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The Political Economy of Arthur Burns

JAMES L. PIERCE*

DR. ARTHUR F. BURNS' tenure as Chairman of the Federal Reserve Board witnessed a remarkable number of economic and political events that make the Burns' years fascinating to study. Burns began his term when the old economics seemed to fail, when recession appeared to bring greater rather than less inflation. Following the recession, the economy was subjected to price controls, international financial shocks and domestic turmoil associated with reescalation of the Vietnam War. Price decontrols and currency devaluation then presented a new set of problems, only to be followed by an oil embargo and a quadrupling of oil prices by OPEC. The social and political upheaval over Watergate presented their own problems. The economy then plunged into the worst recession since the 1930's. Despite the severity of the recession, inflation remained strong. The economy began its long recovery from the collapse only to watch a slowing of inflation turn to resurgence. Burns left office with an economy that was expanding but which was experiencing strong inflation and worsening international problems.

The purpose of this paper is to discuss the political environment and pressures that existed during the Burns' term of office and to assess the possible implications of these pressures for the conduct of monetary policy. The paper will focus on the first five years of Burns' term because these were the more difficult and interesting years. I served as a senior staff member of the Federal Reserve Board and attended all but a few of the Federal Open Market Committee (FOMC) meetings during Burns' tenure prior to my departure from the staff in 1975. However, I was not privy to all decisions and all pressures exerted on the Fed by Presidential administrations, Congress or foreign governments. While being an insider has lent me insights, my assessment here is derived exclusively from an examination of the economic developments plus material from Congressional testimony and press accounts. The analysis will avoid attributing motives to the various players but rather will stick to facts. The discussion will associate monetary policy with Arthur Burns, because for all intents and purposes monetary policy was Burns. His colleagues on the Board and FOMC exerted little influence on monetary policy.

The conclusions of the analysis are a little sad. After presiding over monetary policy for many difficult years in which the economy was subjected to a seemingly unending string of shocks, both external and self-inflicted, Burns left the Federal Reserve a weaker institution than he found it. Despite his impressive public presence and forceful statements of intent, Burns' tenure was marked by serious policy errors that weakened the economy and the credibility of the Fed. Congressional oversight of the Fed has begun and will likely strengthen in coming years.

* University of California, Berkeley. I wish to thank William Dudley for his resourceful research assistance for this paper. Hilde Wette and Melanie Knight also provided valuable research assistance.

It is unlikely that the Federal Reserve will again enjoy the independence and respect that it once did. It is impossible to say for sure whether some other Chairman would have done a better job. Perhaps the economic and political events of the 1970's made certain policy actions inevitable. However, policy blunders contributed to the process. The Burns' years were not a happy period for the nation, for the economy or for monetary policy.

1970

The nation entered the decade with a new chairman of the Federal Reserve and a restrictive monetary policy. In the second half of 1969 the annual growth of M_1 was slightly over 2.5% and the growth of M_2 was nearly zero. Not surprisingly, interest rates climbed to what were, at the time, record levels. Fiscal policy had turned restrictive. The inflation rate, against which these restrictive policies were directed, was at its highest level in nearly twenty years. Unemployment was not yet a concern; at year end, it was only 3.5%. Industrial production and real GNP declined in the fourth quarter.

For 1970, the Nixon Administration hoped to reduce the rate of inflation and revive the growth of output. These objectives were to be achieved through a fiscal policy that maintained a modest surplus at high employment and a moderate rate of expansion of the monetary aggregates [1, 1970, p. 60]. The Council failed to specify separate inflation and real GNP targets, contenting itself with a goal of a 5.5% increase in nominal GNP.

During the last FOMC meeting before Burns became chairman, William Martin, the outgoing head of the Federal Reserve System gave his support to a policy that stressed the trend of the monetary aggregates rather than interest rates and money market conditions. At the first FOMC meeting he chaired, Burns made the new policy operational by calling for a "moderate growth in money and credit over the months ahead" [2, May 1971, p. 150]. The platitudinous "moderate growth in money and credit" was to characterize Fed announcements of policy for some time.

