

Statement of Alice M. Rivlin
Director, Congressional Budget Office
Before the Committee on the Budget
U.S. Senate

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There should be
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Mr. Chairman, in 1978, unemployment declined substantially, but inflation accelerated to near record levels for the postwar period. As a result, the Administration and the Federal Reserve have undertaken an anti-inflation program of tightened credit, wage-price guidelines, and proposed spending cuts. As you begin your deliberations on the First Concurrent Resolution on the Budget for Fiscal Year 1980, the central question facing this Committee is: How should the budget respond to this anti-inflation effort? To assist your consideration of this question, my statement this morning will cover five topics:

- o The outlook for the economy over the next two years as forecast by CBO;
- o The prospects for slowing inflation;
- o The main outlines of the fiscal year 1980 budget--both the budget prepared by the Administration and the budget if current policies were continued with no changes;
- o Long-run fiscal policy options; and
- o Long-run economic goals.

THE ECONOMIC OUTLOOK

Two cross-currents in the economy today make forecasting especially uncertain. On the one hand, economic growth was quite robust at the end of last year. The fourth-quarter gains in retail sales, production, and employment were substantial, and the momentum of this increased activity should carry over into early 1979.

But, on the other hand, the high rate of inflation has planted the seeds of a slowdown in the economy:

- o In response to the increase in prices and the associated depreciation of the dollar, the Federal Reserve has tightened monetary policy. Short-term interest rates are up sharply from mid-1978, and the growth of the money supply has slowed dramatically since last fall. The resulting credit restraint is expected to affect housing and business investment adversely later this year.
- o Rapid inflation apparently has also led to buy-in-advance behavior by consumers. This response is reflected in the record high ratios of consumer debt to income and may be borrowing sales from later in the year.
- o Finally, consumer and business confidence dropped sharply toward the end of last year, in part because periods of high inflation are typically followed by recession.

There is widespread agreement among forecasters that the outcome of these cross-currents will be a slowdown in the pace of economic activity this year. But there are differences of opinion concerning the timing and the severity of the slowdown.

In preparing our forecast, CBO has made two policy assumptions:

- o As usual, the fiscal policy assumption is that current policy will be continued, resulting in estimated federal outlays of \$494 billion in fiscal year 1979 and \$551 billion in fiscal year 1980. Thus, the CBO forecast does not assume either the spending cuts proposed by the Administration or its real wage insurance program.
- o Monetary policy is assumed to remain restrictive, with short-term interest rates rising somewhat further and peaking in the second quarter.

As shown in Table 1, CBO forecasts real output to slow significantly, growing at a 0 to 2 percent rate during 1979; while continued strength is anticipated in the first half of the year, a small downturn is expected to begin later in the year. A mild recovery is foreseen in 1980, with real growth averaging 3 to 5 percent. As a result of the weaker economic activity, the unemployment rate is projected to rise to a 6.2 to 7.2 percent range by the end of this year and to continue in the same range throughout 1980. Meanwhile, inflation is expected to remain stubbornly high. The increase in the Consumer Price Index (CPI) is forecast to range between 7 and 9 percent this year and between 6.5 and 8.5 percent in 1980.

TABLE 1. SUMMARY OF CBO ECONOMIC PROJECTIONS UNDER CURRENT POLICY, CALENDAR YEARS 1979 AND 1980

Economic Variable	1976:4 to 1977:4 (actual)	1977:4 to 1978:4 (actual)	1978:4 to 1979:4	1979:4 to 1980:4
GNP (current dollars, percent change)	11.9	12.9	7.0 to 11.1	9.7 to 13.9
GNP (1972 dollars, percent change)	5.5	4.3	0.0 to 2.0	3.0 to 5.0
Consumer Price Index (percent change)	6.6	8.9	7.0 to 9.0	6.5 to 8.5
Unemployment Rate, End of Period (percent)	6.6	5.8	6.2 to 7.2	6.2 to 7.2

We prefer to express a forecast as a range rather than a single number in order to illustrate the uncertainty that surrounds all forecasts. For purposes of comparison, however, CBO's "best guess" estimates are shown in Table 2 together with forecasts of the Administration and three well-known commercial forecasting services. As can be seen, CBO is somewhat more pessimistic in our forecast of real growth in 1979 than the Administration, but we are more optimistic than two of the private forecasters. The differences are not huge, however; indeed, given the uncertainty about economic conditions today, the range of views is surprisingly narrow.

