government was 8.2 per cent of the G.N.P. and the Federal government was but 1.2 per cent of the G.N.P. In 1969 total government was 22.7 per cent of the G.N.P. and the Federal government's demand was 10.4 per cent of G.N.P. In addition there now exists a wide range of government transfer schemes and trust funds which underpin disposable income: as unemployment increases wages stop but social security payments do not. These programmes were non-existent or of minute size at the time of the great depression.

Even if a financial collapse occurs, which is most unlikely as the Federal Reserve System is aware of its responsibilities, what would follow would be different from what happened when similar events occurred in years gone by. In the past, when the government sector was small, a financial crisis triggered a collapse of investment and a large fall in income. Today government demand and transfer payments moderate the decline in income, which in itself tends to moderate the "collapse" in investment. In addition with the downturn a decline in government tax receipts and a rise in transfer payments occurs without any change in the tax and spending laws. Assuming normal growth in the money supply, the resulting large deficit will feed liquid and secure assets into the portfolios of corporations, households, banks and other financial institutions at a time when they value assets highly. As a result of the increase in the supply of secure assets the fall in the price of risky assets will be moderated. A large government sector sets floors not only to income but also indirectly to the price of private sector liabilities.

In current discussions of monetary policy reference is often made to "the crunch" of 1966, which was a mini-financial crisis that centred around some special liquidity and position making problems of savings banks (building societies) and the largest commercial banks. "The crunch" occurred soon after the Federal Reserve took action designed to constrain commercial bank activity. The Federal Reserve is often indicted for reacting to quickly to the disturbed conditions in the money markets that followed and for then permitting too great a rate of increase for too long in the money supply. In this argument the inflation of 1967-69 is laid to the errors of the Federal Reserve. The inference is drawn that if monetary constraint is eased now a quick renewal of inflationary pressures will result. This argument is based upon a misinterpretation of the 1966 experience and a lack of appreciation of the striking differences between the two situations.

Those who cavalierly place all the blame on the Federal Reserve conveniently neglect what was happening to government spending. Over the four quarters ending in the quarter of the crunch Federal purchases of goods and services in current prices grew by 19.1 per cent, in the next four quarters they grew by a further 13.4 per cent, and in the year ending in the third quarter of 1968 by another 10.5 per cent. This 49 per cent increase over a three-year period was mainly but not entirely due to Vietnam and defence spending. Over this interval the high employment budget went from a surplus to substantial deficit.

In contrast to the above, Federal government purchase grew by only 0.7 per cent over the four quarters ending in the first quarter of 1970 and the prospect is for at most modest growth in government spending over the near future This reflects the combined influence of a rundown of the war in Vietnam, the lack of new weapons systems entering large-scale production and the administration's strong opposition to increased spending on civilian projects.

In 1966 the liquidity of savings banks and large money market commercial banks were at issue as a result of flaws in the financial system. Although these flaws have not been corrected, special arrangements have been set up which renders them relatively harmless from the point of view of the stability of the financial system. As will be made evident tomorrow the liquidity problems of 1970 centre around the liability structure of corporations and the explosive growth of non-bank short-term financing of business via commercial paper and consumer finance houses.

Furthermore, 1966 came after two years, 1970 is after six years of an investment boom during which investment grew at a faster rate than output.

Thus the government demand, financial, and capital stock factors are different in 1970 than in 1966. Given the tone of government a rapid build up of government spending will not occur in the near future. The corporate liquidity picture indicates that a relaxation of Federal Reserve constraint will not lead to a rapid burst of investment. A prompt execution by the Federal Reserve of its lender of last resort responsibilities, even if it is followed by a sustained fairly high rate of growth in the money supply, will not now, by itself, be inflationary.

Both extremes, a great breakdown and a quick resumption of an investment boom with inflation, are not likely to happen. The middle ground consists of the Administration's position and the view that something more serious though far short of a disaster is in the offing.

The Administration's view is that this is and will continue to be a mild recession, and that reasonable price stability along with a resumption of economic growth will be achieved within six months if the current policy posture is sustained. This view is based upon a combination of forecasts, some based upon monetarist views —those identified with Professor Milton Friedman, of Chicago—and some based upon the views of the American Keynesians of the Kennedy-Johnson era. These apparently conflicting ways of looking at the world agree in that they attach little or no weight to the financial attributes of the economy as factors determining private investment and consumption demand.