Attempts to attain the goal of a smoothly expanding money stock at a "moderate" rate were to take a back seat to money market exigencies in May. The Cambodian invasion began in late April. The sudden reescalation of the war was a major surprise that produced turmoil in financial markets. The Fed moved to stabilize interest rates.

In June, the Federal Reserve had to cope with the effects of the Penn Central bankruptcy which resulted in default on Penn Central's commercial paper. The Fed eliminated the Regulation Q ceiling for large certificates of deposit of one to three months maturity and decided "to shift emphasis temporarily from long-term monetary goals to 'moderating pressures on the financial markets'" [2, May 1971, p. 254]. Banks were urged to extend funds to firms having difficulty refinancing their commercial paper. Banks would support most of the credit extension through sales of newly liberated CDs, but they were also told that borrowing from the discount window for such a purpose was encouraged. For these actions the Federal Reserve and Arthur Burns received high praise.

Despite the heavy burden placed on the Federal Reserve during the first six months of 1970, it was able to keep to a path of "moderate" monetary growth. In the first quarter of 1970, M_1 grew at a 3.5% annual rate and M_2 at a 1.4% annual rate. In the second quarter the rates were 4.8% and 7.0% respectively. Long-term interest rates continued to rise and did not peak until the third quarter of the year.

From December 1969 to June 1970 the unemployment rate increased and industrial production continued to decline. But inflation stubbornly persisted at about 6%. The Nixon Administration joined the Congress in calling for a more expansive monetary policy.

The economic recovery began in the third quarter. In the second half of the year, M_1 increased at about a 5.5% annual rate, M_2 at about a 10.5% annual rate. Both short-term and long-term interest rates dropped sharply.

1971

The Administration, however, was not satisfied with the rate of monetary expansion. It set a target for nominal GNP of $1,065 billion for the year. The target was about $20 billion above the consensus of private forecasters [3, February 6, 1971, p. 16]. These forecasters predicted an inflation rate of approximately 4.5%, with real growth in the 2½–3½% range. George Shultz claimed that the target was attainable if the Federal Reserve followed the correct monetary policy. He rested his case, in part, on an econometric model developed by Arthur Laffer which showed that, for every dollar increase in the money stock, nominal GNP would immediately increase by four to five dollars. Arthur Burns publicly rejected this model [4, 1971, p. 263] and Shultz's assertion that a monetary policy existed that would enable the Administration to attain its goals.

In the early months of the year, the Administration exerted intensive pressure both publicly and privately for a more expansionary monetary policy. The Laffer model was only the tip of the iceberg. Burns' public opposition to the Administration caused great displeasure and led to an unleashing of the White House ruffians on Burns and the Fed. Aside from meetings between Fed representatives and the White House group, Burns was subjected to a personal smear campaign. After his conversion to "born-again Christianity," Charles Colson apologized publicly to Burns for the "dirty tricks" that were played on him. Even a casual reading of transcripts from the Watergate tapes will give one an indication of the low esteem in which the Administration held Burns.

In the first quarter of 1971, real GNP increased at a 9% annual rate as the economy rebounded from the effects of a General Motors strike. In the second quarter, the economy experienced a slowdown, real GNP increasing at a 3.0% annual rate. Unemployment, which had been falling, climbed back up to its December 1970 level of 6%. Prices continued to rise, although at a somewhat slower rate.

Despite Burns' public proclamations, monetary policy was highly expansive during this period. In the first half of 1971, M_1 increased at almost a 9% annual rate and M_2 at about 15%. Fiscal policy also turned more expansive in 1971. Social security benefits were raised; the investment tax credit restored; excise taxes cut, and personal income tax exemptions raised.

