

The Economic Club of New York

67th Year

The Honorable Robert Bourassa
Prime Minister of Quebec

The Honorable Alan Greenspan
President, Townsend Greenspan & Company

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Questioners: Alphonse De Rosso
Exxon Corporation

H. Erich Heinemann
New York Times

Introduction

Chairman George R. Vila

I want to welcome you to the 2nd meeting of the Economic Club of New York, of our 1972, '73 meeting. Now when I got my first job, some 150 years ago, my boss, the big boss called me into his office, now, the big boss was the guy that my immediate boss was working for and he said, young fella, I want to tell you three things. And I said, what's that. So he said, number one, I want you to come into work every morning, shaved and a clean shirt, and I don't give a damn what time you get in at night, I was single of course in those days. He said, I want you to be here on time. He said, number two, whatever your boss asks you to do I want you to do it, give that the top priority. And he said, number three, you pull a boner or anything goes wrong, you go tell your boss about it before somebody else does. Now I want to advise you folks here tonight, that I was introduced as an Ambassador tonight, and I want to disclaim that because I am not an Ambassador and I have no intention or no qualification to be one. Now, social peace cannot be maintained in Quebec unless economic growth is accelerated.

Our first speaker this evening must be rather proud of these words that he pronounced some time ago. As the economic growth of Quebec accelerates under his leadership, we find this beautiful province once again peaceful, though far from stagnant. Since his election of May 1970, on a ticket pledged to support federalism, the Prime Minister of the Province of Quebec has done an outstanding job in winning the confidence of the international business community, while at the

same time promoting the welfare of his constituency. He is a talented man. He is a scholar trained in law, in political and economic science and in public finance, a former student of Montreal, Oxford and Harvard Universities. He is a liberal with a capital L, which means totalitarian up in Quebec, (laughter) lest you be misled, sensitive to social problems, a pragmatist who understands a language of business as well as that of politics. He is less than 40, and 39 for the last three years they tell me (laughter). Many years and many opportunities of serving society lying before him. Gentlemen, it is my very real privilege to present to you the Honorable Robert Bourassa, the man to committing la belle province to become the rich province as well.

(Applause)

The Honorable Robert Bourassa

Prime Minister of Quebec

Mr. Chairman, distinguished guests, ladies and gentlemen. Of course it gives me great pleasure to be here this evening to share with you some ideas on the present and future of Quebec, about the plans of my government, and the hopes and aspiration of the people of Quebec. 1972 was the year marked by renewed confidence and a future of our province. Workers and businessmen, the rest of Canada and abroad are showing a new optimism as a result of our improved social climate. We organized public finances and government initiatives designed to insure rapid economic progress.

As you all know, and as it was warmly mentioned, our top priority is the economic growth. And I can quote a lot of figures to show that there is real economic growth this year in our province. But we must step-up our action to guide that growth and to hide technology sectors and industrial sectors where our economy has been weaker. We must keep this long-term goal while continuing in the short run to generate employment for our labor force of which nearly half are under 24 years old. To achieve this, and in order to coordinate the different roles of government agencies in the economy, we have created an Interministerial Economic Affairs Committee and also many other tools, like the Quebec Industrial Development Corporation, to have a more fruitful collaboration with the business community. Governments, which have to intervene more and more to ensure citizen demand, require the cooperation and often the participation of the people and organizations affected by these programs.

The business world accordingly recognized that it has a responsibility in the solution of these problems. Not only it is going to be in the general good, but also it is going to be in its own interest. The state cannot do everything alone and must operate with the assistance of the private sector. But the state itself must also be a modern instrument of public administration.

Quebec public administration enjoyed a very great phenomenal growth during the 60's. It was a period where improvisation and the expedience of the moment at times, overrode administrative effectiveness. When we came to power three years ago it was high time that someone should roll up its sleeves and proceed with the governmental cleanup that seemed imperative. For good

government means that the functioning of the administration be smoothed out and to achieve that, all its mechanisms must be known perfectly.

In the Civil Service, it is also an accessory that less importance be given to job security. This must be replaced by appropriate remediation, corresponding to extremely rigid selection criteria to fill position competently and with more flexibility. Top Civil Servants should not do the same work for many years. Rather it seems desirable that to the extent that they are real administrators they may be permitted to exercise their competence and revive their creative imaginations in different fields in cycles of three to five years for example. The new system of goal oriented controls that we are implementing also gives departments and agencies a greater freedom to manage their own affairs through delegations of authority. To plan and to carry out operation within the budgets approved for them. In planning their financial management systems, departments and agencies are given the authority needed to match the responsibility allocated to every level of management.

What we are seeing is that even in public enterprise, we have the responsibility of presenting to the people, through the government, the cost/benefit relationship between resources spent and benefits obtained and it is this relationship which will serve as the basis for decision. All of this does not imply that the consideration of political and cultural factors will be absent from decision making. But it does imply that the full force of economic considerations will be brought to bear on government programs. Quebec believes strongly in consideration, believes strongly in the

federal system. It is obviously the best system for its aspirations; giving us cultural autonomy or serenity and a good working economic federal system.

Why should we break the federal link when we see for instance what is happening, in a common market, where countries for obvious economic reasons, like a common currency, realize that one day or another they will have to have direct representation? Why we should break that link, when it is obvious that we will have to reestablish that link because we have even here in Canada stronger economic reasons to have a federal parliament. Obviously we can have a new sharing of powers taking into account that we are a vast country but we need obviously for economic reasons, which everybody will agree, that federal parliament.

The results of the last federal elections can be interpreted as a sign of resurgence of regionalism in Canada. In that view, the population sees the central government as one more distant from the reality of everyday life. Busy as it is with the wide national and international problems. The Canadian Federal System must thus, respond as soon as possible to the aspirations of Canadians from all regions. But we must not only consider Canada, we must also look to the North American community. In the last year and a half, this special relationship between Canada and the United States, which was always very strong, appears to be changing.

On the one hand Canadian nationalists worry about economic domination of the United States over Canada. On the other hand, the trend is to a rapid world-wide expansion of American

multinational cooperation. Again, I believe that the European common market can take the lead and bring us answers to these questions and making us realize that unless everybody grows, nobody grows.