Even though a great collapse seems most unlikely a period of financial trauma can occur which will affect views as to the "preferred" or "best" liability and asset structure for corporations, households and financial institutions and so affect the level of capital expenditures.

Aside from "the crunch" of 1966, the current financial strain comes after more than 35 years of financial stability in the U.S. These financial stresses and strains will make managers of portfolios—whether they be corporate financial officers, households, or officers at financial institutions—reconsider their position and the subjective value of safe portfolios will increase. (One immediate reaction to the Penn-Central debacle has been to lower the interest rate on Treasury Bills relative to that on other open market paper). As households businesses and financial institutions try to achieve more conservative portfolios, spending on investment and consumption will be constrained.

Thus the current recession will be deeper and will last longer than the administration view allows. It is likely to be followed by a weak recovery. The sluggish, recession-prone Eisenhower era might be a model for the first part of the 1970's.

The Nixon Administration sets a high priority to halting inflation. It is willing to pay a price in terms of lost output, higher unemployment rates and decreased growth in order to achieve this. According to the "game plan"—which reflects its model of how the economy works—the costs are to be modest in both extent and duration. If inflation is strictly a demand pull phenomenon which operates with no significant lags, the Administration game plan might have some validity. If inflation has cost push elements then their game plan, that inflation can be eased by a slight recession, is inconsistent with the way in which cost push operates.

Wage, price and thus real wage movements during the expansion have been such that sharp cost push pressures may be building up.

Between 1961 and 1965, prices were remarkably stable even though nominal G.N.P. rose by 32 per cent and the unemployment rate fell from 6.7 per cent to 4.5 per cent. Over these years the consumer price index rose by 5.5 per cent, average weekly earnings rose by 16.7 per cent in manufacturing and 17.2 per cent in contract construction. As a result the average weekly spendable real income of manufacturing workers, that is their real income after tax deductions rose by 11.7 per cent.

In the second half of the expansion, between 1965 and 1969, consumer prices rose by 16.2 per cent, nominal G.N.P. rose by 36 per cent and the unemployment rate fell from 4.5 per cent to 3.5 per cent. Weekly earnings in manufacturing rose by 20.7 per cent and in contract construction they rose by 31.1 per cent.

When union contracts in manufacturing come up for negotiation, wage demands designed to offset the lack of growth in real spendable income over the past four years will be made. Serious strikes are likely this summer and autumn, especially in the automobile industry. The outcome will depend upon whether the economy is following the Administration's scenario or the recession takes a turn for the worse.

If the economy is following the Administration's game plan, by the autumn unemployment rates will have stabilized or declined and there would be apparent evidence of improved demand. The signs of recovery will strengthen union power and employers eager for output and sales will be prone to settle.

On the other hand if a second wave inventory contraction is in process in the autumn, if signs of a slowdown in consumption and fixed investment can be discerned and if unemployment rates are higher than at present employer resistance will be increased and union strength will be diminished.

The Administrations objective of braking inflationary pressures will be in jeopardy from the cost side if the recession is not bottoming out; if the recession is deepening and being extended then the cost push pressures will be eased. If the latter happens the Administration might claim victory, but the price in terms of unemployment will be higher than anticipated, it will be a Pyrrhic victory.

America: the financial problems

IN 1964 AN investment boom began in the United States. Corporate fixed investment in current prices was $41,200m. in 1963 and $80,000m. in 1969. This massive accumulation of fixed capital over a relatively short time period may by itself tend to retard further growth in investment. In addition the way in which this investment was financed may act to constrain further investment.

Over this six-year period gross corporate internal funds grew from $43,900m. to $62,700m. Whereas the flow of retained profits and depreciation allowances exceeded fixed investment by $2,700m. in 1963, in 1969 fixed investment exceeded internal funds by $17,300m. If inventory investment is added then corporation investment exceeded internal funds by $24,800m. in 1969; net external funds financed some 28.3 per cent of total corporate investment. These financing relations are now imbedded in corporate balance sheets.

As is shown in the chart on the right, a similar though smaller excess of fixed investment over internal funds occurred in 1956-57. In 1958 fixed investment fell back to an amount that internal funds could finance. A replication of 1958 now could mean a decline of fixed investment by some $20,000m.