By mid-year the Administration was in a quandary. Expansive policies had been followed, yet the economy remained below the target path for reaching the

Administration's goal of $1,065 billion GNP. Stronger medicine was apparently required. Burns called for an incomes policy to attack the inflation problem but stopped short of advocating price controls: "I am not calling for price controls; this is a drastic remedy. The time may come when we need it, but I definitely do not think the time has come. We ought to try milder medicine before taking anything so drastic" [5, 1971, p. 261].

Meanwhile, years of balance of payments deficits coupled with expansive monetary policy took their toll in international financial markets. In late April and early May a large movement of short-term funds to Canada and Europe occurred. On May 5, German authorities, after an inflow of $1 billion in 40 minutes, decided to stop supporting the dollar. The German mark was left free to float against the dollar. Other countries having strong currencies quickly followed suit.

The problem of inflation coupled with unacceptably high unemployment and the growing run on the dollar was met by the Administration's "New Economic Program." On August 15, 1971, Richard Nixon announced a ninety-day freeze on prices.

The Fed announced that it would keep money stock growth at a low level to reduce expectations that the controls would be accompanied by excessively expansive policy. In the fourth quarter M_1 grew at a 3% rate following a nearly 7% rate in the third quarter. M_2 growth remained at about 8%. Short-term interest rates fell sharply and long-term rates moved little, if at all, mirroring the continuation of inflationary expectations. The freeze was effective in limiting price increases. The Consumer Price Index rose at a 1.6% annual rate from August to November. Industrial production moved ahead at a 6.8% annual rate. Only unemployment seemed to remain as a serious problem, declining only slightly over the period.

Congress was unhappy with the Fed's policies which it saw as maintaining unemployment and stifling housing. Some members of Congress wished to freeze interest rates at a low level to aid the housing industry, and the Fed was threatened with a General Accounting Office audit of its operations [6, p. 28–31]. Burns was called by Congress to defend the practices of the Committee on Interest and Dividends of which he was Chairman. There were frequent complaints about high interest rates.

In November 1971, the wage-price freeze was replaced with Phase II. Wages and prices were allowed to rise but only within predesignated guidelines. The goal of the program was to reduce inflation to a 2–3% annual rate by the end of 1972. In December 1971, international negotiations led to the Smithsonian agreement.

1972

For 1972, the Council of Economic Advisers forecasted a 9.5% increase in nominal GNP. For the first time, they explicitly stated the composition of this increase—6.25% increase in real GNP and 3.25% increase in prices as measured by the GNP deflator. The CEA's 1972 estimate, unlike their 1971 estimate, was very close to the consensus estimate of other forecasters [3, December 25, 1971, p. 12].

With the new year, the focus of concern became unemployment and the budget deficit. In hearings before the Joint Economic Committee, the CEA emphasized the Administration's efforts to reduce unemployment. The budget, as measured by the high employment surplus, had become sharply stimulative. The Council argued that the budget would not be inflationary because substantial excess capacity existed. Senator Proxmire wondered whether the budget was not politically self-serving as most of stimulus would come before the 1972 election.

Burns testified that monetary expansion would be consistent with the needs of an expanding economy. He attributed the variation in monetary aggregate growth rates during 1971 to "the public's changing demand for cash balances." Proxmire questioned Burns' concern about unemployment: Burns answered by reiterating that "the economy will be ... supported fully by the authorities" [4, 1972, p. 127]. Interestingly, no questions were raised or innuendo offered that monetary expansion would be excessive to support Richard Nixon's reelection efforts. Instead, Burns was urged by the Democrats to follow an expansionary monetary policy in order to reduce the level of unemployment.

In 1972, the Fed added a new operating target in an attempt to improve its performance in meeting its monetary aggregate targets or at least to show critics that it was "doing something" about control of the monetary aggregates. In the future, the Fed would pay more attention to the growth of bank reserves held against private deposits.