Canada being a relatively small nation in terms of population and markets needs to have a broad international economic outlook. To achieve its economic goals, Quebec will thus have to seek out new economic goals within the North American community. I did not tell you that this approach is hardly unique. To quote your own countrymen, Peter Drucker, the old world has become one economy in its expectations and its responses. Professor Drucker also points out that today's global economy was achieved by business rather than by government. Business which cut across national borders. I recently returned from a conference in England. During these meetings and in meetings I had in the last two years in Belgium, Germany, France, and Italy, I was struck again and again by the many parallels and strong similarities between the EEC and the de facto economic community that has come into existence in North America. Although political economies must be maintained, the existence of a transnational economic community, that transcends national and provincial borders, is nevertheless a reality that we must use to our greatest advantage.

For instance, in the near future, we expect to build a year-around deep water port in the lower St. Lawrence River. This super port will be able to accommodate 300,000 ton tankers. Bring in crude oil from the wells in the Middle East as well as from South America. The crude will then

be transshipped to Montreal to what is already Canada's biggest refinery complex. For refining at the initial rate of one-half million barrels daily.

The finished product will thus be available to users in Canada and in the United States at substantial savings. It is obvious that business is the major driving force in this era of international economic relationship. No government can by itself achieve this. What government can do, however, is to adopt policies which will help create a climate in which industry will prosper and grow. We have tailored our economic growth actions to what we conceive to be the present and future needs of the North American economic community. We can use public spending as a lever establishing policies that encourage investment in the types of industries we want to attract. All of this can be done without sacrificing our respective sovereignty.

International business has the capacity of good citizenship. We have the capacity to accept it in our community as a partner in our process.

Looking towards the future, perhaps the best example of this type of growth, prospect lies in the sector of energy. You know of course that Quebec has made itself a world leader in the growth of electric power resources, but what is more to the point, is that Quebec would have an abundance of low-cost electrical power well into the 80's and we expect that this will have a tremendous affect on our capacity to attract secondary industry. While the James Bay Project, the world's largest hydroelectric complex, is being undertaken primarily to satisfy the future power needs of industry in Quebec, it will have significant secondary affects on our economy. The

development of this sector will enable us to maintain our leadership in the resources industries. Even if we go about increasing our industrial capacities.

Also, we are looking at the possibility of supplementing Quebec's oil refining operations with gas from the eastern Canadian arctic. At the present time, proven reserves of 15 trillion cubic feet have been found in the far north. And it seems probable that 25 trillion cubic feet or more will be discovered. It thus seems that the construction of a gas pipeline will be undertaken within the next three years. Quebec will be in a unique position to benefit from this project. A gas pipeline along the eastern shore of Hudson Bay will be 400 miles shorter than one erected along the alternative route on its western shore. And soil condition in our province are more favorable for construction. Furthermore, the development of the James Bay Project also favors this possibility. Northern Quebec is thus our opportunity to build today with the vision for tomorrow.

Looking at tomorrow, one of the most crucial problems is the need to streamline and make more efficient our transportation. Especially in the field of aviation, with their present problems. In order to plan for future passenger and cargo traffic, construction is underway at the Mirabel Jetport about 30 miles northwest of Montreal. When completed, in 1975, this giant facility which by way of comparison will be six times the size of the new Dallas Fort Worth airport which advertises itself as being as big as Manhattan Island. It will become an international distribution and transportation center. It will accommodate effectively, sub and supersonic jets. It will be equipped with the most modern materials, handling equipment for containers and air freight.

With more and more cargo being shipped by air, we expect the facilities at Mirabel to serve as a transshipment center for the North American industrial centers.

At the same time, because short-run transport also needs to be more efficient, we are currently working on a short takeoff and landing aircraft capable of using a 2000 foot runway. This system will soon be tested and used between Montreal and Ottawa. Activities such as these can be dependent on to build a solid future for Quebec. But we have not forgotten our duties to deal with the general good and the welfare of future generations.

One of the problems which we in North America will have to face in the long-term is the concern with the positive and negative aspects of growth. Some studies have been done recently on this subject, and although I admit that Quebec is now more concerned with more pressing problems, such as the creation of jobs and short-term economic growth, we will have to consider in a rather near future the rational of growth, particularly in terms of population increase and resource exploitation. We must evidently manage and guide our society in a planned and rational way. We must ask ourselves for instance whether our economic system is capable of the uninterrupted upward movement required to support the continued satisfaction of all our expanding needs and goals. But while it is true that growth and material wealth is not necessarily synonymous with the ultimate and human or social contentment. We should be on guard against those who disparage economic growth as being either of little account or downright prejudicial to the human condition.

Nations which opt for economic stagnation are unlikely to be either exciting or attractive places in which to live. The debate on growth need not be one against growth, but rather an exploration of causes and effects, a testing of the limits of our growth, and an investigation into the nature of future development patterns.

The visions we have for tomorrow, must not make us forget realities as they exist today. For the great danger governments or for that matter, individuals and corporations, face when they get involved in some aspect of long-term planning, is forgetting the problems of today. You cannot achieve the one without first solving the other. But one should not labor under the illusion that one cannot have both a short and a long-term view. The great difficulty, whether pressure comes from shareholders or electors, lies in the conciliation of solution and objectives. And watching the step-by-step process, while keeping an eye on the long-term.

In conclusion, you see that Quebec today, has changed in many ways from the traditional society of yesterday. Quebec has become a pluralist society; open to the great currents of opinion which are steering up our modern world. Our government is thus firmly turned towards the future, for we are among the privileged societies of the world. We are situated at the heart of what is technically the most advanced continent. A continent whose exuberance is extraordinary. We now have a very high level of competence in technical effectiveness, which will enable us to overcome the challenges of today. This meeting of American technique and French culture which is taking place in our province gives us an opportunity which we will not miss to build a

modern, original and dynamic society. A society which is today ready for the challenges of tomorrow. Thank you. (Applause)

Chairman George R. Vila: Thank you Mr. Prime Minister for that very thoughtful talk and I am sure that you have made all of us in this room feel a resurgence of confidence in the relationship between our two countries in the opportunities for economic collaboration to our mutual benefit.