A case can be made for more growth than CBO is forecasting. Momentum from the rapid gains at the end of last year could propel the economy for some time, and there are few signs of a slowdown in the measures of current activity. But, indicators of future activity that have become available since we made our forecast point to significant weakness toward the end of 1979:

- o Monetary policy has remained tight, and the growth in the money supply continues to be abnormally slow;
- o The Commerce Department's survey of anticipated spending on plant and equipment suggests a sharp deceleration in the growth of fixed investment by business this year;
- o New orders for nondefense capital goods fell for the second month in a row in December;
- o The workweek was down last month; and
- o Consumer confidence has declined further to the lowest level since 1975.

TABLE 2. COMPARISONS OF RECENT ECONOMIC FORECASTS

Economic Variable/Forecaster	<u>Fourth Quarter to Fourth Quarter</u>		<u>Calendar Year to Calendar Year</u>	
	1979	1980	1979	1980
Real GNP (Percent change)				
Congressional Budget Office <u>a/</u>	1.0	4.0	2.9	2.4
Administration (January 25)	2.2	3.2	3.3	2.5
Wharton Associates (December 28) <u>b/</u>	1.4	NA	2.7	1.6
Data Resources, Inc. (January 22)	0	5.4	2.6	2.7
Chase Econometrics (January 22) <u>c/</u>	-0.6	4.1	1.9	2.1
Consumer Price Index (Percent change)				
Congressional Budget Office	8.0	7.5	8.4	7.8
Administration	7.5	6.4	8.2	6.7
Wharton Associates	8.3	NA	8.4	7.8
Data Resources, Inc.	8.1	6.9	8.6	7.2
Chase Econometrics	7.5	6.1	8.3	6.3

	<u>Level, Fourth Quarter</u>		<u>Average for Calendar Year</u>	
	1979	1980	1979	1980
Unemployment Rate (Percent)				
Congressional Budget Office	6.7	6.7	6.2	6.8
Administration	6.2	6.2	6.0	6.2
Wharton Associates	6.1	NA	5.9	6.5
Data Resources, Inc.	6.8	6.8	6.3	6.9
Chase Econometrics	7.3	7.3	6.5	7.4

a/ Assumes a continuation of current policy; the estimate is the midpoint of the CBO forecast range.

b/ Assumes a \$20 billion tax cut in 1980 and a one-year delay in the social security tax increase scheduled for 1980.

c/ Assumes a \$19 billion tax cut in 1980.

A composite measure, the Commerce Department's Index of Leading Indicators, fell in both November and December; three consecutive months of decline in this index is sometimes said to signal a recession.

Probably the most significant difference between the CBO and Administration forecasts is the outlook for inflation. If inflation slows as rapidly as the Administration predicts, then credit conditions might become easier than CBO expects, and the chances of avoiding a recession would be improved. But CBO expects a smaller deceleration of prices, and thus the Federal Reserve is assumed to continue its policy of credit restraint.

THE INFLATION OUTLOOK

Why won't inflation slow more quickly? The answer lies in the nature of our economic institutions. If prices are to decelerate, wage increases must be brought more in line with productivity gains, and profit margins must not rise. Since compensation per hour rose by more than 9 percent last year, while productivity increased hardly at all, we clearly have a long way to go to rectify this imbalance.

In the current anti-inflation policy, two approaches are being used to slow this rapid wage growth:

- o First, more restrictive monetary and fiscal policies are expected to retard economic growth, with the increased slack in product and labor markets putting downward pressure on prices and wages.
- o Second, a wage-price standards program has been adopted, in order to influence wage and price decisions directly.

Policies that increase unemployment are likely to slow the pace of inflation, but this will not happen quickly. The formal or informal indexing of wages and other income adjustments to past price increases imparts great momentum to inflation; consequently, a prolonged period of economic slack would be needed to slow the rise of prices and wages significantly. Therefore, the attempt to cure rapid inflation with restrictive monetary and fiscal policies alone has considerable costs in terms of lost employment and production. Furthermore, experience shows that these costs are distributed very unevenly over the population.