At the beginning of the year Burns was under pressure to expand the money stock. Writes *Business Week*: "Says a Burns confidant, the Chairman 'was getting calls from the White House in December, saying "what are you doing with this tight money?"'" [3, April 15, 1972, p. 82]. After a high rate of monetary expansion in the first quarter, Burns was faced with the problem of slowing the rate of monetary expansion while keeping interest rates from increasing. Interest rates were not controlled but were monitored by the Committee on Interest and Dividends which encouraged "voluntary" compliance with moderation in interest rate increases.

At mid-year, with a strong recovery underway, the Administration expressed happiness with monetary policy. Herbert Stein testified before the Joint Economic Committee, "We think that the policies have been quite compatible ... We have had a fairly moderate rate of growth in the money supply" [5, 1972, p. 27]. M_1 grew at about an 8% annual rate in the first half of the year and M_2 at over 11%. Burns did not consider the rate of monetary expansion excessive [5, 1972, p. 104]. He did express concern with the budget deficit. The Administration also called for a control on expenditures but shied away from recommending a tax increase. Hobart Rowen of the Washington Post summed up the situation: "... the fact is that the federal budget is out of control ... Thus, what may be in store is a boom for 1973, but one with an inflationary bust and high interest rates at the end of it." [7, July 23, 1972]. There was little discussion in Washington of a runaway monetary policy. Many Democrats were concerned that the rate of expansion was not fast enough to bring down the rate of unemployment to acceptable levels.

Economic performance in 1972 appeared to be excellent. The sharp rise in real GNP surpassed the CEA's earlier projections and the rate of inflation was barely above target. The recovery was led by strong housing and business fixed investment sectors. The decline in the unemployment rate was limited by the large reduction in the size of the Armed Forces but the unemployment rate fell from 6.0% in December 1971 to 5.1% in December 1972.

Stimulus was provided by both fiscal and monetary policy in 1972. In 1971, the high employment surplus was $1 billion. In 1972, it was −$4 billion. This swing is probably understated because 1972 receipts include $9 billion in overwithheld income taxes. If these receipts were to be excluded, the net swing to stimulus was $14 billion. The money stock grew at a rapid rate in 1972. M_1 grew at over 8.0% during the year and M_2 at over 11%. Short-term interest rates bottomed about the first of the year, rising thereafter. Long-term rates declined slightly as the year progressed. There was remarkably little criticism of these stimulative policies from either political party.

1973

The CEA foresaw an excellent year in 1973, predicting a 9% increase in nominal GNP and a 6% increase in real GNP. By year-end, the CEA expected the economy to approach its long-term potential growth path. Unemployment at year-end was expected to be 4.5%. The CEA forecast was close to the consensus estimate of private forecasters.

In testimony before the JEC, Burns noted the need to practice greater moderation during 1973. He argued that the 1972 money stock expansion was not excessive. " ... If the money supply had grown at a significantly lower rate, we probably would have experienced smaller gains in real output and employment last year" [4, 1973, p. 39]. Burns, as always, declined to name a target for monetary expansion in 1973 but pledged that the Fed would not keep market interest rates at artificially low levels or "permit severe stringencies to develop."

Phase II of the economic stabilization program was replaced by phase III in January 1973. Under phase III, the regulation of wage and price changes became self-administered. With the end of phase II, control of the inflation rate also ended. From January 1973 to April 1973, the CPI increased at a 9.4% annual rate and the WPI rose at a 20.0% rate. In March, phase III controls were tightened for fuel and meat, two items whose price had been rising rapidly. The rate of inflation diminished slightly in May and June. For the December 1972 to June 1973 period, the CPI increased at a 8.0% annual rate.

The economy continued to advance strongly. Industrial production climbed at a 7.4% annual rate during the December to June period. The growth of the monetary aggregates remained rapid in the first quarter of the year and slowed in the second quarter. Short-term interest rates climbed sharply but long-term interest rates, including mortgage rates, moved up modestly.