Our second speaker this evening, like Merrill Lynch is bullish on America, and he does not hedge in his forecast for 1973. His predictions for the Gross National Product, unemployment, inflation, real growth, business investment and profits are all published for the record in the January 8th issue of *Time Magazine* which I believe most of us have read. And the *New York Times* annual economic review quotes him as saying, “It is very rare that you can be as unqualifiedly bullish as you can now”. Now those of us in this room struggling with low price earnings ratios might take heart from what he has to say. (Laughter) He is a man whose words carry a lot of weight. He has been a close advisor to President Nixon and has served in a consulting capacity to many government agencies since 1967. His influence has been, and remains; particularly great because he is a practical economist and a political realist and you will recall that our Prime Minister who we just heard from was a practical politician and an economic realist. So the combination seems to work.

He has helped government officials temper their politics with sound economics and we all know

that is a big order. Of course, these are mere extracurricular activities, his many concerns, as many of you know, is acting as a consultant to large corporations. I present to you, Mr. Alan Greenspan, President of Townsend Greenspan and Company. (Applause)

The Honorable Alan Greenspan

President, Townsend Greenspan and Company

Thank you very much Mr. Chairman. I am delighted that the stock market is closed tomorrow, so no one can contribute anything I say this evening to what happens then. (Laughter) It is certainly a pleasure to share the platform this evening with Prime Minister Bourassa. While I will focus my attention on U.S. economic policy generally, all of my Canadian friends know that for better or worse. What happens here is obviously not irrelevant to their fate.

Although the degree of Phase II's success in suppressing price and wage increases is a matter of dispute, there can be little doubt that controls have rested rather lightly on the economy at least to date and their distorting affects have accordingly been minimal. In fact, most companies, until very recently, have had considerable difficulty obtaining prices in the marketplace to which they were legally entitled by the ceilings. As recently as last fall the gap between term limit pricing agreement ceilings for example and price realizations was close to a full percentage point. Profit margin controls were beginning to pinch toward the end of Phase II, but problems were still localized. Hence, with the exception of a few well publicized cases notably passenger cars,

plywood, fuel oil, and so forth, surprisingly few marketing or pricing policies were significantly affected by Phase II.

On the wage side a number of exceptionally large union agreements were obviously pared but in the nonunion area where three-fourths of the work force resides, predominant wage increases were falling, not at the 5 ½% guideline, but well under 5%. More than half of first year non-union wage agreements approved by the pay board were for less than 5% and a fifth were for less than 3%. While some will argue that the very existence of the pay guidelines enabled companies to hold down wage increases, there can be little doubt that it was the same dis-inflationary forces which suppressed price increases which engendered the marked receding of wage pressures.

In recent months, however, distortions have begun to proliferate and it is becoming fairly clear that the continuation of the Phase II structure, much longer, would have led very shortly to gross imbalances and inequities. Moreover, the almost certain welling up of inflationary pressures under a rigid control program would soon have overwhelmed the mechanism and left it a shambles.

The difficulties started with the acceleration in economic activity during the late fall of last year. As lead times on deliveries of materials began to stretch out, purchasing agents, as they typically do, began to try to rebuild inventories fairly quickly to protect their supplied positions. And as a result, price realizations began to close the gap on both list prices and the TLP ceilings. In

addition, the heavy industrial equipment markets, those most closely associated with capacity expansion, finally began to exhibit some quickening in demand after being exceptionally lethargic for a very long period.

Accordingly, the pace of the recovery which have been surprisingly unimpressive for over a year, turned late last fall dramatically towards a more typical durable goods oriented industrial recovery. In this demand-pull type of environment, few economists would give much probability of success to the suppression of inflationary pressures. However, it should be emphasized that what we are observing currently, and probably will be observing for the next year, is not a resurgence of inflationary pressures in the longer run sense, rather it is a purely cyclical phase of price and wage pressure, superimposed on what may well turn out to be a more fundamental disinflationary trend. However, I will get to this problem a little later. We are looking at a very interesting set of various forms of inflationary cycles, superimposed upon each other. And at the moment what we have is sort of an intermediate trend going down into 1974 and '75, but, for 1973 the pressures look very significant as though we are sort of building a little bulge on that downtrend and that is what we are confronted with at the moment.

There are basically two key elements which are in a sense part of the Phase III program and these promise, if successful, to return us to a set of balanced product and labor markets some time in 1974 and that period should last probably through 1975, possibly 1976 but I will get to that a little later.

The first is the administrations impressive initiatives to bring federal spending under control. The second is the most recent addition to the Phase III program, the remarkable change in agricultural policy. The extraordinary efforts to increase production will inevitably impact on food supplies, and of necessity their prices. So while I envisage continued unacceptably large increases in food prices, for the period ahead, I also expect food prices to be heading downward some time in 1974 if not earlier.

Consequently, if we look beyond the cyclical wage price pressures of the next 9 to 15 months, this sort of long-term disinflation we are looking at, the one that is going into 1975, gives us every reason to believe that the more virulent elements in the inflation picture will have been largely dissipated by the end of this year or some time in 1974.

While there were many considerations governing the fashioning of Phase III, one purpose which I discerned was it will certainly allow a far more flexible response to rapidly changing economic events, than would the Phase II structure. Unfortunately, it is by no means obvious that the Congress will be willing to hold still long enough to allow the adjustment process to take place. The political time-frame considered acceptable for governmental policies to work out has been shrinking for years. The Congress could conceivably become unduly impatient with processes that take in their view, and inordinately long time to resolve.

As a consequence there may be considerable pressure to tighten the controls or impose, for

example, interest rate ceilings. These would be essentially unenforceable but could aggravate the underlying inflationary trend, the short-term trend, should they be attempted. Or of even greater concern, would be any actions undermining the administrations attempt to bring the federal budget under control. One can safely conclude that the road traveled by Phase III will be a lot rockier than that traversed by Phase II. Policies will be more difficult to implement and certainly more controversial.

