“Indexing and Inflation”
An AEI Round Table discussion with William Fellner, Robert J. Gordon, Milton Friedman, and Charls Walker
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EILEEN SHANAHAN, *The New York Times:* Good evening. Tonight we’re going to discuss a subject that is so new that there isn’t even any complete agreement on its name. It’s sometimes called indexing or indexation, sometimes called monetary correction, and many people may be familiar with it by an earlier name, escalation.

We all remember, I think, when the first escalation clause, in modern times at least, was written into a labor contract right after World War II—the contract of the United Auto Workers. It was based on the idea that, if prices were going up, wages ought to go up in some direct relation.

Now a proposal has been made—or rather revived, I am told—that indexing be made more general than that. We have here to talk about it four distinguished economists, one of whom is currently the most prominent advocate of the adoption of escalation, or indexation, in a certain form. I think you will find there is disagreement not only about the overall wisdom of the proposed policy, but also over how widely it should be applied, what should be left in, what should be left out.

Because the subject is so new, we’re going to ask each of the panelists for a three-minute opening statement to define what it is we’re talking about, where we agree and disagree. Our first speaker is Professor Milton Friedman of the University of Chicago, who is perhaps at the moment the most noted advocate of indexation.

MILTON FRIEDMAN: Indexation may appear new in the United States because we have been so fortunate as to have relatively stable prices over the past century and a half, except during wartime. But it is a very old idea that goes back centuries and that has arisen into prominence whenever a country has gone through periods of rapid inflation or rapid deflation.

Indexation is a plan whereby contracts which have a time duration are expressed in dollars adjusted for the rate of inflation, instead of being expressed simply in dollars. The escalator clauses in wage contracts are of this form. In these cases, a wage agreement is made for, say, three years with the proviso that if prices rise during that period wages will be adjusted accordingly. In the same way, an adjustment for inflation can be made in contracts for mortgages on houses and for loans.

Indexing is badly needed in the United States to adjust the income tax because, under current circumstances, rises in prices push people up into higher income brackets, so that their tax load is heavier than was intended by Congress. In fact, because of such automatic effects of price inflation, the United States government last year realized something over $25 billion in the form of tax revenues which were never legislated by Congress on anybody.

I am strongly in favor of indexation for two reasons: First, I would like to see legislated indexing of governmental contracts in order to make the government honest, in order to eliminate taxation...
without representation, in order to make it possible to sell government bonds without conducting a bucket-shop operation. Second, I am in favor of voluntary indexing on the part of business enterprises and people engaging in contracts over a period of time in order to ease the withdrawal pains from our present high level of inflation.

Indexing per se will not, in my opinion, do anything to reduce inflation. But what it will do will be to make it easier to terminate our inflation. It will make it easier by reducing the incentive for government to inflate and by making the withdrawal pains from inflation less severe.

MS. SHANAHAN: Now, an opponent of the whole idea, Dr. Charls Walker, former deputy secretary of the Treasury and now an economic consultant in Washington.

CHARLS WALKER: Thank you very much. Miss Shanahan. I disagree very much with my friend, Dr. Friedman. I do not think that he has the right answer for the big problem confronting us at this particular time.

I’m very grateful to him for his article on indexing in the current [July] issue of Fortune magazine. It reminded me of that old statement, “Oh, that my enemy would write a book”—because his arguments for indexing gave me some thoughts as to how I might respond.

Professor Friedman’s first sentence in that article reads as follows: “The real obstacles to ending inflation are political, not economic.” I strongly agree, and I think that many of the things he says in that article and has said in the last few minutes and will say tonight make a great deal of economic sense.

But since he has said that this is basically a political problem, it seems to me it has to be approached in political terms. I think that indexing is not only politically unnecessary but can be politically damaging through the economic process for a variety of reasons.

The question that Professor Friedman raised about the government being honest or dishonest in its offering of fixed term securities to the public—I’m tempted to say, rubs me the wrong way—does raise questions in my mind. We have a representative government—a democratic system of government—and when we talk about whether the government is straightforward or not, we’re really talking about whether the people of this country are exercising their role as citizens and voters in the proper ways.

So my fundamental points tonight will be on the political side, although I will make a point or two on the economic side as the argument goes along.

MS. SHANAHAN: Our next speaker is a supporter of the idea of indexing, Dr. Robert Gordon of Northwestern University.

ROBERT J. GORDON: I think it’s wise to set the discussion in context by going back to the very beginning and asking why it is at the present time that most members of the press and most everyday people, in reacting to their own life, find inflation so difficult to live with.

One may wonder why inflation is considered to be so bad, because, if you think about it, what is the difference between one state of the world with constant wages and constant prices and
another state of the world with all wages going up 5 percent a year and all prices going up 5 percent a year?

Now, if we contrast this ideal situation with what’s actually happened in the United States in the last two years, we get an idea what the argument is all about. The problem is, of course, that in the United States we have not been experiencing this ideal escalation of prices and wages moving together.

Representatives of various groups in society could step up right now and tell us they have not gained under the inflation. Although the rise in prices has been accelerating particularly due to the increase in food costs and oil prices, we have not had any acceleration in the average wage increase until very recently. Therefore the income that people have to spend after adjusting for inflation has been going down. In the same way, those people who have been saving for their retirement, for the education of their children, and for the proverbial rainy day have found that the value of their savings accounts, adjusted for inflation, has been going down as well.

What inflation has been doing has been redistributing economic benefits from one group in society to another. There are some gainers—for instance, the farmers and those people who were lucky enough to negotiate a mortgage at 5 or 6 percent interest ten years ago—but other people are losing.

Now, what can we do about this? The basic argument in favor of indexing is simply fair play. It would make the real world more like my ideal world.

Instead of having some gainers and some losers, we would bring everybody together by raising the value of savings accounts, wages and other contracts in line with the price level, and so we would stop this redistribution of income.

The people who gained because they got cheap mortgages ten years ago would have the value of those mortgage obligations go up. At the same time, the losers, those people who invested in savings accounts which are now paying interest rates actually lower than the rate of inflation, would gain because those savings accounts would go up with the price level.

MS. SHANAHAN: Our final speaker—who describes himself as an opponent, but not an all-out opponent, of indexing—is a former professor of economics at Yale University and now a member of the President’s Council of Economic Advisers—Dr. William Fellner.

WILLIAM FELLNER: Well, Miss Shanahan, I think the inflationary process in this country and in most others has in recent times had the characteristic of keeping the level of activity in these economies, the degree of resource utilization, at a higher than sustainable rate. In other words, inflation has caused very large numbers of decision makers in the market sector to expect to earn larger real incomes than they actually turned out to have earned, and this, in turn, has stimulated economic activity to a level that, in the long run, has been unsustainable.

Now governments, under strong political pressure, have been accommodating this process for quite some time. In each round it turned out that the bulk of the decision makers had earned lower real incomes than they expected. Then they tried even harder to raise their money incomes.
And the governments accommodated this for fear of causing a recession or even a slowdown of economic activity.

While this phase of an inflationary process is developing, I think that indexation would have harmful consequences because the amount of inflation and acceleration of inflation which would have to be accommodated by governments that were accommodating it for fear of a recession would represent even more acceleration and even more inflation. Subsequently, governments usually have to shift to monetary restraint because this kind of inflation is an explosive process that cannot be sustained for very long, or at least not indefinitely.

Then, for a while—and this is the second phase of the process—prices still rise steeply, markets weaken, and consequently the shifting of previous cost increases to buyers takes place in a cooler, weaker economic environment.

And finally comes the third phase: if the governments are credible and if the governments are consistent in this policy of restraint, then prices decelerate.

Now I think that in the first two phases—not only in the first phase, but also in the second phase of the process which I was describing—indexation would increase the difficulties faced by policy makers. In the third phase, it would help. However, the third phase might easily be postponed by the same policy makers, if we introduced a device that would make it possible to live with inflation somewhat longer. Then the day of reckoning would be postponed and the day of reckoning might also become darker.

Yet I do agree with much of what Professor Friedman said about the tax structure. That needs to be adjusted periodically if prices are rising. This is because of the reasons which he pointed out and also because depreciation allowances get to be insufficient.

MS. SHANAHAN: Professor Friedman, I wonder if you’d start the counterpunching.

PROFESSOR FRIEDMAN: Well, let me start with something that Dr. Walker said. He said, and quite properly, that ours is a democratic government, a representative government and that what happens in Washington is largely what the people want to happen. That’s true. But it’s also true that there is a very real problem of structuring our political system so as to make it responsive to the people. What I want to do in requiring indexation is to require officials to respond more directly to the will of the people.

Let me illustrate very simply. I was myself converted to indexing government bonds—that is to say, to issuing purchasing power securities—back in 1942 when, as a junior official in the Treasury Department, I was asked to write a speech for I believe it was the secretary of the Treasury in which he was going to promote the sales of savings bonds. I found that it was impossible, literally impossible, to write an honest speech. That converted me to cost-of-living clauses in government bonds.

It ought not to be necessary for the secretary of the Treasury—or even the deputy secretary—to make speeches in which he tells the public, the unsuspecting public, “Buy government savings bonds to protect your own future,” when he knows that that’s a bucket-shop operation—when he knows that given the rates of inflation that seem likely, everybody who buys such a government
bond is going to end up getting less purchasing power back for his bond than he paid for it to begin with and, to add insult to injury, paying taxes on the so-called interest he receives.

It seems to me that it would be a great improvement in our democratic system, it would strain the moral fiber of our leaders less, if they did not have this temptation to engage in bucket-shop operations. I wonder whether Dr. Walker, as deputy secretary of the Treasury, was always comfortable in the speeches he made encouraging people to buy savings bonds.