The Committee on Interest and Dividends attempted to restrain the rise in the prime rate. In March, *Fortune* commented: "In effect, the committee urged the banks to set their loan rates on the basis of the average cost of funds rather than the cost of attracting additional funds" [2, March 1973, p. 26]. When some banks raised their prime rates by 1/2% in March, Burns summoned their presidents to Washington for a showdown. Wright Patman attacked the banks for attempting to increase the prime rate and promised to bring up consideration of mandatory interest rate controls before the House Committee on Banking and Currency. Firms shifted from the commercial paper market to banks for short-term credit because of the artificially low prime rate. Banks complained about the cost squeeze but minimized its effects by raising the standards for qualifying for the prime rate and increasing compensating balance requirements. In April, the Committee on Interest and Dividends implemented a dual prime rate, a market rate for large corporate borrowers and a lower rate for small businesses and farmers. By this device the Committee hoped to satisfy Congressional critics, and, at the same time, minimize financial market distortions. In testimony before the Joint Economic Committee in August, Burns proclaimed the dual prime rate system a success.

In January 1973, the dollar fell to the floor of its trading range with all major currencies. In February, the dollar was devalued by 10%. Speculation continued, however, and in March the fixed exchange rate was abandoned. Over the first half of the year, the value of the dollar dropped by 12% on a trade-weighted basis.

Nixon responded to public unhappiness with the rapid rate of inflation by implementing a new freeze on June 13, 1973. Most prices were frozen at June 1–8 levels. Wages, rents, and agricultural products at the first sale were excluded from the freeze. Interest rates and dividends remained subject to voluntary control. Burns was reported to be unhappy with Nixon's response [3, June 16, 1973, p. 23].

Arthur Burns argued that the most important cause of the resurgence of inflation was the coincidence of business expansions in the United States, Europe, and Japan. He testified that the thrust of past policy was correct: "Both monetary and fiscal policy moved in the right direction [in 1972. But] ... in retrospect, it appears that restraint should have been greater" [5, 1973, p. 231]. When the growth of the monetary aggregates did not slow in the first half of 1973, the Fed raised the discount rate and reserve requirements. Burns promised that further measures would be taken if these actions did not reduce the growth of money and credit to an acceptable rate.

In the third quarter of 1973, M_1 and M_2 grew at annual rates of 5.2% and 7.9% respectively. Short-term interest rates rose rapidly and longer-term rates followed more gradually. Disintermediation occurred with thrift institutions suffering net savings outflows in the third quarter. Housing starts fell.

In September, the House Banking and Currency Committee held hearings entitled, "The Credit Crunch and the Reform of Financial Institutions." With these hearings came renewed calls for a GAO audit and for interest rate controls. Burns also came under attack for the inability of the Federal Reserve to achieve its monetary aggregate targets. He rejected the contention that the monetary aggregates are easy to control. He further argued that the Federal Reserve's shortcomings in this area were unimportant. He believed that short-term variations in the money supply of less than six months had no economic significance. The dissatisfaction with monetary policy was widespread. In a poll of 415 business economists, only 1.4% rated monetary policy excellent over the past year, while 41% rated it poor [3, October 6, 1973, p. 101].

In October 1973, during the October war, OPEC raised prices to $5.12 a barrel.

A short time later, Saudi Arabia declared an embargo against the United States and the Netherlands. The embargo created a shortage that demonstrated to the members of OPEC their power to increase the price of oil. In December, the posted prices was doubled to $11.65 a barrel.

Industrial production had slowed even before the oil embargo and the oil price hikes. Real income fell and consumer spending declined. The unemployment rate edged up only slightly from June to December. Inflation hesitated during freeze II, then shot ahead with the imposition of phase IV controls. For June–December, the CPI increased at a 9.2% annual rate.

In the final quarter of the year M_1 increased at a 5.3% annual rate and M_2 at a 9.3% annual rate. Short-term interest rates declined. Long-term rates remained virtually unchanged. Net savings inflows to thrift again turned positive. Fiscal policy became more restrictive as the effects of inflation on revenues were not offset by discretionary changes in policy. For the second half of 1973, the budget was $1.85 billion in surplus, and the high employment surplus was running at a $8.8 billion annual rate.