I have no doubt that as a result; the support for Phase III will probably erode as these short-term cyclical forces accelerate. And one critical problem which of course I think most people are much aware of, is the pending wage negotiations for the Teamsters, auto, electrical, rubber workers amongst others, scheduled for this year. It is going to be difficult to envisage any of the major contracts coming in at a 5.5% rate, the current guidelines. But the grave concern I often hear expressed that these contracts could turn out to be frighteningly high, has little justification. The big contracts of 1970 and 1971 resulted largely from unions caught with long-term contracts in 1967 and 1968 prior to the inflationary escalation in prices and wages.

The 1970, 1971 agreements necessarily reflected the catchup's required to restore the historic relationships with other industries. However, the contracts which will be renegotiated this year, were exceptionally generous when signed mainly in 1970. On average, those agreements including subsequent cost of living increases, averaged, 9.1% per year, 7.4% for manufacturing agreements, and 10.8% for non-manufacturing. As a result, there is very little catching up

required in this year's bargaining. As a consequence I look for wage increases within tolerable limits of the 5.5% guideline. Somewhere maybe a percentage point or so higher than that.

With fringes I would guess that we are looking at something in the area of about 7%. I will acknowledge however that numbers much above say 8% on average, and maybe 8.5 or 9% possibly with fringes in it, accommodated by expansionary monetary policy, would disturb my view that inflation should be significantly simmering down next year. If the problems of reaching moderate wage settlements run into difficulty because of the heavy front-loading of the typical industrial contracts, agreement on a one-year contract may be possible to get us through the cyclical bulge of 1973. Standard front-loaded contracts which for example might call for 10% the first year and 5.5% in the second and third year, for an average of 7% for the three year period, might be negotiated at 7% for the one year contract, rather than the 10% figure. A renegotiation next year should be in a far more favorable environment, for non-inflationary bargaining than certainly this year is.

I am willing to assume, however, that it is....and it is probably the most reasonable assumption that one could make at this point, that in one way or another we will work our way into the spring of 1974 with inflation rates having peaked and on their way down. At that point, the Cost of Living Council should become largely inactive. While I doubt that we will return to the pre-August '71 degree of government involvement, hopefully Phase IV will at least approximate it.

But, what about the period beyond that. Another words, even if in 1974 and 1975 we have come off this big post-Vietnam War inflation and everything is in re-balance, can we look forward to a stabilized long-term period of non-inflationary rates. Was the inflationary experience of the past several years an aberration triggered by the war, and hence a nonrecurring episode. Or has an inflationary bias developed in the economy, which if not reversed will confront us with chronic bouts of inflation, controls, and instability in the later years of this decade and into the 1980's. I fear that the latter best describes our situation. The combination of the increasing commitment to full employment and the burgeoning federal programs of the 1960's have added an inflation bias to the economy which will be difficult to diffuse. More specifically we can isolate two major trends which have imparted this secular bias.

The first is the acceleration in federal expenditures, which currently show signs of being gradually brought under control. The second is the shift in the balance of bargaining power between labor and management in favor of labor. I find it difficult to believe that this trend will be reversed. But I trust that an awareness of its economic costs will at least temper further moves in this direction. I hope that as a consequence, while we will still have some difficulties with inflation, that the improvement that I envisage for next year and 1975 will basically be what we will see thereafter. Perhaps we will have to be confronted with something higher than I see, next year, but at least I have considerable hopes that the really virulent type of inflation we have been looking at since the late 1960's is a thing of the past. But we do have problems and we do have things which are going to have to be resolved.

Another increasing share of the nation's output has come under the direct or indirect control of the federal government. While this need not in itself be inflationary, such trends have invariably led, both here and abroad, to chronic budget deficits. In order to prevent the financing of such deficits from driving up interest rates, the monetary authorities have tended to expand the money supply inordinately. This in turn has been the major factor in past demand pull inflation episodes. It is folly to imagine that monetary policy can somehow hold the line on inflation in the face of heavy deficit spending.

I am surprised, but delighted at the success to date of the Nixon administration attempt to reign in the growth in federal spending and support a far broader sense of fiscal responsibility than we have experienced in the past decade. It is safe to predict that the budget which is due to go to the Congress in a few days, will engender a colossal uproar. As I read it, the budget process this time has been most even-handed. Almost every program is getting clobbered. (Laughter)

Accordingly, hordes of Congressmen will doubtless feel the political necessity of denouncing any cuts in their favorite programs. This is especially understandable when we realize that the federal budget has become a vehicle through which our politicians woo the voters with new programs or extensions of old ones.

The only difference between Democrats and Republicans on this issue has been that when Republicans engage in the practice, we, I am a Republican; we at least sometimes have the good

grace to feel guilty about it. (Laughter)

Nonetheless, I sense that the orgy of new programs and spending is over. Under the growing realization of the necessity of bringing the budget under control. This, however, will not diminish the confrontation between the administration and the Congress which is about to be joined. In fact, I sense that such a ritual may well be a precondition of the major change in policy which I believe is underway.

If I am correct in this view, and I do admit that there is a modicum of hope overlaying my analytical conviction, the major factor in the inflationary bias of the past decade will have been successfully diffused. The second, though somewhat less contributed to the inflation bias, has been the marked shift during the past five to ten years in the balance of bargaining power between labor and management. This has had the affect of increasing labor share of the national income and reducing the return to capital. This shift has occurred largely as a result of the marked increase in coverage and duration of unemployment insurance, welfare, and Social Security benefits. Changes in unemployment insurance have made unemployment a good deal less onerous than it was say a decade ago. The dramatic increase in welfare coverage has reduced the number of unskilled workers in the labor force, while increased Social Security benefits have enabled numbers of workers to retire earlier than would otherwise have been the case. In a growing number of instances, even strikers have been receiving unemployment insurance and welfare. The Long Island Railroad strike being the most notorious of recent examples.

The net effect these government programs has, by reducing the hardship of being on strike, being unemployed, or being out of the labor force, progressively lessened the urgency of seeking work at any wage available. The minimum wage, especially for teenagers, has also priced out of the market a number of unskilled, first-time job seekers who would be willing to add their supply to the overall market, were they not legally prevented from doing so.

All of these elements, other things equal, induced workers to offer progressively less work at the same wage or the same work at only progressively higher wage levels. Without going into the intricacies of the market adjustment process, it should be clear that part of the increased wages was passed on as higher prices and part created labor's increasing share of the national income.