Corporate balance-sheets were also affected by the merger movement of the late 1960s and the more efficient management of cash positions. One aspect of the conglomerate movement was the use of "funny money", Wall Street's jargon for complicated debt and equity packages, to finance acquisitions. Acquisitions were often financed by debt and the cash position of both the taker and the taken were depleted in order to repay such debt. As a result, the merger movement added to debts and depleted liquid assets without increasing cash flows due to output.

A third phenomenon was the "discovery" by corporations of "principles" of efficient cash management. High and rising interest rates made it worthwhile for even moderately sized corporations to cut their cash holdings, using temporarily excess funds to hold interest-earning assets such as treasury bills, certificates of deposit, or commercial paper. Indirectly this released cash financed the investment expenditure of other units.

The combined effect of how investment was financed, the merger movement and the management of corporate cash can be seen by examining the changing corporate sector balance-sheets.

Corporate debts are payment commitments. Aside from rolling debts over, funds to pay debts are acquired from either current income, the running down or disposing of assets or the sale of new liabilities.

Thus the ratios of debts to gross profits after taxes and to various financial assets measure the liquidity of corporations and the extent to which their financial position can restrain investment if the desired portfolio changes.

From the early 1950s to 1967 no trend was discernible in the ratio of corporate debts to corporate gross profits after taxes; however, from 5.6 in 1967 the rate increased to 6.5 in 1969, an increase of 17 per cent. Changes in the liability cash flow ratio understate the change in the cash payments as the rise in interest rates and the associated shortening of the terms of debts has further increased the ratio of payments and refinancing to the value of debts.

In 1952 corporate demand deposit and currency stood at $28,800m. In 1969, in spite of the increase in sales and a tripling of liabilities, demand deposits and currency still stood at $28,600m. Time deposits, mainly negotiable certificates of deposit, increased greatly over this period, offset by a decrease in government bonds.

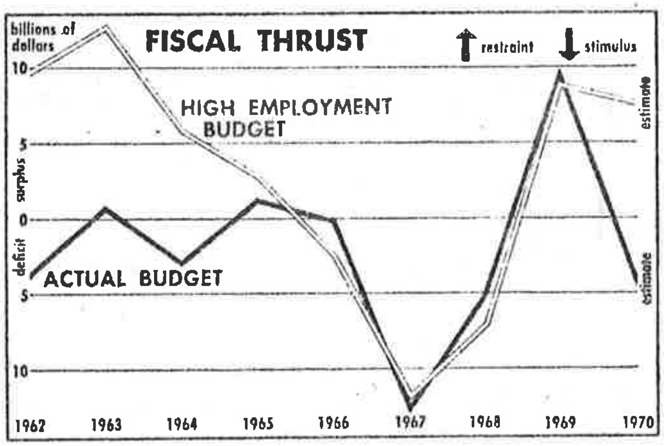
A noticeable change in corporate balance-sheets is the growth in holdings of open market paper. In 1961 corporations held $3,000m. of such paper, some 5 per cent of their liquid assets. In the first quarter of 1970 corporations held $27,500m. of such paper, some 35 per cent of their liquid assets. Because of this explosive growth in commercial paper owned, the corporate sector liabilities/liquid asset ratio did not increase anywhere near as radically as the liabilities/protected asset (deposits plus government debt) ratio. It is clear, after the Penn-Central debacle, that open market paper is not always a liquid asset.

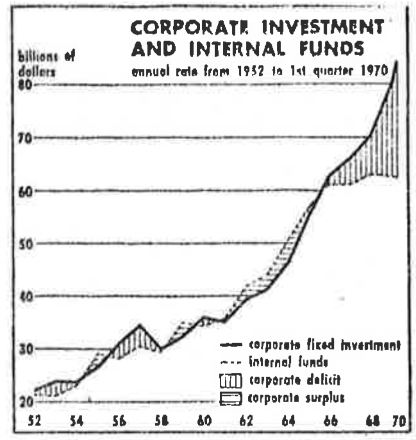
It is not known at what levels these aggregate financial attributes become critical; however, the higher the ratio the greater the likelihood that it will cause "trouble". An investment decision is taken with future results in view, it is inescapably speculative. One aspect of this speculation is the debt structure that a set of real assets, collected in a firm, is believed capable of supporting. During the investment boom of the late 1960s more firms than usual felt is desirable to finance investment by increasing their debts or running down their financial assets. Financial markets operated so that they were able to satisfy their portfolio desires at a modest current price.