DR. WALKER: Well, I’d like to make three comments on that. First of all, I’m no longer deputy secretary of the Treasury.

PROFESSOR FRIEDMAN: Lucky man.

DR. WALKER: Second, I was deputy secretary of the Treasury in the first Nixon administration. And third, I was very comfortable in making the speeches that I made for people to buy savings bonds.

You made a comment, Dr. Friedman, in—

MS. SHANAHAN: Why?

DR. WALKER: In terms of savings bonds?

MS. SHANAHAN: Yes. If it is true, and I think maybe it is, that those who bought savings bonds had every reason to expect they would do less well financially than if they just put the money in their friendly neighborhood savings and loan, then why were you completely comfortable in suggesting—

DR. WALKER: I’d like to get to my fundamental points, but I will answer that in terms of the public good that I see in inducing individuals to save, to promote thrift—which they probably wouldn’t do if it were not for the convenience of things like payroll system and the bond-a-month system and so on.

But this is not getting down to the fundamental point that we are debating here tonight. Nor is it getting down to the fundamental point when Professor Friedman expresses faith in representative government and, in the next breath, says that representative government isn’t working because the will of the people is being frustrated by some nebulous, amorphous group out there that is inflating the economy for its own interest, presumably to get more money to spend.

I want to tell you one very short anecdote on that score. I was in the Treasury twice—first, in 1959–60 as economic adviser to Secretary Anderson and, then, in 1969–73 as deputy secretary.

In those earlier days we were trying very hard to get the Congress to remove a crazy, archaic, nonsense ceiling on interest rates on long-term government bonds. Interest rates had gone through the ceiling then—they went to 4½ and 5 percent, as you remember, and the ceiling was at 4¼ percent.
There was no ceiling on securities under five years so the only thing the ceiling did was to prevent us from borrowing beyond five years—we had to borrow five years or less.

One day Secretary Anderson and I went to the Congress to visit a very good friend, a fellow who represented an agricultural district from the Southwest. The secretary explained why this thing did not make sense. He explained that having to borrow short rather than long was more likely to create money and was inflationary. It took twenty to thirty minutes to get his point across. When he finished he said to the congressman, who is no longer with us on this earth, “Joe, do you agree with me?”

The congressman said, “Yes, I agree with you.” The secretary said, “Are you going to vote for me?” And he said, “No, I’m going to vote against you.”

Secretary Anderson asked, “What do you mean—you’re going to vote against me?” The congressman replied, “I’m going to be running, Bob, in a couple, three months. I’m going to be down on the hustings, or visiting the farmers at the side of the road. And when I talk to a farmer, the first question he will ask me is this: ‘Did you vote with Dwight Eisenhower for high interest rates or with Wright Patman for low interest rates?’ And I won’t have thirty minutes to explain to him why I voted with you for removal of that interest rate ceiling.”

Now, I have a very fundamental point here. The will of the public to stop inflation—and I agree with your article very much on this score—the will to stop inflation here and abroad is growing daily by leaps and bounds.

But the understanding of what to do about it, the costs involved and the trade-offs involved are not at all that simple.

And it is not an indictment of the people in Washington who are reflecting their constituents’ wills because, as Pogo said, when you get right down to it, “We have met the enemy and he is us.”

PROFESSOR GORDON: I have a little story to show that the farmer in Texas is not the only person in the world and that low interest rates don’t benefit everybody.

We have a congressman in Illinois who goes down and talks to a little old lady who has her money in a savings account and she says, “Now listen, an election is coming up. Did you vote with Dwight Eisenhower to let the interest I’m receiving on my retirement income and my savings account rise or did you vote with Wright Patman to keep my income down? I’m going to vote for Eisenhower.”

DR. WALKER: That’s one lady. That’s one out of a thousand.

PROFESSOR GORDON: You see, we get back to the original point I made. There are some gainers from inflation and some losers from inflation. We can’t pretend that the world is going to be a better world if we keep ceilings on interest rates and wages and other contracts instead of allowing them to respond to the changes in prices.
DR. FELLNER: Well, may I say just a word about purchasing power bonds. I think that the advocates of indexation do have an argument there but that they are overstating the merits of that argument. I also think that the logical underpinnings of that argument are somewhat less secure than is frequently maintained.

These underpinnings involve balancing equity considerations for savers, on the one hand, and for taxpayers, on the other. Now let’s disregard the fact that the people who try to sell bonds frequently exaggerate the bonds’ merits—or don’t speak about the demerits, the deficiencies.

If a person buys Treasury securities that yield, say, 8 percent or more, he has some expectations concerning future price trends, and he may turn out to have earned a negative real rate of interest.

The alternatives would involve risks which this security does not involve. If you don’t deliberately misrepresent the properties of this security or your own expectations concerning inflation, you do not misinform him. He is free to buy it, and he is also free not to buy it.

He can choose between buying the Treasury bond, which may have a zero expected real rate of return, and buying a security that is riskier but has a so-called positive “expected” rate of return. He is free to choose the one or the other.

Now, it is quite true that you would benefit this saver if you offered him a choice, a choice which could crudely be expressed as involving, on the one hand, a higher money rate of interest but no purchasing power guarantee, or a lower rate of interest and a purchasing power guarantee. He is better off if you offer him the choice. But that choice would be part of a deal, on the other side of which you have the taxpayer whom you have not asked what mix he prefers.

So there has to be a weighing of equity considerations one against the other. It’s not, after all, a deal that is coming about in the free market.

PROFESSOR FRIEDMAN: I don’t agree with you at all. In the first place, it’s not a question of equity between taxpayers and bondholders; it’s a question of taxation with or without representation. Bonds have been issued on the firm prediction announced by every government official for the last “X” years that inflation will be controlled and held down. Inflation is not an act of the free market either. Inflation is produced in Washington and nowhere else—it’s produced by government. If citizens have bought bonds on firm promises by government officials that inflation is going to be held down and if subsequently inflation is increased, in effect a tax has been imposed on those people who have bought the securities.

Indeed, that’s what’s so devilish about inflation under present circumstances. It is the one form of taxation that can be imposed without legislation.

I mentioned that I believe that last year the U.S. government took in some $25 billion or more from this source. No congressman voted for it.

Representative government is what we want. But just to point to the fact that we have a representative process, as Dr. Walker does, doesn’t mean that our present institutions ensure the most effective form of representation. They do not.
MS. SHANAHAN: We really need to have a fast round, perhaps just between the two supporters of indexation, exploring how extensive indexing ought to be.

Before we do that, I’d like to explain—for the people who might not know—what Dr. Friedman is referring to on the tax problem. He is referring to a very simple phenomenon—which is that as your income rises, whether from inflation or from real purchasing power, you move up into a higher tax bracket. In that way you get a tax increase and, as he suggests, no one has legislated it.

This is now happening at a galloping rate. To give you an idea, this past year median family income was slightly over $12,000. Our present tax rates were put in when $12,000 was an income of only the top 15 percent or so.

DR. FELLNER: Quite true.

MS. SHANAHAN: Now let’s look for a minute—assuming we believe in indexation—at the questions of what should be indexed and why.

PROFESSOR GORDON: Let me give you a menu as a basis for discussion. There are two different divisions. There are the things the government can do directly and there are the things which it can encourage the private sector to do.

The things that the government has already escalated or indexed to the inflation rate are social security payments, food stamps, and some government wages. Moving on, we can allow the tax brackets in the personal income tax to rise and the exemptions to rise. After all, what is a $600 or $700 exemption in terms of today’s price level? In real terms it’s much lower than it was twenty years ago. We can do the same to the standard deduction. And we can exempt from taxation those capital gains which are made purely because of inflation and not because of any real addition to purchasing power. We can exempt those paper capital gains from tax by simply writing up the base on which capital gains are calculated.

The same thing would be done to the corporation income tax. We can allow corporations to write up the base on which they calculate their capital stock—their plant and equipment and inventories—when they figure their profits. This would mean that they would pay less tax. As it is now, they’re paying a tax on fictitious profits.

We can also, as has been said, make every government security except short-term securities have a principal which rises with the price level or else an interest rate which is some small figure, 2 or 3 percent, plus this year’s rate of inflation.

Those are the steps the government can take. Now, what would happen in the private sector with this kind of encouragement from the government?

There are several things. At the moment, wage agreements which contain purchasing power clauses, which provide for upward adjustments in terms of the price level, cover only 10 percent or so of all wage earners, and those adjustments are partial. They give only about ⅔ of a percent wage increase for every 1 percent increase in the price level. It has been calculated that, if we had a doubling of the rate of inflation, the effect on wage increases would be trivial because at the moment so few wage earners are explicitly covered by escalators.
Now there may be some implicit escalation in the nonunion part of the economy, although I must say I haven’t noticed it in universities. When we hear about what our universities’ salaries are going to be next year, there are various discussions about how much tuition increase the university can pass off on its students, but no discussion at all of the cost of living and how much it’s gone up. So escalation would certainly help us professors. Not only would we index more wages, we would also encourage the issuance of indexed securities or bonds by private corporations.  

And if we wanted to go all the way, there are a couple of extra wrinkles which I doubt even Professor Friedman would support. We could index the demand deposits the people hold—

MS. SHANAHAN: That’s an economist’s word meaning checking accounts.

PROFESSOR GORDON: —the checking accounts and the currency, and, of course, as inflation proceeds these lose value just like any other kind of account. We could have a little chart on the currency that tells you, “On December 31st, this piece of paper is worth 5 or 10 percent more than it was on January 1st.”