Moreover, as labor share rises and that of capital falls, an ever greater part of the wage increase is...(Audio ends and starts again on next side)...the economic costs involved. Payment of unemployment insurance to workers on strike, and the teenage minimum wage are cases where I find the costs in the broader sense, clearly exceeding any measurable benefits. Hopefully these practices will disappear or at worst not spread. I fear, however, that the impact of such programs on the economy has not as yet been fully recognized.

We are already in a position where long-term profit potentials in many industries may be inadequate to attract the capital investment necessary to maintain the growth rates required for an improvement in our overall standards of living.

Accordingly, I am particularly concerned with the recent advocacy of making the federal government the employer of last resort as a beguiling solution for reducing unemployment.

There is little doubt that if such a program were to become extensive, the balance of bargaining power would shift still further in the direction of labor. Under such a system there would surely be a growing tendency towards the federal government becoming the employer of first resort.

Within a very short time, the effect of salary rate for federal, make work or welfare jobs, could be expected to become a politically visible number. It would then tend to be bit up by members of the Congress in the same way and for the same reasons that Social Security benefits have accelerated at such a rapid rate in recent years. Eventually the federal welfare wage would become the cutting edge of wage determined in the private market.

The foregoing analysis may appear somewhat abstract to many of you who perceive what appears to be growing union power at the bargaining table. However, it is an oversimplification to attribute the shift in the balance of income shares to some recent increase in the power of unions. Undoubtedly monopoly and quasi monopoly powers have increased for certain unions such as the Construction Trades and Municipal Workers. But these unions comprise a very small share of the workforce and I am unimpressed with the argument that they set a precedent for wages for the rest of the economy. No group for example has been able to match the extraordinary wage increases of the construction trades during the past decade. Desire is one thing, implementation is another.

However, it is certainly true that the social environment in which the unions are functioning has changed in the past decade. With the result that their ability to wield power is under less restraint, one cannot view the economy in isolation. It is...necessity reflects the values of the society. Regrettably reason and persuasion are not longer the virtues they once were. While power tactics whether practiced by student dissidents or municipal labor unions have been elevated to a state of respectability.

Nonetheless, union's ability to wield power reflects the more fundamental shift in the economics of the wage bargaining process. Hopefully the recent trends towards increasing the share of labor in the national product and its consequences to the viability of our economy will soon stabilize and perhaps even be reversed. When profit margins are low, wage increases tend to exert disproportionate upward pressure on prices. In fact, low margins reduce the response of the economy to dis-inflationary forces generally. In any event, if the pressure on profits is not significantly eased, it will make non-inflationary fiscal policy and hence monetary policy an even more important element in repressing the inflation bias from the wage side.

We must be particularly vigilant in holding the reign on federal expenditures since our political system has exhibited an ever increasing willingness to accept controls in lieu of a flexible economic adjustment process. I was particularly distressed by the support given controls by large segments of the business community. Most were obviously apprehensive because of what was happening to wages and profits. But I know of no way in which a wage price control mechanism

can ultimately redound to the benefit of business or for that matter anybody else.

The diffusing of the inflationary biases in our system requires a concerted attack on the underlying causes. Controls are not a substitute. At stake is the viability of our free enterprise system and more importantly, the political freedoms which are both required and fostered by it.

Thank you. (Applause)

Chairman George R. Vila: With the very thoughtful views you have expressed Alan, I am sure we all hope that you remain in your consulting capacity to the President and the economic advisors, the Treasury and the Federal Reserve Board and maybe the AFL/CIO if you can (laughter) corral them into your clientele.

QUESTION AND ANSWER PERIOD

CHAIRMAN GEORGE R. VILA: We now will proceed to the phase of the program where we have the questions by Erich Heinemann of the New York Times and Alphonse De Rosso of the Exxon Corporation. Everybody heard of the Exxon Corporation. What is a Uniroyal? Alright, who's the first questioner?

ALPHONSE DE ROSSO: I guess I will start it. Can you hear me? Mr. Prime Minister, as you well know, since you made a reference to it, the federal election results of last October which you reassuringly labeled as a resurgence of regionalism, caused both confusion and concern among American investors, especially as to future developments in Quebec, and in particular in relations with the federal government. A recent press comment, in this country, as if anything heightened our anxiety. For example, a reputable newspaper called the *New York Times*, indicated on January the 1st that the assessment is made that Canada has arrived at a new political crossroads. And that Quebec's future, of course, is in the control of those who live outside the province. My question is, in view of the present political complexion, will the divisions between Quebec and the federal government become deeper and less reconcilable?

PRIME MINISTER ROBERT BOURASSA: There are various ways to interpret the last election. Of course every year we talk about new crossroads, as you know, in politics. I would say that if we want to analyze the reasons for the results of the election, for me, I would say it is mainly economy. If we can remember, two weeks before the election, statistics went out concerning the unemployment and the rate of inflation. And they were very bad. Of course we can always discuss the way...the unemployed....our account in Canada, but still they were very bad for the government, and it came at the worst time for them, because the undecided vote switched to the other party, to the opposition parties. The linguistic question or the national question, I would say was only a relatively small factor compared with the economic reasons for the vote, except perhaps in certain regions like the Federal Capital for the bilingual policies

which were proposed by the Trudeau Government. But I would not interpret that as being increasing the danger let's say of the threatening of Canada being broken because of this election. There were bi-election in the Province of Quebec a few weeks before the federal election, which shows clearly, what this showed clearly that the separatist threat was much weaker than it was let's say a few years ago. In fact, they lost their deposit in both writing and in one writing they came as a low third. So I would say that is a rather pessimistic approach to conclude from the last federal election that the future of Canada is weaker. We had in the past, non-minority governments which were beneficial to some extent to the regions of all Canada and we are, I would say a natural for a federal system. We are a vast country, and we have different regional particularities in the old country. So if that minority government will increase the needs and the attentions to various regions of Canada, I think Canada will be strengthened rather than weakened by the last election. (Applause)

ALPHONSE DE ROSSO: You answered my second question, so I will go to my third. You have been making efforts personally in your government to attract foreign investment from Europe and the United States; meanwhile the federal government is planning to introduce measures of control over foreign investment, which I don't think are calculated to encourage the flow of investment into Canada. How do you plan to reconcile these divergent approaches in your continuing appeal to foreign investors?

