

Promoting Keynesian Liberalism: Walter W. Heller and US Economic Policy, 1933–1987

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Declaration

I, James Hillyer, confirm that the work presented in this thesis is my own. Where information has been derived from other sources, I confirm that this has been indicated in the thesis.

Abstract

This thesis explores the economist Walter W. Heller's career and maps the rise, ascendancy, and eclipse of Keynesian liberalism in the United States. Heller served as chairman of the Council of Economic Advisers to Presidents John F. Kennedy and Lyndon B. Johnson. He successfully persuaded both to deploy Keynesian policies to underwrite the liberal expansion of the 1960s. Consequently, Heller was one of the most significant and influential political economists in US history. However, historians have curiously overlooked him.

This thesis reasserts Heller's importance to the making of modern America. It shows that Heller was a more significant figure in the rise of Keynesianism than existing scholarship has appreciated and demonstrates how he educated two presidents in the merits of Keynesian ideas. It illuminates the role Heller played in the formulation of the Great Society and explores how he adapted his Keynesian views during the more conservative times of the 1970s and 1980s. Through examining Heller's career, this thesis assesses how Keynesianism interacted with liberalism in the United States. It illustrates how both merged in the 1930s, demonstrates how liberals utilised Keynesian thinking during World War II, and shows how Keynesian ideas intersected with liberal policies during the post-war period. In doing so, this thesis adds to recent scholarship that argues liberalism was a much stronger force in post-war American politics than assumed, especially since the scholarly 'rediscovery' of conservatism in the 1990s.

A positive appraisal of Heller emerges from this thesis. It also provides an overview of the rise and decline of Keynesianism in the United States, breaking new ground in explaining the significance of a presidential adviser who has not hitherto been the subject of specialist study.

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Introduction

Walter W. Heller: A Keynesian Liberal

*“Few economists...influence significantly and positively the events and public policies of their time. Few academicians earn intellectual renown in their professions mainly by contributions incident to policy-making in government service. Walter Heller did both.”*¹

- **James Tobin (CEA Member, 1961-62 and Nobel Laureate), 1996**

*“Walter Heller was a marvellous [CEA] chairman, the Stan Musial of CEA chairmen...[He]knew just how to insinuate our ideas into the White House mill. That does not mean that we won all the battles...But we always felt we had a chance.”*²

- **Robert Solow, (CEA Staff Member, 1961-62 and Nobel Laureate), 1997**

When Barack Obama took office in January 2009, he inherited the most severe economic crisis since the 1930s. In the final quarter of 2008, output contracted by 8.2 percent and unemployment stood at 7.3 percent.³ Although George W. Bush acted to revive the banking sector, the source of the crisis, the broader economy was on the brink of a depression when his successor took office. Obama enacted a Keynesian stimulus package to get America moving again. Known as the American Recovery and Reinvestment Act (ARRA), this pumped \$787 billion into the economy over a three-year period. Around 60 percent of ARRA consisted of increased spending on public works, interstate highway improvements, school enhancements, and aid to the states. To secure Republican support for the measure, tax cuts formed the final 40 percent. “With this act,” Obama declared, “we begin the process of restoring the

¹ James Tobin, *Essays in Economics: National and International, Volume 4* (Cambridge, MA, 1996), 747.

² Robert Solow, ‘It Ain’t the Things You Don’t Know That Hurt You, It’s the Things You Know That Ain’t So,’ *American Economic Review* 87:2 (May. 1997), 107.

³ Jared Bernstein, ‘The Economies Inherited by Obama and Trump are as Different as Night and Day,’ *Washington Post-Blogs*, 2 December 2016. Online at ProQuest Central [Henceforth PQC]

economy and making America a stronger and more prosperous nation.”⁴ However, not everyone supported the president’s plan, especially two of the nation’s most eminent Keynesian economists. In January 2009, Princeton’s Paul Krugman said he would “make the stimulus 50 percent larger...I’m not sure if the \$800 billion stimulus plan is adequate to the problem. We’re facing one hell of a crisis and we’ll need more than a band-aid.”⁵ At best, Columbia’s Joseph Stiglitz added, ARRA might prevent the recession from deepening, but it would far from revive the economy.⁶

Not only did the size of ARRA dismay Krugman and Stiglitz, so did its composition and timing. With almost 40 percent set aside for tax cuts, both complained that debt-burdened consumers would save rather than spend such an increase in their disposable income.⁷ Each acknowledged that ARRA amounted to the largest job-creation bill in American history, but a sizeable proportion of its spending measures consisted of funds to extend unemployment benefits, sustain Medicaid, and offset a lack of revenues for the states. “Only a fairly small piece,” Krugman said, was “for the kind of spending – building and fixing roads, and so on – that we normally think of when we talk of stimulus.”⁸ Unsurprisingly, Stiglitz claimed in August 2009 that ARRA had “not been enough,” especially as only a quarter of its spending measures came into effect during its first year. “[W]hat is needed now, is another dose of fiscal stimulus. If that does not happen, we can look forward to an even longer period in which the economy operates below capacity, with high

⁴ Barack Obama, ‘Statement on Signing the American Recovery and Reinvestment Act,’ 17 February 2009. Online at the American Presidency Project Website [Henceforth APP]

⁵ Cited in No Name [Henceforth n.n.], ‘Bailout Not Adequate,’ *Targeted News Service*, 30 January 2009. PQC.

⁶ Cited in n.n., ‘Can Obama Stimulus Plan Create Jobs?’ *Weekend All Things Considered*, 10 January 2009. PQC.

⁷ Ibid; Paul Krugman cited in n.n. ‘Economists Offer Two Takes on Obama Stimulus Plan,’ *All Things Considered*, 21 January 2009. PQC.

⁸ Krugman, *End This Depression Now* (New York, 2013), 109, 121.

unemployment.”⁹

Obama did implement a second stimulus. In 2010, the president agreed to extend tax cuts passed by Bush in both 2001 and 2003.¹⁰ Yet, the American economy continued to experience a sluggish recovery, leading Krugman and Stiglitz to call in vain for a more activist response to the Great Recession. “America is still an economy in depression,” Krugman said, “and the rules of depression economics still apply: what we need, above all, is more spending, to put unemployed workers and idle productive capacity back to work.”¹¹ Krugman may have wished his influence was akin to that enjoyed by Keynesians almost half-a-century earlier. In the 1960s, Keynesians held important positions in government, had the president’s ear, and saw tax cuts (rather than spending increases) as the panacea for a strong and robust economy. From the 1940s through the 1960s, liberal politicians relied on Keynesian advisers to expand the New Deal legacy. For them, Keynesianism ensured job creation, underwrote higher standards of living, and fuelled enhanced growth that produced the wherewithal to fund social programmes and public-sector improvements. In short, Keynesianism facilitated “a broad-based prosperity that obviated the need for liberalism to engage in a politically costly struggle to redistribute wealth and generated the revenue to fund the expansion of federal programs without incurring huge budget deficits.”¹²

I

Walter Wolfgang Heller served at the centre of policymaking circles when Keynesian liberalism reached its peak in America. An economist from the University

⁹ Joseph Stiglitz, ‘Stimulus or Bust,’ *The Guardian*, 10 August 2009. Available at: <http://www.theguardian.com/commentisfree/cifamerica/2009/aug/10/economy-stimulus-bailout> [Accessed M.06/D.28/Y.2015]

¹⁰ Krugman, *End This Depression Now*, xvi.

¹¹ *Ibid*, xvii.

of Minnesota, Heller served as chairman of the Council of Economic Advisers (CEA) between 1961 and 1964. He helped persuade Presidents John F. Kennedy and Lyndon B. Johnson to use Keynesian ideas to undergird the liberal state's expansion during the 1960s. As the quotations at the beginning of this thesis highlight, this was the highpoint of his career. Indeed, Heller wrote in 1966, "Economics has come of age in the 1960's."¹³ Keynesian ideas had put at the president's "disposal, as nothing else can, the resources needed to achieve great societies at home and grand designs abroad."¹⁴ To achieve this, Heller and his colleagues had adapted Keynesianism since the doctrine's emergence in America. Conceived by British economist John Maynard Keynes to revive the stagnant economy of the 1930s, Keynesianism was "attenuated greatly by both economists and politicians" in the more abundant post-war era.¹⁵ Keynes described his ideas as "'moderately conservative,'" but as the "Keynesian revolution" evolved in the United States his theory mostly became "identified with left-wing liberalism and the Democratic party."¹⁶ Heller's tenure as CEA chairman saw Keynesian ideas expressed in their most expansive form, leading his contemporaries to credit him for fully installing the "new economics" as the dominant orthodoxy in public policy. In doing so, the CEA chairman paved the way for policymakers to engage in liberal reform.

This study explores the career of Walter Heller. No individual offers a better lens through which to assess and understand Keynesian liberalism. Heller was at the centre of policymaking circles when Keynesian liberalism enjoyed its heyday in

¹² Iwan Morgan, 'Hubert Humphrey's Last Hurrah: The 1977 Senate Leadership Election and the Decline of the New Deal Tradition,' *Mid-America: An Historical Review*, 79:3 (Fall 1997), 288.

¹³ Walter Heller, *New Dimensions of Political Economy* (Cambridge, MA, 1966), 1.

¹⁴ *Ibid*, 11.

¹⁵ Charles David Shreve, 'A Precarious and Uncertain Liberalism: Lyndon Johnson and the New Economics,' PhD Thesis, Louisiana State University (1995), 5. Online at ProQuest Dissertations and Theses [Henceforth PQDT].

¹⁶ *Ibid*, 6.

America, but also acted as an important agent of Keynesian and liberal ideas before and after this period. As a public service-orientated economist, Heller worked in government throughout his pre-CEA career. There, he applied Keynesian political economy and honed his views about how it could advance liberal aims. Though conservative doctrines rose to the fore after he left his position as CEA chairman, Heller was an important figure in the defence of Keynesian liberalism when American politics and political economy turned rightward in the 1970s and 1980s. His career offers both a valuable insight into how Keynesian economists worked in government during liberalism's heyday and gives an important perspective onto how they reacted to the eclipse of their doctrine during a more conservative era. Despite this, historians who have explored post-war Keynesian liberalism have overlooked Heller, choosing instead to focus on the role of other Keynesian economists. The recipient of greatest attention is Leon Keyserling, a former New Deal adviser who served as CEA chairman under Harry Truman. Keyserling has been the subject of two biographies and countless studies of post-war growth economics, so undoubtedly offers an important lens onto the development of Keynesian liberalism.¹⁷ Yet, he had a limited influence on public policy compared to Heller.

Harvard's John Kenneth Galbraith has also attracted much attention.¹⁸ Though Galbraith served as an important campaign adviser for many Democratic politicians, his ideas also gained little traction in policymaking circles. The same is true for other Keynesians. MIT's Paul Samuelson, famous for penning the nation's leading post-

¹⁷ W. Robert Brazelton, *Designing US Economic Policy: An Analytical Biography of Leon H. Keyserling* (Basingstoke, 2001); Donald Pickens, *Leon H. Keyserling: A Progressive Economist* (Lanham, MD, 2009); Robert Sobel, *The Worldly Economists* (London, 1980), 10-37; Alonzo Hamby, *Beyond the New Deal: Harry S. Truman and American Liberalism* (New York, 1973), 293-310.

¹⁸ Sobel, *The Worldly Economists*, 65-92; Richard Parker, *John Kenneth Galbraith: His Life, His Politics, His Economics* (Chicago, IL, 2005).

war textbook on Keynesian economics, has been the subject of many book chapters.¹⁹ Yale economist James Tobin, best known as the monetary expert in the Keynesian profession, has been the subject of one monograph.²⁰ No doubt, these individuals deserve recognition, but none influenced public policy as much as Walter Heller did. True, each served in an advisory capacity to various political figures, but Heller tutored Kennedy and Johnson in the virtues of Keynesian economics. Galbraith once said that no “study of Keynesian economics should ever be written without giving nearly equal credit to the scholars who took Keynes out of the realm of theory and into the real world.”²¹ Heller’s career gives the most important insight in this respect. This study reasserts Heller’s significance vis-à-vis his contemporaries and shows how Keynesian economics reached the zenith of its influence in the 1960s.

Through doing so, this thesis reaffirms Heller’s importance as an influential presidential adviser. Whereas biographies exist of Harry Hopkins, Robert McNamara, Walt Rostow, and Henry Kissinger, Heller has not been the subject of detailed study.²² This is surprising, especially because he struck up an intimate relationship with Kennedy and Johnson and advised more presidents and presidential aspirants than any other economist during his lifetime.²³ Unsurprisingly, Heller appears in most of the historiography on US public policy in the 1960s, but only as a secondary actor.²⁴ Amy Elisabeth Davis and David Shreve both provided coverage of Heller’s

¹⁹ Sobel, *The Worldly Economists*, 93-118; and William Breit and Roger L. Ransom, *The Academic Scribblers* (New York, 1982), 107-137.

²⁰ Robert Dimand, *James Tobin* (London, 2014).

²¹ John Kenneth Galbraith, Interview in David Colander and Harry Landreth (eds.) *The Coming of Keynesianism to America* (Cheltenham, 1996), 141.

²² See, for example, George T. McJimsey, *Harry Hopkins: Ally of the Poor and Defender of Democracy* (Cambridge, MA, 1987); Deborah Shapley, *Promise and Power: The Life and Times of Robert McNamara* (New York, 1993); David Milne, *America’s Rasputin: Walt Rostow and the Vietnam War* (New York, 2008); and Walter Isaacson, *Kissinger: A Biography* (London, 1992).

²³ See n.n., ‘Walter Heller: Presidential Persuader,’ *New York Times*, 21 June 1987, F1. Online at ProQuest Historical Newspapers [Henceforth PQHN]

²⁴ For important texts other than those listed in this paragraph see Irving Bernstein, *Promises Kept: John F. Kennedy’s New Frontier* (New York, 1991), 118-157; *Guns or Butter: The Presidency of*

tenure as CEA chairman in their 1988 and 1995 PhD theses, but though both demonstrated how Keynesianism reached its highpoint in the 1960s, neither illuminated just how important Heller was.²⁵ Similarly, both Robert Collins and Andrew Yarrow have written important studies of post-war growth economics, yet neither afforded Heller the recognition he deserves.²⁶ Why might this be the case? Partly, it stems from the relative neglect of Kennedy's economic policies, which have not been the subject of a published monograph.²⁷ It is further attributable to the fact Heller's influence took place behind-the-scenes. He was also unfortunate in that soon after he rose to prominence conservative economic doctrines eclipsed Keynesianism, resulting in diminished interest in Heller and his ideas.

II

Historians have neglected Heller to their cost. Not only does he provide an important lens onto the history of American Keynesianism, but examination of his career also challenges conventional scholarly assumptions about the intersection of Keynesian ideas and liberal politics. One is that, in the late 1940s, liberals adopted a watered-down Keynesianism, to the extent that they embraced and implemented a conservative form of the doctrine up to the mid-1960s. To put this argument into perspective, it is necessary to explain how liberals came to focus upon economic ideas. As noted by Gary Gerstle, the "primacy of political economy...established

Lyndon Johnson (New York, 1996), 27-43, 82-117; Allen Matusow, *The Unraveling of America: A History of Liberalism in the 1960s* (New York, 1984), 1-60, 97-131, 153-180; Edward Flash, *Economic Advice and Presidential Leadership: The Council of Economic Advisers* (New York, 1965), 173-275; Seymour Harris, *Economics of the Kennedy Years* (New York, 1965), 23; Hobart Rowen, *The Free Enterprisers: Kennedy, Johnson and the Business Establishment* (New York, 1964), 153-182; E. Ray Canterbury, *Economics on a New Frontier* (Belmont, CA, 1968), 11-13, 139-152, 263-270, 298-301.

²⁵ Amy Elisabeth Davis, 'Politics of Prosperity: The Kennedy Presidency and Economic Policy,' PhD Thesis, Columbia University (1988). PQDT; Shreve, 'A Precarious and Uncertain Liberalism.'

²⁶ Robert Collins, *More: The Politics of Economic Growth in Post-War America* (New York, 2000); Andrew Yarrow, *Measuring America: How Economic Growth Came to Define American Greatness in the late Twentieth Century* (Amherst, MA, 2010).

itself in liberal circles in the prosperous 1920s.”²⁸ Prior to that, early twentieth century progressives prioritised social and cultural issues. However, following the exclusion of “a mass socialist or labor party from serious electoral competition from World War I,” 1920s liberals refocused their efforts on “banish[ing] poverty, unemployment, excessive concentrations of economic power, and other ills associated with industrial capitalism.”²⁹

The Great Depression magnified this. Accordingly, liberals developed potent economic ideas, emphasising the need to regulate capital, labour, and consumer markets extensively to stimulate the economy and promote a fair society.³⁰ For Gerstle, however, Hitler’s rise to power toned down economic liberalism. By the early 1940s, the Nazi regime had caused liberals to question whether “the taming of capitalism was the preeminent problem confronting industrial societies.”³¹ It also forced liberals to grapple more directly with “issues of racial and ethnic discrimination.”³² Previously, liberals believed resolving class conflict via economic reform would indirectly improve racial and ethnic problems. Yet, as the 1940s progressed, they began to see social activism issues as rational.³³ The impact of World War II also revived the economy, so by the end of that conflict liberals committed themselves to promoting a rights-based and consumer-orientated liberalism far different from the powerful economic liberalism of the interwar years. Keynesian ideas proved central to achieving this. As Gerstle, Steve Fraser, and Alan Brinkley have argued, a strong “social Keynesianism” emerged in America during the

²⁷ See Morgan, ‘Promoting Prosperity: John F. Kennedy and the New Economics,’ Conference Paper. British Library. 4 November 2013. Author’s copy.

²⁸ Gary Gerstle, ‘The Protean Character of American Liberalism,’ *American Historical Review*, 99:4 (Oct. 1994), 1045.

²⁹ Ibid, 1045.

³⁰ Ibid, 1068.

³¹ Ibid, 1070.

³² Ibid, 1070.

³³ Ibid, 1071.

late 1930s thanks to economist Alvin Hansen. This emphasised the need for permanent deficit spending, buffered by increased social welfare provision, to ensure prosperity and achieve social justice. However, wartime economic growth brought a renewed faith in capitalism.³⁴ For Brinkley, liberals thus adopted a less statist Keynesianism, one that deprioritised redistributing wealth. Instead, it was “committed above all to a newer vision of a consumer-driven economy.”³⁵

According to Gerstle, Fraser, and Brinkley, the need to promote a consumer-orientated liberalism precipitated the development of a “more conservative” Keynesianism in post-war America.³⁶ This primarily involved the use of automatically-induced deficits to ensure a stable rate of non-inflationary growth. When a more activist approach was necessary, this came through the revenue side of the budget. Conservatives, newly ascendant at the end of the war, accepted the use of Keynesian ideas to prevent another Depression, but succeeded in convincing liberals to adopt this much-diluted Keynesianism compared to the late 1930s. Several scholars have accepted this narrative. They have claimed liberals were “on the defensive” in the late 1940s so abandoned the powerful economic liberalism of the interwar years.³⁷ Against the backdrop of the Cold War, liberals embraced the “vital center” of the political-economic spectrum.³⁸ Coined by liberal historian Arthur Schlesinger Jr in 1947, the vital center mandated the use of Keynesian ideas both to promote stable levels of consumption and to prevent economic breakdown.³⁹ Liberals accepted a conservative Keynesianism to achieve this, to the point whereby it found

³⁴ Gerstle and Steve Fraser, ‘Introduction,’ and Alan Brinkley, ‘The New Deal and the Idea of the State,’ in Gerstle and Fraser (eds.) *The Rise and Fall of the New Deal Order, 1930-1980* (Guildford, 1989), xiii-xv, 85-121.

³⁵ Brinkley, *The End of Reform: New Deal Liberalism in Recession and War* (New York, 1995), 174.

³⁶ Gerstle and Fraser, ‘Introduction,’ xiv.

³⁷ Gareth Davies, *From Opportunity to Entitlement: The Transformation and Decline of Great Society Liberalism* (Lawrence, KS, 1996), 20.

³⁸ Hamby, ‘The Vital Center, the Fair Deal, and the Quest for a Liberal Political Economy,’ *American Historical Review*, 77:3 (Jun. 1972), 653-678.

ultimate expression in the early 1960s, when Walter Heller convinced John F. Kennedy to promote a tax cut to speed up the rate of growth. Scholars such as Kevin Mattson, Irwin Unger, and Debi Unger have described Heller as a “conservative Keynesian,” not least because he “stressed things such as tax cuts as a means to grow the economy.”⁴⁰ True, Heller convinced Kennedy and Johnson to implement a consumption-boosting tax cut, but suggestions that he embodied a conservative post-war Keynesianism underestimate the strength of Keynesian ideas in certain liberal circles.

The main reason this narrative has developed is due to the works of Robert Collins and Herbert Stein, who, in 1969 and 1981, published the two seminal studies of American Keynesianism. They argued that both post-war liberals and conservatives embraced “the right-wing of the Keynesian spectrum.”⁴¹ This was because the business community succeeded in taming Keynesian ideas in the more abundant post-war climate. In fact, business groups were such a driving force behind post-war economic policy that they, more so than Heller, compelled JFK to promote a tax cut.⁴² Several scholars have built upon this argument.⁴³ Writing in 1988, Louis

³⁹ Arthur Schlesinger Jr., *The Vital Center: The Politics of Freedom* (Boston, MA, 1949), 182-183.

⁴⁰ Kevin Mattson, *When America Was Great: The Fighting Faith of Post-War Liberalism* (New York, 2004), 167, 154-155 (quotation); Irwin and Debi Unger, *Turning Point: 1968* (New York, 1968), 17.

⁴¹ Robert Collins, *The Business Response to Keynes, 1929-1964* (New York, 1981), 16-17 (quotation); Herbert Stein, *The Fiscal Revolution in America* (Chicago, IL, 1969).

⁴² Collins, *The Business Response to Keynes*, 186-187; Stein, *The Fiscal Revolution in America*, 417-420.

⁴³ In addition to the sources discussed below, the following show indications of being influenced by Collins and Stein: Margaret Weir, ‘The Federal Government and Unemployment: The Frustration of Policy Innovation from the New Deal to the Great Society,’ in Weir, Theda Skocpol, and Ann Shola Orloff (eds.) *The Politics of Social Policy in the United States* (Princeton, NJ, 1988), 149-199; Weir and Skocpol, ‘State Structures and the Possibilities for ‘Keynesian’ Responses to the Great Depression in Sweden, Britain, and the United States,’ in Peter Evans, Dietrich Rueschemeyer, and Skocpol (eds.) *Bringing the State Back In* (Cambridge, 1985), 108. Footnote 7; Bartholomew H. Sparrow, *From the Outside In: World War II and the American State* (Princeton, NJ, 1996), 152-154; Mark Blyth, *Great Transformations: Economic Ideas and Institutional Change in the Twentieth Century* (New York, 2002), 51, 90-95; Gary Mucciaroni, *The Political Failure of Employment Policy: 1945-1982* (Pittsburgh, PA, 1990), 26-32; Elizabeth A. Fones-Wolf, *Selling Free Enterprise: The Business Assault on Labor and Liberalism, 1945-60* (Chicago, IL, 1994); Ronald Cox and Daniel Skidmore-Hess, *US Politics and the Global Economy: Corporate Power, Conservative Shift* (London, 1999), 114-115; Jacob S. Hacker and Paul Pierson, *American Amnesia: How the War on Government led us to Forget*

Galambos and Joseph Pratt claimed that, with the passage of the tax cut in 1964, “the policy of business-orientated fiscal stabilization reached its highest stage of development.”⁴⁴

One year later, Margaret Weir argued the influence of business groups, coupled with that of the Farm Bureau, facilitated a “limited commitment of post-war US governments to Keynesian management.”⁴⁵ Citing Collins and Stein, Weir blamed the lack of a centralised post-war government bureaucracy, the way business and agricultural groups successfully characterised liberal Keynesianism as planning, and general concerns that liberal Keynesianism could facilitate a strong welfare state, for the taming of post-war Keynesianism.⁴⁶ By the 1960s, she concluded, the “Keynesianism espoused by liberals had increasingly come to resemble that fashioned by [a business group called] the CED...it was in this form that the United States finally embraced Keynesianism with the tax cut that Kennedy proposed in 1962 and Congress passed in 1964.”⁴⁷

Godfrey Hodgson and Iwan Morgan have also argued that, during both the late 1950s and early 1960s, a “consensus” united liberals and business leaders around the implementation of conservative Keynesianism. For Hodgson, the “essential promise” of conservative Keynesianism “was that it would allow government to

What Made America Prosper (London, 2016), 131-163; G. Williams Domhoff, *Myth of Liberal Ascendancy: Corporate Dominance from the Great Depression to the Great Recession* (London, 2016), 109; Mark S. Mizruchi, *The Fracturing of the American Corporate Elite* (London, 2013), 66-67; Kim McQuaid, *Uneasy Partners: Big Business in American Politics, 1945-1990* (Baltimore, MD, 1994), 119-122; Cathie J. Martin, *Shifting the Burden: The Struggle over Growth and Corporate Taxation* (Chicago, IL, 1991), 18-81; Lynn Turgeon, *Bastard Keynesianism: The Evolution of Economic Thinking and Policy-Making since World War II* (Westport, CT, 1996), 1-20; John J. Coleman, *Party Decline in America: Policy, Politics and the Fiscal State* (Princeton, NJ, 1996), 35-38; Aaron Major, *Architects of Austerity: International Finance and the Politics of Growth* (Stanford, CA, 2014), 129-131.

⁴⁴ Louis Galambos and Joseph Pratt, *The Rise of the Corporate Commonwealth: US Business and Public Policy in the Twentieth Century* (New York, 1988), 180.

⁴⁵ Peter Hall, ‘Introduction,’ in Hall (ed.) *The Political Power of Economic Ideas: Keynesianism Across Nations* (Princeton, NJ, 1989), 15-16.

⁴⁶ Weir, ‘Ideas and Politics: The Acceptance of Keynesianism in Britain and the United States,’ in Hall (ed.) *The Political Power of Economic Ideas*, 72-78.

guarantee low and diminishing unemployment without inflation. It could thus banish at a stroke the worst terrors of both liberals and conservatives.”⁴⁸ Though Morgan has acknowledged slight nuances between how both liberals and business groups wanted to deploy Keynesianism, he concludes that both sides’ iterations of that doctrine were “hewed from the same oak” of the conservative Keynesianism identified by Gerstle, Fraser, Brinkley, Collins, Stein, Galambos, Pratt, and Weir.⁴⁹

This ignores how different, strong, and powerful Keynesian ideas were in post-war liberal circles, something various scholars have persuasively illuminated. In contrast to Brinkley, Fraser, and Gerstle, Jonathan Bell has highlighted how a “powerful forum for social democratic ideas” existed in America at the end of World War II, with Keynesianism providing the bedrock for this.⁵⁰ Tony Badger has pointed out that, well into the 1950s, liberal Senators such as Albert Gore Snr., continued to espouse social Keynesianism.⁵¹ Steven Gillon and Kevin Mattson have disputed the idea of a post-war consensus, showing that, in the late 1950s, liberals such as John Kenneth Galbraith and Leon Keyserling broke its boundaries.⁵² Robert Collins also published a book in 2000 that suggested Keynesian ideas pioneered by liberals were both different to those pioneered by businesspersons and far more important to post-war economic policy than he had earlier realised.⁵³ This built upon liberal economist

⁴⁷ Ibid, 86.

⁴⁸ Godfrey Hodgson, *In Our Time: America from World War II to Nixon* (London, 1977), 79.

⁴⁹ Morgan, ‘The Keynesian Consensus and its Limits,’ in Morgan and Robert Mason (eds.) *The Liberal Consensus Reconsidered: American Politics and Society in the Post-War Era* (Gainesville, FL, 2017), 86-108 (quotation 100). See, too, *Beyond the Liberal Consensus: A Political History of the United States Since 1965* (London, 1994), 8-12.

⁵⁰ Jonathan Bell, *The Liberal State on Trial: The Cold War and American Politics in the Truman Years* (New York, 2004), xiii. See, too, Landon Storrs, *The Second Red Scare and the Unmaking of the New Deal Left* (Princeton, NJ, 2013).

⁵¹ Tony Badger, ‘Albert Gore Sr., Liberalism and the South in the 1960s,’ in Bell and Timothy Stanley (eds.) *Making Sense of American Liberalism* (Urbana, IL, 2012), 163.

⁵² Steven M. Gillon, *Politics and Vision: The ADA and American Liberalism, 1947-1985* (New York, 1987), 124-125; Mattson, *When America Was Great*, 140-172; and Mattson and Eric Alterman, *The Cause: The Fight For American Liberalism from Franklin Roosevelt to Barack Obama* (London, 2012), 52-64.

⁵³ Collins, *More*.

Robert Lekachman's 1966 publication *The Age of Keynes*. In this book, Lekachman suggested that policymakers implemented conservative Keynesian ideas in the early 1960s, but championed the significance of liberal economists to post-war economic policy, crediting them for shaping and consolidating the Keynesian revolution.⁵⁴

This thesis also reinterprets the vibrancy of post-war Keynesian liberalism. It shows that although Walter Heller did tentatively endorse conservative Keynesian ideas in the late 1940s, he and others broke significantly from them in the late 1950s. In fact, though Heller championed a tax cut in the early 1960s, this thesis shows that he did so to expand liberalism's legacy. It also illustrates that, if it were politically possible, Heller would have preferred to increase spending to achieve that goal. Furthermore, the ideas that underpinned Heller's liberal Keynesianism were far more potent and daring than assumed. As David Shreve has noted, the Keynesian policies implemented by Heller "represented a unique and relatively untested attempt at macro and microeconomic policy configuration."⁵⁵ By using Heller to explore post-war Keynesian liberalism, this thesis argues that liberal Keynesianism was significantly different (and more powerful) than the Keynesian ideas championed by the business community. It also gives credit to liberals, instead of business groups, for shaping the post-war consolidation of American Keynesianism.

III

Examination of Walter Heller's career sheds new light on a second assumption reached by historians who have assessed post-war Keynesian liberalism. This is the idea that, following its heyday in the mid-1960s, Keynesian liberalism became insignificant. Several scholars have argued that liberal politicians (and, by extension, Keynesian economists) "wandered the political wilderness" in the 1970s

⁵⁴ Robert Lekachman, *The Age of Keynes* (New York, 1966).

and 1980s, often depicted as decades of conservatism.⁵⁶ Historians have blamed the controversy of Vietnam, the development of the counterculture movement, and the rise of New Politics liberals for this, but they have also argued that the Keynesian ideas championed by Walter Heller played a role too. Writing in 1984, Allen Matusow contended that, by the end of the 1960s, Heller's ideas had "played no small role in the unraveling of both liberalism and the economy – and no small role, therefore, in the unraveling of America."⁵⁷ This paved the way for conservative political ascendancy. According to Matusow, Heller and others mistakenly focused LBJ on preventing cost-push inflation, ignored the monetary forces underpinning the booming economy of the 1960s, and persuaded Johnson to engage in fiscal policy mistakes that unleashed inflationary pressures.⁵⁸ This helped the Republicans regain control of the White House and discredited Keynesianism, precipitating the rise of conservative economic and political ideas during the 1970s and 1980s.

Matusow influenced several scholars writing on Keynesian liberalism. Many contended the economic ideas associated with Walter Heller played a crucial role in causing liberalism's decline in the 1970s and 1980s. Writing in 1988, Galambos and Pratt said that, in the mid-to-late 1960s, "effective macroeconomic planning proved difficult to sustain."⁵⁹ For them, the problems that beset the economy in the 1970s – notably the phenomenon of stagflation – were attributable to the failure of Keynesian economics a decade earlier, which subsequently caused the revival of conservatism. Doug Rossinow and Gareth Davies have also criticised both Heller and other Keynesians for helping sow divisions within the liberal movement by the early 1970s.

⁵⁵ Shreve, 'A Precarious and Uncertain Liberalism,' vi. See too Davis, 'Politics of Prosperity,' 52-53.

⁵⁶ Jeffrey Bloodworth, *Losing the Center: The Decline of American Liberalism, 1968-1992* (Lexington, KY, 2013), 2.

⁵⁷ Matusow, *The Unraveling of America*, 179.

⁵⁸ Ibid, 154-179.

⁵⁹ Galambos and Pratt, *The Rise of the Corporate Commonwealth*, 199, 200-207.

According to Rossinow, Heller's "regressive version of Keynesianism" laid "the basis for an estrangement between Johnsonian liberals and critics to their left who, in the course of the 1960s, came to see either big business or American capitalism itself as the enemy of progress."⁶⁰ True, the Vietnam War "brought liberals and leftists almost to blows, [but] the seeds of such conflict had already been planted."⁶¹

Davies has criticised Johnson's Keynesian advisers for adhering to the "misguided" faith "that human ingenuity could engineer universally beneficent social change through economic expansion."⁶² This thinking led to the creation of liberal programmes in the 1960s that failed. In turn, certain liberals championed an unpopular, redistributive Keynesianism embodied by presidential candidate George McGovern in 1972, paving the way for a divided liberal movement in the 1970s.⁶³ Others have advanced a similar interpretation. In 1984, Charles Murray blamed Keynesian economists for putting Johnson under "the mistaken impression" that "the boom was no longer part of an ungovernable cycle of economic expansion and contraction."⁶⁴ For Murray, not only did this encourage the development of liberal programmes that did not work, these programmes created a class of welfare recipients who became dependent on the state.⁶⁵ This played a role in creating the economic problems of the 1970s, as these individuals lacked an incentive to work.⁶⁶ People thus questioned the significance of economic liberalism, leading to the rise of conservative policies.

Thomas and Mary Edsall also claimed Keynesian ideas underwrote the

⁶⁰ Doug Rossinow, *Visions of Progress: The Left-Liberal Tradition in America* (Philadelphia, PA, 2008), 226.

⁶¹ *Ibid*, 228.

⁶² Davies, *From Opportunity to Entitlement*, 31.

⁶³ *Ibid*; Bloodworth, *Losing the Center*; Dominic Sandbrook, *Mad as Hell: The Crisis of the 1970s and the Rise of the Populist Right* (New York, 2012), 221-223.

⁶⁴ Charles Murray, *Losing Ground: American Social Policy 1950-1980* (New York, 1984), 25.

⁶⁵ *Ibid*, 25-69, 146, 227.

⁶⁶ See Shreve's analysis of Murray's argument in 'A Precarious and Uncertain Liberalism,' 43-44.

expansion of a liberal state during the 1960s that turned many white working and middle-class Americans away from the liberalism of the Democratic Party.⁶⁷ Judith Stein has blamed 1960s Keynesianism's lack of an active labour market policy for helping cause the decline of liberalism in the 1970s. Using US Steel as her lens, she claimed the prosperity generated by the 1964 tax cut masked the need to engage in structural economic policies to alleviate barriers to employment for African Americans, particularly in areas such as Birmingham, Alabama, and Gary, Indiana, where steel plants were located.⁶⁸ True, the 1964 tax cut produced a booming economy that complemented passage of anti-discrimination legislation, but African American unemployment stayed very high in the 1960s, precipitating race riots that highlighted significant problems for liberalism. Though Stein claims liberalism evolved to include the concerns of African Americans by the early 1970s, she argues the problems of the 1960s strained it. This ensured it could not cope with the economic turmoil of the 1970s, causing many Democratic Party voters to embrace an alternative political and economic vision outlined by Ronald Reagan in 1980.⁶⁹

Other scholars have also portrayed the 1970s and 1980s as decades of conservatism, with liberal economic ideas no longer relevant. For Gary North, Heller continued to believe in the mistaken idea that growth could be the panacea for the nation's problems, to the point whereby he "issue[d] the Keynesians's SOS: Same Old Solutions."⁷⁰ According to Kim Phillips Fein, conservatives benefited in the 1970s because "liberalism seemed no longer able to deliver on its promises, even

⁶⁷ Thomas and Mary Edsall, *Chain Reaction: The Impact of Rights, Race, and Taxes on American Politics* (London, 1992).

⁶⁸ Judith Stein, *Running Steel, Running America: Race, Economic Policy, and the Decline of Liberalism* (London, 1998), 195.

⁶⁹ *Ibid.*, 3-6.

⁷⁰ Gary North, 'Why Murray Rothbard Will Never Win the Nobel Prize!' in Walter Block and Llewellyn H. Rockwell, Jr. (eds.) *Essays in Honor of Murray N. Rothbard* (Auburn, AL, 1988), 99-100 (quotation 100).

from the standpoint of economics...[Keynesian economists] were stymied by the simultaneous inflation and unemployment that began to afflict the economy during the decade.”⁷¹

Examination of Walter Heller’s career casts new light on this narrative. Keynesian economists undoubtedly overestimated their abilities to produce a continuously growing economy in the 1960s, but to blame them for the unravelling of economic liberalism is fallacious. In fact, Keynesians like Heller reacted constructively to the unprecedented problems of the 1970s, triggered primarily by the policies of Republican Richard Nixon who ignored the advice of economists such as Heller.⁷² True, Heller lacked the same amount of influence he enjoyed during the 1960s, but this did not stop conservatives writing off his ideas as dangerous and irrelevant. By illuminating the significance of Heller’s Keynesianism to the 1970s and 1980s, this thesis adds to recent scholarship challenging the idea of liberal decline during those decades. As Scott Kamen, Patrick Andelic, and Bruce Miroff have demonstrated, politicians such as Gary Hart and Paul Tsongas emerged in the Democratic Party during the 1970s to help alter it to the new economic and political environment.⁷³ The same is true for Walter Heller, who engaged in an empirically based adaptation of his Keynesianism to the point whereby, before he died in 1987, Heller anticipated President Bill Clinton’s New Democrat approach to economics.

By challenging the notion of Keynesian liberalism’s decline, this thesis builds upon other works that undercut the idea that the 1970s and 1980s were unremittingly

⁷¹ Kim Phillips-Fein, *Invisible Hands: The Businessmen’s Crusade Against the New Deal* (London, 2009), 167.

⁷² Shreve, ‘A Precarious and Uncertain Liberalism,’ 387-448.