Now, those last two are the most extreme. But we can array these things in a spectrum ranging from what we are indexing already—social security payments and food stamps—all the way to checking accounts and currency.

MS. SHANAHAN: Professor Friedman, do you agree that that’s a pretty comprehensive menu?

PROFESSOR FRIEDMAN: That’s too comprehensive, because I think the crucial thing is that we want to index any contract which has a substantial time duration. Demand deposits do not have a time duration; currency does not have a time duration; one-month Treasury bills don’t have much of a time duration, and casual labor doesn’t either.

I would restrict the private indexation to those contracts that have a substantial time duration. Let me make one more comment. So far as the government arrangements for taxes and borrowing are concerned, they are provided for in a bill that Senator James Buckley of New York has introduced into the Senate and Representative Crane and fifteen co-signers have introduced into the House. I have been amazed at how little attention that bill has received from the newspapers, the television people, and so on, because I think it is a bill that 99 percent of the citizens of the United States would approve.

MS. SHANAHAN: And it’s a bill that does what?

PROFESSOR FRIEDMAN: It provides for exactly what Dr. Gordon referred to as indexation of taxes on the government side, both the personal and the corporate tax, and for requiring the government to borrow in an indexed form.

I might make explicit an element that was implicit in Dr. Gordon’s menu, that is, mortgages and savings and loan deposits, both of which are time contracts. Our thrift institutions are now facing a very serious problem because they have borrowed on demand and loaned on time. They are stuck with mortgages written at very much lower rates of interest than the rates of interest that are now ruling in the marketplace. They would be in a far better position if they had both sides of
their balance sheets indexed—if their savings liabilities were adjusted for inflation and if, in the same way, we had a variable interest rate mortgage.

I might note that in the private market there is now a great expansion in this area. For an example, take the “floating notes” which Citicorp is going to issue to the tune of $850 million—

MS. SHANAHAN: Say a few words about how they would work.

PROFESSOR FRIEDMAN: Their notes are going to be issued in a form so that the rate of interest received on them will be equal to the rate of interest in the market on six-month Treasury bills plus 1 percentage point.

Now, the reason why that’s similar to the kind of indexation we’ve been talking about—

DR. FELLNER: Three-month Treasury bills.

PROFESSOR FRIEDMAN: Is it the three-month Treasury bill? Excuse me.

DR. FELLNER: But, as it was originally intended, they were to pay the money back on demand in six months. That has now been changed.

PROFESSOR FRIEDMAN: To two years.

DR. FELLNER: To two years, yes.

PROFESSOR FRIEDMAN: But the important point is that the yield would be linked to the Treasury bill rate.

DR. FELLNER: Yes.

PROFESSOR FRIEDMAN: Now, the Treasury bill rate has, on the average, reflected inflation. Treasury bill rates were 2 or 3 percent twenty years ago and are now 8 or 9 percent, because of the acceleration of inflation from then to now. Consequently, to link a yield to a Treasury bill rate is very close to providing the equivalent of a purchasing power guarantee on the security.

PROFESSOR GORDON: Let’s put some numbers on this, just to be specific for the benefit of the small saver. People who now, if they want to obtain their money on demand, have to invest at 5 percent or 5¼ percent in a savings and loan deposit would, under the Citicorp note or under an indexed savings account, be able to receive in the present circumstances about 9 percent. These are just the people who would gain. In order to finance this, the people who would lose, among others, would be those who have mortgages that they obtained, say, ten years ago at 5 or 6 percent. They are now reaping great capital gains on their houses and yet they are paying off their banks at this low interest rate. This is an unfair shift caused by inflation.

DR. WALKER: I’m not going to debate the Citicorp notes with you. I think they’re the greatest thing since sliced bread. [Laughter.]

PROFESSOR FRIEDMAN: Well, we’ve got another proponent of—
DR. WALKER: No, no. And I think that the Federal Reserve, in talking Citicorp into moving the first redemption date out into the future—I don’t think that made a lot of sense.

But I think we’re dancing with shadows and punching at pillows here. We haven’t gotten down to the fundamentals of the arguments which are involved in indexing.

I was delighted to see that Dr. Friedman started his article in *Fortune* by saying that the real obstacles to ending inflation are political, not economic. Then he went on to say, “Ending inflation would deprive Government of revenues that it now obtains without legislation,” a statement that I would argue with, but we don’t have time enough to discuss that tonight. More important, he wrote: “Ending inflation would also produce a temporary, though perhaps fairly protracted period of recession or slowdown and relatively high unemployment.”

Now I would hope, Professor Friedman, that as a teacher, you would let me follow the Socratic tradition and try to make a point or two by a question or two.

Later in the same article you stated that the major objection to indexation is the allegation that escalators have an inflationary impact on the economy. “In this form,” you state, “the statement is simply false. Escalators have no direct effect on the rate of inflation.” Talking in terms of pure classroom economics, I agree with you 100 percent. Prices can go up and stay up only if total spending so justifies it.

But you yourself said that inflation is a political, not an economic, problem. Query: Would you not agree that widespread indexing would create the “relax and enjoy it syndrome,” and reduce the political will—we’re not talking economics, we’re talking politics—reduce the political will to curb total spending and as a result put us on an inflationary treadmill?

PROFESSOR FRIEDMAN: I would not agree with the conclusion, though I agree with many of the separate statements.

DR. WALKER: Because you don’t think we’ve got representative government.

PROFESSOR FRIEDMAN: No, you are wrong.

DR. WALKER: Yes, you said a while ago that a bunch of people here in Washington, in effect, decide to tax the people—

PROFESSOR FRIEDMAN: No, but you are wrong as to why I disagree with your statement. The reason I disagree with your statement is the following: You are correct in saying that widespread indexation would reduce the public pressure to end inflation.

DR. WALKER: Right.

PROFESSOR FRIEDMAN: You are quite right, because by eliminating the inequities, by eliminating the distortions, by reducing the amount of unemployment associated with various fluctuations in policy, it would reduce the political pressure to end inflation.
But there’s another side of that story. We’ve got to look at both sides of the ledger. It would also reduce the political pressure to inflate.

DR. FELLNER: No.

PROFESSOR FRIEDMAN: The reason you have inflation is precisely because there is political pressure to inflate—for two reasons: first, to be able to finance in a supposedly painless way governmental expenditures and, second, in order to offset the undesirable effects of a slowing-down of inflation. That is to say—

DR. WALKER: What caused the governmental expenditures in the first place that have to be financed?

PROFESSOR FRIEDMAN: Public pressure.

DR. WALKER: Exactly.

PROFESSOR FRIEDMAN: But public pressure caused them because the—

DR. WALKER: I rest on that argument.

PROFESSOR FRIEDMAN: No, you cannot rest on that argument.

DR. WALKER: Sure.

PROFESSOR FRIEDMAN: You’ve got to go further. You’ve got to add—

DR. WALKER: Public pressure through the democratic system—

PROFESSOR FRIEDMAN: Excuse me. You have to ask whether public pressure was well-informed, whether our system provided the public with the information needed to make the right choices. The public pressure for those expenditures partly arose because the public was fooled into believing that we could raise expenditures without raising the taxes. One of the major purposes of indexation is to make the public face up to the costs and to recognize that if they’re going to insist on government raising expenditures, they’re going to have to have higher taxes.

And so I say to you that indexation would reduce the political pressure to inflate more than it would reduce the political—

DR. FELLNER: Well, this is not a generally valid argument—quite obviously, because in my youth I lived through very, very steep inflationary processes in Europe. And those inflations were proceeding at a fantastic rate after indexation.

PROFESSOR FRIEDMAN: Yes.

DR. FELLNER: What you are really saying, I think, is that if the pay-off for governments to inflate were reduced to zero, then this would take care of the problem. But that’s not what’s happening. The pay-off is just reduced to such an extent that the government has to do more
inflating in order to get the pay-off that it is shooting for. That is what is happening there in those cases.

So I think indexation would actually worsen conditions during those phases which we are discussing.

DR. WALKER: Maybe so, Dr.—

DR. FELLNER: Now, may I just finish that for a moment? Indexation would improve conditions in a subsequent process of deceleration. It would do that because then, obviously, when prices have started decelerating, you would get an automatic deceleration of wages and then a feedback on the price deceleration. That point needs to be admitted even if you are critical about the whole scheme of indexation. There is a phase in which this would be helpful, but the price deceleration will have to start first—with or without indexation—in an environment of austerity. The price deceleration will have to start as a result of monetary restraint and fiscal restraint, and indexation will not help before the price deceleration has started. After it has started, indexation will indeed help, but the only weakness in that part of the argument is that the beginning of that phase of deceleration may be postponed by governments that find it less painful to administer the phase of acceleration.

MS. SHANAHAN: I want to inject with a question. On the down side, as I observe the politics of economics, it seems that the forces against deflation—since the only way we know how to do it seems to involve an increase in the unemployment rate—are even stronger than all the forces you’ve all mentioned for inflation.

How would indexation ease the pain of the transition with its higher rate of unemployment? What would indexation do to the depth and intensity of the unemployment in the transition?

PROFESSOR FRIEDMAN: I agree completely with Dr. Fellner’s analysis. What it does is the following: Three times in recent decades we have started on the path to end an inflation. And each time we have not been able to stick to that path. Why? For the reasons you cite, because that path led to unemployment and recession and there was political pressure against it.

You cannot end an inflation without going through a period of austerity. I agree completely with Dr. Fellner on that. But, with indexation, it will not go so far or so deep; it will be a much milder recession, and therefore—

MS. SHANAHAN: Why?