As there is no objective standard for debt/cash flow ratios or debt/protected assets ratios, waves of optimism and pessimism, of experimentation and conservatism, can alternate in determining desired ratios at given market terms. However, these waves are not random; eras in which financial difficulties are minimal will induce optimism and experimentation, days in which financial difficulties are acute will induce pessimism and conservatism.

Although we cannot be certain, current developments in financial markets seem to be such as would tend to induce a desire for more conservative liability structures than now exist. One way this desire can be expressed is by floating long-term debt to repay short-term debt. This is happening at a great rate. Another way is to constrain fixed investment to a value more in line with cash flows. This second reaction is yet to come.

The stock market decline has decreased households' wealth enormously. At the end of 1968 the market value of corporate stock owned by households stood at $873,200m. Assuming that the approximately 30 per cent decline in the Dow Jones Average repre-





Source: Flow of Funds Accounts, Board of Governors of the Federal Reserve System

sent what has happened to the price of common stock, the market value of households net worth has fallen by about $260,000m. in 18 months.

In 1969 households saved $38,000m. out of a disposable income of $630,000m. The decline in Wall Street has cost households more than six years of savings out of disposable income, and this loss is widespread among households: about 25 per cent of American adults own stock in publicly-owned corporations. The percentage of personal disposable income saved during the 1960s varied from a low of 4.9 per cent in 1960 and 1963 to a high of 7.4 per cent in 1967 (following the milder stock market decline of 1966). If the savings ratio had been 7.4 per cent rather than 6 per cent in 1968 then consumption spending would have been some $9,000m. smaller. Any attempt by households to make up this lost net worth would result in a rise in the savings ratio out of disposable income.

In the Eisenhower recessions households were "heroes": consumption expenditures were sustained and housing led the way in the recovery. One factor sustaining consumption was the absence of any decline in household net worth. Housing led the way because financing terms for housing improved during the recession. Currently the pressure on corporate liquidity is such that corporations are issuing large amounts of long term bonds in order to decrease their dependence upon short term financing. This will tend to keep mortgage and other interest rates high. Until mortgage terms ease households will not be heroes: this time a longer lag will intervene before household spending leads the way.

Commercial bank financing of business has grown faster than commercial bank deposits since the Second World War. There has been an upward trend in the ratio of assets at risk to bank liabilities, rising from 35.7 per cent in 1947 to 82.2 per cent in 1969. In the early 1960s when assets at risk were about 2/3 of liabilities, the more tightly pressed money market banks introduced negotiable certificates of deposit in an effort to make their liabilities grow faster. In this they were successful. the instrument grew explosively from its introduction in 1960, reaching $16,000m. oustanding at the end of 1965 and $23,000m. at the end of 1968.

As bank certificates of deposits were run off in 1969 in response to the ceiling that the Federal Reserve placed on interest rates on deposits, non-financial corporations and finance companies floated their own short-term paper on a rapidly growing scale. As a result, a second banking system has grown up in the commercial paper market and business financing by consumer finance houses.

By the end of the first quarter of 1970 this second banking system was financing some $28,400m. of loans to business. This compares with $18,900m. 15 months earlier at the end of 1968.

This second banking system is to a large extent a company-to-company financing arrangement. Its viability depends upon confidence as to the financial strength of the borrowers. As we now know an event such as the Penn-Central debacle can lead to a "run" on this market.

Once a run occurs, commercial bank loans must be made available as replacements for second banking system financing. The Federal Reserve must allow bank reserves and resources to grow if this is to take place. The action taken to remove the ceiling on interest rates on certificatese of deposit needs to be supplemented by flexible and responsive policies with respect to the growth of bank reserves.

In the longer run the retardation of the growth of commercial banks relative to the rest of the economy poses threats to the stability of the financial system. The post-Second World War era has been characterized by rising monetary velocity and an increased proportion of risk assets in commercial bank portfolios. A shift to a mode of operation of the economy in which the money supply grows at the same rate as nominal income and which does not see a trend in the ratio of risk assets in bank portfolios might be necessary. If this is so the rules for monetary policy, derived from an analysis of the past 20 years, will not be valid.