⁷³ Scott Kamen, ‘Old Liberals, New Politics: The Americans for Democratic Action and the Transformation of American Liberalism, 1947-1976,’ PhD Thesis, Trinity College Dublin (2016). Author’s copy; Patrick Andelic, ‘Donkey Work: Redefining the Democratic Party in an ‘Age of Conservatism,’ PhD Thesis, University of Oxford (2015). Author’s copy; Bruce Miroff, *The Liberals’ Moment: The McGovern Insurgency and the Identity Crisis of the Democratic Party* (Lawrence, KS, 2009).

conservative. Tim Stanley has analysed Senator Edward Kennedy's challenge to Jimmy Carter in 1980, showing that traditional Keynesian ideas remained popular at that time.⁷⁴ David Courtwright has highlighted how conservatives achieved "little progress on abortion and school prayer, and lost ground on obscenity, gay rights, and legalized gambling" in the 1970s and 1980s.⁷⁵ Gareth Davies has shown that the federal role in education policy continued to grow throughout those decades.⁷⁶ This examination of Walter Heller adds to these works, demonstrating that Keynesian liberalism remained significant in the fourth quarter of the twentieth century.

Because it also argues that, up to the 1960s, liberal Keynesian ideas were more potent and daring than scholars assume, this thesis demonstrates that liberalism was a much stronger force in post-war American politics than historians have appreciated. A new wave of literature has made this argument. Jennifer Delton has shown that the 1950s were anything but a conservative decade.⁷⁷ Jonathan Bell has drawn attention to the strength of liberal ideas in Californian politics from the 1940s to the 1970s.⁷⁸ Doug Rossinow and Kevin Mattson have emphasised the influence of left-wing ideas within the post-war Democratic Party.⁷⁹ This thesis uses Heller's Keynesianism to show that liberalism was a more powerful force in post-war America than appreciated. True, liberalism itself had changed by the final quarter of the twentieth century, which raises the question as to whether Keynesianism remained important to liberal ideas during this period. Liberals placed more emphasis on promoting rights to disadvantaged groups, which extended beyond the issue of jobs to

⁷⁴ Timothy Stanley, *Kennedy vs. Carter: The 1980 Battle for the Democratic Party's Soul* (Lawrence, KS, 2010).

⁷⁵ David Courtwright, *No Right Turn* (London, 2010), 4.

⁷⁶ Davies, *See Government Grow: Education Politics from Johnson to Reagan* (Lawrence, KS, 2007).

⁷⁷ Jennifer Delton, *Rethinking the 1950s: How Anticommunism and the Cold War Made America Liberal* (Cambridge, 2013).

⁷⁸ Bell, *California Crucible: The Forging of Modern American Liberalism* (Philadelphia, PA, 2012).

⁷⁹ Rossinow, *Visions of Progress*; Mattson, *When America Was Great*.

healthcare, environmental protection, social justice, labour reform, and education. However, unemployment stayed a core focus of liberalism in the 1970s and 1980s and proved central to the presidential campaigns of both Bill Clinton and Barack Obama in 1992 and 2008. Even though liberalism became more complex in the final quarter of the twentieth century, Keynesianism still had much value in guiding its assumptions. By building upon attempts to prove the vibrancy of liberalism during the second half of the twentieth century, this thesis reasserts its importance in the American political tradition.

This is also important because, since the mid-1990s, many historians have focused on explaining either the revival or persistence of mid-twentieth century conservatism. Following calls by Alan Brinkley and Michael Kazin, a plethora of literature emerged on this topic.⁸⁰ Though certain scholars pre-empted this development, the first publication that truly grasped the strength of post-war conservatism was Mary Brennan's *Turning Right in the Sixties*.⁸¹ This offered a sophisticated analysis of grassroots conservatism during that decade. Others built upon Brennan's efforts. Lisa McGirr provided further analysis of local conservative activism in the particular case of Southern California.⁸² Others focused on the roles of both Barry Goldwater and George Wallace in explaining either the conservative persistence prior to the 1960s or its political revival during that decade.⁸³ Certain historians focused on some of the key issues that turned voters away from liberalism

⁸⁰ Michael Kazin, 'The Grass-Roots Right: New Histories of US Conservatism in the Twentieth Century,' *American Historical Review*, 97:1 (Feb. 1992), 136-155; and Alan Brinkley, 'The Problem of American Conservatism,' *American Historical Review*, 99:2 (Apr. 1994), 409-429.

⁸¹ Mary Brennan, *Turning Right in the Sixties: The Conservative Capture of the GOP* (Chapel Hill, NC, 1995).

⁸² Lisa McGirr, *Suburban Warriors: The Origins of the New American Right* (Princeton, NJ, 2001).

⁸³ Rick Perlstein, *Before the Storm: Barry Goldwater and the Unmaking of the American Consensus* (New York, 2001); Dan T. Carter, *From George Wallace to Newt Gingrich: Race in the Conservative Counterrevolution* (Baton Rouge, LS, 1996).

during the 1960s, notably racial politics and crime.⁸⁴ Others looked at specific movements that emerged to propel conservatism, such as the legal movement or the rise of youth organisations.⁸⁵ This historiographical development has had two important consequences for this study. It has meant that, until recently, scholars have neglected the strength of liberalism during its post-war heyday. Consequently, historians have overlooked the role of Keynesians like Walter Heller in shaping this moment. Instead, they have helped perpetuate the narrative that conservative forces helped tame, shape, and define the terms under which Keynesianism developed during the post-war years – to the consequent neglect of this doctrine’s influential interactions with liberalism.

IV

This thesis offers a necessary corrective to that neglect. In doing so, it reasserts the importance of Walter Heller to the making of modern America. As mentioned, certain scholars have paid attention to Heller in studies of 1960s public policy. However, not only do they treat him as a secondary actor, Heller has come under criticism for glorifying his achievements during that decade. In his analysis of how Heller tried to sell the 1964 tax cut to both Congress and the public in 1963, Martin Prachowny argued the recollections of Heller and his contemporaries excessively influenced initial assessments of Keynesianism’s highpoint in the 1960s.⁸⁶ For this reason, Prachowny advanced a critical interpretation of Heller, scolding him for failing to deploy the most relevant quantitative model to sell the

⁸⁴ Michael Flamm, *Law and Order: Street Crime, Civil Unrest, and the Crisis of Liberalism in the 1960s* (New York, 2005); Thomas Sugrue, *The Origins of the Urban Crisis: Race and Inequality in Postwar Detroit* (Princeton, NJ, 1996).

⁸⁵ Steven Teles, *The Rise of the Conservative Legal Movement: The Battle for Control of the Law* (Oxford, 2008); John Andrew, *The Other Side of the Sixties: Young Americans for Freedom and the Rise of Conservative Politics* (New Brunswick, NJ, 1997).

⁸⁶ Martin Prachowny, *The Kennedy-Johnson Tax Cut: A Revisionist History* (Cheltenham, 2000), 1-5. For examples see Heller, *New Dimensions of Political Economy*; Arthur Okun, *The Political Economy*

Kennedy-Johnson tax cut to Congress in 1963.⁸⁷ This argument is refuted in Chapter Five of this thesis. Nevertheless, Hugh Norton earlier made the point that Heller helped shape the initial historical debate about his legacy. He wrote, “One can seldom determine how much routine policy [during the Kennedy-Johnson years] was glamorized and made to seem important by observers who were on the scene.”⁸⁸ Consequently, Norton exercised caution in his evaluation of Heller, arguing the performance of the CEA under Heller’s stewardship did not live up to its potential.⁸⁹

Norton and Prachowny’s assessments contrasted with contemporary works that covered Heller’s CEA chairmanship. Published in the mid-1960s, these included studies undertaken by Edward Flash, Seymour Harris, Hobart Rowen, and E. Ray Canterbury.⁹⁰ Flash credited Heller for turning the CEA into “the most single creative force in the development of a new approach to economic policy.”⁹¹ Not only did Heller convince Kennedy to promote the 1964 tax cut, he successfully persuaded other advisers to support that policy. Undoubtedly, scholars must treat the recollections of their subjects with care, as Prachowny and Norton did. Nevertheless, this thesis’ assessment of Heller conforms to the more favourable interpretation advanced by his contemporaries. It argues he was one of the most impressive presidential advisers of modern times.

The fact debate concerning Heller has mostly concerned his role as CEA chairman also illuminates the extent to which scholars have neglected the broader lens that he offers onto the development of post-war Keynesian liberalism. This thesis

of Prosperity (Washington DC, 1970); Tobin, *The Intellectual Revolution in US Economic Policy-Making* (London, 1966).

⁸⁷ Prachowny, *The Kennedy-Johnson Tax Cut*, 5, 11, 48-101.

⁸⁸ Hugh Norton, *The Employment Act and the Council of Economic Advisors* (Columbia, SC, 1977), 189.

⁸⁹ *Ibid*, 190-191.

⁹⁰ Flash, *Economic Advice and Presidential Leadership*, 173-275; Harris, *Economics of the Kennedy Years*, 23; Rowen, *The Free Enterprisers*, 153-182; Canterbury, *Economics on a New Frontier*, 12-13, 139-152, 263-270, 298-301.

helps rectify that neglect. To achieve its aims, it follows Heller's career chronologically. Chapter One lays the foundations for the dissertation by detailing how Keynesianism emerged and evolved in the US up to the mid-1950s, the point Heller started to become well-known. It defines Keynesianism, illustrates how it fused with liberalism during the 1930s, and explains that during the post-war period, certain liberals developed a more expansive iteration of Keynesian ideas than did the business community. This lays the foundations for Chapter Two, which introduces Heller and focuses on his career up to the beginning of the 1960s. It shows that although Heller played a role in helping fashion a conservative Keynesianism during the late 1940s, he embraced the more daring and expansionist iteration of the doctrine by the late 1950s, eventually emerging as one its foremost champions.

Chapter Three examines Heller's first year in the Kennedy administration. It demonstrates that, during 1961, Heller was unsuccessful at convincing JFK to move beyond implementing conservative Keynesianism, but argues that he laid the foundations for JFK to do so later in his presidency. Chapter Four focuses upon 1962 and shows how Heller convinced JFK to promote his potent ideas. It undercuts the idea the business community convinced JFK to embrace a tax cut, showing instead Heller and Kennedy persuaded businesspersons to adopt liberal Keynesianism. Chapter Five examines how Heller and Kennedy sought to sell liberal Keynesianism to both Congress and the public in 1963. It shows that, before Kennedy's assassination in November, Heller played a significant role in helping push the tax cut through Congress.

Chapter Six surveys how Heller worked with Lyndon Johnson to secure enactment of that measure. It also examines Heller's contribution to the development

⁹¹ Flash, *Economic Advice and Presidential Leadership*, 271.

of Johnson's Great Society programme of liberal reform, thereby illustrating how Keynesian liberalism reached its peak in the mid-1960s. It acknowledges that certain Great Society programmes did not achieve all they set out to do, but offers a positive assessment of Heller's contribution to the Great Society's development. Chapter Seven assesses Heller's response to both the inflation generated by the Vietnam War and the rise of monetarist theory in the mid-to-late 1960s. The chapter is critical of Heller for the advice he gave Johnson throughout this period, but praises him for responding in a far more effective manner to the rise of monetarism than appreciated by existing scholarship. Chapter Eight deals with the way Heller reacted to both the onset of stagflation and the rise of Reaganomics in the 1980s, arguing he responded in an effective manner to these two developments. In doing so, it helps show that economic liberalism stayed vibrant in the final quarter of the twentieth century.

V

A positive appraisal of Heller emerges from this thesis. It not only augments the claims advanced in contemporary studies of his CEA chairmanship, it also offers a strong endorsement of the way he acted as an agent of Keynesian liberalism both before and after this period. By providing the first comprehensive analysis of Walter Heller's career, using his hitherto untapped personal papers at the University of Minnesota, this thesis breaks new ground in the literature on presidential advisers.⁹² It also re-examines certain interpretations about the post-war vibrancy of Keynesian liberalism and gives an overview of the rise, ascendancy, and eclipse of Keynesian political economy in the United States. This sets the thesis apart from existing historical surveys of that doctrine that have only analysed Keynesianism's rise to the

⁹² The thesis also makes use of two interviews conducted by the author. The author obtained approval from the UCL Research Ethics Committee for both interviews. Each interviewee also signed a consent form. This project's UCL Ethics ID Number is 6516/002.

mid-1960s.⁹³ This dissertation is also suggestive of how current policymakers and economists can learn from Heller's career, particularly in an era when Keynesianism has made a partial and incomplete comeback.

⁹³ See Stein, *The Fiscal Revolution in America*; and Collins, *The Business Response to Keynes*.

Chapter One

The Keynesian Revolution in America, 1933-1955

In 1936, *The General Theory of Employment, Interest, and Money* debuted in the United States. Written by British economist John Maynard Keynes, *The General Theory* advanced an innovative approach to end the Great Depression. Considered “a leading authority on economic theory and policy,” Keynes and his ideas encountered fierce opposition from his transatlantic peers, most of whom saw nothing wrong with the ‘classical’ economics that Keynes so vigorously challenged.⁹⁴ Over the next twenty-five years, however, Keynes’ ideas eventually gained credence. In the early 1960s, policymakers implemented them to an extent unimaginable during the Depression, bringing the Keynesian revolution in America to its peak. This thesis outlines how that revolution was developed, consolidated, and defended by exploring the career of Walter W. Heller, but before doing so, it is essential to understand what Keynesianism was.

This is important, not least because Keynes’ ideas broke substantially with prevailing economic wisdom during the 1930s before going through three significant manifestations up to the mid-1950s. The first occurred during the late 1930s, whilst the second and the third both concurrently rose to prominence in the post-war years. Accordingly, this chapter starts by explaining what Keynes argued during the 1930s – particularly in relation to the severity of the Depression and the existing doctrines that he challenged – before outlining the extent to which his ideas gained credibility prior to the first manifestation. It then describes each manifestation in turn, taking the history of Keynesianism’s rise to the mid-1950s. Only after defining the doctrine and outlining its evolution up to this period can one fully appreciate Keynesianism’s post-

⁹⁴ Breit and Ransom, *The Academic Scribblers*, 67.

war interaction with liberal political ideas.

I

The 1930s were the most miserable years in twentieth century American history. In the four years prior to Franklin Roosevelt's inauguration in March 1933, unemployment rose from 3 percent to 25 percent of the labour force, whilst consumption and GNP both fell by 20 percent and 30 percent respectively.⁹⁵ Roosevelt's predecessor, the Republican Herbert Hoover, did engage in anti-Depression activism. Nevertheless, his policies fell woefully short of producing full recovery, leading to Roosevelt's election in November 1932. Hoover's response to the Depression signified that, in the early 1930s, most people believed the private economy would correct itself.⁹⁶ This was an idea strongly linked to classical economics and it had deep historical roots in America. Indeed, when depressions hit the economy at various times in the nineteenth century, the belief that economic crises were not the responsibility of the federal government prevented every president from intervening to facilitate recovery.⁹⁷

Throughout the 1930s, classical economists argued the main way the economy would correct itself was through workers accepting reductions to their wages, a process they viewed as natural. This would enable businesses to expand employment and thereby boost production, the factor classical economists identified as crucial to economic expansion. When he started teaching economics in 1908, Keynes was a supporter of this line of thinking. The failure of recovery to materialise during the early 1930s led him to reconsider his views, culminating in the publication of his *magnum opus* in February 1936. It is worth noting that Keynes was certainly not alone in questioning classical economics, particularly the argument production drove

⁹⁵ Morgan, *Deficit Government: Taxing and Spending in Modern America* (Chicago, IL, 1995), 20.

the economy forward. The popular economists William Foster and Waddill Catchings had done so at the end of the 1920s, whilst from 1931 so did Utah banker and future Federal Reserve chairman Marriner Eccles.⁹⁸ Nevertheless, classical economics still held considerable sway by the mid-1930s, primarily because it remained a doctrine that “no one [had] succeeded in making a strong *theoretical* case against.”⁹⁹

Keynes did that. He showed cogently in *The General Theory* that reductions in wages would not precipitate recovery from the Depression. This was mainly because unemployment was so severe that a serious lack of overall demand prevented consumers from buying goods and services.¹⁰⁰ Businesses were thus unable to take on more workers, even if they were willing to work for lower pay. Accordingly, the economy was stuck in a continuous cycle of unemployment and depression and the only way out was if the government intervened, primarily by boosting demand. To do this, Keynes argued for deliberate deficit spending, saying this would stimulate mass purchasing power, boost consumption, and thereby reflate the economy by creating a “multiplier effect” stimulus.

According to Keynes, increasing purchasing power would encourage people to spend more money, and those paid this money would spend it, creating a significant increase in consumption that would at least double the government’s original outlay.¹⁰¹ This would significantly drive up employment, induce businesses to increase investments, and thereby generate recovery. Hence, boosting consumption by stimulating mass purchasing power formed the Keynesian remedy for the

⁹⁶ Tom Kemp, *The Climax of Capitalism* (London, 1990), 73-75.

⁹⁷ Davis, ‘Politics of Prosperity,’ 7-8.

⁹⁸ Brinkley, *The End of Reform*, 75-85.

⁹⁹ Alvin Hansen, *A Guide to Keynes* (New York, 1953), 6. Emphasis added.

¹⁰⁰ John Maynard Keynes, *The General Theory of Employment Interest and Money* (London, 1936). The ensuing discussion of Keynes’ ideas relates to 15-17, 28-29, 55, 95-98, 112-131, 128-129, 257-271, 374-378.

¹⁰¹ Morgan, *The Age of Deficits: Presidents and Unbalanced Budgets from Jimmy Carter to George W. Bush* (Lawrence, KS, 2009), 25.

Depression. To achieve this, Keynes called for deliberate deficit spending on relief, public works, and credit as the fastest means of putting money into peoples' pockets. Importantly, Keynes did not envisage a permanent expansion of the public sector. Instead, he wanted to scale back deficit spending – or 'pump priming' – as soon as the private economy recovered. He pressed this argument upon Roosevelt both before and after publication of *The General Theory*, but he did not persuade the president of the merits of his approach.

II

As soon as he came to power in March 1933, FDR sought to revive the economy by enacting a programme called the New Deal. As early as December 1933, Keynes tried to influence New Deal policy. He did this by penning an Open Letter to Roosevelt that called on the president to increase purchasing power through "governmental expenditure which is financed by loans."¹⁰² He followed this up with a trip to the US in the summer of 1934. Here, he personally met FDR and again stressed the need to run deficits. Roosevelt was unreceptive to Keynes' approach. True, the president did run deficits every single year of his presidency, but when he took office FDR viewed them only as temporary and humanitarian solutions to the nation's problems, certainly not as a route to full recovery.¹⁰³ Instead of embracing Keynesianism, Roosevelt preferred both to balance the budget and promote sound finance during the early-to-mid-1930s.¹⁰⁴ He believed this would facilitate recovery by boosting confidence in the private sector.

Additionally, FDR implemented a mixture of reforms, regulations, and redistributive measures as part of the early New Deal. These aimed to punish big

¹⁰² Keynes, 'An Open Letter to President Roosevelt,' *New York Times*, 31 December 1933. Available at: <http://newdeal.feri.org/misc/keynes2.htm> [Accessed 03/05/2015]

¹⁰³ Collins, *The Business Response to Keynes*, 3-4.

¹⁰⁴ Stein, *The Fiscal Revolution in America*, 60-68.

business and monopolies for reckless behaviour during the 1920s, reorder society along fairer lines, and provide psychological and institutional supports to increase levels of business activity. This initial emphasis on what Alan Brinkley dubbed “reform” signified the emergence of modern liberal ideology in America.¹⁰⁵ Modern liberalism built upon the legacy of 1920s progressives by accepting the state had a responsibility to promote and manage the economy. Accordingly, the New Deal eschewed classical economics. As Roosevelt said, New Deal liberalism “was plain English for a changed concept of the duty and responsibility of government toward economic life.”¹⁰⁶ However, his focus on reform helped ensure Keynesian theory did not initially feature as a key element of New Deal policy. Keynes described this as misguided, not least because reform placed little emphasis upon recovery. As he told the president in December 1933, it was first essential to revive the private economy, only after should the government think of overhauling it.¹⁰⁷

Roosevelt’s commitment to reform diminished towards the end of 1937, however. This cleared the path for him to embrace deficit spending partially. The reasons for this were threefold. Firstly, the Supreme Court had declared many early New Deal measures, such as the National Industrial Recovery Act, unconstitutional by the mid-1930s. Secondly, Roosevelt’s failed attempt in 1937 to pack the Supreme Court with justices who would uphold those measures made it difficult to implement further pieces of similar legislation.¹⁰⁸ Thirdly, these developments occurred just as Roosevelt’s adherence to sound finance proved disastrous. Believing the economy was finally on the road to recovery, he took drastic actions in early 1937 to balance the budget by Fiscal Year (FY) 1938. This coincided with both a tightening of

¹⁰⁵ Brinkley, *The End of Reform*, 3-5.

¹⁰⁶ Cited in *Ibid*, 10.

¹⁰⁷ Keynes, ‘An Open Letter to President Roosevelt.’

¹⁰⁸ Brinkley, *The End of Reform*, 18-20.

monetary policy and a scheduled collection of social security taxes, all of which drained demand from the economy and produced a recession within the Depression.

This incident “demonstrated to many people the powerful effect of changes in the budget position upon the economy.”¹⁰⁹ It had a decisive impact upon many of Roosevelt’s closest advisers, particularly Harry Hopkins, Leon Henderson, Harrold Ickes, and Thomas Corcoran. They were familiar with the ideas of Foster and Catchings as well as other advocates of deficit spending during the 1930s, including the Harvard economist and New Deal adviser Lauchlin Currie. Nevertheless, it was not until the onset of the 1937-38 recession that they fully grasped the potential of fiscal policy to reflate the economy.¹¹⁰ As noted by Richard Adelstein, also appealing to these individuals was fiscal policy offered a technical solution to economic management that eschewed radical experimentation.¹¹¹ In turn, they urged Roosevelt to abandon reform and embrace pump priming, a decision the president – after much debate in his administration – took.¹¹² The 1937-38 recession thus precipitated “a restatement of the New Deal philosophy, turning it towards the values implicit in [Keynes’ approach].”¹¹³

On April 14, 1938, the US government intentionally employed deficit spending as its chief weapon against the Depression. On that day, Roosevelt asked Congress for \$3 billion in emergency expenditures and used Keynesian rhetoric to justify his request.¹¹⁴ This caused a significant rise in the deficit from \$0.1 billion in

¹⁰⁹ Stein, *The Fiscal Revolution in America*, 114.

¹¹⁰ Brinkley, *The End of Reform*, 83-84.

¹¹¹ Richard Adelstein, “The Nation as an Economic Unit’: Keynes, Roosevelt, and the Managerial Ideal,’ *Journal of American History*, 78:1 (Jun. 1991), 160-187.

¹¹² Collins, *The Business Response to Keynes*, 69-71.

¹¹³ Dean May, *From New Deal to New Economics: The Liberal Response to the Recession* (New York, 1981), 160.

¹¹⁴ Franklin Delano Roosevelt, ‘Message to Congress on Stimulating Recovery,’ 14 April 1938. APP.

FY 1938 (0.1 percent of GDP) to \$2.9 billion by FY 1940 (3 percent of GDP).¹¹⁵ However, although Roosevelt eventually made use of deficit spending in the late 1930s, it would be wrong to describe the deficits for FYs 1938-40 as truly Keynesian. In fact, the deficits FDR ran during those years were too small to boost recovery meaningfully.¹¹⁶ Thus, despite his 1938 “conversion” Roosevelt “engaged in a salvaging program and not in a program of positive expansion.”¹¹⁷ Keynes, too, acknowledged this. In July 1940, he wrote disappointedly that only “war conditions” could “organise expenditure on the scale necessary to make the grand experiment which would prove my case.”¹¹⁸

After reluctantly running deficits early in his presidency, Roosevelt hesitantly accepted their use following the 1937-38 recession. This demonstrated that ideas akin to Keynesianism had gained credence by the end of the 1930s. It is important to note that the reform impulse of the New Deal did not simply end after 1937, but the programme’s architects downgraded its significance. This ushered in the start of what John W. Jeffries called a “‘new’ New Deal,” a core part of which featured liberals making use of deficit spending to manage the economy.¹¹⁹ No sooner did this development occur, than certain academics directly influenced by Keynes expressed concern the American economy had grown mature and stagnant, having seen proof of this in the 1937-38 recession. In response, they adapted the British economist’s ideas and came up with a new policy for Roosevelt, one more radical than pump priming. Later described by Margaret Weir and Theda Skocpol as “social Keynesianism,” this

¹¹⁵ Unless otherwise stated, all figures in this thesis relating to the size of the deficit as a percentage of GDP are from ‘Historical Tables of the President’s Budget, FY 2016.’ Available at: <https://www.whitehouse.gov/omb/budget/Historicals>, Tables 1.1 and 1.2 [First accessed 05/19/2015]

¹¹⁶ Morgan, *Deficit Government*, 39.

¹¹⁷ Hansen, *Fiscal Policy and Business Cycles* (London, 1941), 84.

¹¹⁸ Cited in Patrick Renshaw, ‘Organised Labour and the Keynesian Revolution,’ in Stephen Baskerville and Ralph Willett (eds.) *Nothing Else to Fear: New Perspectives on America in the Thirties* (Manchester, 1985), 231.

new policy constituted the first manifestation of Keynes' ideas in the United States.¹²⁰ By the mid-1940s, it was an integral feature of the 'new' New Deal.

III

The efforts of economist Alvin Hansen were central to the development of social Keynesianism. Born in Viborg, South Dakota, in 1887, Hansen obtained his PhD in 1918 from the University of Wisconsin and then joined the University of Minnesota, where he stayed for eighteen years. Here, Hansen "was, by contemporary standards, an orthodox economist...His 1927 work on the business cycle was widely accepted as a standard reference in that field."¹²¹ Hansen's orthodoxy was also evident in a very sceptical review he wrote of *The General Theory*, in which he concluded that Keynes' new book was "not a landmark in the sense that it lays a foundation for a 'new economics.'"¹²² He only embraced Keynesianism during the 1937-38 recession but would champion the doctrine throughout the rest of his career, leading many to label him the 'American Keynes.'¹²³

Hansen's conversion to Keynesianism coincided with his move to Harvard in 1937. There, he provided "a breath of fresh air" to the Economics Department's young graduate students, who saw little merit in the classical economics preached by their professors.¹²⁴ They enthusiastically signed up to Hansen's famous fiscal policy seminar, where alongside key Washington policymakers they debated how to apply Keynesian theory in America. Hansen "was active and persistent in looking for

¹¹⁹ John W. Jeffries, 'The 'New' New Deal: FDR and American Liberalism, 1937-1945,' *Political Science Quarterly*, 105:3 (Aut. 1990), 397-418.

¹²⁰ Weir and Skocpol, 'State Structures and Social Keynesianism: Responses to the Great Depression in Sweden and the United States,' *International Journal of Comparative Sociology*, 24 (Mar. 1983), 4-29.

¹²¹ Breit and Ransom, *The Academic Scribblers*, 85.

¹²² Hansen, 'Mr. Keynes on Underemployment Equilibrium,' *Journal of Political Economy*, 44:5 (Oct. 1936), 34.

¹²³ Breit and Ransom, *The Academic Scribblers*, 84.

¹²⁴ Walter S. Salant, 'Alvin Hansen and the Fiscal Policy Seminar,' *The Quarterly Journal of Economics*, 90:1 (Feb. 1976), 16.

positive programs that would make the economy work better, and he had definite views about what should be done.”¹²⁵ He took these views to Washington in the late 1930s, where he joined both the National Resources Planning Board (NRPB) and the Federal Reserve as a part-time consultant. In Washington, Hansen played a crucial role in the development of the ‘new’ New Deal. However, one factor distinguished his Keynesianism from Roosevelt’s ‘Keynesian’ advisers. This was Hansen did not believe private investment could “be raised to a point where deficit financing can be suspended.”¹²⁶ Instead, he saw the 1937-38 recession as proof the private economy had grown solely reliant upon fiscal and monetary stimuli, which meant that pump priming would not do enough to get the economy consistently running at full capacity. This, he argued, was because the Depression was more a structural rather than a cyclical phenomenon, something “hinted at by Keynes” during the 1930s.¹²⁷

To substantiate his case, Hansen argued the factors that previously spurred private investment and thereby underpinned economic expansion were no longer available to do so.¹²⁸ One was the rate of population growth, which had decreased by half during the Depression. Another was the cessation of territorial expansion in the early twentieth century, a development that had left fewer natural resources for private enterprise to exploit. A third was the lack of technological progress during the 1930s. On this last point, Hansen pointed out the growth of the railways and the development of electricity both previously spurred prominent levels of private investment. The rise of the automobile during the 1920s had done the same. Yet, no innovations appeared on the horizon during the 1930s. For Hansen, the factors that

¹²⁵ Ibid, 21.

¹²⁶ Lewis Kimmel, *Federal Budget and Fiscal Policy, 1789-1958* (Washington DC, 1959), 199.

¹²⁷ Theodore Rosenof, *Economics in the Long Run: New Deal Theorists and Their Legacies*, (London, 1997), 53.

previously spurred private investment had all but disappeared. As a result, the US was experiencing a phenomenon in which economic growth was short-lived and depressions were the norm.¹²⁹ This explained why the private economy went back into recession following the withdrawal of fiscal and monetary stimuli in 1937.

Hansen argued only permanent deficit spending could compensate for the structural problems holding back private investment. He contended the deficit needed to be large enough to keep the national income at around \$60 billion a year, the smallest level he felt necessary to reassure private enterprise of enough demand.¹³⁰ Only then would businesses boost investments, which would spur productivity and keep the nation at full employment. Importantly, Hansen advocated protracted deficit spending for more than just economic reasons. This was because increased outlays on healthcare, education, housing, the environment, and urban renewal would be socially beneficial.¹³¹ Additionally, Hansen wanted to consolidate the redistributive achievements of the early New Deal by calling for an expanded system of social security, unemployment insurance, and old age pensions. His forceful advocacy of permanent deficit spending, buffered by social welfare provision, proved crucial in turning the 'new' New Deal away from pump priming and towards his approach, described by Weir and Skocpol as social Keynesianism.¹³²

Hansen was not alone in his view that only permanent deficit spending could secure future prosperity. In 1938, a group of economists from Harvard and Tufts published *An Economic Program for American Democracy*, in which they advanced a

¹²⁸ The ensuing discussion comes from Hansen's following publications: 'Economic Progress and Declining Population Growth,' *American Economic Review*, 29:1 (Mar. 1939), 1-15; *Full Recovery or Stagnation* (London, 1938), 28-30, 273-315; and *Fiscal Policy and Business Cycles*, 347-365, 445-446.

¹²⁹ Hansen, Comments in Debate with David Coyle and Robert Warren, 5 October 1938. Alvin Harvey Hansen Papers. Call No. HUG (FP) 342. Box 4. Harvard University Archives.

¹³⁰ Hansen, 'Economic Progress and Declining Population Growth,' 14.

¹³¹ Tobin, 'Hansen and Public Policy,' *Quarterly Journal of Economics*, 90:1 (Feb. 1976), 35.

¹³² Jeffries, 'The 'New' New Deal,' 402-405.

similar case to Hansen.¹³³ However, many economists took issue with the idea the American economy had become mature and stagnant. Some pointed out that private investment did not depend upon territorial expansion, whilst others argued the rate of population growth started to reverse as far back as the 1850s with little effect on the economy.¹³⁴ Rather than attributing the lack of private investment during the 1930s to the structural factors identified by Hansen, the critics of social Keynesianism blamed “increases in tax burdens, other increases in costs, and the generally adverse reaction of the investing and business community to the New Deal’s policies.”¹³⁵ For them, the “possibilities of further development of private enterprise *are* adequate to absorb the nation’s capital and labour resources for many years to come,” so there was no need for prolonged deficit spending.¹³⁶

As the Depression gave way to World War II, it quickly became clear there was an element of legitimacy to these critiques. Between FYs 1941-46, increased defence spending caused a large rise in the deficit from 3.1 percent of GDP to 21 percent of GDP. This underwrote a 56 percent rise in real GNP, as well as a 1943-45 unemployment rate of less than 2 percent.¹³⁷ The economic boom legitimised Keynesian economics. However, it also showed the social Keynesians the economy, far from suffering from stagnation, had enormous potential to grow. This did not stop Hansen from continuing to argue for social Keynesian policies. Rather than abandon his proposals the Harvard economist simply reformulated the rationale underpinning them. He did this by arguing wartime economic growth was a temporary phenomenon

¹³³ Richard Gilbert et al, *An Economic Program for American Democracy* (New York, 1938)

¹³⁴ George Terborgh, *The Bogey of Economic Maturity* (Chicago, IL, 1945), 76; James Angell, *Investment and Business Cycles* (New York, 1941), 261-265.

¹³⁵ Angell, *Investment and Business Cycles*, 279.

¹³⁶ This was the view of the Brookings Institution, which published a report on the stagnation thesis in 1940. See ‘What Holds Back Business,’ *New York Times*, Editorial, 27 May 1940, 17. PQHN. Emphasis added.

¹³⁷ Morgan, *Deficit Government*, 47.

and that the economy would go back into depression at that conflict's end, something that developed into a very prominent concern by the end of the war. Exemplifying this, in 1942 Hansen wrote a NRPB report called *After the War – Full Employment*, in which he explained a “positive program of post-war expansion...boldly conceived and vigorously pursued, is imperative.”¹³⁸ He followed this up in 1943 by calling for the government to sustain a post-war national income of \$70 billion, as this would eradicate “fears that private manufacturers, retailers, wholesalers, and farmers will not come forward and supply the market” with goods.¹³⁹

As the end of World War II drew near, social Keynesianism was a central feature of the ‘new’ New Deal. Importantly, as he continued to advance and reformulate his proposals, Hansen found dedicated support for them amongst members of the Democratic Party. This included Franklin Roosevelt, who feared a large-scale post-war slump. Reflecting this, FDR's 1944 Economic Bill of Rights address outlined ambitious plans to sustain post-war full employment and expand social welfare, which Hansen called for in his 1942 NRPB report.¹⁴⁰ Roosevelt's death in April 1945 left unanswered just how far he would have implemented social Keynesianism. Nevertheless, Senator James E. Murray of Montana moved it onto the policy agenda at Roosevelt's behest. In early 1945, Murray proposed the Full Employment bill to ensure post-war full employment through permanent deficit spending.¹⁴¹ This measure met scathing criticism from the right, whose revived power in wartime had brought about the NRPB's abolition in 1943.¹⁴² This conservative

¹³⁸ Hansen, *After the War-Full Employment* (Washington DC, 1942), 1.

¹³⁹ Hansen, ‘The Postwar Economy,’ in Harris (ed.) *Postwar Economic Problems* (New York, 1943), 22, 14 (quotation).

¹⁴⁰ Roosevelt, ‘State of the Union Message to Congress,’ 11 January 1944. APP; Hansen, *After the War-Full Employment*, 1-19.

¹⁴¹ For insightful contemporary analysis of the bill see James G. Patton, ‘A Plan for Prosperity,’ *New Republic*, 111:19 (Nov. 1944), 587. Online at EBSCOhost [Henceforth EBSCO]

¹⁴² For the wartime conservative revival see Weir, *Politics and Jobs: The Boundaries of Employment Policy in the United States* (Princeton, NJ, 1992), 51.

resurgence caused the eclipse of social Keynesianism and its replacement in peacetime by a less activist iteration of Keynes' ideas, later described as "commercial Keynesianism." This new manifestation completely defined post-war economic policy right through to the late 1950s.

IV

Crucial to the development of commercial Keynesianism were the efforts of the corporate community. Its members completely opposed protracted deficit spending, considering it inflationary, socialistic, and inappropriate for a peacetime economy that was fundamentally strong and abundant.¹⁴³ Contrary to Hansen's prediction that there would be a post-war Depression, the release of pent-up consumer spending guaranteed a surge of post-war economic growth. This underwrote a huge expansion of the American economy from 1945 onward. Roosevelt's successor, Harry Truman, thus presided over a prosperous and booming economy, one that was also very large, more complex, and more internationalised compared with the Depression years.

Two business groups, the National Association of Manufacturers (NAM) and the Chamber of Commerce of the United States (COCUS), played important roles in preventing enactment of a post-war social Keynesian agenda.¹⁴⁴ Under their influence, Congress enacted the Employment Act of 1946 in place of the Full Employment bill that epitomised Hansen's ideas. This only provided a vague and ill-defined federal commitment to sustain maximum employment, which signified the failure of social Keynesianism.¹⁴⁵ It is essential to note, however, that passage of the Employment Act certainly did not amount to what historian Robert Collins described

¹⁴³ Stephen Bailey, *Congress Makes a Law: The Story Behind the Employment Act of 1946* (New York, 1950), 129-149.

¹⁴⁴ Ibid, 129-149; Collins, *The Business Response to Keynes*, 100-109.

as “a significant victory for moderate conservatives.”¹⁴⁶ Whatever its shortcomings, a strong case supports the idea the final measure constituted a “victory for the so-called liberals.”¹⁴⁷

As W. Robert Brazelton and Hugh Norton have argued, the Employment Act offered considerable scope for bold and expansionary post-war policies.¹⁴⁸ Exemplifying this, the Executive Director of liberal interest group Union for Democratic Action, James Loeb, wrote shortly before the bill’s passage that he and his colleagues “have not been fighting a battle of catch phrases or slogans. We have been fighting for a Congressional statement of policy which would require that it is the responsibility of the federal government to use all its vast resources to assure employment opportunities to all of our citizens able to work and seeking work. This is accomplished.”¹⁴⁹ It is of little surprise that many conservatives remained threatened by the measure, even though it contained no explicit commitment to implement social Keynesianism. As noted by Amy Davis, its pledge to sustain “maximum employment” suggested there remained considerable scope for “a frightening experiment in economic planning.”¹⁵⁰ However vague its terms, the Employment Act thus offered liberals the means to advance activist and expansionary policies.

As a result, certain segments of the business community reworked Keynes’ ideas in the late 1940s and came up with a policy restricting the need to implement such measures. This precipitated the development of what Herbert Stein and Robert

¹⁴⁵ Harry Truman, ‘Statement by the President upon Signing the Employment Act,’ 20 February 1946. APP.