PROFESSOR FRIEDMAN: Because the depth of the recession is now produced in part by the fact that people get stuck with unrealistic contracts.

Here is an employer who has committed himself to paying higher and higher wages at a fixed rate without an escalator clause. When the process of slowing down inflation starts, he suddenly discovers that the prices at which he sells his product aren’t going up as fast as they were before. What’s he going to do? His costs stay up. He can’t do anything about his costs, so he has to cut down his output. With indexation, his costs would, after a lag—I’m not saying there wouldn’t be
a lag—his costs would also adjust. Therefore, he would not be under anything like as much pressure to reduce output and employment. And this would happen all over.

DR. FELLNER: That, Professor Friedman, is obviously correct.

PROFESSOR GORDON: If you stipulate that, the game’s over.

DR. WALKER: No, it sure isn’t. I will not, absolutely not, accept the dichotomy made here tonight between the government, on the one hand, and the people on the other hand. I will not accept that dichotomy, and I think it’s at the heart of this argument.

PROFESSOR FRIEDMAN: I don’t believe it is, because I believe, as I said to you before—

DR. WALKER: But do you think we have representative government?

PROFESSOR FRIEDMAN: Absolutely—imperfect representative government. Do you think we have perfect representative government?

DR. WALKER: Certainly there is a degree of imperfection in our representation in government. But we’ve still got the right to go out there to vote the guy in or out on election day.

Now, you said earlier that the government uses this power to create fiat money, this power to use inflation to pay for its bills, to pay for its expenditures. How do those expenditures get generated? Who votes them? Where do they come from? Where are the forces in the opposite direction? Why don’t the people all ride into Washington and say, “Spend less money”?

PROFESSOR FRIEDMAN: If you ask the people, “How do you vote on having higher taxes?” what would they say?

DR. WALKER: They’d say, “Lower taxes.”

PROFESSOR FRIEDMAN: Right. If you say, “How do you vote on higher expenditures?” what do they say? “More expenditure.”

DR. WALKER: In other words, it’s a problem of economic education, and—

PROFESSOR FRIEDMAN: No, it is not.

DR. WALKER: —you would be the last one in my book to favor an elitist form of government that had a better judgment than the people to say—

PROFESSOR FRIEDMAN: I am not arguing that in the slightest.

DR. WALKER: That’s precisely what you’re arguing.

PROFESSOR FRIEDMAN: I am arguing that I want to have our institutions set up, as far as possible, so that the public at large—

DR. WALKER: Right.
PROFESSOR FRIEDMAN: —has to answer the question of taxes along with the question of expenditure, so that we can have a better representative government.

I don’t want an elitist government. On the contrary, I think elitism has led us to where we are now.

PROFESSOR GORDON: Ask yourself, “Who are the elite?” The invisible elite consists of those politicians who benefit when inflation raises tax brackets automatically, generating revenue for the government.

Nobody sees the revenue, so of course the public says, “I want the expenditures” because there’s no culprit there that’s raised the taxes.

All we want to do is to make the balance fair and to say, “You can have your increase in expenditures if you accept an explicit increase in your tax rates, but if you will not accept this increase in tax rates, then you can’t have the increase in expenditures.”

We’re simply making the choice obvious and in that sense it is a matter of education.

DR. FELLNER: You are not making it obvious. You can still run a deficit.

DR. WALKER: Dr. Fellner is correct. It’s no more obvious.

PROFESSOR GORDON: But the deficit cannot be financed by the bucket-shop operation of putting out government bonds which are cheap for the Treasury because their real value will decline in the future.

DR. FELLNER: A moment ago you said that the Treasury bill rate reflects the inflation rate correctly.

PROFESSOR FRIEDMAN: The Treasury bill rate does. The Treasury bill is purchased by highly sophisticated investors—

DR. WALKER: The bill rate does not, but the bond rate does—

PROFESSOR FRIEDMAN: Will you explain to me, Dr. Walker, how it is an indication of perfectly representative government—

DR. WALKER: I didn’t say perfect.

PROFESSOR FRIEDMAN:—that the minimum size of Treasury bill which may be purchased is $10,000—in order, I suppose, to protect the small saver from being corrupted by a high interest rate?

DR. FELLNER: That’s dreadful.

PROFESSOR FRIEDMAN: I have seen no other justification for it.
DR. WALKER: That wasn’t the reason for that decision. That decision was made in January 1970, primarily to promote housing. It’s being rescinded today finally, because the financial consumer is getting sense enough to know that “Regulation Q”—which is a deal dating from the depression that forbids banks from paying more than such and such on savings deposits—is an archaic, gerry-built, nutty rule which says that I get 5 percent on my money and John D. Rockefeller gets 12 percent on his money because he’s got more than $100,000 to invest.

But that doesn’t have anything to do with the point that I’m making here tonight. Both you and Professor Gordon are saying, in effect, that the issues of inflation, deflation, government spending, monetary policy and so on cannot be explained to the people sufficiently for them to understand and differentiate at the polls.

PROFESSOR GORDON: Why didn’t you come out in January 1970 for interest rates for small savers that would allow them to live with inflation? In other words, why didn’t you come out against Regulation Q? Why didn’t you come out for lowering the minimum denomination on the Treasury bill to one cent or one dollar?

DR. WALKER: Well, it had been lower. It was raised then. But I just—

PROFESSOR FRIEDMAN: I just think that this is all a red herring. Nobody denies that we—Bob Gordon and I—have the right, in accord with the dictates of our representative government, to try to persuade the voters to instruct their legislators to vote for indexing the income tax, to vote for the issuance of government purchasing-power securities, to vote to encourage private indexation. That is all we are doing, and how anyone can in any way represent that as trying to be elitist or as trying to avoid representative government—

DR. WALKER: Your red herring is a red herring. I mean it’s—

DR. FELLNER: Well, may I make a suggestion? Don’t we all agree that once you get into a process of deceleration, then indexation has merits because it gives you a feedback—

PROFESSOR GORDON: That’s right, and put this in concrete terms for 1974—

PROFESSOR FRIEDMAN: Right. I would agree with that.

DR. FELLNER: We should also agree, I think, that when a government accommodates an accelerating inflationary process for a while because it fears that its refusal to do so would lead to a recession and it wants to postpone that—when it does this, it is subordinating the long-run to short-term considerations. We should agree that, while it is acting in this fashion, indexation would be harmful. At least I don’t see how you can deny that indexation would lead to a more explosive process which is accommodated by such governments that are doing this. And all governments have been doing this in the past, in the recent past even.

Now I think there’s a big difference between the way in which, shall we say, the unqualified advocates of indexation see it and the way in which those of us who have some skepticism in this regard see it.
Professor Friedman looks at it this way. You get now, hopefully, into a period of deceleration, then we all admit indexation is helpful. And we all hope that the governments will be intelligent enough not to get us into a new phase of acceleration. Now those of us who would not accept that without qualification would say indexation is spreading—it will be spreading, but it will have its dark sides, too. and some of them may be quite serious.

In the first place, won’t governments postpone administering this deceleration and postpone it to a point where then it will be an even more burdensome process to bring about that initial price deceleration which will have an effect on wages and back on prices? Won’t this phase in which indexation will be helpful be postponed? And secondly, say that we get it under control this time: Won’t there be other flare-ups and won’t we then go through this process of acceleration again, which will be worsened by indexation?

MS. SHANAHAN: We’re now ready to go to audience questioning on this marvelously complex, controversial and, it seems one could even say, emotional subject of indexing, indexation, or escalation.

MURRAY WEIDENBAUM, Washington University, Saint Louis: I have a question for Dr. Walker. Would he address himself to the point that Milton Friedman has been making in the course of the evening, which is that so much of the pressure for inflation comes from government itself, anxious to generate more revenue. What empirical evidence do you have, in your dealings with the Congress, to support that point?

DR. WALKER: I think this is not only a very good question, but it is in one sense the gut question.

I’ve been associated with the federal government—not as long as Dr. Friedman, who went back to speech writing in 1942, and I was not speech writing then [Laughter]—but for fifteen or twenty years. And in my experience with the federal government over that period I’ve found that no group—executive or congressional—sits down and says: “Okay, fellows, how much are we going to inflate this week, or next week, or next year?”

Obviously, it’s too broad to say it that way. With the pressures for spending that you have, there are all sorts of scrambling for ways to finance federal spending, and through that process I think you get some of the things that Professor Friedman is worried about.

I would try to attack that problem through an educational process of informing the public of what the tradeoffs are. For example, if taxes are cut this year, what it might mean in terms of inflation next year. In particular, I find it very difficult to believe that the Federal Reserve authorities—who are at least semi-insulated from inflationary pressures—sit down and say, “Well, boys, how much are we going to inflate the currency this week for the purpose of making the government serve these goals and motives?”

I suspect somebody will respond to that also.

PROFESSOR GORDON: Yes, but both of these agencies—the Congress, as well as the Federal Reserve Board (which decides how much money is going to be created)—are hot advocating a
positive, that is, are not deciding how much inflation there is going to be. They are fighting a negative.

“How can we prevent unemployment? What is the least money increase we can get away with?” And for the congressman, “How can we avoid a tax increase?” They are going to spend as much as they can possibly spend, stopping short at that point where a tax increase would be necessary to finance it.

With indexing, we would be taking away the automatic painless source of revenue they have, which now allows them, painlessly, to go further than they should.

DR. WALKER: But it is not painless now, because of all—

PROFESSOR GORDON: Painless to them.

DR. WALKER: —the trouble they are going through. Why don’t you rather devote your resources to reducing the social and political cost of rising unemployment in a period of slow economic growth? There are lots of ways to do it.