The current situation is an inflationary recession accompanied by financial disturbances. Each of these attributes calls for a different mix of monetary and fiscal measures. Given the lags in the American legislative process, the only active weapon available, aside from some already scheduled tax reductions, is monetary policy.

The Federal Reserve action in response to the Penn-Central crisis shows that it is prepared to feed reserves into the banking system so that the shift of borrowers from the second to the regular banking system can take place. A purely lender of last resort operation, designed to smooth financial markets over a disturbed situation, will lead to an accelerated rise in the money supply. Although this may have an expansionary effect in the longer run, during the period in which the commercial paper market is shrinking and while balance-sheets are being adjusted it will be at most sustaining.

We can expect that business will attempt to reduce inventories. As the inventory/sales ratio in April, 1970, was the highest in a decade, there is a great deal of room for such a reaction. A rundown of inventories means that a quick decline in income will occur. Monetary policy actions will be ineffective in stemming this, fiscal policy given the legislative process is not available. A further decline in real national income seems likely in the second half of 1970.

The second income impact from the attempt by the corporate sector to improve its balance sheet will be to reduce fixed investment. Reconsiderations of investment programmes have been underway since the first of the year, and we can expect to see some signs of an actual decline later this year. Whereas there may be no policy options within the American machinery which can offset the inventory reaction, investment reaction has a longer lag and the declining tendency could be offset by fiscal action.

In the United States the current budget is a misleading indicator of the Government's effect upon gross national product; it is possible for the government to run a deficit with a tax and spending programme that is a barrier to the achievement of full employment. This is so because tax and spending programmes are set as schedules which are not easy to change. A better guide than the current budget to the thrust of the government's fiscal programme is found in the high-employment budget, which is an estimate of government spending and tax receipts at a target level of gross national product. If at this high level the government would run a surplus, then the government programme is constraining demand. If income is below the target level then with the same programme the government might run a deficit. Such a deficit sustains income, but it is not expansionary. A truly expansionary budget position involves a deficit at the target level of income.

The 1970 estimates are that the Federal government will run a \$4,300m. current deficit even though the high employment budget surplus is some \$7,600m. Given our forecast of a more sluggish economy in the second half of 1970, the government's budget posture should change so that the high-level budget is balanced. As a minimum this means a rise in expenditures and a cut in taxes that add up to \$7,600m. at target income.

If the financial pressures in households and corporations lead to the large decline in income that our argument indicates as being likely, then the target should be a deficit at high employment income. Only such a government programme would sustain corporate cash flows so that they can readily achieve their desired balance-sheet structure.

The less painful the resolution of the current liquidity pressures on corporations, households and financial institutions the greater the likelihood that an inflationary investment boom and associated financial experimentation will soon take place. There are obvious inflationary dangers from using an active fiscal programme to sustain aggregate demand. In principle active fiscal policy can lead to a cycle without a cycle, i.e., a cycle in investment offset by a cycle in the full employment budget so that there is no cycle in aggregate demand.

An active monetary and fiscal policy, striving to achieve a cycle without a cycle has an obvious inflationary bias. Such a fiscal and monetary programme implies a willingness to explore not only an incomes policy but also a means of effectively controlling investment booms and the liability structures of publicly held financial and non-financial corporations. Aside from the difficulties of designing and then administering such a programme, such instruments of economic policy are anathema to the present administration.

I doubt whether an active expansionary fiscal policy will be readily adopted by this administration. A tendency to rely upon steady growth in the money supply as the major policy tool is even now apparent. Thus we can expect a period of slack in the American economy during which monetary policy will be expected to carry the burden for expansion and, as in the past when monetary policy attempted to overcome liquidity desires, it will not be a quick success.

Keynes remarked that "When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill done" American investment booms are speculative—which is the meaning of Keynes' casino—and they induce experiments with financial instruments, institutions and postures.

Unless offset such booms serve the economy ill, not so much in leading to a poor choice of investment projects as in bringing about unstable financial positions, which in turn lead to depressions and stagnation. Although fine tuning is beyond the powers of the authorities for an economy with the propensities to speculate of the United States, successful economic policy requires that active fiscal policy be used to ameliorate the effects of investment booms and economic stagnation. The view of the world that favours active fiscal policy is not now in favour in Washington. The prospect is that the American economy will be depressed during the first part of the decade. The soaring sixties will be replaced by the sluggish seventies.