¹⁴⁶ Collins, *The Business Response to Keynes*, 109.

¹⁴⁷ W. Robert Brazelton, *Designing US Economic Policy*, 21.

¹⁴⁸ Ibid, 21; Norton, *The Employment Act and the Council of Economic Advisors*, 100.

¹⁴⁹ James Loeb, ‘Draft Letter to President Truman,’ 7 February 1946. Americans for Democratic Action Papers. [Henceforth ADA Papers]. Reel 6. British Library [Henceforth BL]

¹⁵⁰ Davis, ‘Politics of Prosperity,’ 14.

Collins respectively described as “domesticated,” or “commercial,” Keynesianism, a conservative manifestation of Keynesianism that, according to Stein, “profoundly influenced fiscal discussion, fiscal thinking, and fiscal policy in the two decades that followed it.”¹⁵¹ Central to its formulation was the Committee for Economic Development (CED), a business group established in 1942 that rose to prominence later in the decade. Unlike COCUS and the NAM, the CED was a progressive organisation that prided itself on offering technical rather than partisan advice. The group rejected the ideas of the Keynes-Hansen school, but recognised a return to Depression-era conditions would be disastrous. Conscious of this, the CED “sought a middle path between statist formulas for the organization of society and the traditional laissez-faire creed of conservatives.”¹⁵² Additionally, the CED acknowledged the importance of maintaining an affluent peacetime economy in the newly forged Cold War climate, as this would enable America to fulfil its expanded role in global affairs.¹⁵³ For these reasons, the CED believed the government should guarantee a strong and stable post-war economic system, so it endorsed the use of limited Keynesian measures.

In 1947, the CED developed the ‘stabilizing budget policy,’ the underlining

¹⁵¹ They both used different terms to define post-war Keynesianism, with Stein describing “commercial Keynesianism” as “misleading” because it implied the business community in general tamed post-war Keynesianism (for him, the CED consisted of “businesspeople outside the mainstream of the business community”). However, both “commercial Keynesianism” and “domesticated Keynesianism” still denoted the importance both afforded progressive business leaders in shaping a watered-down iteration of post-war Keynesianism. Thus, the use of different terminology pertained to a minor disagreement regarding who exactly in the business community outside the CED was important to this. For further discussion see Julien Zelizer, *Taxing America: Wilbur D. Mills, Congress, and the State, 1945-1975* (Cambridge, 1998), 149. Footnote 6; Stein, ‘The Fiscal Revolution in America, part II: 1964-1994,’ in W. Elliot Brownlee (ed.) *Funding the Modern American State, 1941-1995: The Rise and Fall of the Era of Easy Finance* (New York, 1996), 195. Footnote 1. Robert Lekachman coined the phrase “commercial Keynesianism” in *The Age of Keynes*, 287 and Collins adopted it in *The Business Response to Keynes*, 17. Stein’s quote in the main body is from 227 of *The Fiscal Revolution in America*. For similar sentiment from Collins see *The Business Response to Keynes*, 115–211. This thesis adopts the phrase “commercial Keynesianism” as it is more common in the scholarly literature on post-war political economy.

¹⁵² Collins, *The Business Response to Keynes*, 85.

¹⁵³ Ibid, 132.

feature of commercial Keynesianism. In contrast to permanent deficit spending, the stabilizing budget policy sought to use fiscal policy to moderate the fluctuations of the business cycle, purely to maintain economic stability. For the CED, this entailed relying upon the automatic stabilisers built into the taxation system rather than discretionary measures. Automatic stabilisers were the automatic decline in tax receipts and increased outlays on unemployment insurance that naturally accompany a recession due to the fall in the national income. Accordingly, the CED argued the government should set tax rates to yield an expansionary deficit automatically during a recession, followed by a moderate surplus to keep inflation at bay and to pay off debt when the economy recovered, with the goal of balancing the budget over the course of the business cycle.¹⁵⁴

Though the stabilizing budget policy's guiding principle was automaticity, the CED approved use of discretionary policies (such as tax cuts, increased expenditures, lower interest rates, and an expansion of the money supply) during serious downturns. However, it argued in favour of using the monetary, not fiscal, side of economic-management and only sanctioned discretionary fiscal activism as a last resort.¹⁵⁵ Accordingly, the CED campaigned for the termination of the "peg" agreement reached between the Treasury and the Federal Reserve during World War II to help fund US involvement in that conflict. The Fed bought Treasury securities at pre-determined price levels, which stripped it of its powers to manipulate interest rates. The eventual termination of the peg in 1951 liberated monetary policy and further bestowed legitimacy upon the CED's ideas.¹⁵⁶

In the late 1940s and early 1950s, a consensus crystallised around the use of

¹⁵⁴ CED, *Taxes and the Budget* (1947), 27-32.

¹⁵⁵ CED, *Monetary and Fiscal Policy for Greater Economic Stability* (1948); and *Flexible Monetary Policy* (1953).

¹⁵⁶ Stein, *The Fiscal Revolution in America*, 242-280.

the stabilizing budget policy. Conservatives welcomed the fact it broadly adhered to the principles of sound finance, whilst liberals were pleased automatic stabilisers would safeguard the economy from large-scale unemployment.¹⁵⁷ True, certain liberals preferred discretionary fiscal measures to the combination of automaticity and discretionary monetary policies.¹⁵⁸ However, deficiencies in economic forecasting, the wartime development of a large and efficient withholding taxation system, and the fact discretionary fiscal measures were subject to congressional approval, all persuaded them to accept built-in flexibility.¹⁵⁹

Resultantly, a goodly number of liberals embraced commercial Keynesianism. This mirrored the broader movement of liberal ideals to the centre during the late 1940s. Exemplifying this, in 1949 sixteen prominent economists with very different viewpoints, including Keynesians Paul Samuelson and John Kenneth Galbraith, signed the ‘Princeton Manifesto.’¹⁶⁰ This document recommended a “policy system centered on ‘automatic flexibility’” to manage the economy.¹⁶¹ It played a role in convincing presidents Harry Truman (1945-53) and Dwight Eisenhower (1953-61) to follow the guidelines of the stabilizing budget policy throughout their presidencies, although neither explicitly acknowledged doing so. When recessions hit the economy in 1948-49 and 1953-54, each refused to increase discretionary spending and instead relied upon automatic stabilisers and, in Eisenhower’s case, an expansionary

¹⁵⁷ Paul Samuelson, ‘Built-in Stabilizers of Our Economy,’ *The Reporter*, 17 February 1953, 13-15. BL.

¹⁵⁸ Ibid. See too Heller, ‘Postwar Municipal Finance in National Economy,’ Speech, St Louis, 15 June 1944, reprinted in *American Civic Annual*, 15 (1946), 61-72.

¹⁵⁹ Karl Schriftgiesser, *Business and Public Policy: The Role of the Committee for Economic Development* (Englewood Cliffs, NJ, 1967), 30.

¹⁶⁰ Howard Bowen et al, ‘Federal Expenditure and Revenue Policy for Economic Stability,’ *American Economic Review*, 39:6 (Dec. 1949), 1263-1268.

¹⁶¹ Nicolas Spulber, *Managing the American Economy From Roosevelt to Reagan* (Indianapolis, IN, 1989), 33.

monetary policy to fight those downturns.¹⁶²

The stabilizing budget policy formed the bedrock of commercial Keynesianism and its development in the post-war years, coupled with its broad acceptance by liberals and conservatives, owed much to the efforts of the CED. For Robert Collins, Herbert Stein, and others, John F. Kennedy also implemented commercial Keynesianism, not least because fiscal policy in the early 1960s sought to stabilise the economy through the revenue side of the budget (albeit at a higher level of employment).¹⁶³ In fact, these scholars went as far as arguing the business community impelled JFK to promote a demand-orientated tax cut that brought the Keynesian revolution to its peak in the 1960s.¹⁶⁴ As Collins put it, “The popular view of John F. Kennedy pulling a benighted business community, kicking and screaming, into the modern age of political economy is clearly mistaken.”¹⁶⁵

In contrast, this thesis argues the existing historiography does not appreciate the role played by liberals in shaping Keynesianism’s post-war consolidation. The passage of the Employment Act was not a success for conservatives, as there remained scope for enactment of activist and expansive policies. This proved significant, for during the late 1950s many Keynesian economists interpreted the Employment Act along these lines and, by doing so, they urged policymakers to break with commercial Keynesianism. They then successfully pressed their innovative ideas upon President John F. Kennedy. Moreover, though Collins, Stein, Iwan Morgan, and Godfrey Hodgson suggest that liberals and executives adhered to a

¹⁶² See Collins, *The Business Response to Keynes*, 152-158, 175-177; Stein, *The Fiscal Revolution in America*, 292-308, 281-346; and *Presidential Economics: The Making of Economic Policy from Roosevelt to Reagan* (Washington DC, 1994), 80.

¹⁶³ See Stein, *The Fiscal Revolution in America*, 372-421; *Presidential Economics*, 106-108; Collins, *The Business Response to Keynes*, 173-211. For others see the Introduction of this thesis.

¹⁶⁴ Collins, *The Business Response to Keynes*, 186-187; Stein, *The Fiscal Revolution in America*, 417-420; and *Presidential Economics*, 106-108.

¹⁶⁵ Collins, *The Business Response to Keynes*, 199–200.

“Keynesian consensus” during the late 1950s and early 1960s, such an argument underestimated the differences between each group’s respective iterations of Keynesian ideas.¹⁶⁶ This was especially because, rather than focusing merely upon achieving economic stability, liberals expounded a far more growth-orientated vision for post-war political economy, which they hoped could underwrite the liberal state’s expansion during the third quarter of the twentieth century. That they could do so was down in no small measure to the efforts of liberal economist Leon Keyserling, whose post-war advocacy of a third manifestation of Keynes’ ideas laid the groundwork for this development. That third manifestation was “growth liberalism.”¹⁶⁷

V

Keyserling was born in Charleston, South Carolina, in 1908. By the end of World War II, he was not what one would describe as a typical Keynesian economist.¹⁶⁸ He completed his undergraduate degree at Columbia University in 1928. Then, Keyserling moved to Harvard and received an LL.B., before returning to Columbia to start an economics PhD. In 1933, Keyserling abandoned his doctoral studies and joined the Roosevelt administration as an attorney. It was there – in politics and not in academia – where Keyserling felt most comfortable: he had a distain for the academy and preferred the company of politicians. Keyserling held many government positions throughout the Depression and World War II and in the process impressed Harry Truman, then the Senator for Missouri. Thus, whilst Keyserling’s contemporaries were polishing off their PhDs by the early 1940s, he was developing his own economic philosophy in a completely different environment.

¹⁶⁶ Hodgson, *In Our Time*, 79-89; Morgan, ‘The Keynesian Consensus and its Limits,’ 86-108; and *Beyond the Liberal Consensus*, 8-12.

¹⁶⁷ Collins coined this phrase in *More*, 40-98.

¹⁶⁸ The following biographical discussion of Keyserling’s early career is based on Sobel, *The Worldly Economists*, 12-17. Keyserling did not really see himself as a Keynesian economist. However,

This did not mean he was immune from the impact of Keynesianism in America. In fact, by the mid-1940s Keyserling had formulated some very solid Keynesian ideas, which he cogently laid out in various publications.¹⁶⁹ A key theme running throughout these works was Keyserling's assertion the economy could, and should, "be stimulated in peacetime as it had been during the war."¹⁷⁰ For him, that conflict had shown American capitalism had an unlimited capacity to grow. Accordingly, the government should seek not simply to expand the economy to reach full employment – as social Keynesians argued – but aim to foster "pure economic growth – the long-term growth of economic potential."¹⁷¹

To facilitate this, Keyserling called for establishment of an expert committee that would set post-war production, consumption, employment, and investment goals.¹⁷² The president, Congress, and the Federal Reserve, through expansionary fiscal and monetary policies, would seek to attain those goals, which would be redefined as the economy reached full capacity.¹⁷³ Later referred to by Keyserling as the "National Prosperity Budget," this concept would ensure the use of the budget to maintain high levels of consumption and production, even if the economy was not in a recession.¹⁷⁴ This would create "an ever-expanding economy... [one that] could produce undreamed-of abundance and material gain for all."¹⁷⁵ Because he envisioned such a prosperous economy, Keyserling saw no need to redistribute wealth. As he put it, "There can be so much for all that the removal of unmerited

Keyserling made use of ideas akin to Keynes' when formulating his views about post-war policy. See Brazelton, *Designing US Economic Policy*, 141.

¹⁶⁹ Sobel, *The Worldly Economists*, 18-19.

¹⁷⁰ Ibid, 19.

¹⁷¹ Collins, *More*, 18.

¹⁷² Brazelton, *Designing US Economic Policy*, 18.

¹⁷³ Ibid, 18, 84, 93, 134, 145-146.

¹⁷⁴ Leon Keyserling, 'For "A National Prosperity Budget,"' *New York Times*, 9 January 1949, SM7. PQHN.

¹⁷⁵ Hamby, *Beyond the New Deal*, 300.

poverty will remove the threat to merited wealth.”¹⁷⁶ This, too, distinguished growth liberalism from social Keynesianism, as did the fact Keyserling’s National Prosperity Budget was advisory.¹⁷⁷ In fact, growth liberalism had more in common with commercial Keynesianism than social Keynesianism, as neither sought to reallocate output and both relied primarily upon private enterprise to grow the economy.¹⁷⁸ As such, there is a certain amount of evidence to suggest that liberal and business iterations of post-war Keynesianism had much in common.

Importantly, Keyserling was not alone in his view that the American economy had a limitless capacity to grow. In 1946, the former head of the Office of Price Administration, Chester Bowles, argued the government should make full use of the nation’s productive capacity to achieve a \$200 billion economy (in GNP terms).¹⁷⁹ However, Keyserling’s leading role in Truman’s Council of Economic Advisers, first as vice-chairman (1946-49) and then as chairman (1949-53), enabled him to infuse pro-growth ideas into policy discussion.¹⁸⁰ Unsurprisingly, his influence was greatest when he was head of that body. His predecessor – the Brookings economist Edwin Nourse – shunned Keyserling’s calls for growth-orientated policies. Instead, he preferred to moderate the business cycle rather than engage in expansionary economics. Nourse acknowledged this in the CEA’s January 1949 *Economic Report*, which stated, “Policies needed to develop our resources and to prevent

¹⁷⁶ Keyserling, ‘Deficiencies of Past Programs and Nature of New Needs,’ in Harris (ed.) *Saving American Capitalism: A Liberal Economic Program* (New York, 1948), 91.

¹⁷⁷ Whereas the social Keynesians’ full employment proposals would have been mandatory if enacted.

¹⁷⁸ Morgan, ‘The Keynesian Consensus and its Limits,’ 100-101.

¹⁷⁹ Howard Schaffer, *Chester Bowles: New Dealer in the Cold War* (Cambridge, MA, 1993), 20-21. It is also worth noting that, in 1943, the NRPB published a report, which stated, “we stand on the threshold of an economy of abundance. This generation has it within its power not only to produce in plenty but to distribute that plenty.” *National Resources Development Report for 1943* (Washington DC, 1943), 4.

¹⁸⁰ See, for example, Keyserling, ‘Must We Have Another Depression?’ *New York Times*, 8 June 1947, SM7. PQHN; and ‘Excerpts From Remarks at ADA Full Employment Conference,’ Washington, D.C., 19 July 1949. ADA Papers. Reel 95. BL.

depression...must be reconciled with policies needed to curb inflation.”¹⁸¹ However once Keyserling ascended to the chairmanship later that year – following a public dispute with Nourse over the role of the CEA – economic growth became the Council’s main policy focus.

The CEA’s 1950 *Economic Report* made this clear. This outlined such an optimistic and expansive view for the economy that, according to Princeton economist Richard Lester, Keyserling effectively made growth liberalism the centrepiece of Truman’s economic programme.¹⁸² This is important, as certain scholars have made the argument that “Truman was never really sold on the merits of the Keyserling expansionist economics.”¹⁸³ However, as Lester’s comment and Truman’s own section of the *Economic Report* both indicated, the president certainly flirted with growth liberalism during his time in office.¹⁸⁴ Whilst visiting Kansas City in the fall of 1950, Truman went as far as commenting that the US should aim to achieve a \$300 billion economy, saying, “This is not a pipe dream.”¹⁸⁵ Following the outbreak of the Korean War in June 1950, Keyserling also convinced Truman to pay for that conflict through an expansion of national output rather than through increased taxation.¹⁸⁶ This experiment was short-lived due to Chinese intervention in that conflict, but it demonstrated that Truman was not as opposed to growth liberalism as some scholars have insisted – even though he did implicitly follow the guidelines of the stabilizing budget policy.

When he left the Truman administration in 1953, Keyserling had not established growth liberalism as a core element of national economic policy.

¹⁸¹ *The Economic Report of the President, 1949* (Washington DC, 1949), 8. APP.

¹⁸² Richard Lester, ‘Truman Economics-1950 Model,’ *New Republic*, 122:4 (Jan. 1950), 11-13. EBSCO. See too *The Economic Report of the President, 1950* (Washington DC, 1950), 78. APP.

¹⁸³ Norton, *The Employment Act and the Council of Economic Advisors*, 122.

¹⁸⁴ *The Economic Report of the President, 1950*, 6-8.

¹⁸⁵ Cited in Collins, *More*, 22.

Undeterred, he continued to argue in favour of its enactment through newspaper articles, establishment of a Washington think-tank called the Conference on Economic Progress, and service as vice-chairman of Americans for Democratic Action (ADA). The return of a Republican to the White House for the first time since Hoover provided Keyserling with a target that he could critique. Eisenhower was highly committed to the stabilizing budget policy, partly because it enabled him to establish what Robert Griffith has described as a “corporate commonwealth” (essentially a mixed economy).¹⁸⁷ Eisenhower also worried that discretionary fiscal measures would unbalance the budget and drive up inflation.¹⁸⁸ Automatic stabilisers induced the deficits that he ran for FYs 1954-55, both of which amounted to less than 1 percent of GDP. This was even though the economy experienced a recession in 1953-54. For some contemporary observers, this was a satisfactory response to that downturn.¹⁸⁹ For Keyserling, Eisenhower’s policies were not only inadequate but also symptomatic of an economic philosophy that hindered long-term growth.¹⁹⁰

Throughout 1954, Keyserling slammed commercial Keynesianism as practised by Eisenhower. He argued that the president’s passive embracement of Keynes’ ideas had resulted in output falling 8 percent below full capacity.¹⁹¹ For Keyserling, the government needed to make use of the National Prosperity Budget so that it could raise the national income by \$40 billion by early 1955.¹⁹² This entailed increasing spending by “a few billion dollars” and lowering taxes for middle and

¹⁸⁶ Morgan, ‘The Keynesian Consensus and its Limits,’ 97.

¹⁸⁷ Robert Griffith, ‘Dwight D. Eisenhower and the Corporate Commonwealth,’ *American Historical Review*, 87:1 (Feb. 1982), 87-122.

¹⁸⁸ See Morgan, ‘Managing the Economy,’ in Chester Pach (ed.) *A Companion to Dwight D. Eisenhower* (Hoboken, NJ, 2017), 235.

¹⁸⁹ See A. E. Holmans, *United States Fiscal Policy, 1945-1959: Its Contribution to Economic Stability* (London, 1961), 211-242; Wilfred Lewis, Jr., *Federal Fiscal Policy in the Postwar Recessions* (Washington DC, 1962), 131-187; and Stein, *The Fiscal Revolution in America*, 305-306.

¹⁹⁰ Keyserling, ‘Eisenhower’s Program For America,’ *New Republic*, 130:6 (Feb. 1954), 6. EBSCO.

¹⁹¹ Keyserling, ‘Full Employment,’ in Schlesinger Jr., and Quincy Howe (eds.) *Guide to Politics* (New York, 1954), 11.

lower income earners.¹⁹³ It also necessitated expanding the money supply, lowering interest rates, increasing the minimum wage, and enlarging expenditures on public housing.¹⁹⁴ If Eisenhower's commitment to the stabilizing budget policy continued, Keyserling argued, there would be "altogether over the six years [up to 1960] at least \$200 billion *less* of total output – goods and services that we need – than if we quickly regain, and then maintain, full employment."¹⁹⁵ Keyserling believed that it was possible to achieve a \$600 billion economy by 1960.¹⁹⁶ This would permit the government to increase spending on social security, healthcare, and education without "encroach[ing] upon national security needs."¹⁹⁷ It was an argument that he consistently made throughout the early-to-mid-1950s.¹⁹⁸ The ADA's various policy statements during those years also reflected his thoughts.¹⁹⁹ However, Eisenhower remained completely indifferent to growth economics.

VI

By the mid-1950s, Keynesianism in America had gone through three manifestations since both the publication of *The General Theory* and Roosevelt's half-hearted embrace of ideas akin to those of Keynes' in the late 1930s. The development of social Keynesianism, the first of these, came in response to concerns the US economy was mature and stagnant. It gained temporary ascendancy during World War II thanks to Alvin Hansen. After the war, opposition from the business community led to social Keynesianism's eclipse, setting the stage for the ascendancy of commercial Keynesianism. A conservative manifestation of Keynes' ideas, this

¹⁹² Ibid, 12.

¹⁹³ Ibid, 12.

¹⁹⁴ Ibid, 12-13.

¹⁹⁵ Ibid, 13. Emphasis in the original.

¹⁹⁶ Ibid, 13.

¹⁹⁷ Gillon, *Politics and Vision*, 113.

¹⁹⁸ Keyserling, 'The Prospects for Prosperity in 1955,' *New Republic*, 132:11 (Mar. 1955), 13-17. EBSCO; and 'Testimony on Behalf of ADA before Democratic National Convention,' 8 August 1956. ADA Papers. Reel 92. BL.

was implemented by Truman and Eisenhower in the form of the stabilizing budget policy.

As commercial Keynesianism gained political ascendancy, Leon Keyserling emerged as the foremost advocate of growth liberalism, another post-war iteration of Keynesianism that had certain similarities with commercial Keynesianism. Keyserling's recommendations never made it onto the statute books. However, his advocacy of growth liberalism laid the groundwork for an extensive debate over economic growth in Eisenhower's second term. This resulted in Keynesian economists breaking with the consensus on post-war economic policy, before pressing their suggestions upon President John F. Kennedy. At the heart of this development was Walter Wolfgang Heller, a man curiously understudied by historians and the subject of this thesis.

¹⁹⁹ Gillon, *Politics and Vision*, 112-114.

Chapter Two

A Keynesian Economist in the Eisenhower Era

Born in Buffalo, New York, in 1915, Walter Heller was head of the Economics Department at the University of Minnesota as liberal economists reassessed commercial Keynesianism's merits. Not widely considered an eminent economist at this point in time, Heller played a significant role in facilitating this development. He then served as chairman of the Council of Economic Advisers under Presidents John F. Kennedy and Lyndon B. Johnson. In this capacity, he was a crucial figure in the Keynesian revolution's consolidation. The aim of this chapter is to lay the groundwork for consideration of Heller's CEA chairmanship. It shows how both he and his contemporaries sought a break with commercial Keynesianism in the late 1950s, paving the way for the ascendancy of growth liberalism. To put Heller's contribution into historical perspective, the chapter starts by examining Heller's early life and career. It then examines why and how he and his contemporaries reappraised commercial Keynesianism, before exploring the process and factors that prompted Kennedy to appoint Heller to his administration.

I

According to one historian, Walter Heller's life and career up to the mid-1950s were both "conventional insofar as college professors were concerned."²⁰⁰ The son of German immigrants who moved to the US in 1910, Heller was born into a family that valued education and public service.²⁰¹ After his father (a civil engineer), moved them to Seattle and then to Milwaukee, Heller attended public schools until

²⁰⁰ Sobel, *The Worldly Economists*, 121. Unless otherwise cited, the biographical information on Heller's early career that features in this chapter is from 118-125 of Sobel's book and from Joseph Pechman, 'Walter W. Heller, 1915-1987,' *Brookings Papers on Economic Activity*, 18:2 (1987), viii-xi.

²⁰¹ Heller, 'Transcript of Interview for CBS,' 9 September 1962. Walter Heller Papers [Henceforth Heller Papers]. Box 11. John F. Kennedy Presidential Library [Henceforth JFKL]

1931. Then, he won a four-year scholarship to Oberlin College in Ohio. Unemployment stood at 25 percent, but Heller did not initially aspire to be an economist. Instead, he preferred to study law. Within a year, however, he switched his major to economics, mainly because the Depression showed few signs of abating.²⁰² “Those of us who were growing up then,” Heller later explained, “saw the economy flat on its back. To explain why, and to try to do something about it, seemed a high calling.”²⁰³ At Oberlin, Heller’s economics instructor was Benjamin Lewis, who served as a New Deal adviser. Lewis often rushed into the classroom having just come from Washington, something that inspired Heller to combine his future academic life with public service.²⁰⁴

Awarded his undergraduate degree in 1935, Heller moved to the University of Wisconsin. His was supervised by Harold M. Groves, an expert in the field of public finance. Groves had also been a state senator, so he reinforced Heller’s public service-orientated academic outlook. He helped introduce his student to the ‘Wisconsin idea’ – the belief that knowledge produced at universities should be deployed by the state.²⁰⁵ By now, the Depression was in its sixth year. Having closely watched the evolution of the New Deal, Heller had become convinced “that an aggressive, interventionist approach to economic maladies was needed.”²⁰⁶ This was unsurprising, as his father had been unemployed for several years and had found a job in the Works Progress Administration for a time.²⁰⁷ Seeing this liberal economic

²⁰² Heller, Transcript of Interview for *The Margin Magazine*, October 1985. Author’s copy. The author is grateful to Professor Eric Heller and Kaaren Davis for providing a copy of this from Heller’s privately held papers.

²⁰³ n.n., ‘The Pragmatic Professor,’ *Time*, 77:10 (Mar. 1961), 18-25. EBSCO.

²⁰⁴ Heller, Interview for *The Margin Magazine*.

²⁰⁵ As the economist Louis Johnston has noted, Heller “really absorbed that idea.” Louis D. Johnston (CSB/SJU), Interview with the Author, 16 June 2015.

²⁰⁶ Sobel, *The Worldly Economists*, 122.

²⁰⁷ Peter Ackerman, ‘Walter Heller: Operating on Idea Economics Can Be Fun,’ *Minneapolis Star*, 2 October 1974, 24B. Walter Heller Papers [Henceforth Heller Papers]. Box 10. University of Minnesota Archives [Henceforth UoM]

outlook in his student, Groves directed Heller towards the ideas of John Maynard Keynes in 1938. Yet, Heller's embrace of Keynesian economics did not take place immediately. Though he had questioned the principle of non-intervention, Heller found *The General Theory* "very tough-going...It was so far off the beaten track – that is the beaten track as of 1938 – that it was really hard to get hold of."²⁰⁸

With the help of Groves and other faculty members, Heller did eventually see in deficit spending "a way out [of the Depression]...that the classical theory seemed to be unable to cope with."²⁰⁹ He soon developed a strong understanding of and commitment to Keynesianism, but it is highly unlikely he was attracted to the ideas of Alvin Hansen. True, he later admitted he held "the old Wisconsin belief in the importance of the public sector as a means of achieving welfare for the people," but at the time Hansen first espoused social Keynesianism, Heller had not fully grasped the merits of pump priming.²¹⁰ Furthermore, after obtaining his PhD in 1941 Heller joined the tax research division of the US Treasury. There, he helped embed automatic stabilisers into the economy by playing a role in devising the withholding taxation system that funded World War II. This experience had a profound impact upon Heller, who found himself "among the worshippers at the shrine of fiscal automaticity."²¹¹ Thus, whilst Hansen and other social Keynesians called for permanent deficit spending to avert a post-war recession, Heller saw little need for such policies. In his reckoning, the built-in flexibility of the taxation system would prevent the economy from experiencing a severe downturn.

Despite his respect for automaticity, it would be wrong to describe Heller as a staunch supporter of commercial Keynesianism. He did serve as a technical

²⁰⁸ Heller, Interview for *The Margin Magazine*.

²⁰⁹ Ibid.

²¹⁰ n.n., 'How Kennedy's CEA Sees Road to Growth,' *BusinessWeek*, 18 February 1961, 46. BL.

consultant to the CED during the post-war period and certainly recognised the potential of the stabilizing budget policy to manage the economy. However, Heller always stressed that discretionary fiscal policies should help moderate the business cycle. Shortly before the CED's concept gained credibility, Heller remarked that while "the policy of maintaining high tax rates during a boom and cutting tax rates in a slump is good," it was essential "to spend money during a slump...[as] expenditures on such things as public works...[give the economy] a shot in the arm."²¹² In addition, despite in the post-war years acknowledging the importance of balancing the budget during good times, Heller stressed discretionary fiscal policies were always desirable when the economy faltered. This was an argument he made in 1951 whilst serving as a fiscal adviser in West Germany, where the reconversion from war and that country's division into East and West caused unemployment to rise to 8 percent. Dismayed with what he called the "classical, anti-Keynesian policies [that] have ruled the West German economic roost since mid-1948," Heller stressed there needed to be "fuller use of modern monetary-fiscal instruments."²¹³

As a liberal economist in the early post-war years, Heller advocated Keynesian measures primarily for countercyclical purposes. Still, while he favoured greater reliance upon discretionary fiscal policies compared with the CED, he never went as far as advocating their use to achieve the growth economics espoused by Leon Keyserling. Moreover, compared with his contemporaries – including MIT's Paul Samuelson, Harvard's John Kenneth Galbraith, and Yale's James Tobin – Heller

²¹¹ Heller, 'CED's Stabilizing Budget Policy After Ten Years,' *American Economic Review*, 47:5 (Sept. 1957), 634. Footnote 2.

²¹² Heller, 'Post-War Municipal Finance in National Economy,' 70.

²¹³ Heller, 'Economic Policy and Political Equilibrium in Post-War Germany,' in Hans J. Morgenthau (ed.) *Germany and the Future of Europe* (Chicago, IL, 1951), 66, 75. For his similar views about the US economy see Heller, 'Lectures on The Federal Budget and Taxes,' University of Minnesota, 27 and 28 August 1953. Copy in Hugh Gaitskell Papers [Henceforth Gaitskell Papers]/C/100.22. UCL Special Collections. National Archives. Kew. [Henceforth NAK]

was not initially a prominent advocate of Keynes' ideas. His liberal Keynesian outlook certainly developed in the post-war years – as his experiences in World War II and his advisory role in West Germany showed – but macroeconomics did not originally occupy Heller's attention. Like Groves, he initially established a name for himself as an expert in public finance.

This was hardly surprising given Heller had always aspired to be an applied economist. As he put it, public finance was “the critical area, the jugular area, of Government economic policy,” one where his expertise would be in high demand.²¹⁴ Hence, after leaving the Treasury in 1946 to join the University of Minnesota (where he rose to chair the newly-created Economics Department in 1957), Heller in 1947-48 served as Chief of Internal Finance for the American Military Government in West Germany. In this capacity, he helped devise the tax and currency reforms that underwrote that country's economic miracle. He then worked in Washington during the Korean War creating the tax system adopted to fund that conflict, before serving as a tax consultant to both the Minnesota Governor Orville Freeman (from 1955 onwards) and to King Hussain of Jordan (in 1960). Furthermore, Heller's lack of both mathematical skills and theoretical training influenced his decision to initially specialise in public finance. As his son, Eric Heller, has noted, “I never knew whether he was poorly trained or had very little ability, but my father was not good at mathematics.”²¹⁵ Thus, Groves directed Heller's attention towards the techniques of state income taxation – the topic of his PhD – and Heller's academic pursuits in the early post-war years focused mostly upon evaluating both the merits of various taxation methods and the nature of the tax code, not the development of complex

²¹⁴ n.n., ‘The Pragmatic Professor.’

²¹⁵ Eric Heller (Harvard University), Interview with the Author, 12 May 2015.

macroeconomic theory.²¹⁶

Heller's passion for applied economics, coupled with his lack of mathematical training, thus ensured he primarily sought to create good tax policy up to the early 1950s. This meant that, after Eisenhower assumed the presidency in 1953, Heller did not initially comment on the first Republican post-war president from either an overtly macroeconomic or explicitly Keynesian perspective. His main critique of Eisenhower during the first year of his presidency focused on refuting the argument, "apparently endorsed" by the president, that it would be unwise to set federal, state, and local taxes so they consumed more than 25 percent of the national income.²¹⁷ Limiting taxes this way, Heller said, would result in a loss of revenue, would impair the ability of the federal government to deploy discretionary fiscal policies, and would shift too much of the tax burden onto low-income earners.²¹⁸ At the beginning of Eisenhower's presidency, then, Walter Heller was neither a prominent Keynesian economist nor a widely recognised authority on macroeconomic policy.

II

From the mid-1950s, Heller's academic and public policy interests underwent an important transformation. In short, he shifted his focus from public finance towards macroeconomics.²¹⁹ At the same time, Heller stopped advocating use of discretionary fiscal policies purely for countercyclical purposes to champion their

²¹⁶ Inventory of Walter Heller's publications up to 1955. Heller Papers. Box 5. UoM. Importantly, one that does not appear in this list is: 'Appraisals of the Administration's Tax Policy,' *National Tax Journal*, 8:1 (Mar. 1955), 12-28.

²¹⁷ Heller, 'Taxation Developments in 1952,' 10 March 1953 (notes for lecture on B.A. 58). Heller Papers. Box 2. UoM.

²¹⁸ Heller and Irma A. Linse, 'Implications of a Twenty-Five Percent Ceiling on Federal Income and Death Tax Rates,' Reprint from *Iowa Law Review*, 38:4 (Sum. 1953). Copy in Gaitskell Papers/G/Economics. NAK.

²¹⁹ Indeed, such was his switch to macroeconomic policy that by the end of the decade Heller thwarted attempts to define him as a tax specialist. For example, following his appointment as a consultant to Basic Economics Corporation in 1960, Heller had his initial biographical entry in the company's brochure changed to reflect the fact that he considered himself more an expert in macroeconomics. See Heller to Galen Van Meter, 1 November 1960. Heller Papers. Box 2. UoM.

deployment to maximise economic growth. Despite these developments, historians who have assessed the Keynesian opposition to Eisenhower economics in the late 1950s have overlooked Heller's role in it.²²⁰ This is surprising, for according to one scholar Heller was "one of the most outspoken critics of the Eisenhower administration's economic growth record."²²¹ Moreover, whilst Heller and other Keynesians critiqued Eisenhower during his second term, they altered the debate about the parameters of economic policy. This was something Herbert Stein and Robert Collins did not appreciate. Also overlooked were the differences between liberal and business iterations of Keynesian ideas during this period. Assessing why Heller became such a fierce advocate of growth economics, outlining what he argued in this respect, and comparing his criticisms of Eisenhower economics with those of his contemporaries, are each important.

The economy's underperformance in the mid-1950s triggered Heller's decision to re-orientate his interests towards both macroeconomics and growth. This was something he may have become acutely aware of after serving as a UN consultant to underdeveloped nations in 1952 and 1953.²²² Resultantly, Heller appeared before the Congressional Joint Economic Committee (JEC) in early 1955 to make his first statement on behalf of expansionary economics. This followed publication of that year's *Economic Report*, a document that effectively reaffirmed Eisenhower's commitment to the stabilizing budget policy.²²³ Mirroring the arguments previously advanced by Leon Keyserling, Heller complained that

²²⁰ See Morgan, *Eisenhower Versus "The Spenders": The Eisenhower Administration, the Democrats and the Budget, 1953-60* (London, 1989), 24-48; Yarrow, *Measuring America*, 43-66; William M. McClenahan and William H. Becker, *Eisenhower and the Cold War Economy* (Baltimore, MD, 2011), 77-109; John Sloan, *Eisenhower and the Management of Prosperity* (Lawrence, KS, 1991), 133-151; Collins, *More*, 40-60; and Gillon, *Politics and Vision*, 112-130.

²²¹ Robert P. Bremner, *Chairman of the Fed: William McChesney Martin, Jr., and the Creation of the American Financial System* (New Haven, CT, 2004), 147.

²²² Johnston, Interview with the Author.

²²³ *The Economic Report of the President, 1955* (Washington DC, 1955), 22. APP.

Eisenhower's economic programme was too cautious and timid.²²⁴ He declared it imperative to make use of discretionary fiscal measures because the economy was operating \$20 billion below capacity.²²⁵ The existence of this large gap between actual and potential output particularly concerned Heller. Like Keyserling, he had come to believe the economy had an enormous capacity to expand, something demonstrated to him during the war.²²⁶ Heller felt that increasing the size of the economic pie would make it easier for the US to achieve its goals at home and abroad.²²⁷ As he later stated, growth was "an end in itself and an instrumentality, both the pot of gold and the rainbow."²²⁸

Over the course of the next five years, several developments reinforced this conviction in Heller. The large-scale economic inequality that increasingly became a concern in the late 1950s constituted the most important of these. Though GNP rose by 56 percent between 1947 and 1960, several contemporary studies showed poverty beset a quarter of the population in America.²²⁹ Racial minorities, the elderly, residents of depressed areas, and female-headed households were those hit the hardest. Though many were optimistic that America's growing prosperity would alleviate this problem, Heller argued poverty was in fact much harder to break down. Throughout 1960, he said that although GNP would hit \$1 trillion by 1970 – based on the average rate of post-war growth – "large islands of poverty will still persist in the

²²⁴ Heller, 'Observations on Federal Tax and Fiscal Policy in 1955,' Notes for Panel Discussion on Fiscal Policy Before the Congressional Joint Economic Committee on the Economic Report, January 28, 1955, Washington D.C., Submitted in accordance with the invitation of the Chairman, Senator Paul A. Douglas.' Gaitskell Papers/C/100.23. NAK. See too Heller, 'Observations on Federal Fiscal Policy in the United States, 1955,' Statement before the Joint Economic Committee [Henceforth JEC]. Reprinted in the *Canadian Tax Journal*, 3:2 (1955), 81-86. The latter was an edited reprint of Heller's testimony. Gaitskell Papers/G/Economics. NAK.

²²⁵ Heller, 'Observations on Federal Fiscal Policy,' 81.

²²⁶ Johnston, Interview with the Author.