PROFESSOR FRIEDMAN: The easiest way to do it is to reduce the amount of unemployment.

But, to answer Dr. Weidenbaum’s statement, I agree with Dr. Walker: no government official ever sits down and pulls a number out of the hat about how much inflation he’s going to cause. Of course not.

The causing of inflation is an Indirect consequence of the pressures, on the one hand, to raise expenditures, and on the other hand, not to impose taxes.

But, when I hear Dr. Walker’s answer—that the thing to do is to educate the public and to have more responsibility for expenditures and so on—I feel this is where I came in.

In 1952, over twenty-odd years ago, the Joint Economic Committee of the Congress held hearings on this subject. One of the proposals that was then under discussion was whether to have a purchasing-power bond. And the Treasury officials came in and said exactly what Dr. Walker is saying. Therein they say: “Just trust us. We’re going to be responsible, the U.S. government is going to follow a noninflationary path.”

Now, doesn’t there come a time when we should conclude that, instead of depending upon that kind of rhetoric, we ought to establish institutions which make it impossible for these indirect forces to produce inflation?

MS. SHANAHAN: If there isn’t another questioner standing up, I have a question.

Dr. Friedman, you said earlier that inflation is only made in Washington. I think most of us understand that inflation is often, or largely, made in Washington through government spending and taxing policies that are wrong. I think many of us also have the impression that the current inflation, beyond all others we remember in history, is not made in Washington. It was made in a worldwide crop failure in ‘72, in the Arab oil cartel, and in a number of other ways, I think.
PROFESSOR FRIEDMAN: Not at all.

MS. SHANAHAN: In any event, my question is this: to the extent that inflation is not fed by bad government tax and budget policies, what good does indexation do you?

PROFESSOR FRIEDMAN: I really don’t want to get diverted from the main task by discussing the sources of the current inflation because, if you look at the history of the proposals for indexation, you find they were initially all made from 1707 to 1807 to the 1880s and 1890s, under circumstances when people did not believe that government was responsible for inflation, and when, under some circumstances, it wasn’t. They were made under circumstances when it was thought that inflation came from gold discoveries, or from increasing economies in the use of gold that reduced the amount of gold per unit of output. Or they were made during periods of deflation.

Why were they made at that time? They were made then because it was believed by such great economists as William Stanley Jevons and Alfred Marshall in Britain and Irving Fisher in this country that a system in which you had indexed contracts would enable the economy to adjust better to these unanticipated fluctuations in prices.

The crucial thing is the word “unanticipated.” If you have an anticipated inflation, if everybody knows that every price is going to go up by 10 percent per year, indexing is of no point or no value. Its great value is to avoid the undesirable consequences of unanticipated inflation. So that, really, the argument for indexing doesn’t depend—

PROFESSOR GORDON: It helps reduce the pain from the crop failure, from the Arab cartel.

PROFESSOR FRIEDMAN: Right, yes,

PROFESSOR GORDON: Now, there are two different points to distinguish here. I don’t think we should get into a debate about how much of the recent inflation was caused by oil and the Arabs and how much was caused here in Washington.

But the important point gets back to my original statement—that the fundamental argument for indexing is fairness and equity. What we’ve had recently is a redistribution of income to the farmer and away from the small saver. Indexing is designed to alleviate the pain that comes when this sort of fortuitous circumstance occurs.

Now, the increase in the price of oil isn’t going to continue forever, and if we had had indexing during the last two years, we would have had more inflation and greater wage increases during the period when indexing was insulating people from this unforeseen pain. But after it was over, then the rate of wage increase would have moderated and would have been slower than it would have been without indexing. So you would have had more of a cycle, and the people would have suffered less reduction in their real income.

DR. WALKER: Yes, but I’m very confused about something Dr. Friedman said, if I understood him correctly—that indexing really makes sense only to cope with conditions of unanticipated inflation. Did you say that?
PROFESSOR FRIEDMAN: Yes.

DR. WALKER: Whereas your recent article in *Fortune* and your advocacy of indexing right now is based upon the fact that we are facing the greatest fear of inflation, and the greatest prospect for inflation, in many, many years. That seems to me to be contradictory.

PROFESSOR FRIEDMAN: Not at all. It is a question of quality versus quantity. When I say “unanticipated inflation,” I mean unanticipated amount of inflation. Everybody around anticipates a lot of inflation. But how much is a lot? How much inflation are we going to have? Is it going to be 6 percent next year, 10 percent, 3 percent? The case for indexing is strongest when you have great uncertainty about the degree of inflation that you will have.

DR. WALKER: Then why weren’t you for it ten years ago?

PROFESSOR FRIEDMAN: I was.

DR. WALKER: Indexation, indexing?

PROFESSOR FRIEDMAN: Yes, in 1952—

DR. WALKER: Purchasing power bonds, I know that, but I’m talking about—

PROFESSOR FRIEDMAN: Oh. If the world in which—

DR. WALKER: In ‘42 you weren’t for that.

PROFESSOR FRIEDMAN: No, no. Ten years ago, you had very little inflation. You had fairly stable prices. In a world of stable prices indexation serves no important function.

I’m in favor of indexation of government contracts all the time, simply to improve the representative system—political system. But in a world of relatively stable prices, indexation would be a nuisance in the private area.

DR. WALKER: Let me raise one quick question that stems out of that.

Why should Mr. Rich Man in the 50 to 70 percent tax bracket who spends a very low percentage of his income, relatively speaking, on the items in the market basket of the cost of living, get the same income tax adjustment—which your indexing scheme would provide—as the man who is at the lowest income tax bracket of, say, 14 percent and spends 40 percent of his income on food?

PROFESSOR FRIEDMAN: As Alfred Marshall said in 1887, “A perfectly exact measure of purchasing power is not only unattainable, but even unthinkable.” The answer to your question is that there is no reason why he should. We are talking about a crude pain killer, or corrective, for a very major and serious problem. It is precisely for this kind of reason that in a world in which inflation rates are fluctuating around 1, 2, or 3 percent, it is not clear that you can improve matters by any widespread use of indexation.
But that’s not the kind of world we’re talking about. We’re talking about a world in which rates of inflation have gone up in the United States to 10 or 12 percent for a short period, and in Japan to over 20-odd percent, and in Britain today to 20 percent. We’re talking about a world in which there is very large inflation, and in such a world, even an imperfect and crude adjustment for inflation is better than no adjustment.

DR. FELLNER: Now, are you really arguing that one can live with this kind of inflation under indexation, or are you arguing that indexation makes it easier to reduce inflation to small size?

PROFESSOR FRIEDMAN: Both.

DR. FELLNER: Well now, if you argue it is possible to live with that kind of inflation for a long time, then I think that is a very unconvincing argument, because I think that that inflation would continue to accelerate. It is an accelerating inflation which we now have. It is an accelerating inflation. You talk about an unanticipated inflation, and that is by its very nature an accelerating inflation.

PROFESSOR FRIEDMAN: Not at all.

DR. FELLNER: Yes, I think so.

PROFESSOR FRIEDMAN: There may be a variable rate—sometimes 12 percent, sometimes 6 percent.

Look, we must not talk about this in the abstract. There is an enormous amount of empirical evidence on these questions. We have the case of Chile which, long before its recent unpleasantness, had 100 years of inflation at rates that varied up to 25, 30, 40 percent a year and back down again without any acceleration in the sense of explosion.

DR. FELLNER: Well, that may not have been unanticipated either.

PROFESSOR FRIEDMAN: The average was not unanticipated, but the amount each year was, to some extent—

DR. FELLNER: But that is called high standard deviation from the expected rate, and that’s something else.

PROFESSOR GORDON: What we’re talking about here fundamentally is the trust, or lack of trust, in the monetary authority, the Federal Reserve Board in the United States, and in its ability to keep the growth of money at a reasonably stable level. All of us would agree that if it allows an explosive growth of money, we’ll have an explosive inflation. That is a separate logical issue from the issue of indexing.

DR. WALKER: It sure is.

PROFESSOR GORDON: As long as the Federal Reserve—
DR. WALKER: That’s exactly my point. If you can’t put your trust in the Fed without indexing, why do you think you can put your trust in it with indexing—which makes it easier to live with inflation?

PROFESSOR GORDON: Because indexing makes it easier for them to be responsible.

PROFESSOR FRIEDMAN: I have more confidence that a man will do a job properly the easier it is to do that job.

DR. FELLNER: Let’s admit that is an argument. There is also an argument on the other side of that issue, and the argument on the other side of the issue is that if it takes more of the vicious act to get the result, then more of the vicious act will be forthcoming.

DR. WALKER: Right.

PROFESSOR FRIEDMAN: You are generalizing from a case in Hungary, Germany, and Austria after World War I and II, which, I think, is a case of a qualitatively different kind.

DR. FELLNER: This is not as I see it.

DR. WALKER: If you’ll vote with Dr. Fellner, Miss Shanahan, we’ve got them three to two. [Laughter.]

EDWIN FUELNER, Republican Steering Committee, U.S. House of Representatives: Professor Friedman, in recent newspaper articles you’ve been accused or credited with looking very closely at the Brazilian case as the model to follow. Yet the Brazilian case seems to be different in very basic respects—such as, how much the government is going to force different sectors of the economy to engage in indexation. Would you care to comment on that?

PROFESSOR FRIEDMAN: I’m delighted to comment on that. I have been preaching indexation for several years, but got no attention until I happened, by accident, to use the Brazilian case as an illustration. And ever since I’ve had Brazil draped around my neck, as if I were a protector of Brazil.