The other anti-inflation approach--wage-price standards--attempts to slow the momentum of inflation without the cost of lost jobs and output. But it is doubtful that this program can reduce inflation quickly, especially since much of the economy is exempt from the measures used to enforce the standards. Over half the labor force is explicitly or tacitly exempt from the wage standard, and about 60 percent of the goods and services that compose the CPI is also formally or tacitly exempt from enforcement under the price standard. The prices of a number of these excluded items, such as food at the farm, increased rapidly last year and may rise significantly again in 1979. In addition, full compliance from the nonexempt portion of the economy may be difficult to obtain, especially from labor unions that are being asked to accept reduced real wages for their members.

THE FEDERAL BUDGET OUTLOOK FOR 1980

The major issue before this Committee is what can fiscal policy do to mitigate inflation? Even if the Congress chose to hold taxes and spending at current policy levels, the budget would most likely exert a mildly restrictive effect on the economy in 1980. If you decide to cut spending below current policy, either moderately as proposed by the Administration or more substantially as recommended by some, fiscal policy will exert more restraint on economic activity.

The Administration's Budget

The Administration proposes to reduce spending growth in fiscal year 1980, both as part of its anti-inflation program and to reduce the share of the Gross National Product (GNP) spent by the federal government. The most significant features of the 1980 budget on the spending side are an absence of major new spending initiatives and a general effort to hold existing programs at or below current policy levels. The Administration estimates total outlays for 1980 at about \$532 billion, 7.7 percent above the estimated 1979 level. This contrasts with the 9.5 percent growth in federal spending expected in 1979 and the 11.9 percent growth in 1978.

The Administration's estimate of total outlays can also be compared with what 1980 outlays would be under a continuation of current spending policies as set forth in the second budget resolution for 1979. CBO estimates that current policy outlays in 1980

would total \$551 billion, or nearly \$20 billion above the President's budget estimate (see Table 3).

TABLE 3. THE FEDERAL BUDGET OUTLOOK: BY FISCAL YEAR, IN BILLIONS OF DOLLARS

	1978 (actual)	CBO Current Policy Estimates		Administration Budget Proposal	
		1979	1980	1979	1980
Receipts	402.0	453.3	502.3	456.0	502.6
Outlays	450.8	493.8	551.5	493.4	531.6
Deficits	48.8	40.5	49.2	37.4	29.0

The Administration's budget shows revenues of about \$503 billion. Revenues on a current policy basis are estimated by CBO to be close to that figure; hence, our estimated current policy deficit exceeds the deficit in the Administration's budget by about \$20 billion.

The Administration's budget differs from CBO's estimate of a current policy budget for fiscal year 1980 for a number of reasons, including both differences in economic assumptions and proposed changes in policy by the Administration.

The differences in economic assumptions do not produce widely divergent revenue estimates for fiscal year 1980, because the

impact of faster real growth in the Administration's forecast is largely offset by its projected lower inflation. The only major policy change for revenues proposed by the Administration is real wage insurance to help achieve compliance with the 7 percent wage guideline. The Administration estimates that this proposal would cost \$2.5 billion (\$2.3 billion in lower receipts, and \$0.2 billion in increased outlays), assuming a 7.5 percent increase in the CPI from the fall of 1978 to the fall of 1979.

On the spending side, however, both estimating and policy differences are more significant. The Administration's expectation of lower unemployment and lower inflation reduces their spending estimates by about \$4.6 billion below CBO current policy estimates (see Table 4). Other estimating differences account for about \$4 billion.

TABLE 4. MAJOR DIFFERENCES BETWEEN CBO CURRENT POLICY ESTIMATES FOR FISCAL YEAR YEAR 1980 OUTLAYS AND THE ADMINISTRATION'S BUDGET: IN BILLIONS OF DOLLARS

CBO Current Policy Estimate	551.5
Administration's Budget Estimate	<u>531.6</u>
Difference	19.9

Major Differences	
Economic assumptions	4.6
Other estimating differences	3.8
Proposed spending reductions	<u>11.5</u>
Total Difference	19.9

CBO Estimates of the Administration's Budget

The Administration's budget meets the President's commitment to hold the deficit to \$30 billion or less in 1980 and to move in the direction of a balanced budget. The first of these budgetary goals may not, however, be realized if CBO's economic forecast turns out to be more nearly correct than that of the Administration. Both revenues and outlays respond quickly to economic conditions without any action by the Congress. With even relatively minor changes in economic assumptions, estimates of revenues and outlays could change significantly, and the resulting deficit in 1980 could be increased well above \$30 billion.