²²⁷ Heller, 'Observations on Federal Fiscal Policy,' 81.

²²⁸ Heller, 'Economic Growth: Challenge and Opportunity,' Speech at the Loeb Awards, New York, 18 May 1961. John F. Kennedy Presidential Papers. President's Office Files [Henceforth POF]. Box 73. JFKL. From here, POF relates to the collection cited here and held at the JFK Library.

sea of affluence.”²³⁰ He contended that if the economy grew 1.5 percent faster during the next decade it would produce an extra \$110 billion, which could lift many citizens above the poverty line and produce revenues to help fund programmes aimed at tackling any hard-core poverty that remained untouched.²³¹

In addition to his concern about the existence of poverty amidst plenty, another reason Heller’s commitment to a faster growth rate solidified during the late 1950s was that, without it, he realised the federal government would be unable to relieve the growing financial pressures upon state-local governments. From 1946-56 the nation’s expanding population (especially its school-age population), the growth of suburban America, and the increased demands of more prosperous times, all forced state-local governments to provide more facilities and public services.²³² This caused their expenditures to treble, but their revenues only increased by 150 percent. Heller argued that, if the economy continued to grow at its average post-war rate, state-local incomes would fall \$10 billion short of their predicted expenditures by 1965.²³³ This necessitated a higher growth rate, so the federal government could boost its own revenues and share this increased income with the states.²³⁴ As Heller put it, “the greatest single contribution federal fiscal and monetary policy can make to the financial stability of state-local governments is to promote full employment and

²²⁹ The GNP figure is in 1954 dollars and is from Collins, *More*, 41. The poverty figure is from Morgan, ‘Managing the Economy,’ 231.

²³⁰ Heller, ‘The Economic Setting for Health and Welfare in the Sixties,’ Address at the Annual PCA Conference, Harrisburg, Pennsylvania, 1 November 1960. Copy in POF. Box 73.

²³¹ *Ibid*; and Heller, ‘An Economic Forecast for the Sixties,’ Address to the Annual Forum of the National Conference on Social Welfare, Atlantic City, New Jersey, 6 June 1960. Heller Papers. Box 8. UoM.

²³² Heller, Memorandum for Robert D. Calkins and Richard Goode, ‘Some Thoughts on a Study of the Federal Tax Crediting Device,’ 18 September 1959. Heller Papers. Box 8. UoM.

²³³ Heller, ‘The Impact of Federal Fiscal and Monetary Policies on State and Local Governments,’ Statement before the JEC, 1 February 1957. Heller Papers. Box 4. UoM.

²³⁴ Later referred to as “revenue-sharing,” Heller outlined this idea in a 1957 article. See ‘US Budget Surpluses and Tax Policy,’ *Canadian Tax Journal*, 5 (Sum. 1957). Cited in David M. Welborn and Jesse Burkhead, *Intergovernmental Relations in the American Administrative State: The Johnson Presidency* (Austin, TX, 1989), 289. Footnote 4.

vigorous growth.”²³⁵

International developments during Eisenhower’s second term reinforced Heller’s desire to increase the rate of output. Following his work for the U.N. it is likely he had become convinced that the US should channel more funds to underdeveloped countries. Consequently, he saw stronger growth as a way of paying for this.²³⁶ He also viewed a faster rate of growth as essential if those nations were to emulate the economic model of American capitalism instead of Soviet communism. The Soviet launch of Sputnik I in October 1957 reinforced this. Not only did this incident give rise to concerns America was losing the Cold War, it drew attention to the fact the US was supposedly growing at a slower rate than the Soviet Union, which was rumoured to be expanding at 6 percent a year.²³⁷ In the month after the launch of Sputnik, Heller argued for increased investment in scientific research and technology, both as a means to bolster America’s military capabilities and as a way to grow the economy.²³⁸ He also said a large increase in defence spending could, and should, take place to facilitate these ends, commenting the subsequent “economic frills” would enable the US to catch-up and overtake the Soviet Union.²³⁹

Heller’s concerns about economic inequality, the pressures upon state-local finances, and developments in the international arena, all reinforced his commitment to expansionary economics during the late 1950s. However, whilst Heller espoused the need for stronger and faster growth, the rate of output slowed to 2.25 percent during Eisenhower’s second term.²⁴⁰ This rallied liberal economists and politicians

²³⁵ Heller, ‘The Impact of Federal Fiscal and Monetary Policies on State and Local Governments.’

²³⁶ See Heller, ‘Observations on Federal Fiscal Policy,’ 81.

²³⁷ n.n., ‘The Pragmatic Professor.’

²³⁸ Heller, Statement before the JEC, November 1957, in *Federal Expenditure Policy for Economic Growth and Stability* 85th Congress: 1st Session (Washington DC, 1957), 42.

²³⁹ Ibid, 42.

²⁴⁰ This compared to a Korean War-affected rate of 4.7 percent in his first term. Cited in Morgan, ‘Managing the Economy,’ 229.

against commercial Keynesianism and Heller played a key role in this debate. Eisenhower continued to follow an economic philosophy akin to the stabilizing budget policy during the late 1950s, even though certain technical developments showed that discretionary fiscal activism was apropos. Writing in the *American Economic Review* in September 1957, Heller stated improvements in economic forecasting, the poor record of monetary policy as a tool to promote stability, and the fact automatic stabilisers could not act as “powerful counterforces” to promote recovery from a recession, all added weight to the case for more activist fiscal measures.²⁴¹ Continued reliance on the stabilizing budget policy, he also warned, would further result in “a relatively weak guarantee of full employment.”²⁴²

This assessment proved prescient. In late 1957, the economy went into its most severe downturn since the Depression. Mirroring his response to the earlier recession of 1953-54, Eisenhower refused to implement discretionary fiscal policies. Instead, he believed automatic stabilisers would do enough to cushion the blow against that downturn.²⁴³ Even though his former CEA chairman, Arthur Burns, pressed the president to implement a temporary tax cut, Ike had received assurance that the tax system’s built-in flexibility would save the economy.²⁴⁴ Such was the president’s fear that unbalancing the budget would also drive up inflation that as soon as recovery from the recession began he strove to achieve a balanced budget by FY 1960. This caused an unprecedented swing from a FY 1959 deficit of \$12.8 billion (2.5 percent of GDP) to a FY 1960 surplus of \$0.3 billion (0.1 percent of GDP). Consequently, the United States entered a double-dip recession during the 1960 Presidential Election. In recent years, it has become fashionable for scholars to praise

²⁴¹ Heller, ‘CED’s Stabilizing Budget Policy After Ten Years,’ 644-645 (quotation 645).

²⁴² Ibid, 637.

²⁴³ See Dwight D. Eisenhower, *The White House Years: Waging Peace, 1956-1961* (London, 1966), 310.

Eisenhower's management of the economy.²⁴⁵ Yet his disastrous drive for a balanced budget following the 1957-58 recession surely ranks "as one of the major fiscal policy mistakes of the postwar period."²⁴⁶

This was not least because, as Heller warned in September 1957, Eisenhower's reliance upon automaticity had denied the economy an important amount of fiscal adrenaline. As a result, the US was experiencing what Heller described as "slack-filled prosperity" in the late 1950s.²⁴⁷ The president's "obsession with [automatic stabilisers,] federal expenditure cutbacks and early budget balance as a pre-requisite to price stability" was "unfounded."²⁴⁸ Taking his cue from Keynes, Heller argued substantial use of discretionary fiscal measures was required. This might entail running a deficit in non-recession conditions, but Heller maintained that in the circumstances of the late 1950s such a strategy would be "constructive."²⁴⁹ The "economy's response...[would be] higher real consumption and investment, higher employment, and higher real national income. In other words, these are deficits which more than pay for themselves."²⁵⁰ Heller further noted that Eisenhower's concern that discretionary fiscal activism would result in inflation was misguided: the large amount of slack in the economy meant there was substantial room for expansion before such a problem arose.²⁵¹

To close the performance gap through greater use of discretionary fiscal

²⁴⁴ Ibid, 310.

²⁴⁵ See McClenahan and Becker, *Eisenhower and the Cold War Economy*; and Sloan, *Eisenhower and the Management of Prosperity*. Interestingly, Sloan commended Eisenhower's attempt to balance the FY 1960 budget, describing it as "the most remarkable budget achievement in the history of the United States." (80).

²⁴⁶ George L. Bach, *Making Monetary and Fiscal Policy* (Washington DC, 1971), 102.

²⁴⁷ Heller, Excerpts from 'A Positive Approach to Economic Policy,' Address to the Annual Convention of the Independent Bankers Association, Denver, Colorado, 25 May 1960. Heller Papers. Box 9. UoM.

²⁴⁸ Heller, 'Ike's Financial Logic Disputed,' *Minneapolis Star*, 13 February 1959. 8A. Heller Papers. Box 9. UoM.

²⁴⁹ Heller, 'Observations on Federal Fiscal Policy,' 83. For similar comments, see Ibid.

²⁵⁰ Ibid, 83.

measures, Heller called for a tax cut throughout the late 1950s. He later said he would have preferred to increase expenditures (not least because of the social benefits such a policy would have), but recognised a tax cut was more likely to gain approval from the strong coalition of Southern Democrats and Republicans in Congress.²⁵² In his 1955 JEC testimony Heller remarked, “tax reduction can help to put \$20 million of unused resources to work and thus help the United States to realize its full economic potential.”²⁵³ Later, in an address in Chicago during the 1957-58 recession, Heller said that in light of both the economic crisis and the persistent slack in the economy “a broad tax cut of \$5 to \$7 billion would be sound economic policy today.”²⁵⁴ To facilitate tax reduction he further noted that a “thorough recasting of the federal income tax” was essential: if Congress closed special exemptions, exclusions, deductions, and stamped down on unreported income, all would boost revenues and make a tax cut politically feasible.²⁵⁵ Additionally, it was important to accompany tax reduction with a flexible use of monetary policy, especially because the Fed had tightened interest rates in the late 1950s.²⁵⁶ However, Heller stressed excessive monetary expansion would impede the utility of fiscal policy to maximise growth, meaning use of monetary policy should be purely for supplementary purposes.²⁵⁷

Following enactment of these expansionary policies, Heller explained it would be essential to increase the economy’s potential. This was something Keyserling had stressed since the late 1940s. According to Heller, crucial to increasing potential were tax cuts for businesses to incentivise production. Also

²⁵¹ Heller, ‘Ike’s Financial Logic Disputed,’ 8A.

²⁵² n.n., ‘How Kennedy’s CEA Sees Road to Growth,’ 48.

²⁵³ Heller, ‘Observations on Federal Fiscal Policy,’ 84.

²⁵⁴ Heller, ‘Economic and Fiscal Outlook,’ Statement for Spring Management Conference, Chicago, Illinois, 19 May 1958. Heller Papers. Box 5. UoM.

²⁵⁵ ‘Heller Urges Plan to Speed US Production,’ University of Minnesota Press Release, 8 November 1959. Heller Papers. Box 9. UoM.

²⁵⁶ See Ibid.

important was large-scale investment in people, particularly in the form of better education and training. Such thinking was attuned to research in the emerging field of Human-capital theory demonstrating that two-thirds of the growth in physical output between 1917 and 1957 was attributable to improvements in both technology and efficiency, which were both dependent upon the advancement of human knowledge.²⁵⁸ This evidence had a profound impact upon Heller, who commented in 1958 that economic capacity was “[based] on an upgrading of human skills and understanding and on [the] technological advance that grows out of the upgrading process.”²⁵⁹ Thus, by the late 1950s Walter Heller had joined Leon Keyserling as a key proponent of growth liberalism. This amounted to an important shift in his views up to that time. Central to his philosophy of expanding the economy was a large tax cut, a measure that entailed breaking with the reliance upon automaticity.

III

At the same time as Heller reassessed the merits of commercial Keynesianism, other Keynesian economists did so too. Yet, there was no agreement between them over the reasons for deploying discretionary measures, let alone what this should entail. Like Heller, two individuals who advocated tax reduction to maximise growth were Charles Schultze of Indiana University and Arthur Upgren of Macalester College. In commenting on Eisenhower’s adherence to commercial Keynesianism, Schultze and Upgren went further than Heller did in terms of their analysis.²⁶⁰ In their assessment, automatic stabilisers were a mixed blessing that helped to generate a

²⁵⁷ See Heller to Hubert Humphrey, Heller to Orville Freeman, and Heller to John Kareken, all on 15 July 1959. Heller Papers. Box 8. UoM.

²⁵⁸ Heller, ‘The Economic Setting for Health and Welfare in the Sixties.’

²⁵⁹ Heller, ‘Teacher Salaries and the Nation’s Economy,’ Address at the National Conference for Teacher Salary Scheduling, Washington D.C., 8 October 1958. Heller Papers. Box 47. JFKL.

²⁶⁰ For Upgren’s views see ‘Will Heller Urge Trying Tax Cuts?’ *Minneapolis Star*, 26 December 1960; and ‘How Affluent will the Sixties Be?’ Midwest Economics Association paper, 28 April 1960. Both in Heller Papers. Box 9. UoM. For Schultze’s views see his statement before the JEC, December 1960,

compensatory deficit against the 1957-58 recession, but retarded growth in the upstage of the business cycle. As the economy recovered, the automatic stabilisers sucked too much purchasing power from it, with the consequence that the budget balanced before the attainment of full employment. This was the chief cause of the “slack-filled prosperity” identified by Heller in the late 1950s. Offsetting it required discretionary fiscal activism. Appearing before the JEC in December 1960, Schultze lucidly illustrated this. He did so by invoking a concept utilised by certain Keynesian economists in the late 1950s. Given Eisenhower’s rates of taxation, Schultze said the automatic stabilisers “would yield an \$11 to \$12 billion surplus” if the economy were operating at full employment.²⁶¹ A tax cut in the range suggested by Heller, he argued, would offset this large “full employment surplus” and touch off a period of vigorous economic growth.²⁶²

Heller did not publicly discuss this concept in 1960, but he was aware of its utility. Additionally, Harvard’s Seymour Harris and Princeton’s Richard Lester mirrored Heller’s argument for a tax cut.²⁶³ Still, not everyone believed tax reduction offered the best way to break with commercial Keynesianism. Despite arguing in favour of tax cuts in the early 1950s, Leon Keyserling now preferred to increase expenditures on education, healthcare, defence, and housing to provide the fiscal stimulus the nation needed. To facilitate this, he continued to state his National Prosperity Budget was applicable. He also argued that because this set goals for

in *Current Economic Situation and Short-Run Outlook* 86th Congress: 2nd Session (Washington DC, 1961), 114-131.

²⁶¹ Ibid (Schultze), 121. For further analysis of Schultze’s views see Davis, ‘Politics of Prosperity,’ 45-48.

²⁶² Ibid (Schultze), 114-131. For other Keynesians using this concept see Upgren, ‘Will Heller Urge Trying Tax Cuts’; E. Cary Brown, ‘Fiscal Policy in the 'Thirties: A Reappraisal,’ *American Economic Review*, 46:5 (Dec. 1956), 857-879; and Heller, Memorandum for the Files, ‘Conversation with Senator Kennedy on Economic Issues,’ 4 October 1960. Heller Papers. Box 4. JFKL.

²⁶³ For Harris’ views see Harris to Archibald Cox, ‘Re: Some Ideas and Material for Senator Kennedy’s Speech on Growth,’ 19 July 1960. Democratic National Committee Papers. 1960 Campaign

production and consumption, the policies he advocated would not be inflationary, as supply would always grow in line with demand.²⁶⁴ This meant the government could continuously deploy discretionary fiscal policies even when the economy reached full employment.²⁶⁵ In comparison, Heller did not advocate such goals so believed the economy could overheat if discretionary policies were utilised at full capacity.²⁶⁶ He said it was imperative to “keep an eye cocked but not glued” on inflation to determine when restrictive fiscal and monetary measures were required.²⁶⁷

Despite this disagreement, both Keyserling and Heller believed discretionary fiscal activism would rectify the persistent slack that beset the economy in the late 1950s. In comparison, other Keynesians argued discretionary measures were more important to re-slice the economic pie than to enlarge it. Foremost among them was Harvard’s John Kenneth Galbraith, who served as chairman of the Democratic Advisory Council’s (DAC) Economic Policy Advisory Committee in the late 1950s. Although Heller did contribute to this group’s deliberations, he did so infrequently because of the expense of travelling from Minnesota to meetings held in Washington DC.²⁶⁸ In addition, though Galbraith served as its chairman, the Advisory Committee often adopted positions reflecting the views of Keyserling. In fact, Keyserling’s influence ensured that, in their 1960 election platform, the Democrats pledged

[Henceforth DNC-1960 Papers]. Box 205. JFKL. For Lester’s views see Lester, ‘Suggestions for Improving Economic Growth,’ Summer 1960, DNC-1960 Papers. Box 205. JFKL.

²⁶⁴ See Keyserling’s following Conference on Economic Progress reports: *The “Recession” Cause and Cure* (Washington DC, 1958); *Inflation-Cause and Cure* (Washington DC, 1959); and *The Federal Budget and ‘the General Welfare’* (Washington DC, 1959).

²⁶⁵ As Keyserling put it, increased spending will “be anti-inflationary in the long run.” Keyserling to Galbraith, 15 July 1959. John Kenneth Galbraith Papers [Henceforth Galbraith Papers]. Box 40. JFKL.

²⁶⁶ See ‘Heller Urges Plan to Speed US Production’; and Heller, Excerpts from ‘A Positive Approach to Economic Growth.’

²⁶⁷ Heller, ‘The Economic Setting for Health and Welfare in the Sixties.’

²⁶⁸ See Heller, Kermit Gordon, Tobin, Gardner Ackley and Samuelson, Interview with Pechman [Henceforth CEA-OH] 1 August 1964, 6. JFKL. Oral History Collection [Henceforth -OHC].

themselves to attaining a 5 percent annual rate of output.²⁶⁹

Despite this, Galbraith's significance should not go overlooked. His views also broke with the central tenets of commercial Keynesianism. Believing the quantitative liberalism espoused by Heller and Keyserling (which involved expanding the economic pie to cater to people's material needs) would be inflationary, Galbraith argued Eisenhower's overreliance upon automaticity had resulted in insufficient investment in America's public sector during the 1950s. This caused it to go into a state of poverty. "We have a great backlog to make up on health and educational facilities, in urban redevelopment and low cost housing, in roads, in recreational facilities...and in resource development," he told the JEC in 1955.²⁷⁰ Additionally, Galbraith said Americans had spent too much wealth on private consumption thanks to the influence and power of advertising, so it was imperative to use discretionary fiscal measures to redistribute output rather than to expand it.²⁷¹

A fierce advocate of qualitative liberalism (which placed emphasis on improving the quality of life through investment in public services), Galbraith called for increased taxation on goods and services to facilitate this.²⁷² Heller vehemently opposed such a policy. In addition to labelling the idea of an 'affluent society' a "myth," he had long insisted that sales taxes failed "to protect a minimum of subsistence."²⁷³ This was because they "hit...the small income earner and [not] the large income family hardest (since they have to spend the greatest part of their income on sales-taxed items)."²⁷⁴ For Heller, Galbraith's argument for a sales tax

²⁶⁹ For Keyserling's influence over the Advisory Committee see its following statement, 'The Democratic Task During The Next Two Years,' 7 December 1958. ADA Papers. Reel 92. BL.

²⁷⁰ Galbraith, 'Fiscal Policy and Economic Prospect,' Statement before the JEC, 28 January 1955. Copy in Heller Papers. Box 5. UoM.

²⁷¹ Galbraith, *The Affluent Society* (London, 1958), 97-107, 121-123, 195-209.

²⁷² Ibid, 243-247. He also placed emphasis on personal and corporate taxation.

²⁷³ n.n., 'The Pragmatic Professor' (first quotation); and Heller to n.n., 'Memo on Sales Taxes,' 16 March 1950. Heller Papers. Box 9. UoM (second quotation).

²⁷⁴ Heller to n.n., 'Memo on Sales Taxes.'

would produce a taxation system that was too regressive. He also said it would be economically unsound to implement a sales tax, as such legislation “cuts into the mass markets which are the mainspring of a high-employment economy.”²⁷⁵ Rather than break with the use of automatic stabilisers by increasing taxes, Heller believed it was more important to do so by decreasing taxes. In addition, while he saw growth as a prerequisite for the advancement of America’s domestic and foreign goals, Galbraith felt it was first more important to redirect output towards needed areas before expanding the economy.

Despite the opposition of both Heller and Keyserling, several liberal economists agreed with Galbraith.²⁷⁶ Robert Lekachman, whilst criticising the president’s drive for a FY 1960 surplus, complained Eisenhower had deprived the nation of essential fiscal resources and thereby worsened “the imbalance in our society between private affluence and public poverty.”²⁷⁷ Writing to Heller in 1960, one of his closest friends and former Wisconsin PhD student, Joseph Pechman, stated that in light of Eisenhower’s reluctance to provide fiscal assistance to state-local governments the only way to relieve the increasing pressures upon their finances was through a sales tax. According to Pechman, “Galbraith was right.”²⁷⁸ This precipitated a defiant response from Heller that there was “[nothing] wrong about being against a national sales tax.”²⁷⁹

Additionally, Yale’s James Tobin identified with certain aspects of Galbraithian economics. Unlike Galbraith, international concerns prompted Tobin’s desire to redistribute GDP. Writing in *The Yale Review* after the launch of Sputnik,

²⁷⁵ Ibid.

²⁷⁶ For Keyserling’s dissenting views, see Keyserling to Cox, 22 September 1960. DNC-1960 Papers. Box 200. JFKL; Keyserling to Galbraith, 31 May 1960. Galbraith Papers. Box 40. JFKL; and ‘Eggheads and Politics,’ *New Republic*, 139:7 (Oct. 1958), 13-17. EBSCO.

²⁷⁷ Lekachman ‘A Primer on Inflation,’ *New Republic*, 142:5 (Feb. 1960), 15. EBSCO.

²⁷⁸ Pechman to Heller, 8 September 1960. Heller Papers. Box 2. UoM.

Tobin claimed Eisenhower's overreliance upon automatic stabilisers had produced a serious deficiency in defence spending that compromised national security. "Orthodox fiscal policies," Tobin stated, "have brought the nation to the brink of catastrophe."²⁸⁰ Like Heller, he called for more activist measures to improve America's military capabilities. "Sputnik," he said, "will be well worth the blow it has dealt our national pride if it frees national policy from the shackles of fiscal orthodoxy."²⁸¹ Yet unlike Heller, Tobin was less inclined to justify his proposals on the basis they would boost economic growth. Instead, he claimed there should be a tax on private affluence to pay for any discretionary policies.²⁸² Though his approach would still give the economy a spurt, Tobin, like Galbraith, wanted to break with commercial Keynesianism for distinct reasons and in a separate way to that of Heller.

As Sputnik gave way to the 1957-58 recession, Tobin and other liberals started to advocate discretionary measures to expand rather than to redistribute output. The Democratic candidate for the 1960 Presidential Election, Senator John F. Kennedy of Massachusetts, summed this up by vowing to "get America moving again."²⁸³ Though JFK often called upon Galbraith for advice, Paul Samuelson served as the Kennedy campaign's economist-in-residence. A professor at MIT, Samuelson had penned the nation's leading post-war Keynesian textbook and in the late 1950s was one of the most important voices advocating a break with automaticity. Like Heller, Samuelson favoured deploying discretionary measures to boost economic growth. However, he placed emphasis upon achieving this for international rather than for domestic reasons. Writing to Kennedy in May 1960, he expressed concern

²⁷⁹ Heller to Pechman, 14 September 1960. Heller Papers. Box 2. UoM.

²⁸⁰ Tobin, 'Defense, Dollars and Doctrines,' *The Yale Review*, 47 (Mar. 1958), reprinted in Tobin (ed.) *National Economic Policy* (New Haven, CT, 1966), 57.

²⁸¹ Ibid, 69.

²⁸² Ibid, 68-69.

²⁸³ John F. Kennedy, 'Remarks of Senator John F. Kennedy, Allentown, PA,' 28 October 1960. APP.

that “the USSR is growing faster than we are and there is good reason to believe that for some years to come this catching up process will go on.”²⁸⁴ It was imperative for the US to grow by at least 4 percent per year, which entailed more use of discretionary policies.²⁸⁵

In this, Samuelson again differed from Heller. He believed that, due to the respective efforts of Eisenhower and Galbraith, many people worried in 1960 that fiscal activism would be inflationary. He informed Kennedy that only through discretionary monetary policies could he achieve his aims.²⁸⁶ By this point, Tobin had accepted Samuelson’s argument. Throughout the summer of 1960, the Yale economist cogently articulated the MIT professor’s ideas. However, he did not break entirely with the views of Galbraith.²⁸⁷ Accordingly, Tobin said that, if elected, JFK should increase taxes to constrain the growth of consumption.²⁸⁸ At the same time, Tobin explained the Federal Reserve should be encouraged to lower long-term interest rates to precipitate private sector investment and stimulate growth. To achieve this, the Fed would have to reverse its “bills only” policy of purchasing short-term Treasury securities, something it had pursued since 1953.²⁸⁹ A politically astute strategy, the Harvard economist Otto Eckstein also recommended combining easy money with tight budgets to the Democratic Senator and JEC chairman Paul Douglas of Illinois. Eckstein did this in his capacity as chair of a 1959 JEC panel to recommend future policies to spur long-term growth. Following its espousal by Douglas, Samuelson, Tobin, and other Democrats, Kennedy ran on a platform to

²⁸⁴ Samuelson, ‘Notes on Economic Growth for Senator Kennedy,’ May 1960. Copy in James Tobin Papers [Henceforth Tobin Papers]. Box 1. JFKL.

²⁸⁵ Ibid.

²⁸⁶ Ibid. See too Samuelson, ‘The Growth of the Economy: Views of Prof. Paul Samuelson,’ Summer 1960. DNC-1960 Papers. Box 205. JFKL.

²⁸⁷ Tobin, Memorandum for Richard Goodwin, ‘Growth, Full Employment and Inflation,’ 16 June 1960. Tobin Papers. Box 1. JFKL.

²⁸⁸ Ibid.

implement it during his 1960 campaign.²⁹⁰

By the end of the 1950s, liberal economists had altered the debate concerning the parameters of economic policy by cogently highlighting the limits of commercial Keynesianism. As a result, Kennedy said that, if elected president, he would make greater use of discretionary measures. It is essential to note that, following the 1957-58 recession, the CED sanctioned more use of discretionary fiscal policies.²⁹¹ However, it did so right at the depths of that crisis and continued to hold fast to the idea that such measures should maintain economic stability rather than expand the rate of output.²⁹² In fact, despite acknowledging the existence of the performance gap in 1960, two CED economists argued there was no need to close it. In an essay that appeared in a book featuring the findings of the Commission on National Goals, a body established by Eisenhower in 1960, they wrote that there was no need to “feel guilty” if it were decided “that accelerating growth is not one of our most critical needs.”²⁹³ This is even though, when it outlined the stabilizing budget policy in 1947, the CED acknowledged discretionary measures could offset a hypothetical surplus that prevented the economy from reaching full employment.²⁹⁴ Concern about growth in the late 1950s was instead emphasised by the Keynesians. Walter Heller played an important but hitherto underappreciated role in this debate. Still, compared with the

²⁸⁹ Tobin, ‘Growth Through Taxation,’ *New Republic*, 143:4/5 (Jul. 1960), 15-18. EBSCO; ‘The Need for Faster Economic Growth,’ 14 June 1960. Attached to Ibid.

²⁹⁰ Importantly, unlike Tobin, both Eckstein and Douglas primarily viewed high taxes as essential to curb inflation rather than to control consumption. For Eckstein’s views see *Staff Report on Employment, Growth and Price Levels*, 86th Congress: 1st Session, (Washington DC, 1959), 422. For Douglas’ see his and Howard Shuman’s article ‘Growth Without Inflation,’ *New Republic*, 143:14 (Sept. 1960), 16-22. EBSCO.

²⁹¹ Collins, *The Business Response to Keynes*, 173-177; Stein, *The Fiscal Revolution in America*, 335.

²⁹² See ‘Anti-Recession Policy for 1958,’ A Statement by the Program Committee of the Committee for Economic Development, March 1958. ADA Papers. Reel 92. BL. As noted by Amy Davis, the CED “was very hesitant to declare that an actual slump was sufficiently severe to require” an activist response. Davis, ‘Politics of Prosperity,’ 37. Footnote 60.

²⁹³ Stein and Edward Denison, ‘High Employment and Growth in the American Economy,’ in Henry Wriston et al (eds.) *Goals for Americans: Programs for Action in the Sixties* (New York, 1960), 189-190.

²⁹⁴ Heller, ‘Taxes and the State of the Economy,’ *Challenge*, 12:8, 1 May 1964, 22. EBSCO.

Minnesotan, Kennedy initially committed himself to a tight fiscal policy and primarily wanted to use monetary policy to get the country moving again.

IV

Given the different emphasis Heller and JFK placed upon using discretionary policies in 1960, it is surprising that, after narrowly defeating the Republican Richard Nixon in that year's Presidential Election, JFK turned to Heller to head his Council of Economic Advisers. The pair had met once before, early in October 1960, but Heller played no role in JFK's run for the White House. Added to this, outside his profession Heller was unknown. He did not regularly attend meetings of the DAC's Economic Policy Advisory Committee. Nor was Heller part of the Finletter Group set up in the late 1950s to bring Keynesian economists and Democratic politicians together.²⁹⁵ Unlike Samuelson, Galbraith, Harris, Lester, and Tobin, Heller did not belong to an Ivory Tower university. Compared with Keyserling, who regularly published his views in the national press, Heller wrote only for Minnesota-based newspapers and political magazines. Given both his lack of celebrity and the difference between his and Kennedy's views on discretionary policy, asking why JFK appointed Heller as his chief economic adviser is important.

Kennedy did not initially select Heller as his CEA chairman. Paul Samuelson turned the job down before Kennedy offered it to Heller. Samuelson's decision showed that the demands of working in government differed from advising a politician in opposition. In the latter, "advisory work was not onerous, did not require extended leave of absence from academia and left public-intellectual economists free to write lucrative articles for the media."²⁹⁶ Service on the CEA, in contrast, involved

²⁹⁵ CEA-OH, 4. This is even though he did briefly join the group whilst serving as an adviser to Democratic Presidential Candidate Adlai Stevenson in 1956.

²⁹⁶ Morgan, 'Liberal Economists and the Cold War: Sputnik to Vietnam,' Paper Presented at the HOTCUS Annual Conference, St Anne's College, University of Oxford, June 2011. Author's copy.

moving to Washington, taking a pay cut, and competing with other advisers for the president's attention.²⁹⁷ Preferring to remain at MIT, Samuelson declined Kennedy's offer. After Galbraith indicated he did not want the job, Kennedy widened his search for a CEA chairman.²⁹⁸ Though Keyserling was influential within the Democratic Party at this time, he considered Kennedy too conservative during the 1960 campaign. In fact, he criticised JFK on various issues and had very little to do with his run for the White House.²⁹⁹

With Samuelson, Galbraith, and Keyserling ruled out, Heller emerged as a contender. Crucially, a development in the fall of 1960 enhanced his appeal to Kennedy. This was the fact that Kennedy abandoned the easy money-tight budget growth strategy in the face of concern it would result in dollar devaluation. The Bretton Woods Agreement of 1944 had fixed foreign currencies to the value of the dollar, which was itself fixed to the price of gold at \$35 an ounce. This enabled the US to flood post-war markets with a strong currency and a steady flow of liquidity, but Bretton Woods only worked so long as US gold reserves covered the number of dollars held abroad. By 1960, foreign nations had built-up substantial dollar surpluses. JFK's proposal to inflate the economy caused concern the US would devalue the dollar in response to a subsequent balance-of-payments crisis.³⁰⁰ By also saying he would use monetary policy to achieve this, JFK indicated he would compromise the Fed's independence.³⁰¹ Consequently, foreign dollar-holders cashed in their holdings, which caused a run on US gold reserves. To stop this, Kennedy announced on 31 October that if he got into the White House he would protect both

²⁹⁷ Ibid.

²⁹⁸ CEA-OH, 107.

²⁹⁹ Sobel, *The Worldly Economists*, 118.

³⁰⁰ See Jay Hayden, 'Gold Rush Anticipates Devaluation of Dollar,' *Boston Globe*, 21 October 1960, 13. PQHN.

³⁰¹ Morgan, 'Liberal Economists and the Cold War.'

the value of the dollar and the Fed's independence.³⁰² This closed off the easy money route to economic growth.

As Kennedy widened his search for a CEA chairman, he heard good things about Heller from Samuelson, Minnesota Governor Orville Freeman, and the Minnesota Senator Hubert Humphrey.³⁰³ This confirmed the favourable impression the economist had made on him at the pair's only meeting in October 1960. *Time* later claimed the encounter had "tipped the decision" in favour of Heller and Kennedy frequently recalled the meeting during pre-inaugural discussions of CEA appointments.³⁰⁴ After Humphrey introduced them at the Leamington Hotel in Minneapolis, the location of a campaign dinner, Heller and the presidential candidate had a "rapid-fire discussion of economic issues."³⁰⁵ To Heller, this indicated JFK had a penchant for economic policy. Kennedy expressed concern about the rate of growth and asked Heller how he could improve this. Making use of Schultze's and Upgren's ideas, Heller explained a tax cut would offset "the repressive effect of a federal fiscal system which would produce around \$7 – 8 billion at full employment *today*."³⁰⁶ While Heller later said Kennedy did not grasp this point, the candidate was impressed with Heller's "manner and approach to problems, as well as his ability to field questions swiftly."³⁰⁷

In addition, weighing in favour of Walter Heller's nomination was the Minnesotan brought an important degree of ideological balance to the new administration. JFK felt he needed a liberal economist because he had appointed fiscal conservatives to other positions, notably Douglas Dillon as Secretary of the

³⁰² Kennedy, 'Statement on Balance-of-Payments,' 31 October 1960. APP.

³⁰³ See Samuelson, CEA-OH, 112.

³⁰⁴ Samuelson, CEA-OH, 77; n.n., 'The Pragmatic Professor.'

³⁰⁵ Heller, Memorandum for the Files, 'Conversation with Senator Kennedy on Economic Issues.'

³⁰⁶ Ibid. Emphasis in the original.

³⁰⁷ Sobel, *The Worldly Economists*, 120.

Treasury. An investment banker, Dillon served in the Eisenhower administration and was a strong proponent of balanced budgets. He feared inflationary deficits would worsen the balance-of-payments and touch off another gold outflow.³⁰⁸ When he formally asked Heller to serve as his CEA chairman, Kennedy remarked, “I need you as a counterweight to him [Dillon]. He has conservative leanings, and I know your leanings are liberal.”³⁰⁹

Kennedy also felt Heller would provide geographical balance to his administration. Most of his advisers in 1960 came from Massachusetts (his native state), so JFK grew “sensitive to comment about the number of ‘Cambridge types’ in his administration.”³¹⁰ Appointing a Minnesotan would invalidate criticisms about the number of Harvard and MIT advisers working for him. Because Heller was from the Midwest, he was ideal.³¹¹ Accordingly, Heller got the nod when summoned to Kennedy’s residence in Georgetown, Washington, on 16 December. Anticipating an offer to serve as Under Secretary of the Treasury, this took Heller by surprise. He told JFK several financial, personal, and professional considerations made it “an awfully tough decision to make.”³¹²

On the financial front, Heller worried about taking a pay cut if he became CEA chairman, especially as he would have to rent a new home in Washington at the same time as his eldest son was about to start college.³¹³ Personally, Heller worried that taking up such a time-consuming post would separate him for too long from Emily, his wife. She suffered from lupus, a chronic autoimmune disease.

³⁰⁸ Jonathan Alan Lee, “‘The Strength of the Currency’: The Multinationalization of American Business, The Balance of Payments Problem, and the United States Foreign Economic Policy in the 1960’s,” PhD Thesis, University of Texas at Austin (1996), 109-112. PQDT.

³⁰⁹ Heller, CEA-OH, 119.

³¹⁰ Norton, *The Employment Act and the Council of Economic Advisors*, 177.

³¹¹ Sobel, *The Worldly Economists*, 120.

³¹² Heller, ‘Notes on Meeting with President-Elect Kennedy, 16 December 1960.’ Heller Papers. Box 5. JFKL.

³¹³ Heller, ‘Notes on the Period of Decision, 16-21 December 1960.’ Heller Papers. Box 5. JFKL.

Professionally, the Ford Foundation had recently granted Heller a fellowship and he had served as chairman of the Economics Department at Minnesota since 1957. If he took up Kennedy's offer, he realised he would have to relinquish these commitments. He also did not relish the prospect of being "very much exposed and on the firing lines as an egghead, ivory-towered liberal," who "would be fair game for every Main Street and Wall Street conservative newspaper."³¹⁴

Still, as a friend told Heller seven years previously, serving as CEA chairman was the job Heller "was practically born to do."³¹⁵ Heller himself recognised this. As he wrote at the time, "it was the most important economic policy job in the world...[I] would be part of a Kennedy administration which gave every indication of being exciting, confident, willing to move forward into the area of sensible fiscal and monetary policy...Having been a policy-orientated, institutional, applied economist all my life and in and out of government for that reason, the job did represent the pinnacle of a career."³¹⁶

After thinking about it for a week, he phoned Kennedy on 21 December to accept his offer, subject to two conditions. The first was that JFK would not appoint a resident White House economist to his administration, something Eisenhower had done in the form of Gabriel Hague.³¹⁷ The second was that Heller would himself select the two members who would serve with him on the Council.³¹⁸ Both were interlinked: as he was more a technician than a theorist, the second enabled Heller to appoint Council members who would do all the empirical and mathematical work.³¹⁹ The first ensured that as he used their work when he advanced his case to Kennedy,

³¹⁴ Ibid.

³¹⁵ Spencer Smith to Heller, 7 March 1961. Heller Papers. Box 49. JFKL.

³¹⁶ Heller, 'Notes on Period of Decision.'

³¹⁷ Heller, 'The Meeting with the President-Elect and the Announcement of my Appointment, 23 December 1960.' Heller Papers. Box 5. JFKL.

³¹⁸ Ibid.