Now, I think the Brazilian experience is fascinating and interesting. I think it is an excellent illustration of the virtues and values of indexation. But Brazil is a country very different from ours. And if all the evidence we had was from Brazil, it would be a very inadequate basis upon which to judge what ought to be done in the United States. Brazil is an authoritarian country, and it engages in indexing on a scale and by a method that I would not approve for the United States.

So I am delighted to respond to this question. I think we should take the evidence not simply from Brazil, but also from such countries as Finland, Netherlands, Canada, Israel. There is a very large number of countries that have had experience with this.

The thing that fascinated me about the Brazilian experience was how closely what they did paralleled in detail what had been recommended in 1886 by Alfred Marshall—although I’m sure the Brazilian people had never read Alfred Marshall’s paper.
ARTHUR CAROL, staff, Senator William Brock: Is there any disagreement among the four of you that, once some deceleration in inflation occurs, employment will not be as bad with indexing as it would be without it? Is there any disagreement on that?

PROFESSOR GORDON: That’s right. Why don’t we work through a little bit more specifically—

DR. FELLNER: I would accept that. But I think that it might be postponed under indexation.

PROFESSOR FRIEDMAN: At least three of the four—

DR. WALKER: I’ll give you a tentative yes.

PROFESSOR FELLNER: That is because the acceleration becomes less uncomfortable for a while, and uncomfortable measures are needed for bringing about the deceleration. And in future phases in which inflation starts flaring up, it will become worse under indexation.

I don’t know how you can weigh these pros and cons against one another. Indexation is going to spread anyway. It will have some favorable and some unfavorable consequences.

The answer to the question which you asked is, yes, once deceleration has started, indexation is helpful in that phase.

DR. WALKER: But there are easier ways to ameliorate the social and political cost of the unemployment problem in our democracy than indexing, in my view.

MS. SHANAHAN: Don’t those ways all involve government outlays, an excess of which you cite as a major cause of inflation?

DR. WALKER: They could involve government outlays, but outlays that would be very much recovered in terms of the benefit resulting from them. Now, for example, I do not look upon a special exemption to the minimum wage for teen-agers, which, I think, would be very important to the manpower picture, as an increase in government outlays.

Manpower training, according to the studies carried out at this institute and other places, could be as effectively, or more effectively, done at less cost than has been the case over the last ten to twelve years.

MS. SHANAHAN: Let’s call it worker training.

DR. WALKER: Worker training, worker-person training—whatever you want to call it.

PROFESSOR FRIEDMAN: When anybody tells me that any government venture can be done at less cost, more efficiently, I agree with him. When he tells me that that’s an easy solution, that’s another story.

DR. WALKER: No, no. This problem, the problem of whether we can reduce the social cost and political cost of unemployment or not, is a very serious one.
PROFESSOR GORDON: What could be an easier solution than reducing the amount of unemployment? This gets back to the questioner. Let’s ask, how would indexing reduce the amount of unemployment?

At the moment we are in a period during which unemployment is going to rise, because workers are now just in the process of becoming compensated for inflation which has already occurred. We’re going to have large wage increases over the next year, which are going to eat up all the spending financed by growth in the money supply, and there isn’t going to be anything left over for real output. So unemployment is going to increase.

This would all have been behind us now if we’d had indexing. Indexing would have made the economy more stable. It would have prevented the expansion in real output that occurred in the last year. It would have made things easier for us from now on.

The big problem is the delay in the adjustment of worker’s pay to price increases. So what we have coming up now is a delayed reaction to the inflation in oil and food prices and other prices, and this is going to create unemployment. If this adjustment were behind us, we would be able to have the same amount of spending, less unemployment, and more real output.

DR. WALKER: Let me pose a question in this connection.

Let us suppose that, one, we initiate indexing tomorrow in all of its great glory, and two, we have over the next six months an exogenous force from overseas that causes the cost of imports we just have to have to double. I mean, some imports and in the short run—energy, manganese, and all these other things we have just got to have. Must we not under those circumstances—that is, indexation and an impact on the price level in the United States because of the increased cost of those imports—have either an increase in the domestic price level that is validated by monetary and fiscal policy or an increase in unemployment?

PROFESSOR GORDON: No.

DR. WALKER: Even with indexation?

PROFESSOR GORDON: No. You’re just suggesting a replay of the last six months, in which we had an increase in the price of oil, supposedly an essential commodity—

DR. WALKER: Yes, I am.

PROFESSOR GORDON:—which consumers learned how to use less of, but this doesn’t have to be validated by monetary policy.

DR. WALKER: But take something you can’t do without, like coffee? [Laughter.]

PROFESSOR GORDON: At $10 a pound, I’ll do without coffee.

PROFESSOR FRIEDMAN: You’re getting us into an area that I really think is outside our main concern, but the main fallacy of this view is the same as the fallacy of the view that Miss Shanahan was expressing before. You have to distinguish relative prices from absolute prices.
and from the average level of prices. If the price of oil and food went up, that meant that consumers had less to spend on other things and that other prices went up less. You mustn’t confuse the arithmetic of a price inflation with the economics of a price inflation.

DR. WALKER: I do not. I agree with you 100 percent that Heller and the others are wrong in saying that exogenous forces can give you an eternal inflation under indexing, not unless the total spending is there to buy—I agree.

DR. FELLNER: We seem to be agreeing on something else, more or less—namely, that the present tax structure leads to very undesirable results. If there is a sustained inflationary development. Exemption limits get to be very different from what had been planned, tax brackets get to be wrongly defined, and capital gains are defined in a way that is not really applicable to economic processes. Money gains can be real losses easily, as many of them are. Depreciation allowances become quite inadequate: you can’t replace plant and equipment from what is accumulating for depreciation.

So there is agreement, perhaps, on this too, isn’t there?

DAVID OTT, Clark University: The discussion was left earlier at a point which I think was very critical, and the panel agreed that it was very critical, but never really explored it. I’m referring to the transitional problem of what to do if you have huge amounts of prior contractual obligations outstanding. How do you go into indexing? If you do adopt indexing and the monetary authorities go wrong, indexing will exacerbate the situation for these particular industries.

This raises another question. If you can get through the transitional period, why shouldn’t we index all the time, because if you don’t index all the time, then any time you hit an inflation you’ll have this block of contractual obligations sitting there that you’re going to have to get around somehow.

DR. WALKER: I agree on the contractual obligations. There are $600 billion, more or less, in savings accounts in commercial banks, in savings banks, and in savings and loan associations, and I don’t know how much more in potential cash value of loans on life insurance. If the Treasury tomorrow issues a purchasing-power bond at even 3 percent plus the cost of living, I see a tremendous increase in disintermediation, which is already a number one priority problem in our society.

MS. SHANAHAN: Disintermediation is the most incomprehensible of all economist’s words. It means people taking their money out of savings and loans mainly, but also banks, because they can get a higher interest rate elsewhere. There is general agreement that this is pretty terrible, mostly because it takes away the money for financing housing.

DR. WALKER: And this would make it more so.

PROFESSOR FRIEDMAN: No, it would not. The general answer to this—

DR. WALKER: Sure it would.
PROFESSOR FRIEDMAN: —basic question is, that the problem of the savings and loan and thrift institutions is a basic and serious problem. It is a problem that is with us now, and it is a problem that—indexing or no indexing—will not be avoided except by a rapid decline in the rate of inflation. But if indexing—

DR. WALKER: Indexing will make it worse.

PROFESSOR FRIEDMAN: I beg your pardon. Indexing will simply unveil what is there, what is already bad, and what is going to get worse if inflation speeds up. If inflation slows down, this problem will also slow down.

Are we better off continuing to inflate without indexing, in the hope that we can postpone the evil day, with the danger that we shall have a still bigger mess later on? Or, are we better off facing up to it right now; improving our arrangements in such a way that if we succeed in slowing down inflation, which indexing will enable us to do more rapidly, we shall get out of the situation more rapidly?

If we both inflate and index, then we just have to face up to the problem of the thrift institutions. But then indexing provides a way of facing up to the problem. Because indexing will then enable us to make any bailout of the thrift institutions—and I am afraid, politically, a bail-out will be necessary—contingent upon their restructuring their assets, their new assets and their new liabilities, so that this necessity of shoring them up will gradually disappear.

If we don’t index, what are we going to do? Are we going to shore up these savings and loan and thrift institutions permanently? Are we going to pour billions of dollars into supporting the mortgage money rate and the mortgages that these institutions have outstanding? Are we going to keep Regulation Q indefinitely?

I believe that the fundamental answer to the very important question that Mr. Ott raises is that we’re facing an extremely difficult and serious problem, and the sooner we bring it out into the open and do something about it, the better.

Don’t kid yourself into thinking that you can reduce the problem by avoiding indexation.

DR. WALKER: But you’re going on the assumption that we are—

DR. FELLNER: There is a bill before the Congress which would restructure the assets and liabilities of financial institutions, but Congress isn’t doing anything about it.

DR. WALKER: Oh, the Hunt Commission recommendation, sure. Congress is going to do something about it.

DR. FELLNER: But not along the lines which you suggest.

DR. WALKER: Congress is going to do something about it, but it’s a long-run solution, not a short-run solution.

DR. FELLNER: Well, three years.
DR. WALKER: It will take a lot longer than three years.

But, Professor Friedman, you’re going on the assumption that without indexing we’re going to let inflation run rampant.

You conclude in your article in *Fortune* that despite the experience of the past forty years—with Hoover defeated in 1932 because of unemployment and Nixon defeated in 1960 because of unemployment—inflation is now a number one political issue. It is causing governments to fall in England, perhaps in Japan, perhaps in other places.