In order to make the Administration's budget estimates comparable with our current policy estimates, CBO has reestimated the Administration's budget proposals for fiscal year 1980 using our own economic assumptions and estimating methodology. On this basis, CBO estimates that receipts would total about \$499 billion, outlays would total \$540 billion, and the budget deficit would be close to \$41 billion.

On the receipts side, CBO estimates that the real wage insurance proposal could cost as much as \$1 billion more than the Administration's estimate because of our forecast of higher inflation rates. CBO also estimates current law revenues in 1980 at \$2 billion less than the Administration, largely because of the differences in economic assumptions.

For outlays, CBO estimates that somewhat higher unemployment and inflation than foreseen by the Administration could add more than \$4.5 billion for programs such as unemployment insurance, social security, food stamps, medicare, and medicaid. Other estimating differences could add roughly another \$4 billion to the Administration's estimate of outlays.

Under the economic conditions forecast by CBO, the committee would have to recommend deeper spending cuts than proposed by the President in order to hold the growth in outlays to below 8 percent in 1980. There is also a question of whether the \$30 billion deficit is achievable with deeper spending cuts, because the more restrictive fiscal policy could result in lower revenues by making the economic downturn more severe.

THE LONGER-RUN BUDGET OUTLOOK

As the committee considers the first concurrent resolution, it should keep in mind that control over the budget and the economy cannot be realized unless decisions on the 1980 budget are regarded as a first step in an overall budgetary strategy that may take several years to implement. The shape of the 1980 budget will significantly affect the outlook for 1981, 1982, and beyond.

Spending reductions proposed by the President and other cuts proposed by the Congress will, if enacted in 1980, have small effects on outlays in 1980 but significant effects on the 1981-1984 budgets. As this committee appreciates, a multiyear framework for considering the first concurrent resolution will insure that the committee has the opportunity to consider the 1980 budget in the light of long-term goals for the economy and the federal budget.

Any formulation of long-run budgetary targets must somehow balance goals for the economy, the size of the government, and the budget deficit. These goals must also be weighed against demands for tax cuts and various programmatic requirements.

Goals for the economy and the deficit are separable from goals for the size of the federal sector. Policies to reduce spending do not necessarily imply less fiscal stimulus and slower economic growth if spending reductions are offset by tax cuts. On the other hand, reduced spending is often advocated as a way to reduce the budget deficit. Other things being equal, the two goals--a smaller federal sector and a lower deficit--probably cannot be achieved simultaneously in the short run without accepting lower economic growth.

As part of our five-year budget projections report, which was published last week, CBO analyzed three general budgetary strategies for fiscal years 1980-1984.

Continuation of Current Policies

One basic strategy would be a continuation of current fiscal and budgetary policies. For our current policy projections, we assumed that the economy would grow at an average rate of 4.5 percent during calendar years 1981-1984. This rate of growth is optimistic, but not unprecedented. It is about 1 percent higher than the average rate since World War II, and about 1 percent lower than the rate sustained in the 1961-1966 period. The unemployment rate is assumed to decline from the projected 1980 level of 6.8 percent to 5.5 percent by the end of 1984. The inflation rate, which is assumed to remain significantly higher throughout the 1981-1984 period than the average since World War II, declines slowly so that by 1984 the rate of increase in the CPI is 6 percent.

Under these assumptions, as shown in Table 5, we project outlays to grow to \$755 billion, and receipts to \$849 billion by fiscal year 1984. The growth in outlays is dominated by adjustments for inflation, especially for programs that are indexed to inflation either directly or indirectly under current law. Real growth in outlays is limited to those programs--such as social security, medicare, and federal employee retirement--in which the number of beneficiaries is expected to increase, and in defense and other programs in response to past appropriation actions.

The growth in federal receipts is dominated by the increases in individual income tax revenues that occur as inflation and

TABLE 5. FIVE-YEAR BUDGET PROJECTIONS: BY FISCAL YEAR, IN BILLIONS OF DOLLARS

	1978 Actual	1979 Estimate	Current Policy Projections				
			1980	1981	1982	1983	1984
Current Policy Receipts	402.0	453.3	502	574	661	749	849
Current Policy Outlays	450.8	493.8	551	604	655	706	755
Fiscal Policy Changes <u>a/</u>	--	--	--	8 to 12	13 to 18	26 to 35	53 to 70
Deficit (-) or Surplus	-48.8	-40.5	-49	-38 to -42	-7 to -12	8 to 17	25 to 42

a/ These changes refer to tax cuts or spending increases.

economic growth move taxpayers into higher brackets. Projected increases in social security taxes as a result of the 1972 and 1977 amendments to the Social Security Act also produce significant growth in social insurance revenues.