Heller would not have to compete with another economic authority for the president's ear. After agreeing to Heller's conditions, Kennedy invited him to his residence in Palm Beach, Florida, on 23 December and announced the appointment. In doing so, Kennedy told reporters he intended "to return to the spirit as well as to the letter of the Employment Act of 1946," a statement that reaffirmed his commitment throughout 1960 to make greater use of discretionary policies.³²⁰

Not everybody agreed with either Heller's appointment or his approach. One *Chicago Tribune* reader argued Heller adhered to a "false economic thinking which promotes inflation and its inseparable bedfellow, socialism."³²¹ That same publication also claimed Heller could give "some mighty bad advice."³²² This was not least because the West Germans disregarded the policies that he pressed upon them in 1951, only for their economy to flourish. These concerns, however, were misguided. Heller's "false economic thinking" would ignite a booming economy in the 1960s and, far from being a cause for concern, Heller's earlier stints in both public service and academia furnished him with important skills that enabled him to achieve this.

His tenure as head of Economics at Minnesota, for example, "significantly honed his skills in management."³²³ Reflecting this, in 1959 Pechman described Heller as "the best administrator in the entire economics profession both here and abroad."³²⁴ Furthermore, Heller's extensive experiences in public service prior to 1960 "taught him the art of briefing people; he learnt that in government people are busy, people have a lot of different things going on, so you've got to write concisely

³¹⁹ Johnston, Interview with the Author.

³²⁰ n.n., 'Transcript of the Kennedy-Heller News Conference,' *New York Times*, 24 December 1960, 5. PQHN.

³²¹ Robert Dingleline, 'Another Keynes?' *Chicago Tribune*, 9 January 1961, 20. PQHN.

³²² n.n., 'On the Unreliability of Certain Pundits,' *Chicago Tribune*, 7 April 1961, 12. PQHN.

³²³ Eric Heller, Interview with the Author.

³²⁴ Pechman to Heller, 20 July 1959. Copy in Frederick Deming Papers. Box 5. Minnesota Historical Society [Henceforth MHS]. Importantly, this was an attribute that Harold Groves saw in Heller as a

and to the point if you want to have influence,” something at which he excelled.³²⁵ Heller brought these skills with him to Washington and, as will be demonstrated, they underwrote his effectiveness as CEA chairman.

V

By 1961, Walter Heller had become an important champion of Keynesian liberalism, even though before the mid-1950s he was far from a prominent advocate of Keynes’ ideas. At the same time, growth liberalism had eclipsed commercial Keynesianism in debates concerning economic policy. In fact, Heller and his contemporaries had discredited the latter by advocating greater use of discretionary measures. As has been demonstrated, Tobin, Samuelson, and Eckstein viewed lowering long-term interest rates as central to expanding the economy. Heller argued that there needed to be greater use of fiscal policy. Though Keyserling believed that increased expenditures should constitute the fiscal route to growth, Heller wanted to implement a large tax cut. After he entered the White House in January 1961, Heller pressed this exact policy upon Kennedy. To Heller’s surprise, JFK initially refused to embrace his recommendation. Heller thus faced the challenge of selling growth liberalism to a president unwilling to move beyond commercial Keynesianism. As he later put it, his key role as CEA chairman was to educate Kennedy.³²⁶ Assessing why this was the case, and how Heller achieved this, is crucial to understanding how Keynesian liberalism enjoyed its heyday in America.

PhD student, so Heller obviously refined it as his career progressed. See Groves to C. A. Dykstra, 8 November 1945. Harold Groves Papers. Box 5. Wisconsin Historical Society [Henceforth WHS].

³²⁵ Johnston, Interview with the Author.

³²⁶ Heller, *New Dimensions of Political Economy*, 15-36.

Chapter Three

A Keynesian Economist on the New Frontier

When John F. Kennedy entered the White House in January 1961, the man who had previously vowed to expand the rate of growth showed himself surprisingly unwilling to do so. While his desire to fulfil his campaign pledge remained strong, JFK adopted a cautious approach once in office. The run on gold in October 1960 helped precipitate this development, as did a host of other factors that this chapter will discuss. For Walter Heller and the two individuals whom he chose as CEA members – James Tobin of Yale and Kermit Gordon of Williams College – the president's new stance amounted to a large blow. The economy had been in recession for seven months, unemployment had risen to 7 percent, and the performance gap stood at \$50 billion.³²⁷ Despite numerous attempts by Heller in 1961, Kennedy proved unwilling to deploy expansionary policies. For one contemporary observer, 1961 was “the year of continuing tradition” in US economic policy.³²⁸ This chapter outlines Heller's failed attempts that year to convince JFK to embrace growth liberalism. It will demonstrate, however, that he laid the foundations for doing so in 1962.

I

After arriving on the New Frontier in late January 1961, Heller first faced the task of formulating a programme to precipitate recovery from the recession, the issue that Kennedy regarded as his most pressing domestic concern.³²⁹ This Heller started doing during the transition period, when he, Tobin, and others served on a Task Force headed by Paul Samuelson. Charged with recommending policies to Kennedy that would improve the economy, the Task Force submitted its report on January 5. It

³²⁷ Ibid, 27.

³²⁸ Flash, *Economic Advice and Presidential Leadership*, 173.

argued that the recession was the least of the new president's worries. Commenting that, within a few months, "the contraction in business can be brought to a halt," the Samuelson Report issued a stern warning "[the recession] has been superimposed upon an economy which, in the last few years, has been sluggish and tired."³³⁰ Because Kennedy did not have a coherent economic agenda – having abandoned his easy money approach at the end of the 1960 campaign – Heller believed the president "could be persuaded by cogent argument."³³¹ Hence, from the outset of the Task Force meetings Heller highlighted the merits of a tax cut.³³² He also pressed such a policy upon Kennedy when the pair discussed his appointment in December.³³³

Forced, too, to rethink their ideas, both Samuelson and Tobin saw the merits in Heller's argument. Therefore, early Task Force discussions gave priority to the notion of proposing a tax cut to get the country moving again. Once word reached Kennedy's inner circle of advisers, it became clear that they would not entertain it. Concerned that a tax cut would deprive the government of essential revenues, presidential aides Theodore Sorensen and Myer Feldman both argued that there would be no funds for pressing defence programmes.³³⁴ Sorensen also adjudged it pointless to waste political capital trying to boost the employment rate to 96 percent when 93 percent of Americans already had jobs.³³⁵ Anxious, too, that JFK had narrowly won the 1960 election, close aides did not want to give the impression that

³²⁹ Indeed, following the announcement of Heller's appointment at Palm Beach, JFK told him to start working on ideas for an anti-recession programme. See Heller, 'The Meeting with the President-Elect and the Announcement of my Appointment, 23 December 1960.'

³³⁰ Samuelson, 'Prospects and Policies for the 1961 American Economy,' in *Hearings before the JEC on the January 1961 Economic Report* 87th Congress: 1st Session (Washington DC, 1961), 703.

³³¹ Tobin and Solow, 'Introduction,' in Tobin and Murray Weidenbaum (eds.) *Two Revolutions in Economic Policy: The First Economic Reports of Presidents Kennedy and Reagan* (Cambridge, MA, 1988), 6.

³³² Samuelson, CEA-OH, 146.

³³³ Heller, 'Notes on Meeting with President-Elect Kennedy, 16 December 1960'; and 'The Meeting with the President-Elect and the Announcement of my Appointment, 23 December 1960.'

³³⁴ Pechman, CEA-OH, 146

³³⁵ Tobin, CEA-OH, 218-219.

he was a reckless spender. This, they reasoned, might alienate conservative Southern Democrats and Republican lawmakers and thereby jeopardise his ambitious agenda.³³⁶ They also wanted Kennedy to stress the theme of national self-sacrifice in his forthcoming Inaugural Address, something a tax cut proposal would contradict.³³⁷ These political considerations forced Samuelson, Heller, and Tobin, to tone down their recommendations. As a result, the Samuelson Report proposed an anti-recession programme that called for either accelerated or increased expenditures on existing measures. If the recession worsened, only then should Kennedy cut taxes.³³⁸

Undaunted that, during the transition period, Kennedy had rebuffed a growth-maximising tax cut, Heller persisted in his efforts for such a measure once in the White House. Though Kennedy made it clear that combatting the recession was his immediate priority, he continued to express concern about the poor rate of growth. This encouraged Heller to reiterate his case for activist economics.³³⁹ Accordingly, during Kennedy's first cabinet meeting on January 26, the CEA chairman gave a brief presentation emphasising how there was "considerable leeway for expansionary policies."³⁴⁰ Two days earlier, he passed Kennedy a copy of a *Business Scope* article written by Harvard's James Duesenberry, which argued that a further \$5 billion added to the Eisenhower-inherited FY 1961 budget would produce sufficient growth and revenues to help fund Kennedy's ambitious agenda.³⁴¹ Despite this, the new president

³³⁶ Samuelson, CEA-OH, 170-173; Davis, 'Politics of Prosperity,' 98-99.

³³⁷ In fact, JFK himself made this point to Heller during their meeting in Palm Beach, saying it "would be awfully hard to square [a tax cut] with the sacrifice theme." Heller, 'The Meeting with the President-Elect and the Announcement of my Appointment, 23 December 1960.'

³³⁸ Samuelson, 'Prospects and Policies for the 1961 American Economy,' 706-708, 710.

³³⁹ Indeed, when Kennedy received the Samuelson Report at the Carlyle Hotel in New York on January 5, Heller said, "he seemed to like both the content and language" of it, despite having rejected a tax cut. Heller, 'Notes on First Ten Days in Washington, January 4-13, 1961,' Heller Papers. Box 3. JFKL. Unless otherwise stated, all documents in this chapter, chapter four, chapter five, and chapter six that are cited from Heller's Papers are from the collection held at the JFK Library.

³⁴⁰ Heller, 'Handwritten Notes for Presentation at Cabinet Meeting, Thursday 26 January 1961.' Heller Papers. Box 6.

³⁴¹ Heller, Memorandum for the President, Untitled, 24 January 1961. Heller Papers. Box 5.

proved unreceptive to greater use of discretionary measures. To the CEA chairman's dismay, Kennedy responded that his sole concern was fighting the recession. Furthermore, the president revealed he had reached agreement with the Democratic leadership in Congress not to operate a deficit in FY 1962, which necessitated combatting the recession through a balanced budget.³⁴² This "bombshell," as Heller described it, revealed the scope of the task involved in converting JFK to modern Keynesian thinking.³⁴³

Reinforcing Kennedy's caution was his growing concern about the balance-of-payments deficit. This was particularly following the findings of another Task Force investigation overseen by Allan Sproul, the former chair of the New York Federal Reserve.³⁴⁴ Kennedy received Sproul's report prior to his inauguration and it warned that expansionary policies could worsen the payments problem, heighten foreign anxieties about devaluation, and thereby spark another run on gold.³⁴⁵ Kennedy heard this argument, too, from Treasury Secretary Douglas Dillon, most notably at the cabinet meeting on January 26 when Heller urged expansionary policies.³⁴⁶ Not only was the president already familiar with Dillon's point, the Treasury Secretary's influence was strengthened by the fact that he could draw on the views of bankers and financiers to bolster his case. By comparison, the Employment Act had formed the CEA purely as an advisory body. Unlike the long-established Treasury Department, Heller lacked a constituency whose anxieties he could represent in the meeting on January 26. Because of this, the Treasury Secretary started out with the advantage over Heller for the president's ear. This ensured that

³⁴² Heller and Samuelson, CEA-OH, 174.

³⁴³ Ibid, 174.

³⁴⁴ For discussion of the Sproul report's impact on JFK see Lee, "The Strength of the Currency," 125-128.

³⁴⁵ Allan Sproul, 'The Economic Situation and the Balance of Payments,' in *Hearings before the JEC on the January 1961 Economic Report*, 722.

Kennedy prioritised Dillon's concerns about the balance-of-payments deficit and the value of the dollar over Heller's anxieties about growth.

In addition, Kennedy refused to heed Heller's call for a tax cut out of concern that such a course of action would antagonise conservative members of the business community (represented primarily in the NAM and COCUS). The confidence of these individuals, the president believed, was integral to facilitating economic expansion.³⁴⁷ However, they failed to support Kennedy throughout 1960, deeming him a reckless spender. The appointment of Heller did little to assuage these concerns, with columnist Arthur Krock describing the new CEA chairman as an "inflationist."³⁴⁸ Unsurprisingly, the president remarked later on in his presidency, "I do not think it wholly inaccurate to say that I was the second choice of a majority of businessmen for the office of President."³⁴⁹ Fearing that business confidence in his administration was low, JFK was prepared to go "out of his way" to court business leaders.³⁵⁰ This initially weighed against his approval of expansionary deficits.³⁵¹

Kennedy's lack of economic knowledge further impeded his embrace of Heller's ideas.³⁵² His previous exposure to views akin to Dillon's, the influence of his father's economic conservatism, and his own proclivity towards spending money efficiently, all ensured that Kennedy's economic outlook was traditional.³⁵³ He clearly had an interest in economics and, having briefly studied the subject when Franklin Roosevelt made a quasi-Keynesian turn in the late 1930s, Kennedy understood the utility of deficits as a countercyclical weapon. Nevertheless, JFK

³⁴⁶ Heller 'Handwritten Minutes of Cabinet Meeting, 26 January 1961.' Heller Papers. Box 6.

³⁴⁷ See Morgan, 'Promoting Prosperity.'

³⁴⁸ Rowen, *The Free Enterprisers*, 155-156 (quotation 155).

³⁴⁹ Kennedy, 'Address before the United States Chamber of Commerce on Its 50th Anniversary,' 30 April 1962. APP.

³⁵⁰ See n.n., 'Wooing Support from Business,' *BusinessWeek*, 18 February 1961, 23. BL

³⁵¹ Matusow, *The Unraveling of America*, 33.

³⁵² See Schlesinger Jr., *A Thousand Days: John F. Kennedy in the White House* (London, 1965), 543; and Theodore Sorensen, *Kennedy* (London, 1965), 395.

worried that, if deployed in the upstage of the business cycle, deficits would generate inflation and thereby produce criticisms of fiscal irresponsibility.³⁵⁴ Once in the White House, he often recalled that, partly because of this, so few Democratic Senators supported a tax cut during the 1957-58 recession.³⁵⁵ As one historian put it, Kennedy was “not persuaded that the professors [on the CEA] were right,” despite Heller’s attempts to sell him a tax cut.³⁵⁶

To Heller’s consternation, the new president decided to tread cautiously. This was evidenced in his January 30 State of the Union address. Despite recognising the slack that beset the economy, JFK pledged “of necessity” to “build on the spending and revenue estimates already submitted.”³⁵⁷ Strictly speaking, this was not a commitment to balancing the FY 1961 budget, as the previous administration had proposed to do so believing there would be an upturn in the economy.³⁵⁸ At the end of January, such an upturn looked unlikely. Therefore, JFK accepted the inevitability of a deficit for FY 1961.³⁵⁹ Nevertheless, he was determined to ensure that it would also be minuscule. Against Heller’s wishes, Kennedy rejected the idea of a tax cut in a press conference on February 1.³⁶⁰ Deeply discouraged, Heller took comfort only from managing to place certain “escape hatches” into the State of the Union address: JFK would waive his commitment to sound finance either if the Cold War got hotter or if the economy continued to remain in recession.³⁶¹ Relieved that Kennedy had not indefinitely closed the door to growth economics, Heller, Tobin, and Gordon, formulated a modest anti-recession programme, one that Kennedy announced on

³⁵³ For the influence of his father see Pechman and Samuelson, CEA-OH, 46.

³⁵⁴ See Erwin C. Hargrove and Samuel A. Morley (eds.) *The President and the Council of Economic Advisers: Interviews with CEA Chairmen* (London, 1984), 165-166.

³⁵⁵ Heller, CEA-OH, 141.

³⁵⁶ Matusow, *The Unraveling of America*, 45.

³⁵⁷ Kennedy, ‘Annual Message to Congress on the State of the Union,’ 30 January 1961. APP.

³⁵⁸ Davis, ‘Politics of Prosperity,’ 107.

³⁵⁹ Samuelson, CEA-OH, 214.

³⁶⁰ Kennedy, ‘The President’s News Conference,’ 1 February 1961. APP.

February 2.

In short, this adhered to the first set of policies outlined in the Samuelson Report. It provided a \$2 – 3 billion stimulus (approximately 0.6 percent of GDP) that affected only the FY 1961 budget, which Kennedy could attribute to Eisenhower.³⁶² To inject money into the economy quickly, it accelerated the construction of post offices and highways, encouraged taxpayers to file earlier returns, called for a minimum wage increase, and unemployment compensation extension.³⁶³ Whilst it certainly provided a shot in the arm, the anti-recession programme was largely devoid of any new discretionary measures. As such, it did little to challenge the prevailing orthodoxy of commercial Keynesianism. Reflecting this, *BusinessWeek* declared that Kennedy was “paying tribute to Eisenhower’s stickiest legacy: the principle of the balanced budget.”³⁶⁴ Such was the anti-recession programme’s lack of fiscal activism, Heller worried that it would be criticised for being too modest. In fact, he had the CEA’s professional staff check that it contained the same useful measures enacted in the previous downturn.³⁶⁵ Nevertheless, he did convince Kennedy to increase social security benefits, but to delay contributory payments until January 1963, which provided the programme with part of its main stimulus. This constituted a notable achievement given the president’s fiscal conservatism: as one Treasury official put it, “Heller made that stick.”³⁶⁶

Because the anti-recession programme eschewed fiscal activism, Heller wanted monetary policy to be more expansionary. Accordingly, he proposed that the

³⁶¹ Heller, CEA-OH, 214; Kennedy, ‘Annual Message to Congress on the State of the Union.’

³⁶² Davis, ‘Politics of Prosperity,’ 110-111.

³⁶³ Kennedy, ‘Special Message to Congress: Program for Economic Recovery and Growth,’ 2 February 1961. APP.

³⁶⁴ n.n., ‘Kennedy Moves-Cautiously,’ *BusinessWeek*, 4 February 1961, 15-16. BL.

³⁶⁵ Heller, Memorandum for Walter Stettner, ‘Catalogue of Anti-Recession Measures,’ 20 February 1961. Heller Papers. Box 20.

³⁶⁶ Cited in n.n., ‘How Kennedy’s CEA Sees Road to Growth,’ 46.

Fed should lower long-term interest rates by purchasing long-term Treasury securities, a policy that Tobin had suggested in 1960.³⁶⁷ By doing this, commercial banks would be able to increase their reserves. This would enable them to provide more credit to fund mortgages, plant and equipment, and state and local facilities, all of which were integral to the economy's productive capacity.³⁶⁸ Heller proposed this policy in spite of JFK's previous vow to protect the Fed's independence. He also did so in face of concerns it would worsen the balance-of-payments by encouraging foreign investors to withdraw funds from the country. In response, Heller argued that foreigners typically purchased short-term government securities, so lowering long-term rates would not be a problem.³⁶⁹ This necessitated keeping short-term rates high. Because the Fed had previously purchased only short-term Treasury securities, the CEA's plan required it to change its policies.³⁷⁰

Known as "Operation Twist," Dillon supported this monetary strategy (as he preferred an easy monetary policy to an expansionary fiscal one). However, the Fed chairman William McChesney Martin was reluctant to sign up to it. A banker who shared Eisenhower's economic conservatism, Martin felt that he and that president "had just won a hard battle against the inflationary psychology of the mid-fifties," having tightened interest rates to achieve this end.³⁷¹ Heller proved influential in getting Martin to adopt the CEA's more expansionary approach. In February, Martin had several White House meetings with Kennedy, after which he agreed to deploy Operation Twist. As one insider noted, "Everyone working on the problem within the administration deserves credit [for Martin's conversion], but if any man was to be

³⁶⁷ Heller, Memoranda for Kennedy, 'Details on Federal Reserve Operations and Policy,' and 'Interest Rates,' both on 30 January 1961. POF. Box 73.

³⁶⁸ Ibid.

³⁶⁹ Ibid.

³⁷⁰ As indicated in Chapter One, the Fed primarily manipulates both short and long-term interest rates through purchasing short or long-term Treasury securities.

singled out, it was Walt. He was at his most persuasive, and that's pretty damned persuasive."³⁷²

As a result, the Fed started purchasing long-term Treasury securities on February 26, two-and-a-half weeks after Kennedy announced a separate programme to help ease the payments problem.³⁷³ Combined with the CEA's anti-recession measures, these constituted Kennedy's opening economic agenda. Whilst this was certainly far more modest than Heller wanted, John Kenneth Galbraith dubbed it "the right first step" toward a more activist approach.³⁷⁴ Seeking to build upon this, Heller renewed his attempt to cut taxes.

II

In his press conference on February 1 and in his anti-recession message a day later, Kennedy declared that he would keep a close eye on the economy throughout the ensuing months. If his anti-recession measures did not stimulate the economy, the president said he would not hesitate to propose further action. Despite Heller's failure in January to convince Kennedy to embrace fiscal activism, the decision to later review the state of the economy gave the CEA chairman another opportunity to reiterate his case.³⁷⁵ Believing strongly that the real economic problem was chronic slack rather than a mild downturn, Heller was convinced that bold measures would be required even if the economy showed signs of recovering.³⁷⁶ On February 20, shortly after he formulated the anti-recession programme, Heller instructed Tobin and Gordon to gather material for "a brief but outspoken memo [to Kennedy] on the tax

³⁷¹ Tobin, *The New Economics: A Decade Older* (Princeton, NJ, 1972), 12.

³⁷² Cited in Charles B. Seib, 'The Mild-Eyed Liberals-David Bell and Walter Heller,' in Lester Tanzer (ed.) *The Kennedy Circle* (Washington DC, 1961), 102.

³⁷³ Kennedy, 'Special Message to the Congress on Gold and Balance of Payments Deficit,' 6 February 1961. APP.

³⁷⁴ Galbraith, Memorandum for the President, 'Economic Saints and Radicals,' 2 February 1961. Heller Papers. Box 5.

³⁷⁵ Davis, 'Politics of Prosperity,' 121-122.

³⁷⁶ *Ibid*, 121-122.

cut issue.”³⁷⁷ Specifically, Heller wanted to highlight “why you ‘can’t go wrong,’ economically, with a tax cut.”³⁷⁸ He suggested it was necessary to provide a “sharp demonstration of our economic slack, showing how far below our potential we are now as compared with the trough of the 1958 recession.”³⁷⁹ Straight after formulating the anti-recession programme, Heller pushed once again for a tax cut.

This time, he wanted to do more than simply use internal channels to make his case to Kennedy. Heller had realised that “to get the kind of political leverage that you wanted on the President, you had to have an outside presence [too].”³⁸⁰ Kennedy previously told Heller to educate the public about the merits of anti-recession deficits and Heller recognised this provided him with an opportunity for presidential education as well.³⁸¹ This was because Kennedy would have to read, correct, and approve every public statement that the CEA made, giving Heller an additional avenue through which the president could absorb his ideas. This was particularly important due to the Council’s lack of political constituency. At first, Heller envisioned doing this by creating an advisory committee comprised of representatives from government, labour, and business that would make statements on behalf of the president on closing the performance gap.³⁸² Upon realising the political difficulties involved in establishing such a committee, however, the CEA chairman focused on using just the Council’s pulpit for public education to bolster his case to Kennedy.³⁸³

Two instances early in March demonstrated this approach. One was an article

³⁷⁷ Heller, Memoranda for Tobin and Kermit Gordon, ‘Eventual Memo to the President on Tax Cuts,’ and ‘Benchmarks for Measurement of Current Recession and Growing Gap,’ both on 20 February 1961. Heller Papers. Box 20.

³⁷⁸ Ibid.

³⁷⁹ Ibid.

³⁸⁰ Heller, Interview in Hargrove and Morley, 188.

³⁸¹ JFK told Heller this on 5 January. See Heller, ‘Notes on First Ten Days in Washington, January 4-13, 1961.’

³⁸² Heller, Memorandum for Kennedy, ‘A Possible ‘Blue-Ribbon’ Advisory Committee on Full Recovery,’ 24 February 1961. POF. Box 63a.

penned by Heller for *Life* magazine. In the lead up to its publication, Heller sent a draft to the president, who made changes to both the content and the language.³⁸⁴ A clear expression of the economy's underperformance, Heller's *Life* article provided the "sharp demonstration" that the CEA chairman expressed the need for in his February 20 memo.³⁸⁵ Noting that "beneath the obvious cyclical recession lie two deeper and harder problems: the slack and the slowdown," Heller explained that in the fourth quarter of 1960 actual output was 8 percent below full capacity.³⁸⁶ This indicated that the recovery from the 1957-58 recession had "petered out too soon and too far short of full employment."³⁸⁷ For Heller, this was "the true measure of our economic problem: not where we have sagged in the past nine or 10 months but the gap between where we are and where we should be."³⁸⁸ To drum home his point to Kennedy, Heller made use of a vivid analogy. "The economy," he said, "is in the position of the .300 hitter who started the 1960 season batting a weak .250, then slumped to .230. It is true that his slump is a mild one, if we look only at his 1960 average. All he need do is climb back to .260 to top his best in 1960. Yet no sports fan would be fooled by this upturn into thinking that the one-time .300 hitter had regained his old batting form."³⁸⁹

Expecting JFK to absorb this message, Heller also used the CEA's March 6 Joint Economic Committee testimony for presidential education. This time, he delved specifically into the causes of the economy's persistent slack. Beforehand, the CEA held a meeting with its economic consultants – including Samuelson, Galbraith, and

³⁸³ Heller, Memorandum for Kennedy, 'The Blue-Ribbon Committee on Full Recovery,' 24 February 1961. POF. Box 63a.

³⁸⁴ The draft Heller sent to Kennedy is available in POF. Box 63a.

³⁸⁵ Davis, 'Politics of Prosperity,' 122.

³⁸⁶ Heller, 'The Economy is like a Regular .300 Hitter,' *Life*, 10 March 1961, 24-25. Copy in Kermit Gordon Papers [Henceforth Gordon Papers]. Box 34. JFKL. From here, every reference to Kermit Gordon's papers relates to the collection held at the JFK Library.

³⁸⁷ Ibid, 24-25.

³⁸⁸ Ibid, 24-25.

Harris – to establish how best it should approach its JEC testimony. There, they decided to emphasise how the automatic stabilisers acted as a restraint on the economy in the upstage of the business cycle.³⁹⁰ As a result, the CEA's testimony attributed the economy's underperformance to the tax system's built-in flexibility. It made the point that "as soon as business conditions take a turn for the better [in 1961], we can expect the federal tax system automatically to cut into the growth in private incomes."³⁹¹ A reiteration of the arguments previously advanced by both Charles Schultze and Arthur Upgren, the CEA's testimony further explained that at full employment the tax system would automatically generate an \$11 billion surplus. This meant that a tax cut was required to offset this.³⁹² Importantly Heller wanted this to be temporary, rather than permanent. He reasoned that once the economy reached full employment and tax rates returned to their previous levels the government could take advantage of the substantial surplus that would ensue.³⁹³ A statement of growth liberalism, Kennedy read all 56 pages of the Council's testimony prior to March 6, which Heller later called "a milestone in the education of the president."³⁹⁴ Still, this did not mean that JFK had become receptive to his CEA chairman's ideas.

As Heller publicly stated his case in early March, dissenting voices created doubt in the president's mind. By arguing that the automatic stabilisers sucked too much purchasing power from the economy, Heller attributed the performance gap to a deficiency in overall demand. Just a day after his JEC testimony, William McChesney Martin challenged this interpretation. Appearing before that same body, Martin

³⁸⁹ Ibid, 24-25.

³⁹⁰ Council of Economic Advisers [Henceforth CEA], 'Minutes of Meeting of Economists to Discuss the Council's Testimony before the Joint Economic Committee,' 22 February 1961. Heller Papers. Box 8.

³⁹¹ 'Statement of Walter W. Heller, Chairman, Council of Economic Advisers, Accompanied by Kermit Gordon and James Tobin,' in *Hearings before the JEC on the January 1961 Economic Report*, 301.

³⁹² Ibid, 296, 303.

³⁹³ Ibid, 307.

advanced an idea shared by certain segments of both the academic community and the Democratic Party. This stipulated that the root causes of the economy's deficient performance were structural rather than cyclical. To justify this, Martin pointed to "the idleness of many West Virginia coal miners, Eastern and Midwestern steel and auto workers, West Coast aircraft workers, and like groups."³⁹⁵ According to Martin, specific changes within the dynamics of the economy had displaced these individuals. Auto plants made more use of machines, whilst coal was less widely used. Others who were unemployed either lacked sufficient training, lived in areas where demand for their skills was non-existent, or were unable to move to areas where there was work. For Martin, the slack that beset the economy was a problem that would persist regardless of how much demand there was. What was required were specific actions that took "into account the who, the where, and the why of unemployment."³⁹⁶ This included retraining or relocating the unemployed, as well as the passage of measures that would stimulate business investment to create more jobs.³⁹⁷

The Democratic Senator Paul Douglas, author of several initiatives to help depressed areas during the late 1950s and early 1960s, shared Martin's concerns.³⁹⁸ Members of the Treasury, the Departments of Labor and Commerce, as well as the Department of Health, Education and Welfare, were also like-minded.³⁹⁹ As a senator, JFK had taken an interest in the New England economy's underperformance, largely caused by its declining textile and shoe industries, which made him

³⁹⁴ Heller, CEA-OH, 297.

³⁹⁵ 'Statement of W. M. Martin Jr.,' in *Hearings before the JEC on the January 1961 Economic Report*, 470.

³⁹⁶ Ibid, 470.

³⁹⁷ Ibid, 471.

³⁹⁸ For a good overview of Douglas' concerns see Roger H. Davidson, 'Eisenhower and Depressed-Areas Legislation, 1955-1961.' Available at: <https://www.american.edu/spa/ccps/upload/Davidson-paper.pdf> [accessed 01/05/2017]

³⁹⁹ For a good overview of those who supported the 'structuralist' perspective see Davis, 'Politics of Prosperity,' 123-125.

sympathetic to the argument that unemployment was structural in nature.⁴⁰⁰ Given the publicity caused by Martin's testimony, Heller recognised he needed to refute it robustly.⁴⁰¹ True, he supported worker retraining and tax incentives for businesses, but the CEA chairman understood that if the president became influenced too much by the 'structuralists' they would "use their analysis as a club to beat down measures for expansionary monetary and fiscal policy."⁴⁰² In the wake of Martin's testimony, he instructed staff members Robert Solow of MIT and Samuel L. Brown to both verify the Council's analysis and evaluate the accuracy of the Fed's data. He also confessed that if the CEA had made a mistake analysing the economy's problems then he would have to back down.⁴⁰³

To his relief, Solow and Brown's review found that there was no evidence to suggest that Heller should do so. This was especially because the source Martin used to substantiate his case "agree[d] that the current scene contains plenty of cyclical unemployment."⁴⁰⁴ Council consultant and Brookings economist Joseph Pechman further pointed out that the unemployment rate had increased by over 2 percent since the previous spring, a trend that structural factors could not have caused.⁴⁰⁵ Accordingly, Heller stood by the Council's conclusions. Nevertheless, he did not want a protracted debate over the root cause of the economy's slack, knowing this would distract him from advancing his case for expansionary policies. Therefore, he advised Kennedy to put the conflict between the CEA, the Fed, and others down to "differences of emphasis" rather than substantial differences of opinion, something

⁴⁰⁰ Harris, *Economics of the Kennedy Years*, 17.

⁴⁰¹ Tobin, CEA-OH, 285. As Tobin put it, the CEA needed to "nail it."

⁴⁰² Heller to Nat Weinberg, 21 August 1961. Heller Papers. Box 50.

⁴⁰³ Davis, 'Politics of Prosperity,' 130.

⁴⁰⁴ Solow, Memoranda for Heller, Gordon and Tobin, 'Martin's Testimony and Structural Unemployment,' and 'More on Structural Unemployment,' 10 March 1961 and 13 March 1961. Both in Gordon Papers. Box 30.

⁴⁰⁵ Gordon to Heller, 'Pechman on Structural Unemployment,' 16 March 1961. Gordon Papers. Box 30.

that Martin and Dillon agreed to do.⁴⁰⁶ Subsequently Kennedy downplayed the issue in a press conference on March 15, allowing Heller to refocus his efforts upon convincing the president to cut taxes.⁴⁰⁷

This he did in a memo to the president on March 17, for which Gordon and Tobin had both gathered material. An amalgamation of the arguments advanced in both Heller's *Life* article and the CEA's JEC testimony, this noted that the president's second look at the economy "will show that we are still in serious economic trouble, even if an upturn is in the making."⁴⁰⁸ The performance gap, Heller explained, would be around \$40 billion by the end of 1961. As JFK had restored confidence in the dollar following the announcement of both his anti-recession and balance-of-payments programmes, the CEA chairman argued that running a deficit would not cause a run on gold. Instead, it would be economically beneficial.⁴⁰⁹ "To illustrate what an aggressive fiscal policy can accomplish, suppose we were to increase government expenditures [by \$2.5 - \$3 billion] and temporarily cut taxes [by \$7 billion] to produce a \$10 billion deficit in fiscal 1962. The production gap will be nearly \$20 billion smaller by the end of the year."⁴¹⁰ Now more mindful of the importance that Kennedy afforded political considerations, Heller highlighted how the president faced the prospect of running for re-election with a higher average unemployment rate than both Truman and Eisenhower.⁴¹¹ He also noted that a \$10 billion deficit for FY 1962 would be neither irresponsible nor inflationary. This

⁴⁰⁶ See Samuel L. Brown, Memorandum for Heller, 'Conflict Between Council's Testimony and that of Chairman Martin Concerning Unemployment, JEC Hearings,' 9 March 1961. Gordon Papers. Box 30. Davis attributes the "differences of emphasis" idea to Robert Solow, who suggested it to Heller a day later. But this memorandum indicates that Brown first used the phrase. Davis, 'Politics of Prosperity,' 131.

⁴⁰⁷ Kennedy, 'The President's News Conference,' 15 March 1961. APP.

⁴⁰⁸ Heller, Memorandum for the President, 'The Economics of the Second-Stage Recovery Program,' 17 March 1961. POF. Box 73.

⁴⁰⁹ Ibid.

⁴¹⁰ Ibid.

⁴¹¹ CEA, 'A Second Look at Economic Policy in 1961,' 17 March 1961. Attached to Ibid.

would be smaller than Eisenhower's largest peacetime deficit (for FY 1959), whilst there was "plenty of slack to take up before inflationary inhibitions" could occur.⁴¹²

With Kennedy unmoved by this logic, Heller reported to his CEA colleagues that he had been "universally complimented on the cogency and clarity of the memo and clobbered...by the assemblage. It was done on the basis of political unacceptability of the tax cut."⁴¹³ Somewhat naively, Heller had suggested that if Kennedy promoted a tax cut but failed to get it passed the president could blame the poor performance that would ensue upon his opponents.⁴¹⁴ This was something JFK did not buy because the Employment Act had made him the chief manager of prosperity.⁴¹⁵ He also continued to believe that the type of deficit that Heller proposed would be inflationary, which would lead to him being labelled a reckless spender. In response, Heller suggested that some of these concerns "might be overcome" by giving taxpayers a rebate for FY 1960. This "would be concentrated now, when we are at or near the bottom of the recession, and most obviously need a shot in the arm."⁴¹⁶ To Heller's frustration, the president issued a statement on March 24 that reaffirmed his commitment to commercial Keynesianism. "The budget," this said, "[should] be in balance over the years of the business cycle – running a deficit in years of recession...and running a surplus in years of prosperity, thus curbing inflation."⁴¹⁷ Heller's attempt to make a compelling case for tax reduction by taking advantage of Kennedy's decision to review the state of the economy, had failed.

III

⁴¹² CEA, 'A Second Look at Economic Policy in 1961.'

⁴¹³ Heller, Memorandum for Tobin, Gordon, and Solow, 'Activities from March 17 to March 24, 1961,' 27 March 1961. Heller Papers. Box 3.

⁴¹⁴ CEA, 'A Second Look at Economic Policy in 1961.'

⁴¹⁵ Gordon, CEA-OH, 370.

⁴¹⁶ Heller, Memorandum for the President, 'Retroactive Income Tax Cut for 1960,' 21 March 1961. Heller Papers. Box 3.

⁴¹⁷ Kennedy, 'Special Message to Congress on Budget and Fiscal Policy,' 24 March 1961. APP.

The economy improved throughout the spring and early summer of 1961, which led Kennedy to further question the need for a strong fiscal stimulus. Reflecting this, as Heller and other Council members talked over lunch in the White House Staff Mess one day, Sorensen walked passed and jested, “There they are, contemplating the dangers of an upturn!”⁴¹⁸ In response, Heller switched to pressing different discretionary policies upon the president to convince him to move beyond commercial Keynesianism. In doing so, the CEA chairman demonstrated that, compared with other liberal economists, he was more pragmatic than doctrinaire. Leon Keyserling and John Kenneth Galbraith, for example, were unwilling to alter their policy prescriptions because they viewed them as more than just an economic necessity: they would also simultaneously advance their respective ideological goals.⁴¹⁹ On the other hand, Heller viewed attaining full employment as his chief objective. In the absence of tax reduction, he was “ready to bend and modify [his] economic philosophy” to facilitate this.⁴²⁰ Accordingly, from mid-March through to June, the CEA chairman championed increased spending.

What prompted him to do so was the fact that Senator Joseph P. Clark of Pennsylvania had earlier introduced a measure that would provide the president with stand-by authority to grant funding to the states for public works if the unemployment rate failed to drop significantly. Even though this would only offer a modest stimulus, Heller recognised that Clark’s proposal could help offset the slack that beset the economy. It would also provide the president with a powerful tool against a future recession. On 23 March, Heller recommended the Clark bill to Kennedy.⁴²¹ Later, he appointed Kermit Gordon onto a three-man White House committee charged with

⁴¹⁸ Heller, *New Dimensions of Political Economy*, 31-32.

⁴¹⁹ Johnston, Interview with the Author.

⁴²⁰ Seib, ‘Their Ideas Will Shape Your Future,’ *Nation’s Business*, May 1961, 64. Copy in POF. Box 73.

appraising its merits.⁴²² Its report, circulated on April 17, recommended that the president should endorse the Clark bill.⁴²³ Only a day later, committee member Robert Turner (from the Bureau of the Budget) changed his mind, which forced Heller and Gordon to defend their case.