PRIME MINISTER ROBERT BOURASSA: There is talk about limit of foreign investments

since many years, and of course, it is always easy to limit foreign investment. It is somewhat more difficult to create new jobs with local investment. Personally I was elected two years ago in saying that I will welcome foreign investment and partly I am here tonight for that. And there was a gallop poll, if we can rely on a gallop poll, but this does not surprise me which shows a few months ago that the Province of Quebec by far is the place which bodes welcome foreign investment and they even approve subsidies and capital investment if that improved the economy or if that creates some jobs. You might know that I was elected in saying that I will do my best to create 100,000 new jobs. I know that Governor Rockefeller created 1 million jobs here, since a few years ago, so that is a good goal for us. For the foreign investment law which is supposed to be proposed by the Federal Parliament, we will have to wait, when the law will be proposed to allow us proposed few weeks before the end of the session, amendments were accepted at that time. It was relatively acceptable to us. I don't know if there will be changes in the new law, but obviously when we have the rate of unemployment we have in the Province of Quebec, around 8%, I think we need foreign investment and in our case I can have that cultural protection because there is a French speaking majority. That is why, perhaps, this is one of the reasons why we are looking more for an investment than other parts of Canada. But I will have to make quite a fight if that new law will prevent investment in my province, and will constitute risk to increase unemployment. (Applause)

H. ERICH HEINEMANN: Good evening Sir, I hope the New York Times is a reputable newspaper. (Laughter) To start off I have a two-part question. First of all you have pinned a good

deal of your optimism about the intermediate term price outlook over the next couple of years, on to use your phrase, the longer-term basic dis-inflationary forces. However, you provided us with relatively few details of just what these forces are, other than the admittedly very important hope that the federal budget will be brought under control. Could you tell us, just exactly what you had in mind, both from the point of view of the average consumer as well as the average businessman, both of whom it seems to me have had a lot of discouraging price news to contend with recently.

THE HONORABLE ALAN GREENSPAN: The inflation outlook is an extremely complex thing in the sense that there are surprisingly number of discouraging number of cross currents going on simultaneously. First, I would say that the major inflationary pressures that we have had say for the period, the late 1960's into 1971 largely came from the Vietnam War, its financing and its aftermath. That, however, is over fortunately, and I think that the budget problem which had gotten terribly out of control as you know, now looks to me to be well on its way to solution. So that if you merely look at that basic fundamental force, you get this big upsurge and then this big down surge. Secondly, you get this exceptional change in agricultural policy, the type of change, which I believe probably could not have been implemented, except in a period such as this. And if I read the numbers correctly on what they are planning to do, there is an extraordinary increase in agricultural supplies in the feed grains area and the food grains, and hence, in meat, animals and the like. And I think we should be seeing food prices on their way down, perhaps fairly substantially in 1974. I use the 1974 period because as you know the timing of agricultural

patterns is often diffused and certainly it takes a long time to get from crops into meat, animals, and into food. So you can't expect food prices to go down for quite a while. I think in fact, in the short term it looks rather bleak as far as I can see. So that I think that if you take the context of just the next say two or three years, I think we have a discouraging period of short-term inflation, followed by some major improvements, coming from the simultaneous coming together of both budget control and major increases in agricultural supplies.

H. ERICH HEINEMANN: The second part of the question, you have already answered to some degree. But let me go ahead with the question I had already prepared. You placed these longer-term dis-inflationary forces within the context of a secular bias in the economy toward inflation. For a number of reasons that you cited in rather great detail. And which it seems to me are by and large operating in the economy, in the society today. To me, reading your prepared summary, this seemed to be a bit inconsistent and could you perhaps expand just a little further on that?

THE HONORABLE ALAN GREENSPAN: Unfortunately, the inconsistency is partly there because I don't know how to unwind it. There are disparate forces going and there are very difficult probabilities in trying to figure it out, but what has happened is that if you take a five and ten year context, which is very much longer term period, you have two forces working towards inflation which really ignited in the early 1960's; the budget getting out of control, and this major shift in the balance of power between labor and capital. The budget problem I see

being resolved in here. So we have one leg continuing up and I can't at the moment envisage any significant improvement in that. But, what I do hope is that with the budget under control and an awareness of the inflationary problems we are confronted with, it will be possible to live with this admittedly biased inflation element from the labor market side, live with it, without actually being involved with chronic inflation, of the type we have had.

ALPHONSE DE ROSSO: Mr. Prime Minister, you have the enviable record of not having raised taxes in your three years of office, but as you indicated to the federal government recently, that if it were to cut taxes and not provide additional help to you and other provinces, that you might be induced to raise taxes. What are the prospects?

PRIME MINISTER ROBERT BOURASSA: Well I would like first to thank you for the publicity you are giving to my government. What can be connected to the last question when I said that if the last election, and we will have to see in the future, if the last election leads us to a more decentralization, then I think this will be good for Canada. I suppose you have the same problem here, sharing of fiscal powers between the two levels of government. The elasticity of federal revenues is much greater than provincial or municipal revenues, because they rely mainly on personal income tax as their main source of revenue. They have a rate of increase between 15 and 20% whereas provincial tax lag, tobacco tax and gasoline tax will have a rate of increase of 4 to 6%, so a much lower elasticity. On the other hand, we have provincial government, it is not only a question of Quebec versus Ottawa, it is provincial government versus the federal

government. The provincial government has increasing responsibilities according to the Constitution in the field of health or education. This is a provincial matter. Therefore, they have lower expenditures, a rate of increase which is lower for expenditures and they have higher revenues than the provinces. So we have a very good case to have a new sharing of fiscal powers and we have had conferences in the last few days, we discussed that matter. I hope that the commonsense will prevail. That means we will get more money. (Laughter and applause)

ALPHONSE DE ROSSO: In a speech you made in London last November, you indicated that Quebec welcomes international investment, but you ended up with a comment that Quebec will push for development, and I quote “Through modern and adequate legislation”. And then you added the aim of the Quebec government is to have understandable protectiveness, not bureaucratic control. Would you mind elaborating on what you mean by understandable protectiveness?