1974

For 1974, the CEA forecasted an 8% rise in nominal GNP, consisting of a 1% rise in real output and a 7% rise in prices. This estimate was slightly more pessimistic than *Business Week's* consensus forecast of a 1.4% rise in real output and a 6.1% increase in prices. The Council predicted a weak first half in 1974, with strengthening occurring in the second half. Inflation would subside because fuel and food price increases were not expected to persist. The unemployment rate was expected to average 5½% for the year. Stein called for a monetary policy " . . . which will be conducive to accelerating the growth of real output in the second half of 1974, but not so fast as to prevent a decline in the rate of inflation" [4, 1974, p. 13].

In testimony before Congress, Burns promised a restrictive monetary policy [4, 1974, p. 725]. Burns ultimately conceded that there was a connection between past monetary policy and inflation: "Of course there is a connection. What would you have wanted the Federal Reserve to do in a year like 1972, when the year started out with an unemployment rate of 6 percent and didn't go below 5½ percent until November, a fact that became public only in the month of December?" [4, 1974, p. 746]. For the future, Burns voiced optimism. He believed that inflation could be tamed over the next 2 or 3 years without forcing the country through a period of heavy unemployment. In the first half of 1974, M_1 grew at about a 6% annual rate and M_2 increased at about a 9% rate. Both short- and long-term interest rates shot upward.

On May 6, 1974, the Franklin National Bank informed the Comptroller of the Currency and the Federal Reserve that the bank had suffered severe foreign exchange losses. Aware that announcement of these losses would cause the bank to fail, the Federal Reserve agreed to lend the Franklin National whatever funds it needed within the limits of acceptable collateral. The Fed became a heavy lender to Franklin until it was finally allowed to fail in October. Burns described the choice the Federal Reserve faced: "We had a choice, in the case of Franklin National, of letting a $5 billion bank go under—closing it down, liquidating it. If that had happened, it would have sent shock waves, not only throughout our financial system, but across the entire world" [8, p. 216]. *Business Week* interpreted the Federal Reserve actions differently: " . . . the Fed's decision to pay whatever is necessary to bail out the Franklin—and any other bank in danger because of record interest rates underscores a central fact: No matter what financial risks it may yet entail, the Fed means to stick with current monetary policy for as long as it takes to reduce inflation" [3, May 18, 1974, p. 22].

In June, Bankhaus I. D. Herstatt failed because of massive foreign exchange losses of $200 million. This failure increased fears that a general banking collapse might be imminent. Interest rates on Euro-deposits jumped nearly 2% points as banks scrambled for funds.

In the first half of 1974, the CPI increased at a 12.1% annual rate. In the first four months of the year, price inflation was dominated by increases in fuel and food. After April 30 and the expiration of wage and price controls, a much broader range of goods was responsible for the increase. From December to June, industrial production fell at a 1.1% annual rate and the unemployment rate climbed from 4.9% to 5.2%.

Despite record interest rates, Burns did not come under strong attack. Perhaps the mind of the nation was on other matters. Arthur Okun commented, "If someone had said several months ago that the Fed would let the prime go to 11½%, I would have predicted that Patman would have Burns turning slowly on a barbecue spit. But the mood has changed. Inflation is now seen as Public Enemy No. 1" [3, June 15, 1974, p. 79]. *Business Week* observed: "Inflation threatens to tear apart not only the economy but American society, and only Burns and his Fed seem to be doing anything about it. Burns stands as a titanic figure at a time when official Washington is woefully short of such figures" [3, June 15, 1974, p. 79]. Milton Friedman took a different view: "I would welcome the Fed making its actions conform with its rhetoric, . . . but there's no sign of tightening" [3, June 15, 1974, p. 80].

In the third quarter of 1974, monetary policy became restrictive by any standard. M_1 increased at a 3.7% annual rate, and M_2 at a 6.2% rate. Short-term rates peaked during the quarter. The CPI rose at a 12% annual rate for the quarter.