By 1982, the federal government would be taking more out of the economy in tax receipts than it would be putting back in the form of wages, transfer payments, and purchases. Assuming moderate growth in demand in the private sector, the drag on the economy caused by these fiscal policies would make it difficult to sustain the growth rate assumed in the current policy projections for 1980-1984. Consequently, to achieve the economic growth assumed for the projections, some changes in fiscal policy--in the form of tax cuts or spending increases--would probably be necessary. If these changes were made, the budget deficit would decline in 1981 and 1982 and an approximate balance could be achieved by 1983 (see Table 5). The 1984 surplus would thus be much less dramatic than the simple computation of current policy receipts minus current policy outlays.

Policies to Reduce Spending

The current policy budget projection presented here is not the only possible scenario over the next five years. Policies to reduce spending are often proposed as a way to cut the budget deficit and to advance the date when the budget would be balanced.

The two goals of a lower deficit and a smaller public sector probably require settling for lower economic growth. We analyzed two possible scenarios with contractionary spending policies in our projections report:

- o Spending reductions, starting with a \$15 billion cut in fiscal year 1980, and real economic growth averaging 3.4 percent in fiscal years 1980-1984; and
- o Larger spending reductions, starting with a \$25 billion cut in fiscal year 1980, and real economic growth averaging 3.1 percent in fiscal years 1980-1984.

When compared with the current policy projection of spending (which is based on an assumption of an average annual rate of real growth of 3.9 percent), reduced spending policies combined with weaker economic growth targets and moderate growth in demand in the private sector could result in a lower deficit in 1980, an earlier date for budget balance, and some reduction in the inflation rate. The budget deficit in 1980 could be as low as \$30 billion, with budget balance achievable by 1982, or possibly 1981 (see Table 6). By fiscal year 1984, the inflation rate under the assumption of weaker economic growth might be about 2 percentage points lower than that under the current policy assumptions. The reduced spending, however, would result in higher unemployment rates--probably in the 6.5 to 7 percent range during fiscal year 1984, as compared with the 5.6 percent rate under the stronger growth path.

TABLE 6. ALTERNATIVE GOALS FOR THE ECONOMY AND THE BUDGET DEFICIT UNDER THE CONTRACTIONARY SPENDING STRATEGIES: BY FISCAL YEAR

	Current Policy Spending Strategy and Moderate Growth Target	Contractionary Spending Strategies and Lower Growth Targets	
		\$15 Billion Cut In 1980	\$25 Billion Cut In 1980
Economic Goals (in percents)			
Real growth (average, 1980-1984)	3.9	3.4	3.1
Unemployment rate (1984)	5.6	6.5	6.9
Inflation rate (1984)	6.2	4.5	4.1
Budget Deficit			
1980 (in billions of dollars)	50	40	30-35
Year of budget balance	1983	1982	1981

The two contractionary spending policies are intended merely to illustrate the wide range of possibilities for cutting federal spending. The smaller reduction could be derived by limiting the growth of the federal budget in response to inflation, and by foregoing action on funds remaining under the Second Concurrent Resolution on the Budget for Fiscal Year 1979 but not yet funded by the Congress. Some major options for restricting inflation adjustments are:

- o Capping federal pay raises at 5.5 percent in 1980 and limiting them to no more than 7 percent thereafter;
- o Limiting cost-of-living increases for retired federal employees to what would be given under a representative private sector plan;
- o Capping at 5.5 percent the cost-of-living increase for social security that will be effective on July 1, 1979, and limiting further increases to no more than 7 percent;
- o Implementing hospital cost containment; and
- o Approving only two-thirds of the discretionary inflation adjustment for federal programs not indexed under current law.

With these actions, the incomes of the elderly and disabled would not keep pace with inflation--at least in the near term; federal pay raises would fall short of comparability with the

private sector; some hospital services would be reduced or eliminated; many federal programs--ranging from defense to federal training and job programs--would be smaller because of a reduction in real funding levels.