This encourages me to conclude that there is a middle course, without indexing, that can reduce inflation. There is a solution that can help you work your way through the shoals of disintermediation—this withdrawal of funds from the savings institutions—without what you call a “temporary” transitional problem, a problem that I think would just knock the financial system right on its rear.

PROFESSOR FRIEDMAN: I agree. I believe that the public at large is willing to take sterner measures against inflation than our leaders recognize. The leaders are subject to a cultural lag.

I’m not one of those who predicts that we’re going to have a runaway inflation, that we’re going to repeat the German experience. We’re not. That isn’t what is in store.

Yet I fear we shall not soon put an end to inflation. Right now everybody would heave a sigh of relief if inflation came down to 6 percent. It was only 4½ percent when—in desperation, supposedly—Mr. Nixon imposed price and wage controls in 1971. So you don’t, have to have inflation run rampant to expect that the chances of 10 percent per year over the next ten or fifteen years are not very small.

HENRY BRIEFS, Georgetown University: I noticed that Professor Gordon’s menu of things to be indexed omitted most of the expenditure side of the federal government’s budget. I suppose, on principle, you would argue that that would have to be indexed as well. I agree that basically the improvement of information would make the public’s process of choice more rational, but I’m not sure this is what is really going to happen. I think the real problem is that, on the expenditure side, you have millions of programs that are for the benefit of not everyone, but of particular interest groups, and the purpose of the exercise is to get the general tax fund to support a good portion of the expense of those programs.

So just getting the news out in the open, I think, is not likely to occur because that involves the hard tradeoff decisions, whereas the way in which we operate our federal government process—in fact, state and local as well—is really a pluralistic process in which competition is on to put together a winning majority by satisfying the demands for public services of some groups.

PROFESSOR GORDON: To go back to the beginning of your question, at the very top of my menu of the items that would be indexed were those federal expenditures which are already indexed, that is, social security payments, food stamps, and, to some extent, government wages. I would extend indexing to all government wages. Of course, other government purchases involve items which are bought from the private sector, and whether those items would be indexed or not
depends on whether the private sector responds to the incentive that we, the indexers, are throwing out to them.

But to get to your more basic point, the fact that many government expenditures are made for the benefit of particular private interest groups and not for the benefits of the society as a whole—this is not a problem that is going to go away whether we have indexing or not. Our point here tonight is that indexing would force the Congress to make hard decisions. If congressmen want to continue logrolling—to vote for a dam in Arkansas in exchange for a colleague’s vote for a military base in Massachusetts—if they want more programs than an indexed tax system would finance, then an explicit increase in tax rates would be required; and this would be publicized so that the public would know that the congressmen were responsible. They wouldn’t be able to get away with financing this logrolling simply by allowing the inflation to provide automatic revenue for them.

FRANK SCHIFF, Committee for Economic Development: I wonder if all the panelists agree with the assumption that seems to have been made, namely, that when external impulses on the economy either raise or lower prices, the economy reacts as quickly to both sides. Doesn’t our experience make it more correct to say that it’s easier for prices to stay up or to be raised—and wages too—than for them to fall or be lowered?

If the latter is the case, then the point that Charlie Walker made earlier about the sudden rise in external prices needs more discussion. The rise might be quite temporary but, with indexation, it could cause a long-term increase in prices and wages to be built into the economy, whereas a fall in external prices would not necessarily produce the corresponding effect on the down side—in practice, given the way our institutions work. I wonder if anyone would like to comment on that.

PROFESSOR GORDON: I think you’ve put your finger on one of the most important arguments for indexing. There is asymmetry now: it is easier for prices and wages to go up than to go down. When spending declines in the economy, the first reaction of an employer is not to cut the wages of his employees, but to lay them off, and this causes unemployment.

The argument for indexing is that it makes the upside of accelerating inflation symmetric with the downside of decelerating inflation. Escalators, or index clauses written into wage agreements, make it just as easy for a fortuitous increase in the price of oil to raise wages as for a decrease in the price of oil to reduce wages. The lack of this two-way flexibility is the reason why it is so hard to stop inflation, and why the price in terms of unemployment is so high.

PROFESSOR FRIEDMAN: I go part of the way, but not all of the way with that. In answer to Mr. Schiff’s question, note first that what’s often involved is not some prices falling and other prices rising, but some prices rising less rapidly than they otherwise would, so that the asymmetry is rather less marked than he would suppose. You are not starting out with a zero inflation. You are starting out in a world in which you already had a 6 or 7 or more percent inflation built-in. The question is, if some prices rise more rapidly, isn’t it perfectly possible for other prices to rise less rapidly?

Second, we’ve seen in farm prices in the past few months that declining prices are not completely ruled out of our society. I think it is easy to exaggerate the asymmetry in commodity
markets. There is a strong asymmetry in the labor market, but I believe it is easy to exaggerate how much of an asymmetry there is in the product and service markets.

EDWARD HYMSON, Department of Economics, George Mason University: Dr. Walker, I’m curious to know whether you would support the limited notion of indexing only the federal income tax if the change in the tax brackets were announced in November, and if Congress were then given one month to specifically lower them again by legislation rather than is currently done, giving them the opportunity to raise them to adjust for inflation, if they should, by some stretch of the imagination, choose to do so?

DR. WALKER: I have two comments on that. First, I’m not all that much attracted to those sorts of gimmicks, with Congress having the right to say this or that after thirty days, sixty days, ninety days, and so forth. I believe fundamentally in the legislative process. I think it works pretty well, and works, basically, according to the will of the people. The people wanted price controls in 1971; they got them. They wanted a price freeze in 1973; and they got it. They were wrong, at least in the second instance, but democracy, that was the name of the game.

Second, I would not support indexing the personal income tax. We gave great attention to that question, at the urging of Professor Friedman, before I left the Treasury in January 1973. In some respects I would be less opposed to that than to other indexing, but still, fundamentally, I’m opposed—for two reasons.

One, unless you change the form, the man with a million dollar income will get the same percentage adjustment as the man in the 14 percent bracket, in terms of cost of living. And I do not believe he should. Professor Friedman tossed this off a while ago in terms of deficiencies of the index.

PROFESSOR FRIEDMAN: But he doesn’t.

PROFESSOR GORDON: He doesn’t.

PROFESSOR FRIEDMAN: He doesn’t, because the man in the top bracket isn’t affected at all because the top bracket—

DR. WALKER: Well, the middle bracket, or next to the top bracket, or somewhere in between.

PROFESSOR FRIEDMAN: No, but the size of the effect is greatest at the bottom and, in general, gets lower as you go up.

DR. WALKER: Size, relative to what?

PROFESSOR GORDON: You are indexing a $750 exemption. That $750 is trivial at—

DR. WALKER: But aren’t you indexing the bands too?

PROFESSOR FRIEDMAN: Yes. But because of the fact that you’ve got a graduated rate and a top rate, increasing the band from 500 thousand to a million dollars for somebody who is at ten million hardly affects him at all.
DR. WALKER: All right. I agree for the top bracket, but not in between.

MS. SHANAHAN: I think you’ll find, if you look at those tax brackets, that the steep climb is at rates that are now not a whole lot above middle income.

PROFESSOR FRIEDMAN: Exactly. I’ve got the tax brackets right here to confirm it.
[Laughter.]

DR. WALKER: Well, the steepest rate, obviously, is between zero and the lowest rate of 14 percent.

PROFESSOR FRIEDMAN: Exactly.

DR. WALKER: There is no question about that.

The other reason why I oppose indexing the personal income tax is this: Professor Friedman said in his article in *Fortune* that, even though one doesn’t agree with his monetarist approach, even if one takes a fiscalist or other approach, his basic argument still applies.

The point is that, to the extent that you index the personal income tax system, you will reduce the “stabilization effect” of higher tax revenues that occur because of the increases in taxes paid as a result of inflation. This is sort of a built-in factor against this “pernicious” government we’ve got.

PROFESSOR FRIEDMAN: But it isn’t. That was exactly the argument of the Treasury in 1952, and it just isn’t so. The reason it isn’t so is because the counterpart to that is that, as inflation increases the revenue, it encourages more spending.

PROFESSOR GORDON: That’s the whole point.

PROFESSOR FRIEDMAN: The argument that this is a built-in stabilizer implicitly assumes that expenditure is somehow independent of how much the tax system raises.

DR. WALKER: And therefore the government limits its spending every year to the amount of tax revenue, right?

PROFESSOR FRIEDMAN: Plus some more.

DR. WALKER: Yes, plus some more.

PROFESSOR FRIEDMAN: Absolutely,

DR. WALKER: And I have not in my experience seen that the level of tax revenue has had all that amount of influence on government spending over the past twenty years.

PROFESSOR FRIEDMAN: Well, all I can say to you is that you find it very hard to read a table.
[Laughter.]

DR. WALKER: Well, look at the deficits over the past—
PROFESSOR FRIEDMAN: Exactly, and why weren’t those deficits ten times as large? Why weren’t they one-quarter as large? How is it?

DR. WALKER: That’s Catch-22—for crying out loud.

PROFESSOR FRIEDMAN: Not at all. Not at all. The fact is that government spending has increased pretty much in line with government tax receipts. The amount of the deficit has gone up gradually over time.

But there is no sign whatsoever that expenditures have been determined independently of what the tax system can raise. And of course it is obvious that that’s the case, if you look at the way the political mechanism works—something of which you know far more than I do, Charlie.

DR. WALKER: I don’t know quite how to take that. [Laughter.]