Turner did so on the grounds that the Clark bill prioritised “those projects that are planned and ready to go,” as opposed to “those which contribute most to national objectives and to long-run economic growth.”⁴²⁴ He also argued that because “a substantial recovery in business activity is under way,” the Clark bill was “*not* the kind of expenditure program best suited to” the more vibrant economic conditions.⁴²⁵ Despite Gordon’s response that the measure would offset the economy’s persistent slack, right through to early May other individuals expressed their disapproval of it – though for different reasons.⁴²⁶ The head of the Department of Labor argued that parts of Senator Clark’s proposal were “too modest,” whilst Dillon opposed it as too bold.⁴²⁷ He argued that, once triggered, it would unnecessarily increase the deficit and worsen foreign fears about the balance-of-payments. Like Turner, the Treasury Secretary also believed that the economy would experience a “vigorous pickup,” so saw no justification for immediate enactment of the Clark bill.⁴²⁸ Undeterred, Heller had already instructed the CEA staff to refine its trigger mechanism and suggest modifications to the measure so that it would provide funds for federal public works

⁴²¹ Davis, ‘Politics of Prosperity,’ 139.

⁴²² Heller, Memorandum for Tobin and Gordon, ‘Activities from March 17 to March 24, 1961.’

⁴²³ Gordon, Robert Turner and Lee White, ‘Proposal for a Second Stage Economic Program,’ 17 April 1961. Heller Papers. Box 21.

⁴²⁴ Robert Turner, Memorandum for David Bell, Untitled, 18 April 1961. Heller Papers. Box 21.

⁴²⁵ Ibid. Emphasis in the original.

⁴²⁶ Gordon, Memorandum for Bell, ‘Stand-by Program,’ 19 April 1961. Heller Papers. Box 21.

⁴²⁷ Arthur Goldberg, Memorandum for Sorensen, Untitled, 19 April 1961. Heller Papers. Box 21.

⁴²⁸ Solow, Memorandum for Heller, Gordon and Tobin, ‘Treasury Comments on Second Stage Program,’ 22 April 1961; and Gordon, Memorandum for Heller and Tobin, ‘Secretary Dillon’s Views on the Stand-by Proposal,’ 5 May 1961. Both in Heller Papers. Box 21.

projects too.⁴²⁹ Having done so, he wrote to Kennedy on May 10 and outlined the economic argument for a measure such as the Clark bill, saying the economy “need[s] the added stimulus.”⁴³⁰ To bolster his case, he also obtained endorsements from 14 economists of various persuasions.⁴³¹

Despite these efforts, by mid-May the prospects of JFK endorsing Senator Clark’s measure all but disappeared. Whilst the president liked the principle that underlined it, two factors made him reluctant to promote it. Firstly, he agreed with Turner and Dillon that it was pointless to ask for greater discretionary measures in the recovery phase of the business cycle. Congress would not entertain this, even if there would be no robust recovery.⁴³² Secondly on March 28, following a review of the nation’s military capabilities, Kennedy had requested an extra \$650 million in defence spending. This, too, gave the economy a boost. It also made him equally determined not to promote any new expenditure (lest he be criticised for being fiscally irresponsible). However, throughout April and May the president continued to worry about the nation’s defence capabilities. This was particularly following the Bay of Pigs fiasco on April 17, which followed the Soviet Union’s triumph of sending the first human into space.⁴³³ As a result, Kennedy returned to Congress on May 25 and asked for \$800 million more in military spending. To reassure his critics that he intended to be responsible, he asked the legislature to “refrain from adding funds or programs...to the Budget,” which sounded the death knell for the Clark bill.⁴³⁴ Heller thus did not persuade Kennedy to promote more spending on public

⁴²⁹ Heller, CEA-OH, 372-373.

⁴³⁰ Heller, Memorandum for the President, ‘Economic Background of the Second-Stage Economic Program,’ 10 May 1961. Heller Papers. Box 21.

⁴³¹ Barbara Berman, Memorandum for Heller, ‘Economists’ Opinion on S. 986, the ‘Emergency Employment Acceleration Bill,’ 10 May 1961. Heller Papers. Box 21.

⁴³² Lee White communicated this to Gordon in a meeting on May 6. See Gordon, Memorandum for Heller, Tobin and Solow, ‘Onward with the Second Stage,’ 6 May 1961. Heller Papers. Box 21.

⁴³³ Davis, ‘Politics of Prosperity,’ 143-146; and Canterbury, *Economics on a New Frontier*, 144.

⁴³⁴ Kennedy, ‘Special Message to Congress on Urgent National Needs,’ 25 May 1961. APP.

works from March through to June. However, believing that it would provide the nation with a stronger means to fight future recessions, the CEA chairman did secure a commitment from the president to sponsor some form of stand-by authority in 1962.⁴³⁵

Knowing that the Clark bill would only give the economy a modest stimulus, throughout the spring and the early summer of 1961 Heller also promoted the use of other discretionary measures. Before turning to these, it is essential to note that to substantiate his case for a more activist approach the CEA chairman attempted to focus Kennedy's attention upon the economic policies of certain European nations. Western European economies were booming in the early 1960s, thanks to the same sort of policies Heller wanted Kennedy to champion. On May 5, after returning from a summit in Paris, Heller told Kennedy that activist fiscal and monetary policies lay behind the impressive growth rates of France, Germany, and Italy. In fact, the Germans were not afraid to "launch a much expanded road and highway program" if "the[ir] economy sags a bit."⁴³⁶ On June 27, Heller sought to justify activist policies by comparing the US economy with the Soviet Union's. He pointed out that increasing the US growth rate "by just one percentage point means a huge difference in our comparative performance."⁴³⁷ Accordingly, should the Soviet economy grow at 6 percent per year, it would not catch up an American economy growing at 4.5 percent (instead of 3.5 percent) until 2010.⁴³⁸

As he used these examples to lay out the case for greater use of discretionary measures, Heller advocated a more activist monetary policy. This was important

⁴³⁵ JFK conveyed this to Clark in August. See 'Draft Letter for Senator Clark,' 7 August 1961. Heller Papers. Box 5.

⁴³⁶ Heller, Memorandum for the President, 'Paris Report No. 1: Why Europe Grows Faster than the US,' 5 May 1961. Heller Papers. Box 5.

⁴³⁷ Heller, Memorandum for the President, 'Comparative US-USSR Growth Rates,' 27 June 1961. POF. Box 73.

because the Fed did not implement Operation Twist to the degree that he expected. Despite the Central Bank's purchase of long-term Treasury securities, it had not acquired enough to bring long-term interest rates down significantly. Reflecting this, Heller complained to Kennedy on April 6 that the economy still needed "a major monetary stimulus."⁴³⁹ Martin had only purchased "3/10 of 1 percent of the \$42.6 billion" of Securities (with maturities longer than five years) that were available.⁴⁴⁰ The Fed needed to "be petted, pressured, or pushed" into keeping interest rates low and when this became the case Heller urged JFK to call a meeting of the 'Quadriad.'⁴⁴¹

Formed of representatives from the CEA, the Treasury, the Budget Bureau, and the Fed, Heller set up the Quadriad following adoption of Operation Twist. It would meet with the president at the CEA chairman's urging. The Quadriad's goal was to convey administration thinking on monetary policy to Martin. As the Fed chairman was facing pressure from the banking community to return to "bills only" (the policy of interfering only in the short-term market), Heller viewed the Quadriad as essential to help "stiffen his back."⁴⁴² Despite later indicating that the meetings of this group generally worked well, Heller appears to have had little influence on Fed policy throughout April, May, and June of 1961.⁴⁴³ Exemplifying this, on June 11 Heller complained to JFK that the Fed chairman clearly "felt neither bound by nor sympathetic to the low-interest-rate language" of the administration, especially

⁴³⁸ Ibid.

⁴³⁹ CEA, Memorandum for the President, 'Monetary Policy: High Time for Action,' 6 April 1961. Heller Papers. Box 5.

⁴⁴⁰ Ibid.

⁴⁴¹ Heller, Memorandum for the President, 'Two Urgent Federal Reserve Matters,' 27 May 1961. Gordon Papers. Box 38.

⁴⁴² Heller, Memorandum for the President, 'Follow-up on Federal Reserve 'Crisis,' 31 May 1961. Gordon Papers. Box 38.

⁴⁴³ Heller, Interview in Hargrove and Morley, 190-191.

because he feared inflation.⁴⁴⁴

As well as not securing added spending measures throughout the spring and early summer of 1961, Heller could not convince Martin to deploy a more vigorous monetary policy. To compound his problems, the CEA chairman also found himself on the back foot during this period after Arthur Burns (Eisenhower's former CEA chairman) labelled the CEA 'neo-stagnationists.'⁴⁴⁵ A member of Kennedy's Labor-Management Advisory Committee, Burns argued the Council's argument that the economy suffered from chronic slack implied that the prospects for future outlets for private investment were very slim. According to him, this was the reason the CEA was calling for greater use of discretionary policies.⁴⁴⁶ In contrast, Burns believed that the economy required no extra fiscal or monetary stimulation, for the foundations of prosperity remained so strong that it would naturally be back to full employment within fifteen to eighteen months.⁴⁴⁷

Burns' involvement on a committee affiliated with the White House gave him access to the president. This forced Heller to refute his argument robustly.⁴⁴⁸ In response, he contended that Burns had misinterpreted the Council's analysis: it had no concerns about the economy's potential to grow, but wanted to stimulate the economy to the point whereby private enterprise could take over and close the performance gap.⁴⁴⁹ By reasserting the Council's case, Heller protected Kennedy from Burns' argument. This was to the point whereby every time Burns wrote to the

⁴⁴⁴ Heller, Memorandum for the President, 'Meeting with Chairman Martin on Current Monetary Policy,' 12 June 1961. POF. Box 73.

⁴⁴⁵ Arthur Burns, 'A Second Look at the Council's Economic Theory,' No Date [Henceforth n.d.] Tobin Papers. Box 1. JFKL. Burns first made this argument in an address at the University of Chicago in mid-to-late April. See Samuelson, CEA-OH, 337.

⁴⁴⁶ Burns, 'A Second Look at the Council's Economic Theory.'

⁴⁴⁷ Samuelson, CEA-OH, 337.

⁴⁴⁸ Heller, CEA-OH, 339.

⁴⁴⁹ CEA, 'An Analysis of Professor Arthur F. Burns' Critique of the Council's Position.' Attached to Heller to Douglas, 10 June 1961. Attached to Heller, Memorandum for the President, 19 June 1961. POF. Box 73.

president in mid-1961 Heller composed the response.⁴⁵⁰ Nevertheless, the Burns critique, the failure to secure immediate sponsorship of the Clark bill, and the failure to influence monetary policy, all served as setbacks for Heller throughout the spring and early summer of 1961.

IV

In late July, the CEA chairman did convince the president to make greater use of discretionary fiscal measures. The reason for this was a national emergency, the third Berlin Crisis, which again allowed Kennedy to invoke one of the “escape hatches” that Heller had written into the 1961 State of the Union address.⁴⁵¹ Even so, this only occurred following a protracted debate. Indeed, on July 25 the president decided to increase military spending by \$3.5 billion (in response to the crisis), but he and his close advisers, including Dillon, initially wanted to pay for this through increased taxation. In a meeting on Thursday July 20 Dillon, Robert Kennedy, and the Secretary for Health, Education and Welfare, Abraham Ribicoff, decided that this offered the perfect opportunity to invoke the theme of national self-sacrifice. It would also satisfy those who might otherwise charge the president with being fiscally irresponsible.⁴⁵²

Because Kennedy did not consult the CEA on his response to the Berlin Crisis, it came as a shock when Heller found out that he had approved a tax increase. In response, Heller fired off a memo to Kennedy on Friday, July 21, in a bid to dissuade him from going ahead with it. This argued that a tax increase would amount to “bad economics,” not least because increased military spending could narrow the performance gap.⁴⁵³ “Inflation,” it added, “has never been more dormant since the

⁴⁵⁰ Heller, CEA-OH, 339.

⁴⁵¹ Davis, ‘Politics of Prosperity,’ 147.

⁴⁵² Heller, Interview in Hargrove and Morley, 199; and Samuelson, CEA-OH, 380.

⁴⁵³ Heller, Memorandum for the President, ‘The Proposed Tax Increase,’ 21 July 1961. POF. Box 63a.

war,” whilst the tax system already acted as a powerful constraint upon the economy.⁴⁵⁴ Advancing political arguments as well, Heller noted that the size of the tax increase was “scarcely large enough to evoke a real sense of sacrifice.”⁴⁵⁵ It would also come “on the heels of the announcement of a \$3.9 billion deficit for fiscal 1961,” so the proposal might well “be viewed as a public apology.”⁴⁵⁶ Instead of recommending a tax rise now, Heller suggested, JFK should wait until the next session of Congress, which would give him time to see how the economy performed before announcing one if conditions warranted it.⁴⁵⁷

Despite Heller’s protests, the decision to increase taxes had been set in stone. In fact, Sorensen had gone off to write the speech that would justify it.⁴⁵⁸ Heller was due to deliver a speech in Dallas on Friday July 21. He recalled leaving the White House that morning feeling dejected.⁴⁵⁹ Nevertheless, over the weekend he persisted in his attempts to dissuade JFK from increasing taxes. Making use of the close friendship that he and the Council had forged with White House special assistant Kenneth O’Donnell, Heller arranged a phone call that evening with Kennedy, who was spending the weekend at Hyannis Port.⁴⁶⁰ Aided also by the fact that Seymour Harris had dazzled the president with the multiplier effects of increased defence spending (having accompanied JFK on his flight there that afternoon), Heller reiterated the points that he made in his memo earlier that day.⁴⁶¹ He subsequently arranged for Paul Samuelson to accompany Kennedy back to the White House on Monday, July 24, which ensured that the president heard the Council’s position once

⁴⁵⁴ Ibid.

⁴⁵⁵ Ibid.

⁴⁵⁶ Ibid.

⁴⁵⁷ Ibid.

⁴⁵⁸ See Douglas Dillon, Memorandum for Sorensen, Untitled, 21 July 1961. Theodore Sorensen Papers [Henceforth Sorensen Papers]. Box 40. JFKL. From here, any reference to Sorensen’s papers relates to the collection held at the JFK Library.

⁴⁵⁹ Davis, ‘Politics of Prosperity,’ 150.

⁴⁶⁰ Heller, CEA-OH, 382.

again.⁴⁶² Now somewhat swayed by their argument, Kennedy scheduled an emergency meeting to discuss the issue. Shortly before this, Heller penned another memorandum. Unsurprisingly, this advanced further political and economic justifications against a tax increase. It explained that even with the new defence expenditures, unemployment would still be around 5 percent in 1962. In fact, because a tax hike would increase unemployment, those who would lose their jobs would be “the real sacrificers.”⁴⁶³

The Council’s counterattack worked. Later that day, Kennedy declared that he would not seek a tax increase to fund the Berlin build-up. He did not reveal exactly what made him change his mind, but in press conferences that summer as well as in private conversations with Heller, the president had started to talk about the repressive impact of the taxation system upon the economy. It is likely, therefore, that Heller’s argument that a tax increase would make this worse had a bearing upon JFK’s thinking.⁴⁶⁴ Thus, Kennedy did not increase taxes and eventually operated an expansionary deficit of \$7.1 billion for FY 1962 (1.2 percent of GDP), which helped bring down the performance gap to \$30 billion by December 1961.⁴⁶⁵ However, JFK accompanied his decision not to ask for a tax rise in late July with a promise to balance the budget for FY 1963.⁴⁶⁶ Despite flirting with growth liberalism during the summer of 1961, JFK remained committed to commercial Keynesianism at that point in his presidency.

⁴⁶¹ Ibid, 382.

⁴⁶² Davis, ‘Politics of Prosperity,’ 150-151.

⁴⁶³ Heller, Memorandum for the President, ‘Attached Check-list on Tax Increase Decision,’ 23 July 1961. Gordon Papers. Box 38.

⁴⁶⁴ See Kennedy, ‘The President’s News Conference,’ on both 28 June and 19 July. APP; and Heller, Memorandum for Okun, Tobin, Gordon and Solow, ‘Memorandum for the President on Implicit Tax Surplus,’ 4 May 1961. Heller Papers. Box 22. In the latter Heller explained that, in a private meeting with JFK, the president displayed an interest in the repressive impact of the taxation system upon the economy.

⁴⁶⁵ The performance gap figure comes from Morgan, *Deficit Government*, 91.

For the rest of the year, the president's adherence to this cautious iteration of Keynesian ideas stayed strong. During this period, he continually rejected Heller's calls for further fiscal activism. True, Heller knew that the July decision not to increase taxes would stimulate the economy, but he maintained that further discretionary measures would ensure a solid recovery. Indeed, unemployment was unlikely to go below 5 percent throughout 1962. Accordingly, Heller wrote Kennedy on September 8 urging him to go further. To substantiate his case, Heller sought to focus the president's attention upon the long-term political implications of not doing so.⁴⁶⁷ He explained that Richard Nixon, Kennedy's opponent during the 1960 election, had said in early 1961 that JFK's prospects of re-election depended on "whether Dr. Heller can avoid poorly timed recessions."⁴⁶⁸ For Heller, Nixon had a valid point, not least because he attached to this memo a selection of correspondence between members of the CEA and the Treasury. These all indicated that if the recovery from the 1960 recession were to last as long as the previous one then the economy would likely go into another downturn in 1963.⁴⁶⁹ It was imperative, Heller argued, to stimulate the economy before this occurred, or else JFK would face re-election in 1964 with the country in a recession. Stimulating the economy before the next recession, the CEA also maintained, offered the "only way of getting out of this perpetually recurrent prosperity-recession cycle, into an era of steady growth."⁴⁷⁰

Kennedy remained indifferent to Heller's arguments. The main reason for this was that, during the fall of 1961, the balance-of-payments deficit seriously troubled

⁴⁶⁶ Kennedy, 'Radio and Television Address to the American People on the Berlin Crisis,' 25 July 1961. APP.

⁴⁶⁷ Davis, 'Politics of Prosperity,' 268.

⁴⁶⁸ Heller, Memorandum for the President, 'The Political Economy of the Next Recession,' 8 September 1961. Heller Papers. Box 5.

⁴⁶⁹ Okun, Memorandum for the CEA, 'Must We have a 1963 Recession?' 1 September 1961; and Tobin, Memorandum for Henry Fowler, 'Avoiding the Next Recession,' 6 September 1961. Both in Heller Papers. Box 5.

⁴⁷⁰ Tobin, Memorandum for Fowler, 'Avoiding the Next Recession.'

him. The influence of both Martin and Dillon was responsible for this. They worried that both the stimulation from the Berlin build-up and the lack of controls on US foreign overseas investments would have a negative impact upon the payments situation. Reflecting this, on August 25 the CEA called a meeting of the Quadriad partly to encourage the Fed to purchase more long-term Treasury securities, only for Martin to explain that the “cloud on the horizon was the balance-of-payments.”⁴⁷¹ Heller had explained that the payments situation was looking much better, for the deficit had declined to \$1.2 billion during the first quarter of 1961 (compared with \$3.8 billion in January). However, both the Fed chairman and the Treasury Secretary countered that the outlook was now pessimistic.⁴⁷² In turn, Dillon indicated to Kennedy at the end of August that it would be unwise to enact activist policies. This was especially because the US had lost \$72 million in gold during the previous two months, with “distinct possibilities of some further losses in the months ahead.”⁴⁷³ After listening to his Treasury Secretary, JFK turned down his CEA chairman’s September 8 request for expansionary measures.

This prompted Heller to confront the president’s concerns over the payments situation directly. On September 14, he pressed upon Kennedy new methods aimed at tackling it.⁴⁷⁴ The administration had already adopted certain policies designed to achieve this goal. These included export-boosting legislation, reduction of overseas outlays on defence, encouragement of high short-term interest rates, and securement

⁴⁷¹ Tobin, Memorandum for the Files, ‘Meeting with Chairman Martin and the President on August 25th,’ 28 August 1961. Heller Papers. Box 6.

⁴⁷² Ibid. The balance-of-payments figures are from CEA, ‘The First Six Months of the Kennedy Administration: Economic Policy,’ 27 July 1961. White House Staff Files of Walter Heller [Henceforth WHSFWH]. Roll 46. JFKL. From here, any reference to Heller’s Staff Files relates to the collection held at the JFK Library.

⁴⁷³ Dillon, Memorandum for the President, Untitled, 31 August 1961. POF. Box 89.

⁴⁷⁴ Heller, Memorandum for the President, ‘The Future of the Dollar,’ 15 September 1961. Gordon Papers. Box 38.

of early payments from European nations of their outstanding debts to the US.⁴⁷⁵ Nevertheless, Heller acknowledged that these policies had not done enough. Worried that Dillon would continue to press fiscal caution upon JFK, Heller urged the president to “resist temptations to seek solutions in directions which would weaken the United States economy.”⁴⁷⁶ He argued that the administration could negotiate increased contributions from other nations to pay for European defence, urge those nations to remove tax incentives that encouraged Americans to invest abroad, and negotiate lower trade barriers across the European common market.⁴⁷⁷

Since April, a Treasury-sponsored Investment Tax Credit had also been making its way through Congress. Enactment of this, Heller understood, would ease the payments problem, as it would enable American firms to modernise and expand their plant and equipment and thereby attract foreign investment into the US.⁴⁷⁸ Additionally, Heller sought to allay JFK’s fears that the nation would go bankrupt if gold continued to leave the country. US reserves, he noted, comprised 45 percent of all monetary gold stock in the free world – a very large amount.⁴⁷⁹ If signs of another run on gold occurred, Heller maintained that borrowing money from the International Monetary Fund could forestall this, as IMF funds would provide a boost to the balance-of-payments and thereby quell foreign concerns about devaluation.⁴⁸⁰

JFK was unmoved by Heller’s arguments. Responding instead to Dillon, the president decided at the end of October to promote modest civilian cutbacks to the FY 1962 budget.⁴⁸¹ In addition to both protecting the balance-of-payments and achieving

⁴⁷⁵ CEA, ‘The First Six Months of the Kennedy Administration: Economic Policy.’

⁴⁷⁶ Heller, Memorandum for the President, ‘The Future of the Dollar.’

⁴⁷⁷ Ibid.

⁴⁷⁸ Ibid.

⁴⁷⁹ Ibid.

⁴⁸⁰ Ibid.

⁴⁸¹ Dillon, Memorandum for the President, Untitled, 3 October 1961. POF. Box 89. As Dillon told JFK in this memo, to protect the payments deficit, it was “important that a strong effort be made to keep the government’s budget deficit this fiscal year as low as possible.”

a FY 1963 surplus, the Treasury Secretary may also have felt that the cutbacks were necessary because certain financial journalists had criticised Kennedy for engaging in irresponsible fiscal policies.⁴⁸² Unsurprisingly, Heller opposed making cuts to the budget, indicating that the economic situation did not warrant it.⁴⁸³ However, events ultimately worked against him. In early October, London bankers started converting copious quantities of dollars into gold out of concern about both the payments and budget deficits.⁴⁸⁴ This indicated that the cutbacks were more than appropriate. Accordingly, in late October JFK called for cuts of \$1 – 1.5 billion to the FY 1962 budget (approximately 1.4 percent of expenditures for that financial year), justifying them on the basis that it was necessary to reduce spending early to pave the way for a balanced budget in FY 1963.⁴⁸⁵

After not dissuading JFK from tightening the government's belt, Heller sprang into action once more to try to counter Dillon's influence during the following month. This was because the payments problem continued to worsen. In the face of this, the Treasury Secretary unsurprisingly advised Kennedy that a growing payments deficit could concern the international banking community, thereby leading to a run on gold.⁴⁸⁶ Fearing such advice could harden JFK's resistance to fiscal expansion, Heller argued that austerity "would be short-sighted folly" because the best way to correct the payments deficit would be to attain full employment.⁴⁸⁷ Indeed, an ever-expanding economy would make US firms more competitive, boost their exports, and

⁴⁸² Dillon, Memorandum for the President, Untitled, 5 September 1961. POF. Box 89.

⁴⁸³ Heller, Memorandum for the President, 'Economic Background for Budget Discussion,' 4 October 1961. POF. Box 73; and Heller, Memorandum for the President, 'Today's Economics of Budget Cutbacks and Announcements,' 16 October 1961. Heller Papers. Box 5.

⁴⁸⁴ Dillon, Memorandum for the President, Untitled, 13 October 1961. POF. Box. 89.

⁴⁸⁵ William Knighton Jr., 'Spending Cuts Asked by Kennedy,' *The Baltimore Sun*, 27 October 1961, 1. PQHN.

⁴⁸⁶ Dillon, Memorandum for the President, Untitled, 7 November 1961. POF. Box 89.

⁴⁸⁷ Heller, Memorandum for the President, 'The Balance-of-Payments Dilemma,' 28 November 1961. Heller Papers. Box 16.

thereby attract foreign capital into the US.⁴⁸⁸ To undermine Dillon's case, the CEA chairman highlighted how, in the mid-1920s, Britain had restricted its economy to protect its gold stock, only for it to face "unemployment and depression long before 1929-30."⁴⁸⁹ To prevent foreigners from cashing in their holdings, Heller also suggested that the US should "guarantee [a] certain [amount] of our debts to foreign central banks against devaluation."⁴⁹⁰

Kennedy did not promote further cutbacks to the FY 1962 budget, but he failed to follow Heller's recommendations to pursue stronger economic growth. This was despite a further barrage of CEA arguments in favour of expansionary policies during the fall of 1961. On December 9, Heller showed Kennedy that, in certain European nations, the ratios of public debt-to-GNP had decreased quickly since the end of World War II, something that highlighted "what economic growth...does."⁴⁹¹ His efforts proved futile, for the president remained committed to sound finance at the end of 1961.⁴⁹²

Whilst the payments deficit was certainly the main cause of this, there was another issue at play. In late November, the CEA's own forecasts appeared to validate Arthur Burns' argument that, on its own accord, the economy would reach full employment. It became apparent that GNP unexpectedly rose by \$16 billion from the third to the fourth quarter of 1961.⁴⁹³ Because of this, CEA staff member and Yale economist Arthur Okun concluded that output would rise from its November level of \$540 billion to a new high of \$616 billion by the second quarter of 1963. This

⁴⁸⁸ Ibid.

⁴⁸⁹ Ibid.

⁴⁹⁰ Ibid.

⁴⁹¹ Heller, Memorandum for the President, 'Public Debt Figures Abroad,' 9 December 1961. Gordon Papers. Box 38.

⁴⁹² Indeed, during a meeting on 8 November, JFK fondly "noted that FDR always had a balanced budget." Heller, Memo to the Files, 'Luncheon Meeting With the President, November 8 1961,' 12 November 1961. Heller Papers. Box 6.

⁴⁹³ Heller, CEA-OH, 412-413.

indicated that the “current economic expansion will continue and achieve full recovery” without the need of further fiscal stimulation.⁴⁹⁴ This forecast proved overly optimistic, but it significantly undermined Heller’s case by reinforcing JFK’s desire not to embrace expansionary economics at the end of 1961.

V

During his first year in the White House, Walter Heller was unsuccessful at installing growth liberalism as the driving force behind US economic policy. Not only did he fail to secure a commitment from Kennedy to promote tax reduction – either as part of the anti-recession programme or following the president’s subsequent decision to keep a close eye on the economy – he also did not convince JFK to promote immediate enactment of the Clark bill. At the same time, he struggled to persuade the Fed to adopt Operation Twist fully, before finding his arguments in favour of activist measures thwarted by Dillon throughout the fall, thanks mainly to the deteriorating payments deficit.

Despite all this, Heller did achieve certain successes. In an internal review conducted at the end of 1961, the CEA listed the president’s decision to promote stand-by authority in the next calendar year, as well as the reversal of the Berlin tax increase decision, as two accomplishments.⁴⁹⁵ Heller had also taken advantage of key policy episodes to advance his case, inserted language into presidential speeches and correspondence that left the door open for Kennedy to embrace his approach later on, and had developed a strong rapport with the president by the end of the year. Kennedy, too, had demonstrated that he possessed an appetite for economic policy, whilst there were signs that he was gradually beginning to understand the Keynesian

⁴⁹⁴ Okun, Memorandum for Heller, ‘Explanation of ‘full recovery’ Revenue Estimates,’ 22 November 1961. Heller Papers. Box 21.

⁴⁹⁵ CEA, ‘A Check List of CEA Impacts in 1961: A Private, Internal Review,’ 27 December 1961. WHSFWH. Roll 28.

analysis that underwrote Heller's recommendations. "We had lots of evidence [of this]," Heller later explained, "because he would say something in a press briefing, or in a discussion with a foreign economic dignitary, or just in a meeting with us that he couldn't have gotten anywhere else."⁴⁹⁶ Heller and the Council had also befriended key individuals who gave them access to the president, notably Kenneth O'Donnell. Thus, although 1961 was "the year of continuing tradition," Heller had laid strong foundations to facilitate JFK's conversion to growth liberalism in 1962.

⁴⁹⁶ Heller, Interview in Hargrove and Morley, 175.

Chapter Four

The Year of Conversion

Out of the four years that he served as CEA chairman, Walter Heller's second constituted his most impressive. Having failed to persuade Kennedy to maximise output in 1961, Heller succeeded in doing just that in 1962. Labelled that year as the "new economics" and later described by Heller as "Keynes-cum-growth," Kennedy's decision to deploy discretionary fiscal activism in non-recession conditions finally signified the triumph of growth liberalism over that of commercial Keynesianism.⁴⁹⁷ As the CEA chairman put it, this set the stage for "the completion of the Keynesian Revolution – thirty years after John Maynard Keynes fired the opening salvo."⁴⁹⁸ At the beginning of 1962 the president's conversion was far from assured, however, because Douglas Dillon continued to command his attention. It took until December for JFK to endorse a tax cut fully, after doing so only tentatively during the summer. This chapter outlines how Heller convinced both Kennedy and Dillon to embrace the new economics by the end of 1962. In doing so, it demonstrates that "the education of a president" was "Walter Heller's greatest achievement" as CEA chairman.⁴⁹⁹

I

In certain respects, Heller's second year on the New Frontier started the same way as his first. Despite showing concern about the poor rate of output, JFK remained reluctant to promote a growth-maximising tax cut. In addition to his concern about the balance-of-payments deficit, the optimistic forecast produced by the CEA at the end of the previous year strengthened the president's resistance to expansionary

⁴⁹⁷ As Tobin later noted, the term "new economics" was first used regarding Heller and the Kennedy administration on 16 July 1962, in a *Newsweek* article entitled 'Question: Is a Tax Cut What the Country Needs?' Tobin, *The New Economics*, 7. For Heller's quotation, see *New Dimensions of Political Economy*, 70.

⁴⁹⁸ Heller, *New Dimensions of Political Economy*, 2.

⁴⁹⁹ Gordon, Interview with Turner #1, 12 July 1964, 6. JFKL-OHC.

economics. Because GNP had risen so quickly in the final quarter, JFK doubted whether the economy truly needed a strong stimulus. The 1962 *Economic Report*, the January Budget Message, and JFK's second State of the Union address, all embodied this assessment. Each "spoke of continued growth, high employment, and price stability, but in a voice of restraint."⁵⁰⁰ In their respective sections of the *Economic Report*, JFK and the Council estimated that GNP would hit \$570 billion in the second quarter of 1962 and raised the prospect that the economy could reach full employment by mid-1963.⁵⁰¹ Because of this, the president felt that a tax cut-induced deficit was not appropriate and instead predicted that the rising revenues generated by the booming economy would produce a modest surplus of \$0.5 billion for FY 1963.⁵⁰² Expectation that the economy would naturally return to full employment discouraged Kennedy from promoting vigorous action.

This, of course, did not mean that Heller realized this might not happen, especially as certain observers dismissed the CEA's expectations "as wishful thinking at best."⁵⁰³ Aware that the "prospects for a lasting expansion rest heavily on the vigor of the upswing" in the quarters ahead, he convinced Kennedy that it was essential to enhance the president's ability to stabilise the economy at the first sign of a potential downturn.⁵⁰⁴ Accordingly, in his various economic messages in January the president called on Congress to enact a three-part programme, developed by the CEA, to improve the nation's anti-recession defences.⁵⁰⁵ Inspired by the Clark measure of the previous spring, two of this programme's three components consisted of stand-by presidential authority to respectively lower tax rates or increase spending on public

⁵⁰⁰ Flash, *Economic Advice and Presidential Leadership*, 219.

⁵⁰¹ *The Economic Report of the President, 1962* (Washington DC, 1962), 11, 66. APP.

⁵⁰² Kennedy, 'Annual Budget Message to the Congress, Fiscal Year 1963,' 18 January 1962. APP.

⁵⁰³ Jim Heath, *John F. Kennedy and the Business Community* (London, 1969), 34.

⁵⁰⁴ *The Economic Report of the President, 1962*, 67.

works if economic conditions warranted both or either. The third called for increased unemployment compensation. An attempt to bolster both the discretionary and automatic elements of the nation's anti-recession arsenal, Heller called this programme "the most significant step forward in policy for economic stabilization since the Employment Act itself."⁵⁰⁶

Despite this, certain observers have downplayed the extent to which the development of the CEA's three-part programme constituted an important shift in economic policy. For Edward Flash, the stand-by proposals were "pale shadows of what it [the CEA] would have preferred to fight for."⁵⁰⁷ Consequently, they were well within the framework of commercial Keynesianism. True, the CEA did acknowledge that its programme was not directly "designed to deal with the problem of high and stubborn unemployment."⁵⁰⁸ The idea of granting the president stand-by authority to cut taxes also received endorsement from the CED at the end of 1961.⁵⁰⁹ However, the CEA's three-part programme, coupled with presidential endorsement of it, signified an important shift in economic policy because it was intended to ensure that the economy would reach full employment and remain at optimum capacity for as long as possible. Far from being merely a tool to promote stability, the three-part programme aimed to guarantee the "economy could be made to expand continuously."⁵¹⁰ Kennedy's endorsement of it revealed his new appreciation of growth economics, even if he remained reluctant to deploy Heller's tax cut.

Assessment of the revived Clark measure further demonstrates this point. Formally submitted to the legislature in February, this aimed to provide \$2 billion for

⁵⁰⁵ Ibid, 17; 'Annual Budget Message to the Congress'; 'Annual Message to Congress on the State of the Union,' 11 January 1962. APP.

⁵⁰⁶ *The Economic Report of the President, 1962*, 72.

⁵⁰⁷ Flash, *Economic Advice and Presidential Leadership*, 225-226.

⁵⁰⁸ CEA, 'Proposed Standby Capital Improvements Bill,' 30 November 1961. Gordon Papers. Box 26.

⁵⁰⁹ Davis, 'Politics of Prosperity,' 262-267.

federal, state, and local public works (and capital improvements) projects if the unemployment rate rose by a certain degree.⁵¹¹ Though it failed to gain congressional approval, the CED did not endorse this measure. Fearing that expenditure programmes would unduly increase the role of government in economic affairs, that organisation preferred to use the taxation side of the budget to manipulate the economy.⁵¹² This demonstrates that the CEA successfully pressed Kennedy to endorse a position beyond that supported by the key architects of commercial Keynesianism. Simply having this measure on the books, Heller further argued, would serve an important purpose for growth economics. Indeed, it would reassure businesses of continuous demand if the economy showed signs of faltering, thereby incentivising them to maintain their investments and power the economy forward.⁵¹³

The proposal for stand-by authority to reduce taxes also represented an attempt to boost business confidence and thereby maximise growth.⁵¹⁴ So, too, did the effort to strengthen the unemployment compensation system.⁵¹⁵ The latter fared dismally, to the extent that it was not enacted. Congress, whose members “were hardly prepared to relinquish the power to tax,” never seriously entertained the former.⁵¹⁶ However, the way that the CEA favoured shaping this proposal differed from the champions of commercial Keynesianism. Though the CED came out in support of stand-by tax authority at the end of 1961, it only favoured providing the president with the power to lower taxes, not raise them. Heller, “a leading proponent, if not *the* leading proponent, of standby plans to *raise* or *lower* taxes” throughout his

⁵¹⁰ Donald Gibson, *Battling Wall Street: The Kennedy Presidency* (New York, 1994), 29.

⁵¹¹ Kennedy, ‘Letter to the President of the Senate and to the Speaker of the House Transmitting a Proposed Stand-By Capital Improvements Act,’ 19 February 1962. APP.

⁵¹² Davis, ‘Politics of Prosperity,’ 262-263.

⁵¹³ Heller, ‘What’s Ahead for the Economy,’ Excerpts from Address to the Harmonie Club, New York City, 17 March 1962. POF. Box 74.

⁵¹⁴ Ibid.

⁵¹⁵ Ibid.

⁵¹⁶ Davis, ‘Politics of Prosperity,’ 265-266.

career, favoured providing the president with both.⁵¹⁷

Worried that requesting authority to both raise and lower taxes would generate too much controversy, Kennedy only promoted the latter in 1962. To gain the approval of Dillon, as well as of sceptical congressional representatives, the CEA agreed to potential repeal of the stand-by tax bill thirty days after its enactment. This did not have the desired effect, as Congress “never even considered the measure seriously.”⁵¹⁸ As well as worrying about relinquishing their taxation powers, its members feared that if the president did lower tax rates then it would fall on them to later increase them, which could prove unpopular.⁵¹⁹ Such was the lack of enthusiasm for stand-by tax authority on the Hill that even the president eventually grew reluctant to promote it. Reflecting this, Heller wrote to JFK on August 16 saying that he hoped the president would “find some way of once again underscoring the importance of this measure,” yet Kennedy never did.⁵²⁰

Thus, none of the standby features of the CEA’s three-part programme gained congressional approval in 1962. Nevertheless, Kennedy did embrace the revived Clark bill and, with enthusiasm, initially promoted the other aspects of the Council’s programme. All of this signified that, as he started his second year in office, the president was open to embracing an economic philosophy more akin to growth liberalism.