Gerald Ford became President in August. The new president advocated the use of the "old-time religion," tight monetary and fiscal policy, to fight inflation. In the fourth quarter M_1 increased at about a 4% annual rate and M_2 at a 6.7% rate. Short-term interest rates fell, but long-term rates continued to rise. Real GNP had been declining throughout the year but industrial production fell at an incredible 20.0% annual rate in the fourth quarter. The unemployment rate climbed from 5.9% to 7.2% at year-end. Housing starts declined to a .88 million annual rate in December. In November, *Business Week* observed: "Even Chairman Arthur F. Burns, convinced until a month ago that the economy would be spared a recession, must now concede that he was wrong . . . " [3, November 16, 1974, p. 30].

1975

For 1975, the CEA predicted that real GNP would be about 3% below the average for 1974. Recovery was expected to commence in the second half of the year and inflation to slow as the year progressed. For 1975, prices, as measured by the GNP deflator, were expected to be 11% higher than in 1974. Unemployment would average 8% for the year. The CEA forecast was more pessimistic than the *Business Week* consensus forecast which predicted −1.2% real growth in GNP and an 8.7% increase in prices.

The economy suffered its largest decline of the recession in the first quarter of 1975. Real GNP fell at a 9% annual rate and industrial production fell at a nearly 32% rate. Inflationary pressures moderated somewhat in the quarter but remained strong. Unemployment rose to nearly 9%. Monetary policy was restrictive as measured by the 2% annual rate of growth of M_1 and the 6% growth in M_2. Short-term interest rates fell sharply in the first quarter and there was a slight decline in long-term interest rates.

In 1975, strong Congressional criticism of monetary policy began to surface. Senators Humphrey, Kennedy and Proxmire were particularly critical of Fed policies and voiced strong displeasure over Burns' unwillingness to specify monetary policy targets for 1975. On the House side of Capitol Hill, the displeasure was perhaps more intense and widespread. Henry Reuss introduced a bill (H.R. 212) instructing the Fed to make M_1 grow at 6% or more and to allocate credit "toward national priority uses and away from inflationary uses" [8, p. 11].

The Administration and Burns defended previous monetary policy and strongly opposed legislative attempts to control that policy. In his opposition to H.R. 212 and subsequent bills, Burns argued that M_1 was obsolete, that the Fed couldn't hit any aggregate targets over intervals as short as 3 to 6 months and that interest rates are an important consideration for policy.

After extensive debate and compromise, the Congress passed in March 1975 House Concurrent Resolution 133 by a wide margin. This resolution instructed the Fed to reduce long-term interest rates, to announce its annual targets for growth in the monetary aggregates and to appear periodically before the Senate and House Banking Committees to explain and defend its policies.

With passage of H. Con. Res. 133, the Fed lost some of its mystery and influence. In hearings during the year, members of both chambers attacked policy and Burns with a new-found vigor. The unfolding of events since passage of the Resolution indicate that the Fed did not change its policy but that the Fed policies have been brought more out in the open [10].

In 1975 Burns announced growth targets for the monetary aggregates that were lower than many observers believed were sufficient for recovery from the deep recession. Burns countered that a sharp rise in velocity would produce the desired expansion [11, p. 176]. Events proved him correct. An M_1 growth of roughly 4% in 1975 supported a rapid expansion in output during the year. In this debate Burns could not lose because he determined monetary policy. If the demand for money and credit were higher than the level Burns envisioned and started to push up interest rates and threaten the recovery, Burns could expand the money stock at a faster rate and silence his critics. If the demand for money and credit were at the level Burns expected, interest rates would not increase even if the rate of expansion of the money stock were at the moderate rate Burns desired. Despite the lack of policy content in the debate, Burns did receive high marks for his accurate forecast of velocity.