PRIME MINISTER ROBERT BOURASSA: That is the problem of all governments, this question of bureaucracy or technocracy. We are living in a world where the administration is more and more complex and where the powers of technocrats is for that reason bigger. So we have to find ways to counterbalance that. Just to connect that again with the first, my first answer, we established the PPBS in the Province of Quebec and we were able to cut the rate of increase of our expenditures substantially. If we can compare, for instance, in the case of Medicare, our per capita costs is somewhat, 35% lower than in Ontario, our neighboring

province, if you can allow me to speak like that. I don't know if Ontario representatives are here, but I would say that this is a permanent problem. We are looking for various ways. We are giving more importance to parliamentary commission to participation of the people, instead of considering whatever is proposed as bad, if it is coming from the opposition parties or after the law is deposed, we will be very much open-minded for any changes which seems to us acceptable. So it is a need for more participation from the people, from all groups, business community, labor, everybody in order to have laws which are conformed to what the common good, and not only let's say to the will of the technocrats.

ALPHONSE DE ROSSO: I will ask another one on the...what new developments can be expected in the use of the French language in the province. In light of the federal government's recent decision to push back from '75 to '78 its requirement that federal Civil Servants speak French, and the recommendations of your Gendron Commission on the role of French, which were recently submitted to you, let me be perhaps a little bit more specific. Will all business executives, regardless of nationality have to be bilingual in Quebec? And another one, will executives transferred to Quebec continue to be able to educate their children in a language of their choice?

PRIME MINISTER ROBERT BOURASSA: That is a good question. (Laughter) The problem is the report is not yet public, and any comment I will make on the report will get a lot of publicity in Canada and they will say I came to New York to speak about the report without speaking

about in the province itself. So it is very delicate for me to comment on the content of the report, but I can give you the government policy, (Laughter) which was always realistic, there is no doubt that there is a problem now for French speaking majority in Quebec because our birth rate is among the lowest now compared with 15 years ago in Canada. We have very few immigrants. So there is a certain amount of insecurity but certainly we don't have to break the country to reply to this insecurity. We can have cultural autonomy or sovereignty within the federal system very easily. And we have all the legal power to that, but this...another principle or another strong principle of government policy is that we have to take into account of our North American contacts that, for horizontal communications, it will be ridiculous to stop the use of English. As to vertical communications, I would say this will be normal, and I have many discussions with the member of the business community and they will always accept with enough time to implement it. They will always accept the fact that the French should be used when it is possible and when it is desirable. But there is no question of using coercion, undue coercion, there are perhaps certain laws which can be changed when there is a worker which has a complaint against the situation, I suppose he can make his complaint in his own language. I think everybody will understand that. They understand that in France, Italy, Germany, everywhere so they could do the same in the Province of Quebec. But, there will be no advantage for us if we are going too far and too quickly, if there is a reduced standard of living. I think the great majority of French Canadians, want to improve the situation but also they want that the government should take into account our particular situation in North America. (Applause)

H. ERICH HEINEMANN: Mr. Greenspan, in your discussion of Phase II, Phase III and Phase I, you had relatively little to say about the role of the Federal Reserve Systems' monetary policy and even less to say about one feature of the control apparatus that some economists believe may in fact be its most serious flaw and a feature which I am afraid is still in place. I am referring to the unique and to some degree anomalous role that Dr. Arthur Burns is playing in Washington today as Chairman of both the Federal Reserve where he is struggling to keep monetary policy proceeding at a moderate pace, and as Chairman of the Committee on Interest and Dividends where he is charged with keeping the money costs down, or at least from rising too rapidly. Now, as any good monetarist will tell you at a drop of Milton Friedman's hat, these two tasks are basically incompatible. Indeed, according to Homer Jones of the St. Louis Reserve Bank, the fat is already in the fire. The inordinate, and that was his word, and I guess yours too tonight, money supply expansion of 1970 due will produce new inflationary pressure in late '73 and '74. What are your views in this, and in particular, isn't the 15% plus growth rate of the money supply in December a good example of one of the dangers in this double hat strategy?

THE HONORABLE ALAN GREENSPAN: Well let me say that the question really isn't whether there is the double hat, as far as I can see, but whether if you have the two jobs, do you dare give it to anybody else. (Laughter) I frankly, am not a great fan of the concept of the Committee on Interest and Dividends. Because it is presumption. I think that it is conceivable that by some governmental regulation or various form of authority, you can regulate interest rates with impunity. And I think the history has clearly demonstrated that to be false. And I

would much prefer somebody who knew about monetary policy and money theory, as Dr. Burns, wearing that hat, is somebody must wear it. Coming to the second part of your question, I don't like the December money supply increase and I am certain that Dr. Burns didn't like it either. And I think there is very little question that if we continue to generate the type of monetary expansion that we have been seeing of late; we will undercut much of the strong pressure, which I think will come from the budget and from the agricultural policies. But I would hesitate to attempt to explain monetary theory to Dr. Burns, who was my professor to begin with, and it is sort of pointless to point out which he already knows better than I. (Applause)

H. ERICH HEINEMANN: I doubt that many people here tonight would quarrel with your emphasis on controlling federal spending, as the principle key to the long-term outlook for reasonably stable prices. But it is also self-evident that there are some powerful forces in this society demanding that the fiscal process be employed increasingly to redistribute income and wealth. Even in the austerity budget for fiscal 1974, where, as you put it, almost every program is getting clobbered, spending is going to be about \$20 billion, that is if some good Republican economists with close Washington connections are right in what they have been reporting from the inner reaches of the administration. Against this background, the President has been adamant in standing against an increase in taxes. For revenue purposes, for stabilization purposes or for any other reason. Do you think this is wise, what would your advice to Mr. Nixon be if you were Chairman of the Council of Economic Advisors? (Laughter)