II

Though the three-part programme aimed to help the economy reach and stay at full employment, Heller remained determined to convince JFK to cut taxes. Due

⁵¹⁷ Seib, ‘The Mild-Eyed Liberals,’ 102. Emphasis added. For more on Heller’s position see Davis, ‘Politics of Prosperity,’ 263.

⁵¹⁸ Ibid, 266.

⁵¹⁹ Ibid, 266.

⁵²⁰ Heller, Memorandum for the President, ‘Stand-by Tax Authority,’ 16 August 1962. Gordon Papers. Box 38.

mainly to the CEA's optimistic forecast, the balance-of-payments problem, and the fact that conservative businesspersons detested deficits, the president was reluctant to heed his CEA chairman's advice. When asked on February 21 whether he might promote a growth-maximising tax cut, Kennedy replied that there was simply "not a chance."⁵²¹ By then, the release of economic data for the previous month had reaffirmed his resistance. This showed that the unemployment rate had dipped below 6 percent for the first time since he took office.⁵²² Heller shared JFK's reasonably optimistic outlook at the beginning of 1962, but remained concerned that the production gap stood at almost \$30 billion.⁵²³ Rather than waiting for the economy to naturally reach its optimum capacity, the CEA chairman preferred Kennedy to enact activist measures. Conscious, too, that the influence of Dillon was holding JFK back, Heller used the CEA's 1962 *Economic Report* to justify an expansionary approach.

Because he knew that this document would be thoroughly scrutinised by both the press and Congress, Heller understood that, like his *Life* article of the previous year and the Council's first JEC testimony, Kennedy would carefully read it. This would give him access once more "not just to the person but to the mind of the President."⁵²⁴ Accordingly, the *Economic Report* cogently translated Heller's liberal Keynesianism into clear and understandable terms. The main way that it did so was by establishing a jobless rate of 4 percent as the full employment target of the administration (inflation was deemed likely to increase beyond an acceptable rate at anything below that level).⁵²⁵ It then made use of important theoretical concepts previously utilised by several liberal economists to justify prompt attainment of this. One was the full employment budget, the device used by the CEA throughout 1961 to

⁵²¹ Kennedy, 'The President's News Conference,' 21 February 1962.

⁵²² Sobel, *The Worldly Economists*, 130-131.

⁵²³ *Economic Report of the President, 1962*, 49.

⁵²⁴ Heller, *New Dimensions of Political Economy*, 53.

demonstrate how the taxation system restricted economic growth. This was something that the president had started to talk about that year. Though the *Economic Report* reiterated this point, it further argued that the full employment budget should serve as the principal guide for fiscal policy. Indeed, Heller stated that to gain a clear indication of how expansionary the administration's overall fiscal policies were it should continuously calculate budgetary programmes at this hypothetical level. Noting that the full employment surplus stood at \$8.5 billion at the end of 1961, the *Economic Report* explained that its elimination through activist policies would bring the economy to optimum capacity.⁵²⁶ Instead of balancing the actual budget, as Kennedy wanted at the start of 1962, the CEA argued the administration should aim to balance the full employment budget. This would factor growth into its policies.

In addition to the use of the full employment surplus to justify expansionary measures, the *Economic Report* made use of "Okun's Law" to capture Kennedy's attention. As conceived by its author, the CEA staff member Arthur Okun, this stipulated that a 1 percent increase in the rate of unemployment translated into a 3 percent increase in the gap between actual and potential output.⁵²⁷ In other words, this meant that an "unemployment rate of 4 percent instead of 6.7 percent for 1961...would have raised production by much more, about 8 percent."⁵²⁸ Described by one historian as a "powerful rhetorical device" that Heller used "to justify a tax cut" to the president, Okun's Law also "served several purposes" in the Council's "intellectual battle" for Kennedy's ear.⁵²⁹ Like the full employment budget concept, it "indicated more dramatically than the unemployment statistic alone the many

⁵²⁵ *Economic Report of the President, 1962*, 46.

⁵²⁶ *Ibid.*, 78-83.

⁵²⁷ Tobin, *The New Economics*, 9.

⁵²⁸ *Economic Report of the President, 1962*, 50.

dimensions and large size of the national loss due to under-utilization.”⁵³⁰ By having Kennedy fully absorb both of these concepts Heller knew that it would become increasingly difficult for Dillon “to advocate policies that held no prospect of reaching the [full employment] target.”⁵³¹ This was regardless of how often the Treasury Secretary used the views of bankers and financiers to gain Kennedy’s attention. The setting of a target for full employment, as well as both the Council’s articulation of the full employment budget concept and Okun’s Law, all served to demonstrate vividly the advantages of growth economics to Kennedy. The fact Heller said that he was “proud of getting presidential approval for” the *Economic Report* highlighted that his student was beginning to embrace the merits of his approach.⁵³²

As well as emphasising the need to attain full employment, the *Economic Report* highlighted the virtues of expanding potential output. This illuminates an underappreciated difference between commercial Keynesianism and growth liberalism. Because he believed that the economy had an unlimited capacity to grow, Heller advocated the use of various supply-side policies alongside demand-side measures, arguing that these would maximise economic capacity together with actual output.⁵³³ Accordingly, the *Economic Report* called for the implementation of the Investment Tax Credit formulated in 1961, which aimed to incentivise production.⁵³⁴ In response to the rise of Human-capital theory in the late 1950s, it also placed

⁵²⁹ Michael Bernstein, *A Perilous Progress: Economists and Public Purpose in Twentieth Century America* (Princeton, NJ, 2001), 134-135; Tobin, *The Intellectual Revolution in US Economic Policy-Making*, 13.

⁵³⁰ Tobin, *The Intellectual Revolution in US Economic Policy-Making*, 13.

⁵³¹ *Ibid.*, 14.

⁵³² Heller to Andreas Papandreou, 29 January 1962. Heller Papers. Box 49.

⁵³³ Heller, ‘Kennedy Economics Revisited,’ in Pechman and N. J. Simler (eds.) *Economics in the Public Service: Papers in Honor of Walter W. Heller* (New York, 1982), 240-246.

⁵³⁴ *The Economic Report of the President, 1962*, 12, 106, 132, 162. It also called for enactment of stand-by presidential authority to negotiate lower trade barriers (discussed below) and praised the Fed for deployment of Operation Twist, as both would help achieve the same end. See 6, 86-91. Furthermore, it outlined a set of wage-price guideposts for business and labour to follow (discussed below), which aimed to keep a lid on inflation as output expanded in the mid-1960s. This moved away

emphasis on investment in education, arguing that this was vital to expanding productive capacity.⁵³⁵ Thus, by focusing upon increasing potential alongside the actual rate of output, Heller viewed full employment as a continuous moving target. In this sense, he wanted to eliminate the business cycle. By contrast, the CED merely sought to tame it by sanctioning the use of discretionary measures to overcome stagnation, a point overlooked by those who have emphasised the similarities between liberal and business post-war iterations of Keynesianism.

Though the president endorsed both the content and the language of the *Economic Report*, the optimistic forecast, the balance-of-payments problem, and the fact that Kennedy worried that deficits would be criticised by certain elements of the business community, all ensured that he started his second year in office determined to balance the books. This forced Heller to be content with allowing the economy to reach full employment naturally by mid-1963. However, as further economic data became available in early March, the CEA chairman worried that he “had been right after all in late 1961, in my initial feeling that we couldn’t struggle to full employment under this heavy over-burden of taxes.”⁵³⁶ Even though unemployment declined to under 6 percent in February, it showed no signs of going down further. This realization followed release of consumption and production data for January showing that the economy was unlikely to reach the \$570 billion GNP target for the second quarter.⁵³⁷

from the CED’s focus on using a full employment surplus to moderate prices, again highlighting another difference between commercial Keynesianism and growth liberalism. See 188.

⁵³⁵ Ibid, 118-120, 190. For more on the development of Human-capital theory and the way in which liberal economists pioneered it in both the late 1950s and the early 1960s see Laura Holden and Jeff Biddle, ‘Walter Heller and the Introduction of Human Capital Theory into Education Policy,’ November 2014, <https://pdfs.semanticscholar.org/06cd/21e2661e380605688c44d07d616d8954c76b.pdf> [accessed 11/02/2017]. See too Carl Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ *Journal of American History*, 69:1 (Jun. 1982), 107.

⁵³⁶ Heller, Interview in Hargrove and Morley, 200.

⁵³⁷ Stein, *The Fiscal Revolution in America*, 407.

Concerned that the recovery from the 1961 recession was slowing down, Heller cogently reiterated his argument for a tax cut in a memo to the president on March 3. This issued a warning that, for the administration's full employment target to be attained, business investment needed to rise by \$17 billion over the final quarter of the year.⁵³⁸ To compound the administration's problems, even with the Fed's continuous deployment of Operation Twist and the impending passage of the Investment Tax Credit, such a rise was unlikely to happen because of a worrying deficiency in demand. What the economy needed, the CEA chairman concluded, was a large stimulus to boost purchasing power and revive business investment. This could be in the form of a \$4 billion increase in spending or "a \$5 billion reduction in taxes."⁵³⁹ Heller made it clear that he preferred the latter.⁵⁴⁰ Importantly, the CEA chairman wanted a tax cut to take the form of a one-time rebate on 1961 incomes and sought to sell this on political as well as on economic grounds, saying its impact upon the economy would "improve the chances for a fiscal 1963 surplus."⁵⁴¹

JFK continued to resist a tax decrease because he believed the economy to be performing strongly. In press conferences on March 7 and 14, the president said that the "economy has more vitality in it than some of its premature mourners [suggest]," noting that the figures for February looked "much better" than those for January.⁵⁴² In contrast, Heller had become "convinced" that the 1961 recovery was stalling.⁵⁴³ Further analysis by the Council indicated that throughout January and February GNP only rose by 1.1 percent over the preceding quarter.⁵⁴⁴ This was "unusually small...at

⁵³⁸ Heller, Memorandum for the President, 'What it Takes to get to Full Employment,' 3 March 1962. Gordon Papers. Box 38.

⁵³⁹ Ibid.

⁵⁴⁰ Ibid.

⁵⁴¹ Ibid.

⁵⁴² Kennedy, 'The President's News Conference,' on both 7 and 14 March 1962. APP.

⁵⁴³ Heller, Interview in Hargrove and Morley, 200.

⁵⁴⁴ Heller, Memorandum for the President, 'The Slowdown in the Recovery and its Implications for Policy,' 21 March 1962. Gordon Papers. Box 38.

this stage of an expansion.”⁵⁴⁵ Also worrying was the fact that long-term interest rates had declined faster than the Council had expected.⁵⁴⁶ True, the Fed had been more vigorously engaged in Operation Twist in 1962 thanks to regular Quadriad meetings. However, the decline of long-term interest rates was also attributable to the fact that businesses were less willing to borrow to spur productivity.⁵⁴⁷ These developments concerned Heller. Not only did they indicate that the recovery from the 1960 recession was stalling, they came “after five years of economic slack in which the preceding recovery had stopped well short of full employment.”⁵⁴⁸ Concerned that the sluggish growth rate of the late 1950s would also be a hallmark of the Kennedy years, Heller pushed harder for a tax cut.

In a memo to Kennedy on March 21, Heller claimed that there was more than “considerable evidence that the private economy’s pump has not yet been sufficiently primed.”⁵⁴⁹ GNP was now unlikely to reach \$570 billion in the second quarter of 1962, a sign that the economy had “been operating in a low gear for five years” and both businesspersons and consumers were too accustomed to this. Clearly, there was now “a high premium on expansionary policy” and the surest way to add “purchasing power all over the country” was through “a temporary reduction of personal income taxes.”⁵⁵⁰ By this point, Heller had dropped the idea of increasing expenditures to give the economy a shot in the arm, not least because the administration was “butting its head against a brick wall” trying to get its stand-by proposal for public works passed.⁵⁵¹ Again, Heller preferred a tax cut to take the form of a \$25 rebate on

⁵⁴⁵ Ibid.

⁵⁴⁶ Heller, Memorandum for the President, ‘The Monetary Situation: Current Federal Reserve Policy,’ 26 March 1962. POF. Box 74.

⁵⁴⁷ Ibid.

⁵⁴⁸ Stein, *The Fiscal Revolution in America*, 408.

⁵⁴⁹ Heller, Memorandum for the President, ‘The Slowdown in the Recovery and its Implications for Policy.’

⁵⁵⁰ Ibid.

⁵⁵¹ Heller, Interview in Hargrove and Morley, 200.

taxpayer incomes for 1961, arguing that Congress would deem this fiscally prudent.⁵⁵² The president remained unreceptive, but the slowdown in the recovery grew more worrying throughout April and May, forcing Heller to drum home his case publicly.⁵⁵³

As the CEA chairman intensified his advocacy of a tax cut, he again sought to focus the president's attention upon Europe's Keynesian policies. Whilst Heller had engaged in such an effort since 1961, his campaign intensified during the spring of 1962. On February 28, he rushed over to the White House to hand JFK a *New York Times* article by reporter Edwin Dale highlighting how France, Germany, and Italy had all been growing faster than the US due to "high and rising government spending."⁵⁵⁴ On March 3, Heller told JFK that, since the 1950s, France and Germany had "been running more frequent deficits than we have."⁵⁵⁵ Two months later, Heller reported from an economic summit in Rome and informed Kennedy that Italian economists believed the "unrelenting pressure of high demand," caused by the "rapid expansion" of the Italian government's budget outlays, was responsible for that nation's impressive growth rate.⁵⁵⁶

To provide what he later described as added "leverage on Kennedy," as well as to make up for the fact that the Council lacked its own political constituency, Heller arranged for European officials visiting Washington to urge their policies upon the president.⁵⁵⁷ On May 23, Heller and Kennedy met in the White House with Emiel van Lennep, Treasurer General for the Dutch Ministry of Finance. Seeking to gain an

⁵⁵² Heller, Memorandum for the President, 'The Slowdown in the Recovery and its Implications for Policy.'

⁵⁵³ See Heller, CEA-OH, 425.

⁵⁵⁴ Edwin Dale, 'Trouble for US, Boon for Europe,' *New York Times*, 28 February 1962, 3. Attached to Heller, 'Note for CEA Files,' 28 February 1962. WHSFWH. Roll 31.

⁵⁵⁵ Heller, Memorandum for the President, 'What Does Western Europe Have that We Don't Have?' 3 March 1962. POF. Box 74.

⁵⁵⁶ Heller, Memorandum for the President, 'Report on Rome Monetary Conference (of the American Bankers Association),' 20 May 1962. POF. Box 74.

insight into what the Europeans thought of America's payments difficulties, JFK asked Van Lennep if he thought that balanced budgets would help solve them. The president was stunned to be told that "a strong competitive position...[created by] a rapid expansion [of economic activity]" offered a better solution, primarily because this would "attract foreign private capital" into one's country.⁵⁵⁸

To hammer home his argument that deliberately induced deficits in Europe were acceptable, Heller prompted Van Lennep to comment upon the differences between transatlantic budgetary policies. "In Europe," the Dutchman replied, "one does not understand why in the US there is still a strong tendency to have a balanced budget as a target for the average...of a business cycle. Such a target of budget-policy means that other, real and important, targets like employment and growth may not be achieved."⁵⁵⁹ An illuminating response, this clearly made an impact upon Kennedy, who commented that Americans needed to "be educated" about the undesirable effects of continuous balanced budgets.⁵⁶⁰ He soon asked Heller to prepare a list of twenty economic myths that needed to be slayed, seeing this as necessary groundwork towards a major speech that would describe the "balanced budget" as "the key myth that needed to be destroyed."⁵⁶¹

Meanwhile, Douglas Dillon grew more appreciative of growth economics. Heller's argument that an expanding economy would help solve the payments deficit – made by the CEA chairman throughout the fall of 1961 and strongly articulated by Van Lennep during the aforementioned meeting – now resonated with the Treasury

⁵⁵⁷ Heller, Interview in Hargrove and Morley, 202.

⁵⁵⁸ n.n., 'Report on Meeting with President Kennedy in White House on 23rd May 1962,' n.d. Heller Papers. Box 21.

⁵⁵⁹ Ibid.

⁵⁶⁰ Ibid.

⁵⁶¹ Kennedy's request to Heller is discussed in Bernstein, *Promises Kept*, 146. For the quote see Okun, Interview with David McComb, 20 March 1969, 14. Lyndon B. Johnson Presidential Library [Henceforth LBJL]-OHC.

Secretary. On May 9, he indicated that Kennedy should engage in economic expansion to boost manufacturing exports.⁵⁶² Hence, for Kennedy the comparisons that Heller made between American and European fiscal policies were a real revelation. Nevertheless, also integral in facilitating his conversion to the new economics was the enunciation by the Council of wage-price guideposts in the 1962 *Economic Report*. In conjunction with certain events and the development of other administration policies in mid-1962, these helped free the president to embrace Heller's approach.

III

The development of the Council's wage-price guideposts dated back to the summer of 1961, when Kermit Gordon started to worry that "upward pressure on prices may originate in those sectors of the economy" where "large corporations and unions have a considerable degree of discretion in setting prices and wages."⁵⁶³ Specifically, Gordon worried about the threat posed to price stability by the steel industry, which "bulks so large in the manufacturing sector of the economy that it can upset the price applecart all by itself."⁵⁶⁴ Knowing that unions and steel corporations were due to negotiate a wage-price settlement that October (three months after the Berlin build-up begun), the CEA succeeded in preventing the steel industry from increasing its prices at that time by arranging a debate in the Senate. There, Democratic politicians cogently argued that steel companies would earn good profits without a price hike.⁵⁶⁵ Still, the incident demonstrated to the Council that a future

⁵⁶² Dillon, Memorandum for the President, Untitled, 9 May 1962. Heller Papers. Box 16. For more on Dillon's gradual acceptance of the new economics in the spring of 1962 see Rowen, *The Free Enterprisers*, 177.

⁵⁶³ Heller and Gordon, Interview with Pechman, 20 July 1965, 1-2. JFKL-OHC; *The Economic Report of the President, 1962*, 45-46.

⁵⁶⁴ Heller, Memorandum for the President, 'The Price Situation in General (and Steel in Particular),' 2 August 1961. Heller Papers. Box 21.

⁵⁶⁵ Heller and Gordon, Interview with Pechman, 2.

increase might occur, which could spark inflationary pressures and harden the president's resistance to expansionary ideas. Accordingly, in the fall of 1961 the Council developed non-inflationary wage-price guideposts for both corporations and labour to follow.

Having sold them to Kennedy without "much difficulty," the CEA made the guideposts the subject of a whole chapter of the 1962 *Economic Report*.⁵⁶⁶ In short, the guideposts tied wage and price levels to the overall rate of productivity in order to ensure that demand grew in line with supply.⁵⁶⁷ By serving as a mechanism to prevent cost-push inflation (where the costs of a business push up prices), the wage-price guideposts constituted one part of a framework that in 1962 helped "free" Kennedy "to pursue continued growth."⁵⁶⁸ At the beginning of that year, JFK also promoted the Treasury-inspired Trade Expansion Act, which aimed to provide the president with stand-by authority to negotiate lower trade barriers to help alleviate the payments problem. He also pushed for enactment of the Investment Tax Credit, knowing that its passage, too, would aid the payments deficit. Hence, by creating a mechanism to ensure price stability, the Council contributed to the formulation of a structure that made JFK feel more positive about pursuing growth.⁵⁶⁹

Disaster struck in the spring of 1962, just as Heller attempted to convince the president to engage in fiscal expansion. On April 10, US Steel announced that it intended to raise its prices by \$6 a ton, an action that defied the administration's wage-price guideposts. For Heller, a firm response to this was imperative: if US Steel got away with its decision, JFK would be less inclined to engage in fiscal expansion

⁵⁶⁶ Ibid, 15.

⁵⁶⁷ *Economic Report of the President, 1962*, 188-199.

⁵⁶⁸ Davis, 'Politics of Prosperity,' 252.

⁵⁶⁹ Ibid, 252.

because the company's action might let the inflationary genie out of the bottle.⁵⁷⁰ Fortunately, Kennedy was furious at US Steel's decision, believing that it constituted a direct challenge to the office of the presidency. After unsuccessfully responding to the price hike by putting direct pressure on US Steel to rescind it, the president turned to a strategy formulated by Heller and Gordon. This involved convincing other steel producers not to follow suit, primarily by threatening to withdraw lucrative defence contracts from them.⁵⁷¹ Though the president's decision to utilise the power of the presidency to force US steel to back down angered many business leaders (with the president of COCUS saying, "dictators in other lands usually come to power under accepted constitutional procedures"), it proved successful. Seventy-two hours after its initial decision, US Steel backed down.⁵⁷²

This was not the end of the administration's problems. On May 27, the stock market experienced its sharpest decline since the late 1920s, an incident the business community attributed to Kennedy's handling of the steel crisis. Importantly, both events influenced the president's economic outlook: having been conscious of courting business leaders with balanced budgets ever since he took office, JFK decided this strategy was folly. He would continue to try to maintain cordial relations with America's executives, but in the wake of both the steel crisis and the stock market crash, the president agreed with Theodore Sorensen not "to appease those who will never support us."⁵⁷³ Now less constrained by the need to satisfy business, JFK's and Sorensen's sympathies for expansionary economics increased.

The steel crisis and the stock market crash both worked in Heller's favour. However, certain scholarly accounts of the change in Kennedy's economic outlook

⁵⁷⁰ Bernstein, *Promises Kept*, 136.

⁵⁷¹ Heller and Gordon, Interview with Pechman, 23-25.

⁵⁷² Cited in Morgan, *Deficit Government*, 91.

⁵⁷³ Sorensen, 'The Kennedy Administration and Business,' 20 June 1962. Sorensen Papers. Box 29.

have arguably afforded them too much importance. According to Allen Matusow, it “took the twin shocks of the steel crisis and the stock-market collapse to prod Kennedy into reappraising his economic policies,” thereby making him more receptive to Heller’s approach.⁵⁷⁴ Whilst these developments certainly removed a barrier to JFK’s acceptance of Heller’s ideas, Matusow does not appreciate the educational process that Kennedy had already undergone. Indeed, there is sufficient evidence to suggest that JFK had converted to the new economics before the stock market crash.

The president’s comments at the end of the meeting with Van Lennep on May 23, coupled with his decision in the wake of it to slay the myth of the balanced budget, both serve as evidence of this. Moreover, in a private meeting three weeks before the stock market slump, JFK manifested sympathy for Heller’s economic philosophy. He suggested “it would be unsound economics and unsound politics to choke off recovery and slow down our growth by repressive fiscal and monetary measures...especially now, when we have plenty of slack in the economy.”⁵⁷⁵ It is unsurprising, that when Seymour Harris forwarded Heller a letter from the Keynes biographer Roy Harrod on May 26, which urged Harris to convince both Heller and Kennedy of the merits of growth economics, the CEA chairman passed a note to Kennedy saying “as if we weren’t!”⁵⁷⁶ Before Kennedy changed his attitude towards the business community, he had been “intellectually convinced of the Council’s case.”⁵⁷⁷

⁵⁷⁴ Matusow, *The Unraveling of America*, 47. Also, see Morgan, *Deficit Government*, 91-92; Stein, *The Fiscal Revolution in America*, 408; Gillon, *Politics and Vision*, 147; Sobel, *The Worldly Economists*, 130-131; Bernstein, *Promises Kept*, 146; Davis, ‘Politics of Prosperity,’ 249-252; Collins, *The Business Response to Keynes*, 178-179; Stein, *Running Steel, Running America*, 32-33; and Flash, *Economic Advice and Presidential Leadership*, 227-229.

⁵⁷⁵ Heller, Memorandum for the President, ‘Care and Feeding of Inflation,’ 8 May 1962. Gordon Papers. Box 38.

⁵⁷⁶ Heller, Memorandum for the President, Untitled, 26 May 1962. POF. Box 74.

⁵⁷⁷ Tobin, *The New Economics*, 24.

This did not mean that the president was committed to immediate enactment of the new economics. In the wake of the stock market crash, Heller upped the pressure on the president for a tax cut, only for JFK to rebuff him following a three-month deliberation on the issue. Concerned that the slump in stock prices had come on top of both a recovery that was slowing down and an economy suffering from chronic slack, Heller warned Kennedy that they were in the midst of “a very severe decline.”⁵⁷⁸ An immediate, or “quickie,” tax cut would “be the most effective governmental action that could be taken in the present-situation.”⁵⁷⁹ Importantly, both the size and the composition of the tax cut that Heller now deemed necessary had changed since earlier in the year. He now considered a reduction of up to \$10 billion imperative, believing that it should take the form of an across-the-board reduction in rates as opposed to a one-time rebate.⁵⁸⁰ To add cogency to his case, the CEA chairman passed the president three items on May 31.

One was an *Economist* article highlighting the virtues of Europe’s fiscal policies.⁵⁸¹ The others were a *New York Times* piece by Alvin Hansen calling for a tax cut and a column by journalist Walter Lippmann also analysing European economic measures.⁵⁸² Heller also sent Kennedy a letter from a prominent business economist that highlighted the merits of tax reduction.⁵⁸³ Additionally, he stressed that an immediate tax cut would be easy to implement, citing the fact that the last time Congress passed emergency taxation (at the start of the Korean War) had resulted in the passage of a measure within weeks.⁵⁸⁴ By seeking to instil in Kennedy a fear that

⁵⁷⁸ CEA, ‘The Present Decline in Perspective,’ 29 May 1962. Sorensen Papers. Box 40.

⁵⁷⁹ CEA, ‘Possible Government Action,’ 29 May 1962. Sorensen Papers. Box 40.

⁵⁸⁰ *Ibid.*

⁵⁸¹ See Heller, Memorandum for the President, ‘Three Prescriptions for Boosting US Economic Performance,’ 31 May 1962. Heller Papers. Box 5.

⁵⁸² *Ibid.*

⁵⁸³ Heller, Memorandum for the President, ‘A Business Prescription for Jacking up the Economy,’ 31 May 1962. POF. Box 74.

⁵⁸⁴ CEA, ‘Possible Government Action.’

the next downturn was imminent, Heller pushed hard for an immediate tax cut.

In the wake of the stock market crash, the president was unsure how to proceed. Whilst he recognised the merits of his CEA chairman's approach, he now had a "new--political--argument" to consider thanks to developments within the Treasury.⁵⁸⁵ Although Dillon, too, had grown more receptive to Heller's ideas, he supported a tax cut of a size much smaller than the CEA's \$10 billion target.⁵⁸⁶ Furthermore, he was determined to crown his tenure as Treasury Secretary with a major overhaul of the tax structure. Accordingly, Dillon saw tax reduction as sugar-coating for a series of unpopular reforms that he wanted, all of which he planned for Kennedy to propose in January 1963.⁵⁸⁷ Thus, Kennedy had to weigh Dillon's argument for a combined tax cut and reform package against the CEA case for an immediate and much larger reduction. Unable to decide immediately following the stock market's decline, he told his advisers that he would see how the economy performed in the following week, before announcing a decision at his next press conference on June 7.

This precipitated "a period of argument within the administration about the wisdom of tax reduction," culminating in a key meeting about the matter on June 6.⁵⁸⁸ In the lead up to this, Heller painted a "grimmer forecast" of the economy's long-term prospects, noting that the slowdown in investment following the stock market crash increased the "odds on a recession beginning in 1962" from 20 to 1 to 5 to 1.⁵⁸⁹ Whilst acknowledging that reform was a worthy undertaking, he suggested that JFK promote a tax cut that summer which could expire in 1963, thereby enabling further

⁵⁸⁵ Davis, 'Politics of Prosperity,' 281.

⁵⁸⁶ Stein, *The Fiscal Revolution in America*, 431.

⁵⁸⁷ Davis, 'Politics of Prosperity,' 281.

⁵⁸⁸ Stein, *The Fiscal Revolution in America*, 408.

⁵⁸⁹ For the first quote, see Davis, 'Politics of Prosperity,' 277. For the recession judgement see CEA, 'Economic Prospects: A New Look,' 5 June 1962. Sorensen Papers. Box 29.

tax reduction to accompany the Treasury's package that year.⁵⁹⁰ Far from creating a climate of fear, as Kennedy also worried, Heller said that a 'quickie' tax cut would "show that the Administration is decisive."⁵⁹¹

To bolster his case, Heller invited Paul Samuelson and Robert Solow (now back at MIT) to the June 6 meeting, both of whom added further political and economic arguments in favour of a tax cut.⁵⁹² Dillon, by comparison, was unconvinced that there might be a recession, saying that he believed the economy would "continue to advance throughout this year and into 1963."⁵⁹³ If further stimulus were required that year, a sufficient amount would come from the tax cut that would lubricate his reform proposals. It was also "advisable not to submit new proposals until the current tax bill [the Investment Tax Credit]" was enacted, something that eventually happened in October.⁵⁹⁴ To add credence to his argument, the Treasury Secretary forwarded the president the views of his Keynesian adviser, Seymour Harris. He made the important political point that it would be difficult to justify a tax cut whilst GNP was rising, something that John Kenneth Galbraith seconded.⁵⁹⁵

JFK seemingly supported Dillon's position in his press conference remarks on June 7. The president dodged questions about an immediate tax cut and announced that he would propose "a net tax reduction" to accompany reform in January 1963.⁵⁹⁶ Whilst this statement certainly pleased the Treasury Secretary, it is worth noting that it also signified a triumph for Heller because Kennedy made use of the full employment budget concept to justify a 1963 tax cut. "If the United States were now

⁵⁹⁰ CEA, 'Proposals for Tax Reduction (draft for discussion),' 5 June 1962. Sorensen Papers. Box 40.

⁵⁹¹ Ibid.

⁵⁹² Heller, Interview with Hargrove and Morley, 202; Samuelson and Solow, Memorandum for the President, 'The Changed Mid-year Outlook,' 6 June 1962. Heller Papers. Box 5.

⁵⁹³ Dillon, Memorandum for n.n., 'The Current Economic Situation and Proposals to Meet It,' 6 June 1962. Sorensen Papers. Box 40.

⁵⁹⁴ Ibid.

⁵⁹⁵ Dillon, Memorandum for the President, Untitled, 7 June 1962. POF. Box 89; Galbraith, Memorandum for the President, 'Tax Reduction,' 6 June 1962. WHSFWH. Roll 16.

working at full employment and full capacity,” the president explained, “this would produce a budget surplus at present taxation rates of about \$8 billion this year.” The “tax structure as presently weighted exerts too heavy a drain on a prospering economy,” meaning that a tax cut was imperative.⁵⁹⁷ Despite not announcing a ‘quickie’ tax cut on June 7, JFK accepted the Keynesian argument for one. At the same time, he proposed to enact a large tax cut at the beginning of 1963.

Recognising, too, that this initiative might involve running a deficit in non-recession conditions, Kennedy followed up his June 7 press conference with a Commencement Address at Yale University that provided further evidence of his conversion to the new economics. In this speech, Kennedy sought to slay the myth of the balanced budget, making use of materials that the Council had gathered for him since May 23. “The myth persists,” he told an audience containing many members of the corporate elite, “that Federal deficits create inflation and budget surpluses prevent it...Obviously deficits are sometimes dangerous – and so are surpluses – but honest assessment plainly requires a more sophisticated view than the old and automatic cliché that deficits automatically bring inflation.”⁵⁹⁸

The president’s ringing affirmation of Heller’s views encouraged the CEA chairman. He was also aware that Kennedy had not explicitly ruled out a quickie tax cut. Therefore, in the month following the Yale address Heller and the Council continued to push for immediate fiscal expansion. They drew the president’s attention to the difficulty of getting congressional approval of a combined tax reduction and reform package in early 1963 (especially because JFK’s tenuous hold over the legislature was likely to weaken after the November mid-term elections) and

⁵⁹⁶ Kennedy, ‘The President’s News Conference,’ 7 June 1962. APP.

⁵⁹⁷ Ibid.

⁵⁹⁸ Kennedy, ‘Commencement Address at Yale University,’ 11 June 1962. APP.

continued to paint a gloomy picture of the economic outlook.⁵⁹⁹ Additionally, Heller passed Kennedy the views of several sympathetic business economists and encouraged Samuelson and Solow to write to the president once more.⁶⁰⁰

Again, political factors forced the president to resist Heller's approach. Theodore Sorensen, while sympathetic to the Council's argument, wondered why JFK should expend political capital seeking a quickie tax cut, especially because the administration was already committed to proposing one in January.⁶⁰¹ Additionally, in a meeting on July 13 with both Dillon and Democrat Wilbur Mills of Arkansas, chairman of the House Ways and Means Committee, the latter told the president "that the prospects [for a quickie tax cut] in Congress were bleak."⁶⁰² As Mills headed the most powerful tax-writing committee in Congress, his support for the tax cut was essential to secure passage of the measure. Though he accepted the necessity of temporary deficits, Mills believed that reduced expenditures should accompany growth-boosting measures. "Without commitment to expenditure control," Mills' biographer has written, the Ways and Means Committee chairman believed "the government might expand to excessive size."⁶⁰³ Aware that Kennedy "would almost certainly bow to the political constraints against a quick [tax] cut," Heller spent the following month arguing that the threat of an impending recession outweighed these considerations.⁶⁰⁴ On July 20, he informed JFK that a Republican businessperson had drawn his attention to "an alarming trend of the past ten days for corporation cut-

⁵⁹⁹ See Tobin, Memorandum for the President, 'The Strategy of Tax Reduction and Reform,' 16 June 1962. Gordon Papers. Box 38; Heller, Memorandum for the President, 'Storm Signals,' 27 June 1962. POF. Box 74; Heller, Memorandum for the President, 'The Economics of 1962 Tax Reduction,' 13 July 1962. POF. Box 74; and Heller, Memorandum for the President, 'Economic Situation Paper for your Meeting today with Businessmen,' 12 July 1962. Gordon Papers. Box 38.

⁶⁰⁰ See Heller, Memorandum for the President, 'Business Economists on the Economic Outlook and Tax Policy,' 12 July 1962. Gordon Papers. Box 38; Samuelson and Solow, Memorandum for the President, 'That Second Look at Need for a Tax Cut,' 13 July 1962. Sorensen Papers. Box 40.

⁶⁰¹ Sorensen, Memorandum for the President, 'Tax Cut,' 12 July 1962. Sorensen Papers. Box 40.

⁶⁰² Bernstein, *Promises Kept*, 152.

⁶⁰³ Zelizer, *Taxing America*, 157.

backs on every front.”⁶⁰⁵ Later, on July 27, he said that economic indicators that had “telegraphed” previous recessions had been “sending out storm signals.”⁶⁰⁶

These efforts culminated in Heller making one last effort for an immediate tax cut at a meeting on August 10.⁶⁰⁷ Although this course of action was looking unrealistic in political terms, Heller once more brought Samuelson and Solow into the fold. They argued that the economy was in a “levelling-off phase of the business cycle, like those of 1956-57 and 1959-60.”⁶⁰⁸ Enacting a tax cut immediately, Heller said, would provide “insurance against a Kennedy ‘recession,’” would offset the economy’s persistent slack, and would give “the Democratic congressional candidates a more activist economic policy to brandish in the 1962 elections.”⁶⁰⁹ Getting “a sizeable January 1 tax cut” through the Hill would also prove extremely tough, especially “when Congress fully recognizes the \$7 to \$8 billion FY 1963 deficit and the larger FY 1964 deficit [that would follow].”⁶¹⁰

By this point, Kennedy was ready to reject the Council’s case. Following private hearings conducted by the Ways and Means Committee that summer, he realised that Congress would not endorse a quick tax cut.⁶¹¹ This was a fact that Mills once again reiterated to JFK on August 10.⁶¹² In addition, as Heller painted a gloomy

⁶⁰⁴ Davis, ‘Politics of Prosperity,’ 295.

⁶⁰⁵ Heller, Memorandum for the President, ‘Report from Scattered Sectors – Economic and Tax Front,’ 20 July 1962. POF. Box 74.

⁶⁰⁶ Heller, Memorandum for the President, ‘Leading Business Cycle Indicators,’ 25 July 1962. POF. Box 74.

⁶⁰⁷ Heller, Memorandum for the President, ‘The Range of Tax-Cut Choices before Us,’ 9 August 1962. Gordon Papers. Box 38.

⁶⁰⁸ Samuelson and Solow, ‘The Final August Look at the Case for an Immediate Tax Cut,’ 10 August 1962. Gordon Papers. Box 38.

⁶⁰⁹ Heller, Memorandum for the President, ‘The Range of Tax-Cut Choices before Us.’

⁶¹⁰ Ibid.

⁶¹¹ This was especially because Mills remained committed to expenditure restraint and was also unconvinced there would be an immediate recession. See Zelizer, *Taxing America*, 194-196. Heller was subject to the committee’s pessimistic outlook when he testified before it on August 9. See Okun, Memorandum for the Council, ‘Hasty Notes on Heller Vs Ways and Means,’ 9 August 1962. Gordon Papers. Box 29.

⁶¹² Gardner Ackley, Memorandum for the Files, ‘Meeting with the President on August 10 re Tax Cut,’ 17 August 1962. WHSFWH. Roll 66.

picture throughout July and early August, new economic data actually contradicted him: this showed the economy to be performing better than he had previously suggested.⁶¹³ To compound his problems, JFK also argued that public opinion was unreceptive to an immediate tax cut, especially following the results of a Gallup Poll on July 31, which indicated that 72 percent of Americans opposed one because such a measure might be inflationary.⁶¹⁴

Due mostly to political reasons, Heller did not convince Kennedy to enact a large tax cut following both the steel price fiasco and the stock market collapse. Still, the president did commit himself to tax reduction at the beginning of 1963 and reiterated his desire to do so on August 13.⁶¹⁵ The way he used the full employment budget concept to justify this course of action, both on June 7 and on August 13, clearly indicated that the CEA chairman had successfully converted the president to liberal Keynesianism. After eighteen long months of presidential education, Heller had finally won over his student.

IV

Whilst the president was on the side of the Council, the Treasury Secretary was not. Still believing that reform was more important than rate reduction, Dillon was unwilling to embrace Heller's ideas fully. True, he had become more receptive to tax reduction throughout the preceding months. He recognized, for example, that expansionary policies might not be inflationary, especially because the country had run a deficit of \$7.1 billion for FY 1962 (1.2 percent of GDP) and still maintained

⁶¹³ Heller, Memorandum for the President, 'The July Returns and Outlook,' 9 August 1962. Heller Papers. Box 17.