MS. SHANAHAN: If we don’t have another ready questioner, I have another question.

Those who oppose indexing worry about accumulation on the up-side. But with a little reluctance both Dr. Walker and Dr. Fellner seem to think that it would have a lot of benefits on the down-side. Query—

DR. FELLNER: Not even with reluctance.

MS. SHANAHAN: In your case, right. Why is it that you don’t fear accumulation on the down-side?

DR. FELLNER: Well, it would be accumulation of price movements and not of a contraction of output.

MS. SHANAHAN: Why not?

DR. FELLNER: Well, let’s begin this way. I do think that you first have to get a price deceleration effect from somewhere and that would, indeed, be monetary and fiscal restraint, just to—

MS. SHANAHAN: To start it.

DR. FELLNER: To start it. But once it is started, you would get deceleration of wage increases, feedback on price increases.

Well, to put it perhaps a little more abstractly, the real wage rates would behave differently and would make it possible to maintain employment.

PROFESSSSOR GORDON: All you’re doing is, you’re simply speeding up the wage price spiral in the downward direction.

DR. FELLNER: I agree.
PROFESSOR GORDON: This first instance that gets the thing started is very simple. Let’s say we have a restrictive monetary policy, and there is a decline in housing starts. Then the price of plywood would fall. The price of plywood will go into the consumer price index and, if we have totally indexed wages, this will begin to slow down the increase in wages, and the process will start. It will be much faster than the very delayed process we have now.

DR. FELLNER: Now it is true, however, that in two of the four recent postwar recessions, the first deceleration of the consumer price index came with a considerable lag after monetary fiscal restraints.

PROFESSOR GORDON: There is no denying there are lags, and not all of them will be eliminated by this—

DR. FELLNER: The first time the CPI started decelerating after monetary fiscal restraints was after the recession in two of the four most recent cases. Now, one needs to add to this that spotting deceleration, a peak, is of course a somewhat arbitrary procedure. It depends on over what periods you define these past changes and so forth. But I think that any reasonable reading of. those data would show that in two of four postwar recessions, the deceleration started after a recession—after the recession was—

PROFESSOR GORDON: If we look at the most recent incident, the problem is very clear. Before price controls were put on in August 1971 and turned the lights out on any uncontaminated data, what did we see? We saw the beginning of a gradual decline in the rate of price increases, and no response at all on the part of wages.

DR. FELLNER: That’s why I say—

PROFESSOR GORDON: Now, what indexing would do is very clear from that episode.

DR. FELLNER: Yes.

PROFESSOR GORDON: The decline in the growth of prices would have fed through much more quickly to wages, and we would not have had as protracted an episode as would have occurred without the imposition of controls.

DR. FELLNER: Yes, and that is not one of the two recessions to which I was referring.

PROFESSOR GORDON: Those 1950 recessions may no longer be relevant.

PROFESSOR FRIEDMAN: No supporter of indexing should oversell his case. Indexing is not a panacea for inflation. It is a pain killer. It is a way of reducing the cost of ending inflation. But I agree completely with what Dr. Fellner says. We must have monetary and fiscal restraint to slow down inflation, and monetary and fiscal restraint must involve a temporary slowdown in the economy and cause temporary difficulties. There is no way out of it.

But the problem is how do you limit those withdrawal pains and make them as small as possible? I do not, myself, believe there is any long-run trade-off between inflation and output or employment.
DR. FELLNER: Nor do I.

PROFESSOR FRIEDMAN: I think, quite probably, we’re all in agreement—there may be some disagreement on that.

But there is no doubt that there is a short-run effect, because it takes time for people to adjust, and one purpose of indexing is to ease the pain of this short-term adjustment.

Now somebody asked this question before (and we never answered): if indexing would ease the short-term pain, why don’t you want to keep it permanently? I don’t object to keeping it permanently. I definitely want to keep it on the government permanently. But I predict, as a matter of experience, that if you had a fairly long continued period of 2 or 3 percent inflation, private escalator contracts would disappear simply because private people would find it too much of a nuisance and too costly to maintain them. I’m not particularly recommending that. Rather, I’m predicting that it is what would, in fact, happen.

PROFESSOR GORDON: One of the amazing things is that in the whole period of the last twenty years, there has been only one major case of escalation clauses being dropped. It was back in 1961, when inflation was slow, and the steelworkers dropped their escalation clauses but later put them back on.

By and large, the surprising thing has been how few are the unions, and how small the number of groups of workers who are now in the midst of this raging inflation, benefiting from escalation clauses.

WALTER SALANT, The Brookings Institution: If escalation clauses were dropped in 1961, I presume that was because the cost of living stopped going up. But your proposal, and your objective of making the decline work out better from a point of view of real output and helping wages to go down when the consumer price index goes down, requires that wage escalation be kept when the consumer price level goes down. Yet the experience you’ve just cited suggests that it will be dropped then; that it’s only accepted by unions as a protection against price increases.

If you’re not going to require it by the government, then you have to get both parties to the private bargain to accept it. And I don’t see how you can reconcile your position with the fact that you’ve just cited.

PROFESSOR GORDON: There are two parties to every labor contract. There are businessmen, and there are workers. When we have a period of accelerating inflation, and escalation clauses are built into the contracts, obviously businessmen are going to want to get out of it, and the labor unions are going to want to keep it. On the down side, businessmen are going to love it, and the labor unions are going to want to get out.

Now that would be a matter of negotiation. I don’t see any way of predicting, before the fact, which way it is going to work out. But your conclusion, in advance of any kind of argument, assumes that the union is the more powerful party to the bargain, and that the union will be able to dictate to the firm that the escalation clause must end the moment the price index starts to fall.
DR. SALANT: Well, using your sample of one case, it—

PROFESSOR FRIEDMAN: But it is just one case.

I might note, as a matter of historical interest, that the argument that I was citing earlier of Alfred Marshall in favor of indexation came not during a period of inflation, but during a period of deflation. He was arguing for it primarily as a way of reducing the harm done in Britain—this was in Britain in 1886—from the deflation that was then going on. So that I think that the argument does work both ways; that indexation has great virtues in any situation where there are unanticipated changes in degree, either up or down.

I believe—contrary, to some extent, to what Bob Gordon just said—that there is a common interest of employers and employees on both sides of the picture; that an employer has an interest in having an escalator clause during an inflation as a way of avoiding growing discontent among his workers, which would cause a very serious labor disruption at the termination of a contract, and that the union and the workers have a great incentive to have an escalator clause during a decline in prices as a way of avoiding the unemployment, which would otherwise be caused by rigid wages if there were no adjustment.

So I think there really is a concordance of interest, and I wouldn’t take this one case as a typical example.

PROFESSOR GORDON: And I think that’s a nice way of summarizing one of the basic arguments for indexing.

If we talk about what the small man, the ordinary person, has to gain from this, actually he gains on both sides. He gains on the way up because the harm done by an inflationary surprise, as in the case of oil, is not going to be as great, and he gains on the way down because the recession is not going to be as long and the layoffs and the unemployment are not going to be as bad. So, in this sense, indexing is a way of stabilizing the economy and reducing the impact on the ordinary person of these surprises that we are not going to be able to prevent.

DR. WALKER: If he gains every which way, who loses?

PROFESSOR GORDON: No one.

DR. WALKER: That’s the best game in town.

PROFESSOR FRIEDMAN: That’s what the free market is, isn’t it—the game under which everybody gains?

DR. WALKER: Not in the sense of the wage bargain, the way Dr. Gordon described it. I’d agree more with him than I would with you, because what you described as the self-interest of the worker was a self-interest that I’m not sure the worker would accept. Some degree of unemployment might involve a very low percentage of union workers, and they may be much more interested in keeping wage rates up than they are in preventing unemployment from rising one or two points.
DR. FELLNER: I want to ask Dr. Gordon the obvious question. What sort of wage bargaining process would have led to the voluntary acceptance of those real wage changes which were available in the midst of the oil crisis?

PROFESSOR GORDON: The workers got a bad deal, and—

DR. FELLNER: But do you think you could have agreed with them on a declining real wage rate?

PROFESSOR GORDON: What we have now is a situation in which the ordinary working person has experienced an unprecedented decline in his real income in the last year.

DR. FELLNER: Yes.

PROFESSOR GORDON: And he is going to make it up by demanding unusually large increases in his wages over the next year. He has had a decline, and now he is going to have an increase, and we’ll be back to where we started.

DR. FELLNER: He will demand the oil that wasn’t here? That’s what you are really saying.

Well that will never lead to an equilibrium of any sort if he insists on that.

DR. WALKER: He’ll demand more money income—

MS. SHANAHAN: I think maybe the time has come to record that most unsatisfactory of all conclusions—that we have agreed to disagree. [Laughter.]

PROFESSOR FRIEDMAN: No. we’ve agreed to agree. [Laughter.] Don’t underestimate the amount of agreement there is.

MS. SHANAHAN: I agree with that. [Laughter.]

DR. FELLNER: That’s quite true.

DR. WALKER: But don’t overestimate the amount of agreement. [Laughter.]

MS. SHANAHAN: I agree with that too.

DR. FELLNER: And don’t underestimate the inspiration we got from Milton Friedman. [Laughter.]

MS. SHANAHAN: I for one certainly feel wiser than I was when I walked in here.

On behalf of the American Enterprise Institute, I wish to thank our truly distinguished panel, Dr. Milton Friedman of the University of Chicago, Dr. William Fellner of the President’s Council of Economic Advisers, Dr. Charles E. Walker, formerly of the Treasury and now a private economic consultant, and Dr. Robert Gordon of Northwestern University. [Applause.]