Funds remaining under the second concurrent resolution, but not yet appropriated, could be foregone under a contractionary spending policy. Some of the major items include:

- o \$1.5 billion in budget authority for defense programs remaining after the deletion of a new aircraft carrier from the 1979 defense appropriations bill;
- o Funds for new energy programs; and
- o Supplementary fiscal assistance to local governments.

The larger cuts implied by the spending policy that starts with a \$25 billion cut in 1980 represent some of the more specific or targeted reductions the Congress might want to consider. They include:

- o Eliminating all funding for countercyclical public service employment programs;
- o Not renewing general revenue sharing for states in fiscal year 1981; rather, restricting the program to local governments; and
- o Reducing or eliminating various social security benefits.

An Expansionary Spending Policy

At the same time that some policymakers are calling for reductions in spending and in the deficit, others are calling for expansion of federal programs. The most significant possibilities for program expansions appear to be:

- o Real growth in defense spending;
- o National health insurance;
- o Welfare reform;
- o Expanded energy programs, including funding for a 1-billion-barrel strategic petroleum reserve.

The Congress might consider pursuing an expansionary fiscal policy that would accommodate demands for increased programs and would move the economy toward the goal of a 4 percent rate of unemployment by 1983, as specified in the Full Employment and Balanced Growth Act of 1978 (the Humphrey-Hawkins Act). An expansionary fiscal policy of this kind would probably mean significantly higher inflation by fiscal year 1984 and continued large budget deficits (see Table 7).

TABLE 7. ALTERNATIVE GOALS FOR THE ECONOMY AND THE BUDGET DEFICIT UNDER THE EXPANSIONARY SPENDING STRATEGY: BY FISCAL YEAR

	Current Policy Spending Strategy and Moderate Growth Target	Expansionary Spending Strategy and Higher Growth Target
Economic Goals (in percents)		
Real growth (average, 1980-1984)	3.9	4.7
Unemployment rate (1984)	5.6	4.0
Inflation rate (1984)	6.2	8.7
Budget Deficit		
1980 (in billions of dollars)	50	50-55
Year of budget balance	1983	—

LONGER-TERM ECONOMIC GOALS

The Congress will, in all probability, encounter difficulties in reaching its longer-term economic goals. The Humphrey-Hawkins Act establishes targets of 4 percent unemployment and 3 percent inflation by 1983, with priority given to the unemployment goal.

Given current economic trends, it is unlikely that both the unemployment and inflation targets can be reached by 1983 using monetary and fiscal policies alone. As I noted earlier, these policies reduce inflation by creating slack in the economy, and this medicine works slowly. To illustrate, the slow-growth option simulated by CBO suggests that five years of unemployment at about 7 percent would be needed to bring inflation down to the neighborhood of 4 percent. And this exercise assumes no adverse price shocks--from the weather, OPEC, government, or other sources.

In contrast, expansionary policy options could reduce unemployment to about 4 percent by 1983, but at the cost of sharply accelerating inflation. It is true that this jobless rate has occurred in the past with less upward pressure on prices than would occur now; however, low levels of unemployment are more difficult to achieve today because of the different demographic structure of the labor force and institutional changes such as increased coverage of unemployment insurance and the minimum wage.

Since the Humphrey-Hawkins goals will be difficult to achieve through the use of monetary and fiscal policies alone, the Congress may want to supplement the traditional tools with structural programs and reforms that may help to achieve the simultaneous reduction of inflation and unemployment. In looking at economic policy over the next five years, the Congress might consider supplementary tools such as the following:

- o The reduction of government regulation of prices, wages, market entry, and methods of production.
- o The reduction of government protection against inflation for various groups in the economy--for example, limiting agriculture price supports, holding down increases in the minimum wage, or reducing the effective indexing of transfer payments;
- o The reduction of trade barriers;
- o Incomes policies such as the President's wage-price program, that attempt to limit the catch-up to past inflation in wages, salaries, and profits;
- o Skill training and public-service jobs programs.

We do not know how effective these structural programs and reforms would be in slowing inflation and reducing unemployment. Some may be rejected for good reasons other than macroeconomic considerations; most would hurt some group in the economy. But there is widespread agreement that inflation is the major economic problem today, and corrective measures can be painful. Restrictive monetary and fiscal policies work slowly and involve a significant loss of jobs and output; structural reforms can hurt particular segments of society; and incomes policies are administratively complex and typically require a high degree of public support and compliance. Unfortunately, there is no simple, costless way to rid ourselves of inflation quickly.