THE HONORABLE ALAN GREENSPAN: Steady as she goes. (Laughter) Yes I do think it is wise, and the reason being, if you take a look at what the fiscal problem basically is, what you come up with is that we developed in the middle 1960's and it accelerated somewhat thereafter a built-in rate of new program growth. That is new federal program growth, which so happened to increase the rate of expenditures at the federal government level, so that it was in excess of the increase in the tax base. So that if that trend continued indefinitely, it would mean that you would need a tax increase perhaps this year or 1974 but far more importantly, it would mean that you would need a tax increase every year because the proportion of the tax base, or I should put it this way, the proportion of total income which is allocable to federal spending is rising and therefore, the arithmetic clearly demonstrates that what you have to do is increase the taxes continuously. The tax rates continuously. Now obviously there is some point down the road where that becomes counterproductive from a revenue producing point of view. That is, you will no longer get increased tax receipts at the IRS. So if the question is, if your problem is the type of expenditure hemorrhaging that has been going on at the federal budget level, it is not a solution to increased taxes, it is a procrastination. You are merely putting the problem off until a later date. And I think the President and administration generally should be complimented to recognize what the problem is that somebody must come to grips with it, and I think now is the best time to do it. I concur wholeheartedly with everything he is doing in that direction.

(Applause)

ALFONSE DE ROSSO: I have been told that this is the last round of questions and I will have

one and Mr. Heinemann will have one, and the Chairman will take over. Mr. Prime Minister, I hope you will forgive me this question on energy. As you know, I am from Exxon. We are all so much interested in energy in this country. Your government recently outlined an energy policy for the province whose major objectives among others was bringing order into the energy sector and reducing cost of energy and dependence on multinational oil companies. At first blush these objectives and most of the objectives of your energy policy would seem to come into collision with evolving federal energy policies as well as the role of the federal government. Not to mention the policies of other provinces. How will all of this be reconciled?

PRIME MINISTER ROBERT BOURASSA: That is let's say one of the problems of any federal regimen, you have one here. We are discussing now with the federal government, this question of energy policy. They have...the federal government has to find the best equilibrium possible between the various regions of Canada and of course we are questioning the oil policy and we will have many occasions to discuss that again with the Department of Energy in Ottawa. On the other hand, we have, in the Province of Quebec an asset and so far as energy is concerned and I mentioned that briefly in my speech, with the development of James Bay with hydroelectric power. It is admitted that it is perhaps one of the cleanest forms of energy and cheapest form also. This is perhaps our greatest economic asset that we ever had in our history and we discussed that. Of course now we are developing resources to meet our internal needs. We had occasion in the past to discuss with member of the American business community the question of financing the James Bay Project and we were very much welcomed. And of course if there is a

great need here, if there is an attractive price which are offered to the Quebec government, of course we can consider also other hydroelectric resources which can be developed. I said very often that we still have additional resources, it can have two uses, either we can use it to attract secondary industry in the Province of Quebec, to solidify our economic structure. Or we can sell part of them, if we can have sufficient financial benefits. So in the past, we were discussing very often where we did not have the good side, we did not have the greatest advantages but in this field of energy, especially with the energy crisis which is existing now in North America, I think it is very encouraging for Quebec to have that great asset. (Applause)

H. ERICH HEINEMANN: I suppose it is inevitable that having once worked closely with the President you should often be called upon to defend the administrations policies. And in point of fact you were a most able advocate of Mr. Nixon during the campaign last fall. But in the case of the basic shift in agricultural policy that was coupled with Phase III, wasn't the White House just a wee bit slow in reacting to a problem that had been developing gradually over a long period of time, and indeed had long since become critical for the average lower-middle income wage earner faced with skyrocketing prices in the supermarket.

THE HONORABLE ALAN GREENSPAN: No, I don't think that they were slow, I think that they were able to do it at all is an incredible feat. It is difficult to realize, despite the change in the population there are still two Senators from every farm state. And with the seniority system in the Congress, I can assure you that the structure of control over agricultural policies in the

Congress is far greater than that of any administration. We have had numerous occasions in the past of administrations attempting to alter fundamentally the agricultural policies which were initiated in the 1930's and I remember poor Ezra Benson with President Eisenhower who attempted much of what is in fact just been accomplished, and the President then, and his Secretary of Agriculture then, worked extraordinarily hard to achieve something which never got achieved. And I think that this is not a partisan question. I think that it has been a very difficult political problem in this country. It goes back to the roots of our founding, and the nature of, remember at the turn of the century were 90% agricultural or at least rural. I think that there was almost no chance to initiate major agricultural policy changes until something like the current inflationary food problem arose. I give them credit for being able to do it under any conditions.

(Applause)

CHAIRMAN GEORGE R. VILA: Well we have time for one more question if either of you gentlemen have anything urgent on your mind.

H. ERICH HEINEMANN: I'd be happy to....One of the most frequent criticisms of Mr. Nixon's tactics in implementing his original economic game plan, the gradualism of early 1969 that was supposed to halt inflation without a recession, has been that early in his first administration he appeared to be taking a hands off attitude toward wage and price increases. If I am not mistaken, the President's remarks provoked pure-in-phrase famous advice to his clients, "Take the money and run" Get your price increases now while the getting is good. Granting your argument that

tight controls won't work, and that in any event wage and price controls don't prevent rising prices but rather simply postpone them, aren't you a bit concerned that in announcing Phase III Mr. Nixon has given the impression that the control apparatus has been relaxed more in fact than is the case. Isn't it possible that this, at a time when major labor negotiations are looming just over the horizon, that this may exacerbate existing expectations of inflation?

THE HONORABLE ALAN GREENSPAN: Well I think the question is, one has it, and second, should it. I think the performance of the stock market in the last several days I think suggests that your statement is that it probably has, but I think the market is mistaken in this respect. I think that while clearly I am far from defender of controls as I have indicated tonight, I nonetheless think that it is a mistake to believe that Phase III is in fact as voluntary as many of the reporters have made it be, and I fear that first of all, let me just say that there are not going to be....there I snot going to be that all easy to raise prices in the marketplace, even with the cycle that we are running into now. I also suspect that we will seek some far more stiffening activities beginning to occur, reflecting the fact that what we have is not a voluntary system at all, it is still mandatory. (Applause)

CHAIRMAN GEORGE R. VILA: Alright, Mr. Prime Minister and Mr. Greenspan, we thank you for a most interesting, stimulating and informative evening and we now declare the meeting adjourned. (Applause)