Conclusion

The years 1976–78 continued the political activity begun in 1975. Attacks on the Fed and Burns remained strong in Congress and several bills were introduced to clip the Fed's wings. Efforts were made in these bills to force the Fed to announce its policies and objectives in advance, and to defend its decisions. The Federal Reserve and the Ford Administration were able to defeat these bills, but with increasing difficulty. Congress also considered the reform of the structure of the Federal Reserve itself, including composition of the FOMC and removal of the Fed from regulatory duties. These efforts were also defeated. Many observers believe that the handwriting is on the wall, however; it appears only a matter of time before the Fed is revamped and until monetary policy is brought more out in the open.

Dr. Arthur Burns presided over monetary policy during an extremely difficult period of our economic history. It is easy with the benefit of hindsight to criticize many of his policies. Events that appear clear and obvious now were not clear and obvious at the time. Nonetheless, I believe that monetary policy made two important blunders during Burns' tenure that injured both the economy and the Federal Reserve. First, beginning in 1971 and running through 1973, monetary policy was too expansive. The hope that price controls could solve inflation and liberate the Fed to pursue policies designed to reduce unemployment was unfortunate and ill-founded. The expansionary policies helped produce inflationary pressures that first produced price controls and then speeded their demise. The monetary and fiscal policies of these years produced a high underlying inflation rate to which was added the surge of inflation following the action of OPEC. The result was double-digit inflation.

The second blunder occurred in 1974. Perhaps stung by criticisms of his policies in 1972, Burns decided to declare war on inflation in 1974. The result was, by some standards, the tightest monetary policy ever experienced in this country and the worst recession since the 1930's.

Arthur Burns was fond of saying that "the whole genius of monetary policy lies in its flexibility." Unfortunately, it was this flexibility that produced the inflationary policies of the early part of the decade and the super-crunch of 1974. It was the exercise of this flexibility that created sufficient political discontent to produce legislation to control the Fed. Admittedly, Burns and the Fed were subjected to extreme political pressure during these years. But more conservatism and less flexibility would have served the the Federal Reserve well.

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DISCUSSION

JERRY L. JORDAN*: A purpose of studying history, even very recent history, is to learn something that might be useful in the future. Emphasis on past errors and short-comings does not necessarily result from any vindictive or malicious streak in the researcher. It may be as much a result of the conjecture that in some activities, as I believe is the case in the conduct of monetary policy, the emphasis is appropriately put on the avoidance of doing harm or making matters worse, rather than on doing good.

Monetary theorists such as Karl Brunner, Milton Friedman, and Allan Meltzer have long emphasized how limited our knowledge is regarding the effects of discretionary monetary policy. Their prescriptions often have reflected a sort of agnosticism about the abilities of monetary authorities to take the appropriate actions at just the right time to offset or compliment other forces affecting economic activity. They have counseled central bankers to guard against the temptations and pressures to use monetary policy actions to try to make the world a better place to live. Contrary to the accusations of their critics, they never have advocated better measurement and control over a nation's money supply as a cure-all for economic or social ills.

The Pierce and Poole papers document the pitfalls of the kind of activism in the conduct of monetary policy that monetary theorists have warned against. In reading these papers, and others to come in the future, be aware of criticisms that are not raised regarding Arthur Burns as Chairman of the Fed. Even the severest critics of monetary policy during the Arthur Burns era cite the Chairman's good intentions. And Burns also is *not* criticized for failing to understand that the lags of monetary policy are variable and uncertain and that the Federal Reserve has had a history of over-staying its policies and behaving in a pro-cyclical way. Burns understood the difference between nominal and real interest rates and the fallacies of arguments regarding real money balances and tried to educate his staff and the other officials. He knew the difference between money and credit, he often lectured Congress that the relation between money growth and interest rates was opposite in the longer-run than in the shorter-run, and he persistently repeated that the only way to achieve and maintain a lower trend rate of inflation was to achieve a lower trend rate of growth of the money supply. Yet, he simply failed to practice what he preached, as both Pierce and Poole convincingly demonstrate.

I agree with Pierce that Burns' eight years at the Fed were a difficult time for

* Pittsburgh National Bank.