⁶¹⁴ Heller, Memorandum for the President, Untitled, 31 July 1962. Gordon Papers. Box 38. Heller admitted on 9 September that the Gallup Poll deterred Kennedy. See Heller, 'Transcript of Interview for CBS.'

⁶¹⁵ Kennedy, 'Radio and Television Report to the American People on the State of the National Economy,' 13 August 1962. APP.

price stability.⁶¹⁶ However, Dillon argued that reform was more important.⁶¹⁷ Any cut to tax rates needed only to lubricate this and should certainly not amount to the \$10 billion target favoured by the CEA.⁶¹⁸ Such a stance posed a threat to Heller: while the president understood the intellectual case for a tax cut, Dillon's insistence on it being much smaller than the Council wanted meant that the eventual measure might not be large enough to close the performance gap. Realising that he needed to win the Treasury Secretary fully to his side, Heller spent September and October trying to do so. Aware that there existed a "network of experts" in the Treasury, who, he later said, "were on our side," the CEA chairman set out to use them to convince Dillon that the size of the tax cut should be around \$10 billion.⁶¹⁹

His vehicle for facilitating this was the Cabinet Committee on Economic Growth. This was a body Heller convinced Kennedy to establish, with the CEA chairman as its chair, on August 21. Conceived by Heller as far back as March as a way to focus the administration's attention on growth policy, this was comprised of top-level representatives from the Treasury, the Budget Bureau, the CEA, and the Departments of Labor and Commerce.⁶²⁰ After establishing it in the summer, Kennedy charged the committee with producing "a general report which will enable growth policy to receive proper consideration in the 1963 budget and legislative program."⁶²¹ Heller later admitted that he "plotted" to use the committee to establish

⁶¹⁶ See Dillon, 'Statement Before the House Ways and Means Committee,' 7 August 1962. Heller Papers. Box 22.

⁶¹⁷ Flash, *Economic Advice and Presidential Leadership*, 252.

⁶¹⁸ Stein, *The Fiscal Revolution in America*, 431.

⁶¹⁹ Heller, Interview in Hargrove and Morley, 204; and Heller and Gordon, Interview with Larry Hackman and Pechman, 14 September 1972, 55-56. JFKL-OHC.

⁶²⁰ For Heller's first espousal to JFK of the need for the committee, see his Memorandum for the President, Untitled, 28 March 1962. Gordon Papers. Box 38.

⁶²¹ n.n., 'Draft Report to the President from the Cabinet Committee on Economic Growth,' 16 November 1962. Gordon Papers. Box 26.

a consensus regarding tax reduction “on the CEA’s terms.”⁶²² This he set out to do during the committee’s first meeting, where it was decided that the Treasury would prepare a report on taxes and growth to be presented at a future meeting.⁶²³ Confident that the exact members of the Treasury who were favourable to the Council’s approach would write that department’s report, Heller’s intervention was an obvious attempt to manipulate the committee’s work to the CEA’s advantage. In terms of convincing Dillon, his scheme was a success.

Following the first meeting, Harvey Brazer wrote the Treasury department’s paper. An economist from the University of Michigan who served as Director of the Treasury’s Office of Tax Analysis, Brazer presented his paper at a committee meeting on October 26. As Heller expected, it came “to quite similar conclusions to our own, and by much the same reasoning.” It “concluded that a \$10 billion net tax reduction would be consistent with the objectives of growth and stability.”⁶²⁴ Crucially, Brazer justified this by utilising the full employment budget concept. This “had an impact on Dillon’s thinking,” to the point whereby the Treasury Secretary accepted Heller’s argument over the size of the tax cut.⁶²⁵ Reflecting this, both the committee’s interim statement and its final report (submitted on December 1) called for “\$7 to \$12 billion net reduction in taxes” to “bring actual levels of output up to the economy’s potential ability.”⁶²⁶

⁶²² Heller and Gordon, Interview with Hackman and Pechman, 55-56; and Heller to Flash, ‘Comments on Manuscript ‘The Politics of Advice,’ 18 October 1964. WHSFWH. Roll 16.

⁶²³ Bernstein, *Promises Kept*, 154.

⁶²⁴ Heller to Flash, ‘Comments on Manuscript ‘The Politics of Advice’; and Flash, *Economic Advice and Presidential Leadership*, 255. See too n.n., ‘Summary of Minutes of Cabinet Committee on Economic Growth Meeting,’ 26 October 1962; and n.n., ‘Minutes of Cabinet Committee on Economic Growth, October 26, 1962,’ 30 October 1962. Both in Heller Papers. Box 17.

⁶²⁵ Harvey Brazer cited in Bernstein, *Promises Kept*, 154; Heller, CEA-OH, 454.

⁶²⁶ n.n., ‘Draft Report to the President from the Cabinet Committee on Economic Growth’; and Heller, Dillon, Bell, William Wirtz and Edward Gudeman, Memorandum for the President, Untitled, 1 December 1962. Attached to ‘Programs to Promote Economic Growth in the 1963 Administration Program: A Report to the President from the Cabinet Committee on Economic Growth.’ Gordon Papers. Box 26.

Spurred on by winning the Treasury Secretary to his side, Heller renewed his attempts for prompt enactment of a large tax cut, which he wanted decoupled from reform. New economic data released in November added grist to his mill. “For the next 6 to 8 months,” this revealed, there was “no promise of a significant speedup” in economic activity.⁶²⁷ Most worrying was the fact that GNP only rose by \$3.3 billion during the third quarter of 1962, the smallest quarterly gain in the recovery from the 1960-61 recession. This meant that the performance gap, which had reduced to \$30 billion at the start of 1962 (from \$50 billion the year before), increased to \$35 billion by November.⁶²⁸ “The long-continued existence of this gap,” the CEA concluded, provided “the basic economic case for fiscal action.”⁶²⁹

Heller mustered a wealth of evidence to try to convince the president to heed this advice. As far back as October 3, he sent Kennedy a “sensible survey” of public opinion on tax reduction conducted by the Michigan Survey Research Center.⁶³⁰ Knowing that the president partly resisted a tax cut following the Gallup Poll of July 31, Heller’s memo sought to demonstrate that public opinion had become more favourable to a quick tax cut. The Michigan Survey revealed that 65 percent of Americans considered tax reduction a “good idea,” compared with 42 percent a year ago (those who thought it was a bad idea went down from 43 percent to 19 percent).⁶³¹ Heller followed this up with a note to Kennedy one month later, following a Council meeting with AFL-CIO chiefs. The labour leaders, Heller asserted, “emphatically expressed their dissatisfaction with the current economic situation, their pessimism regarding the future, their feeling of the great need for an

⁶²⁷ CEA, ‘The Economic Outlook,’ 15 November 1962. Sorensen Papers. Box 40.

⁶²⁸ Ibid.

⁶²⁹ CEA, ‘Why Taxes Should be Cut,’ 15 November 1962. Sorensen Papers. Box 40.

⁶³⁰ Heller, Memorandum for the President, ‘A sensible survey of tax cut reactions,’ 3 October 1962. Gordon Papers. Box 38.

⁶³¹ Ibid.

immediate tax cut and their concern over the lack of urgency in the Administration approach.”⁶³² They urged JFK to “impart a sense of urgency by taking the initiative and mounting an all-out campaign” for a large tax cut.⁶³³ Additionally, the CEA chairman highlighted how certain business economists favoured a tax cut decoupled from reform, a point that he made following a CEA meeting with the Conference of Business Economists on November 10.⁶³⁴

As well as highlighting how the public, labour, and certain members of the business community favoured prompt tax reduction, Heller continued to stress that foreigners did so too. This was particularly after the OECD’s Economic Policy Committee adopted a statement in early November, which “*urged the United States to reduce taxes or increase expenditure or both* in order to restore full employment.”⁶³⁵ A Brookings Institution study of the five-year outlook for the payments deficit, commissioned by Heller earlier in the year, issued its preliminary findings in November and made a similar argument.⁶³⁶ By the fall, Kennedy had secured enactment of both the Trade Expansion Act and the Investment Tax Credit, whilst Operation Twist had enjoyed “modest success” throughout 1962 thanks to meetings of the Quadriad.⁶³⁷ For Heller, all this indicated that Kennedy could engage in prompt fiscal expansion. His efforts to persuade the president to do so culminated in an article written for *Nation’s Business* in November, which coincided with another attempt on the Council’s behalf to advocate a “quick, temporary tax cut.”⁶³⁸ In his

⁶³² Heller, Memorandum for the President, ‘CEA Meeting with the AFL-CIO Economic Policy Committee, November 1962,’ 2 November 1962. Gordon Papers. Box 38.

⁶³³ Ibid.

⁶³⁴ Heller, Memorandum for the President, ‘Business views on the economic outlook and tax cuts,’ 10 November 1962. Gordon Papers. Box 38.

⁶³⁵ Heller, Memorandum for the President, ‘Covering Our European Flank,’ 10 November 1962. POF. Box 75. Emphasis in the original.

⁶³⁶ Heller, Memorandum for the President, ‘Preliminary Brookings Report on the Five-Year Outlook for the US Balance of Payments,’ 21 November 1962. Heller Papers. Box 16.

⁶³⁷ Bremner, *Chairman of the Fed*, 162, 173; Heller, Interview in Hargrove and Morley, 190-191.

⁶³⁸ Davis, ‘Politics of Prosperity,’ 348.

article, Heller justified a tax cut not only by stressing the problem of the economy's repressive taxation system, but also by emphasising the multiplier effects of one.⁶³⁹

This advocacy did not overcome either JFK's commitment to reform or his hesitancy to cut taxes promptly. In fact, the president had retreated from close association with tax reduction after the summer, not wanting to damage the Democratic Party's chances in the November mid-term elections. In addition, the Cuban Missile Crisis of October diverted his attention from domestic issues. Yet, according to both Robert Collins and Herbert Stein, Kennedy was far from ready by the fall of 1962 "to embrace with enthusiasm the idea of a massive deficit-generating tax cut to stimulate the economy."⁶⁴⁰ For both these scholars, JFK's "ultimate conversion" was prompted by the actions of the CED, apparently in the final month of the year.⁶⁴¹

On December 14, Kennedy addressed several prominent business leaders at the Economic Club of New York outlining the case for a tax cut.⁶⁴² Just twenty-four hours beforehand, Heller recalled that he had "never seen the president so anguished and soul-searching and uncertain about the correctness of his course on a domestic matter."⁶⁴³ Several cabinet members and conservative businesspersons all prompted JFK to question a tax cut.⁶⁴⁴ Nevertheless, the CED, according to Collins and Stein, eased these concerns. The morning of his Economic Club of New York address, that organisation finally came out in favour of a large tax cut, having indicated that it

⁶³⁹ Heller, 'Why We Must Cut Taxes,' *Nation's Business*, 50:11 (Nov. 1962), 40. Heller Papers. Box 22.

⁶⁴⁰ Collins, *The Business Response to Keynes*, 179.

⁶⁴¹ Ibid, 177-191 (quotation 179); and Stein, *The Fiscal Revolution in America*, 412-421; and *Presidential Economics*, 106-108.

⁶⁴² Kennedy, 'Address and Question and Answer Period at the Economic Club of New York,' 14 December 1962. APP.

⁶⁴³ Heller and Gordon, Interview with Hackman and Pechman, 60. In this, Heller was reading from handwritten notes he made on the day before JFK's Economic Club of New York address.

⁶⁴⁴ Ibid, 60.

would do so throughout the fall.⁶⁴⁵ Kennedy delivered his speech to some of the nation's most important business leaders and thus received an emphatic reception, with the president telling his CEA chairman, "I gave them straight Keynes and Heller, and they loved it."⁶⁴⁶ Furthermore, traditionally conservative business groups, such as COCUS and the NAM, favoured tax reduction by this point (both out of narrow financial self-interest and because of the size of the full employment surplus), which also impacted on JFK.⁶⁴⁷ From then on, according to Collins, Stein, and others, Kennedy embraced tax reduction fully.⁶⁴⁸

This interpretation gives too much credit to the business community for facilitating JFK's eventual conversion to the new economics. This is not least because the reaction that the business community gave Kennedy following his Economic Club of New York address was more an indication that the president had been educating it during the fall of 1962 about the merits of Heller's ideas. True, Kennedy was nervous before this speech, but a closer reading of Heller's notes twenty-four-hours beforehand reveals that when he met with the president JFK made a "reassuring comment that I was right...and that he would no doubt go ahead" with the tax cut.⁶⁴⁹ Rather than the business community convincing Kennedy to put his heart into tax reduction in December, it was the other way around.

In a meeting with Heller and Gordon three months earlier, JFK expressed his frustration with the inability of certain business leaders to embrace modern economic thinking. He cited the fact that he got a chilly reception from his audience following his Yale Address. "[College] students may absorb these ideas," the president

⁶⁴⁵ Collins, *The Business Response to Keynes*, 186-187.

⁶⁴⁶ Cited in Heller, *New Dimensions of Political Economy*, 35.

⁶⁴⁷ Collins, *The Business Response to Keynes*, 180-187; Stein, *The Fiscal Revolution in America*, 412-414.

⁶⁴⁸ See Sorensen, *Kennedy*, 429; Collins, *The Business Response to Keynes*, 179-187; Stein, *Presidential Economics*, 106-108.

lamented, “but they seem quickly to adopt the standard clichés when they enter the narrow social circle of the business community.”⁶⁵⁰ Expressing bewilderment with the long-held commitment of executives to fiscal conservatism, Kennedy complained that it was so “clearly in conflict with their own self-interest.” An “expansionary economic policy by government would raise the[ir] profits.”⁶⁵¹ Accordingly, throughout the fall of 1962 the administration engaged in a robust effort to acquaint fiscally conservative and progressive business leaders with the virtues of the new economics, culminating in Kennedy’s speech to the Economic Club of New York.⁶⁵²

At the forefront of this effort, Heller provided press secretary Pierre Salinger with material for a presidential address to the White House Conference of Business Editors and Publishers in September, gave the principal talk at the Annual Meeting of the National Association of Business Economists in October, and addressed the Mortgages Bankers Association of America’s annual convention that same month. He also sent a copy of a CEA document called ‘Administration Policies to Promote Business Enterprise’ to *Forbes* magazine.⁶⁵³ In November, he took part in a White House conference for representatives of labour and management, penned the aforementioned article for *Nation’s Business*, and held regular meetings with both the economic policy liaison committee of the administration’s Business Advisory

⁶⁴⁹ Heller and Gordon, Interview with Hackman and Pechman, 60.

⁶⁵⁰ Gordon, ‘Notes on Meeting with the President, Friday 28 September 1962,’ 29 September 1962. Heller Papers. Box 6.

⁶⁵¹ Ibid.

⁶⁵² As James Giglio noted, Sorensen initially spearheaded Kennedy’s attempt to court and educate business as far back as the aftermath of the steel price fiasco and the stock market crash. However, it continued and gained momentum throughout the rest of the year, with the Council playing a key role in the fall. Giglio, *The Presidency of John F. Kennedy* (Lawrence, KS, 2006), 135. See too Rowen, *The Free Enterprisers*, 124.

⁶⁵³ Heller, Memorandum for Pierre Salinger, ‘Suggested Talking Points for Opening Remarks at the White House Conference of Business Editors and Publishers,’ 25 September 1962; ‘Address to National Association of Business Economists, Washington D.C.,’ 26 October 1962. Both in Heller Papers. Box 33; ‘Address to 49th Annual Convention of the Mortgages Bankers Association,’ 1 October 1962; and letter to Malcom Forbes, October 1962. Both in Heller Papers. Box 11.

Council and the Conference of Business Economists.⁶⁵⁴ Thus, Heller made himself “a familiar figure at business meetings” during the fall of 1962.⁶⁵⁵ According to Arthur Schlesinger, “his agreeable intelligence and candour” helped to “disarm” the “earlier suspicions” of the business community towards his ideas.⁶⁵⁶

Demonstrating this, following his address at the National Association of Business Economists in October, one senior business figure praised Heller for doing an “excellent job,” not least because many of his “fellow members came away with a better appreciation of Administration thinking.”⁶⁵⁷ Rather than the business community convincing Kennedy to embrace the new economics fully, JFK and Heller both worked to persuade fiscally conservative and progressive executives that the Council’s approach was sound. Reflecting this, before he gave his Economic Club of New York Address, Kennedy spoke of the educational role that he was playing. “If I can convince them,” he told Sorensen of his audience, “I can convince anyone.”⁶⁵⁸

To do so, the president wrapped up the arguments for a tax cut in orthodox language, emphasising how the measure would boost business profits, increase levels of investment, and spur production. “[An] economy hampered by restricting tax rates,” Kennedy told the Economic Club, “will never produce enough revenue to balance the budget, just as it will never produce enough jobs or enough profits.”⁶⁵⁹ Quite clearly, Kennedy assuaged business fears of his economic policies. The *Wall Street Journal* claimed that nearly all business leaders “generally applauded” it,

⁶⁵⁴ Heller, ‘Fiscal and Monetary Policy for Economic Stability and Growth,’ Address to the Conference on Fiscal and Monetary Policy of the President’s Advisory Committee on Labor-Management Policy, 14 November 1962. Heller Papers. Box 34; Heath, *John F. Kennedy and the Business Community*, 19.

⁶⁵⁵ Schlesinger Jr., *A Thousand Days*, 565.

⁶⁵⁶ *Ibid*, 565.

⁶⁵⁷ Henry Bund to Heller, 31 October 1962. Heller Papers. Box 33. For similar views from another businessperson regarding Heller’s efforts, see R. J. Eggert to Heller, 30 November 1962. Heller Papers. Box 48.

⁶⁵⁸ Sorensen, *Kennedy*, 430.

⁶⁵⁹ Kennedy, ‘Address and Question and Answer Period at the Economic Club of New York.’

whilst one individual wrote Heller on December 28 to say that everything about Kennedy's address was "brilliant...the speech itself, not to mention the manner in which he handled the unknown questions. The President undoubtedly gained significant adherence of business to his program."⁶⁶⁰

The argument that JFK endorsed the new economics because the business community impelled him to do so lacks substantiation: it underestimates the extent to which the administration educated the business community during the fall of 1962 about the merits of liberal Keynesianism. Furthermore, the tax cut that Heller convinced Kennedy to champion in 1962 was different to the one advocated by the business community. Heller wanted a larger tax cut than the CED, who came out in favour of a measure as small as \$6.5 billion (depending on the size of FY 1964 expenditures).⁶⁶¹ The CED also said that, if it were to endorse a tax cut similar in size to that advocated by the Council, expenditures for FY 1964 needed to be kept low, something that Heller opposed.⁶⁶² Heller further viewed the tax cut as a means to expand the economy and thereby fund the expansion of the liberal state during the 1960s, whereas the CED, COCUS, and NAM remained focused solely on the need to both overcome stagnation and achieve their long-held desire to ease the tax burden.⁶⁶³ Important differences thus distinguished Heller's approach to fiscal policy from that of the business community, a point that Heller alluded to later in his career.⁶⁶⁴ This clearly undercuts the notion that liberals and business leaders engaged in a consensus during the early 1960s over how best to implement Keynesian ideas.

⁶⁶⁰ n.n., 'Executives Applaud Kennedy's Tax Speech,' *Wall Street Journal*, 17 December 1962, 3. PQHN; Hans Widenmann to Heller, 28 December 1962. Heller Papers. Box 50. For a similar assessment, see Giglio, *The Presidency of John F. Kennedy*, 139.

⁶⁶¹ Gordon, Memorandum for the President, 'More on CED Tax Proposals,' 10 October 1962. Gordon Papers. Box 38.

⁶⁶² Ibid. For Heller's opposition, see Chapter Five of this thesis.

⁶⁶³ Chapters Two and Three of this thesis have demonstrated the former. For the latter, consult Collins, *The Business Response to Keynes*, 180-188; and Stein, *The Fiscal Revolution in America*, 412-414.

⁶⁶⁴ Heller, Interview in Hargrove and Morley, 197-198.

Instead of the business community convincing Kennedy to embrace the new economics, Heller's education of the president proved more decisive. Heller later said that he had a "marvellous sense all the way through" that Kennedy "was getting it."⁶⁶⁵ So pleasing was JFK's "responsiveness to *analysis*, the force of economic logic and fact; to *analogy*, the demonstrated success of Keynesian policies abroad; and to *anomaly*, the continued sacrifice of human and material resources on the altar of false concepts of 'sound finance.'"⁶⁶⁶ The president's conversion occurred gradually, but his "occasional doubts and concessions to prevailing economic sentiment" were merely "detours on his road to modernism."⁶⁶⁷ In fact, he proved "a quick study with an inquiring mind" and fully embraced Keynesianism, unlike Roosevelt, Truman, and Eisenhower.⁶⁶⁸ Such was JFK's command of modern fiscal theory by December 1962, Kermit Gordon later argued that the president knew as much about the subject as a college professor.⁶⁶⁹

This is significant, as certain historians have criticised JFK for portraying himself as an intellectual.⁶⁷⁰ They insist that this was false, not least because he did not write his Pulitzer Prize-winning Book *Profiles in Courage*. However, JFK developed such a fluent grasp of modern fiscal theory under Heller's tuition – to the point whereby some claim he could have taught it – that this undercuts such an argument: intellectually, Kennedy was not as shallow or as superficial as the revisionists have suggested. It is also worth noting that Kennedy's sophisticated grasp of economics by the end of 1962 sheds light on another key way in which historians have sought to conceptualise his presidency. Some have argued that JFK became a

⁶⁶⁵ Ibid, 175.

⁶⁶⁶ Heller, *New Dimensions of Political Economy*, 35. Emphasis in the original.

⁶⁶⁷ Ibid, 35.

⁶⁶⁸ Morgan, 'Promoting Prosperity.'

⁶⁶⁹ Gordon, Interview with Turner #1, 7.

more mature leader as his presidency unfolded. They cite both his promotion of civil rights legislation and his decision to sign the Nuclear Test Ban treaty in 1963 as evidence of this.⁶⁷¹ Ignored, however, is the way Kennedy's knowledge of economics developed under Heller. The fact that he was the first president to grasp modern fiscal theory fully, having entered the White House committed to commercial Keynesianism, certainly adds credence to this argument.

V

By the end of 1962, Walter Heller had successfully converted John F. Kennedy to growth liberalism, having laid the groundwork the previous year. As this chapter has demonstrated, there were signs in January that JFK was ready to move beyond commercial Keynesianism. His promotion of the CEA's three-part programme indicated this. It took the Council's use of the 1962 *Economic Report*, the fear of a Kennedy recession, the establishment of a framework to free JFK to think positively about pursuing growth, and Heller's relentless advocacy of liberal Keynesianism, to secure the president's conversion. Importantly, this occurred before the stock market crash of May 27 and the comparisons that Heller made with European fiscal policies were integral to it.

After he captured the president, however, political factors prevented Heller from convincing JFK to promote an immediate tax cut. Yet, he did successfully use the Cabinet Committee on Economic Growth to convert Dillon during the fall, before trying to convince JFK to embrace prompt tax reduction in November. The president proved unwilling to do so, but decided to renew his enthusiasm for a tax cut the following month. Importantly, this did not happen because of the attitude of the business community. Instead, Heller's persistence throughout the year, the conversion

⁶⁷⁰ See Mark White, 'Behind Closed Doors: The Private Life of a Public Man,' in Mark White (ed.) *Kennedy: The New Frontier Revisited* (New York, 1998), 267-268.

of Dillon to his ideas, and the conclusion of the November mid-term elections, all enabled Kennedy to reignite his interest in tax reduction. This was manifest in his speech to the Economic Club of New York, which concluded a robust administration effort to educate the business community about the merits of the Council's approach.

In short, 1962 was Walter Heller's finest year in the White House. His education of Kennedy, who entered office knowing little about the new economics, was certainly his greatest accomplishment as CEA chairman. After finally capturing not just Kennedy but also the business community, the CEA chairman quickly told the president to send a tax bill to the Hill. "Congress may be lukewarm," he explained, "but powerful groups throughout the country are *ready for action*. When the Chicago Board of Commerce, the AFL-CIO, the CED, and the US Chamber are on the same side – when repeated editorials in *BusinessWeek* are indistinguishable from those appearing in the *Washington Post* – the prospect for action cannot be wholly dim."⁶⁷² Kennedy heeded Heller's request. In January 1963, he asked Congress to pass a large tax cut. This sparked off a yearlong battle for its enactment. Examining the role Heller played in securing the passage of this legislation – which brought the Keynesian revolution in America to its climax – is the next stage in his story.

⁶⁷¹ See White, 'Introduction,' in *Ibid*, 12-13.

⁶⁷² Heller, Memorandum for the President, 'Recap of Issues on Tax Cuts (and the Galbraithian Alternative),' 16 December 1962. Gordon Papers. Box 38. Emphasis in the original.

Chapter Five

“Mr Tax Cut”

On February 18, 1963, the *Washington Post*'s Robert Thompson proclaimed 'Heller's Concepts Now Prevail.' After two years of presidential education, Thompson explained, Walter Heller's "liberal, expansionist policies" were "the prevailing economic concepts of Mr. Kennedy's regime."⁶⁷³ A response to the fact that, in January, Kennedy called upon Congress to pass a \$13.6 billion tax cut on July 1 (comprising \$11 billion for individuals and \$2.6 billion for corporations), the *Post*'s article highlighted just how much Heller's influence had increased over the previous two years. "In a very real sense," it said, "the proposal is Walter Heller's grand experiment with the American economy."⁶⁷⁴ True, a legislative initiative finally embodied Heller's ideas, but the tax cut's enactment remained a problem. The prospect of substantially increasing the deficit frightened both the American people and their representatives in Congress. Accordingly, this chapter examines Heller's third year as CEA chairman, ending with Kennedy's assassination. It assesses how he promoted and defended the tax cut as it made its way through Congress. It also examines how he sought to shape monetary policy in a way that did not compromise the eventual impact of that measure.

I

The tax cut that Kennedy sent to Congress in January 1963 was the product of much deliberation within the administration. After Heller finally persuaded both the president and his Treasury Secretary Douglas Dillon to promote a large tax cut in December 1962, debate switched to the size of the deficit that the tax cut should induce as well as that measure's timing. This resulted in new disagreements between

⁶⁷³ Robert E. Thompson, 'Heller's Concepts Now Prevail,' *Washington Post, Times Herald*, 18 February 1963. A5. PQHN.

the Council and the Treasury. Of the two issues, the former proved the most contentious. This was because several conservative politicians (including Ways and Means Committee chairman Wilbur Mills) and business groups such as the CED demanded a reduction in the government's FY 1964 expenditures, so as to prevent a large deficit.⁶⁷⁵ Consequently, Dillon advised JFK in early December to limit the administration's projected spending for FY 1964 to under \$100 billion, a symbolic gesture given the fact that expenditures were close to surpassing that figure for the first time.⁶⁷⁶ The president also wanted to keep the FY 1964 deficit under Eisenhower's record peacetime deficit of \$12.4 billion, so that he could not be criticised as a reckless spender.⁶⁷⁷

The Council strongly argued against both. It did not matter, Heller contended, that Kennedy might defend the largest deficit in peacetime history, not least because "even without a tax cut" there was "no insurance that the 1964 deficit could be held below Ike's record."⁶⁷⁸ If a recession occurred in FY 1964, for example, the deficit would increase beyond \$12.4 billion. According to Heller, the choice thus lay "between a weak program that tries to go only a little beyond the record \$12.4 billion deficit, and a strong program that ignores the old mark."⁶⁷⁹ Whilst Heller's arguments were persuasive, Dillon shared with Kennedy another of his concerns that a quick, large tax cut would spark inflationary concerns in financial circles and thereby endanger the nation's gold reserves.⁶⁸⁰ As noted, Dillon and Kennedy no longer believed in this argument, but the Treasury Secretary worried that it remained popular

⁶⁷⁴ Ibid, A5.

⁶⁷⁵ Gordon, Memorandum for the President, 'More on CED Tax Proposals'; Zelizer, *Taxing America*, 197.

⁶⁷⁶ Flash, *Economic Advice and Presidential Leadership*, 261.

⁶⁷⁷ Stein, *The Fiscal Revolution in America*, 435.

⁶⁷⁸ CEA, 'The Treasury's Tax Cut Proposals,' 3 December 1962. Sorensen Papers. Box 40.

⁶⁷⁹ Ibid.

⁶⁸⁰ Stein, *The Fiscal Revolution in America*, 433.

outside the White House. As a result, he wanted to spread the tax cut over the course of three years, with most of it phased into the latter period, so that the measure would not damage business confidence. This prompted Heller to complain that Dillon favoured “virtually a no-stimulus fiscal program for ‘63.”⁶⁸¹ In contrast, the CEA chairman wanted Kennedy to push as much of the tax cut into the first year as possible and went as far as suggesting that he should run a \$14 billion deficit for FY 1964 to facilitate this.⁶⁸²

Due to the concerns expressed by Dillon, Kennedy was reluctant to endorse such a suggestion. To compound Heller’s problems, John Kenneth Galbraith temporarily diverted the president’s attention in December and January. As Heller recalled, Galbraith’s ideas were briefly subjected to “some soul-searching” by JFK.⁶⁸³ Determined that Kennedy should increase taxes rather than decrease them, the now-Ambassador to India argued that this would provide enough funds to modernise the nation’s depleted public sector.⁶⁸⁴ Heller, too, was concerned about the state of America’s schools, roads, and hospitals, but he reminded the president “a vigorous economy, stimulated by tax cuts, will provide a broader economic base and atmosphere of prosperity.”⁶⁸⁵ This would produce the revenues to overhaul the public sector and would create a robust, high-employment economy.⁶⁸⁶ Swayed more by his CEA chairman’s arguments, and aware, too, that expenditure programmes of the size advocated by Galbraith would be near impossible to push through Congress, the small part of Kennedy that entertained the latter’s proposal “gradually disappeared” in “late

⁶⁸¹ Heller and Gordon, Interview with Hackman and Pechman, 63.

⁶⁸² Ibid, 64.

⁶⁸³ Heller and Gordon, Interview with Pechman, 9.

⁶⁸⁴ Galbraith’s argument, as presented to Kennedy in December 1962, is summarised in Heller, Memorandum for the President, ‘Recap of Issues on Tax Cuts (and the Galbraithian alternative)’; and Heller and Gordon, Interview with Hackman and Pechman, 59.

⁶⁸⁵ Heller, Memorandum for the President, ‘Recap of Issues on Tax Cuts (and the Galbraithian alternative).’

⁶⁸⁶ Ibid.

'62 and early '63.’⁶⁸⁷

Despite responding well to Galbraith, Heller needed to square his ideal tax cut package with that of Dillon. This eventually occurred in late December, but not entirely to the CEA chairman's satisfaction. After not reaching consensus over the size and timing of the tax cut earlier that month, Heller, Dillon, and other advisers held a series of post-Christmas meetings at Palm Beach, where “final decisions were reached.”⁶⁸⁸ There, the CEA chairman did not convince Kennedy that both the timing of the tax cut and the size of the deficit should be on his terms. As he recalled, “the Eisenhower budget constraint” was “very prominent, and it was the main tool that the Treasury used” in the negotiations.⁶⁸⁹

Following mid-December discussions between Treasury officials and Wilbur Mills, it had also become apparent that in order to get a tax cut through Congress, JFK would have to “hold the line on expenditures, link reduction with reform, and pace reductions over a number of years.”⁶⁹⁰ What emerged from the meetings in Palm Beach was a tax cut proposal that failed to meet Heller's ideal expectations. Nevertheless, it is worth noting that his “arguments very likely saved the reductions from being even more thoroughly compromised.”⁶⁹¹ This ensured that “the Administration accepted a larger deficit than it originally had had in mind [for FY 1964].”⁶⁹² Content that the proposal formulated at the end of 1962 would provide a boon to the economy, Heller helped draft portions of Kennedy's 1963 Budget Message, which the president issued on January 17.

This came three days either side of both his State of the Union Address and

⁶⁸⁷ Heller and Gordon, Interview with Pechman, 9.

⁶⁸⁸ Flash, *Economic Advice and Presidential Leadership*, 264.

⁶⁸⁹ Heller and Gordon, Interview with Hackman and Pechman, 68.

⁶⁹⁰ Flash, *Economic Advice and Presidential Leadership*, 265-266 (quotation); Zelizer, *Taxing America*, 197.

⁶⁹¹ Flash, *Economic Advice and Presidential Leadership*, 270.

the release of the 1963 *Economic Report*, both of which also outlined the president's tax bill and the rationale that underpinned it. The nation's "obsolete tax system," Kennedy remarked in the first of these statements, "exerts too heavy a drag on private purchasing power, profits, and employment."⁶⁹³ A \$13.5 billion tax cut, phased in over three years with only \$6 billion coming in year one, offered the best means to overcome this problem. To show that he was acting in a responsible manner, Kennedy explained that not only did these staged reductions demonstrate that his programme would be financially sound, they were also going to be accompanied by revenue-raising reforms that would yield \$3.4 billion following projected enactment in January 1964. This meant that the overall reduction in taxes would amount to just \$10.1 billion.⁶⁹⁴ The Budget Message elaborated upon the rationale that underpinned the tax plan. "Our present choice," Heller wrote, "is between chronic deficits arising out of a slow rate of economic growth, and temporary deficits stemming from a tax program designed to promote fuller use of our resources and more rapid economic growth."⁶⁹⁵ By essentially saying that there were "good" deficits and "bad" deficits, this line partly encapsulated what was so "new" about the "new economics." As Heller informed Kennedy, "no president has ever said this before."⁶⁹⁶

Despite the strong Keynesian language that underpinned these messages, both the CEA chairman and the president also paid tribute to traditional economic ideas, so as to not alienate those unfamiliar with the new economics. Much like Kennedy's December 1962 address to the Economic Club of New York, the Budget Message invoked the principle of sound finance, at one point saying that Kennedy felt "obliged

⁶⁹² Ibid, 270.

⁶⁹³ Kennedy, 'Annual Message to Congress on the State of the Union,' 14 January 1963. APP.

⁶⁹⁴ Ibid.

⁶⁹⁵ Kennedy, 'Annual Budget Message to the Congress, Fiscal Year 1964,' 17 January 1963. APP.

⁶⁹⁶ Heller, Interview in Hargrove and Morley, 198.

to limit severely” his “[FY] 1964 expenditure proposals.”⁶⁹⁷ It also stated that whilst the revenue loss for FY 1964 would be \$5.3 billion, the increased revenues that would result from the better performing economy meant that the overall loss would only amount to \$2.7 billion. This would leave a deficit of approximately \$11.9 billion.⁶⁹⁸ Additionally, in the *Economic Report* the Council “presented no estimates of the full-employment surplus” to justify the tax cut, further indicating that Heller did not want to utilise advanced Keynesian thinking.⁶⁹⁹ Meanwhile, all three of the president’s statements emphasised how the tax cut would produce enough growth and revenues to yield a balanced budget.⁷⁰⁰

The president and his CEA chairman, then, sought to tone down their Keynesian rhetoric to sell the tax cut. At the same time, they sought to pre-empt any likely criticisms against it. Resultantly, all the above messages stressed the economy’s unused capacity in order to alleviate fears of both inflation and a potential balance-of-payments crisis. The *Economic Report* also sought to quell concerns that an increase in the size of the deficit would enlarge the national debt, noting that, in relation to GDP, America’s debt had shrunk since 1945 due to the pace at which the economy had expanded.⁷⁰¹ Despite this, Heller found himself in another disagreement with the Treasury, certain members of which favoured “the deletion or drastic shortening and revision of the section on ‘Tax Reduction and the National Debt’” in the 1963 *Economic Report*.⁷⁰² In their view, the inclusion of this section would draw attention to fears about debt, providing critics of the programme with an obvious line

⁶⁹⁷ Kennedy, ‘Annual Budget Message to the Congress, Fiscal Year 1963.’

⁶⁹⁸ Ibid.

⁶⁹⁹ Stein, *The Fiscal Revolution in America*, 432-433.

⁷⁰⁰ See, for example, Kennedy, ‘Special Message to Congress on Tax Reduction and Reform,’ 24 January 1963; and *The Economic Report of the President, 1963* (Washington DC, 1963), xiii-xv. Both APP.

⁷⁰¹ *The Economic Report of the President, 1963*, 78-79.

⁷⁰² Heller, Memorandum for the President, ‘The Council’s Report and the Debt, Chapter 3,’ 15 January 1963. Heller Papers. Box 5.

of attack. In response, Heller informed Kennedy that fear of the debt would “in any case be played up by those in opposition to your program – whether our report deals with them or not.”⁷⁰³ The inclusion of this section would provide those in favour of the tax cut with useful statistics, whilst simply ignoring the issue would open the administration “to the charge (a) that we don’t take deficits and the debt seriously or (b) that we’re ducking the issue because we’re afraid of it.”⁷⁰⁴ Kennedy agreed with Heller’s arguments and the section remained untouched, a decision that demonstrated the extent to which both men sought to forestall likely attacks against the tax cut.

Despite these efforts, the proposal encountered a firestorm of criticism following its announcement. Of its two elements, the Treasury’s reform package generated the most controversy. Many interest groups opposed the tax bill altogether because of the loopholes that the Treasury intended to close.⁷⁰⁵ At the same time, it should not be underestimated how the issues of deficits, debt, and inflation stirred up opposition to the tax cut. This was especially because numerous members of both parties viewed the plan as fiscally irresponsible. “Some thought the budget deficit too large and feared it would engender inflation,” one historian has remarked, whilst congressional Republicans “disliked the administration’s bill in the context of the budget Kennedy had submitted for fiscal 1964.”⁷⁰⁶ As a result, they argued that the tax cut should be matched by reduced expenditures, with Senate Minority Leader Everett Dirksen of Illinois calling the projected deficit for FY 1964 “incredible.”⁷⁰⁷ Taken aback by this hostile response, Heller appeared before the Joint Economic Committee on January 28 and defended the tax bill.

The extent to which Heller defended the tax cut and helped push it through

⁷⁰³ Ibid.

⁷⁰⁴ Ibid.

⁷⁰⁵ Davis, ‘Politics of Prosperity,’ 371-373.

⁷⁰⁶ Ibid, 374.

Congress in 1963 has been subject to differing interpretations. Some have claimed that the CEA chairman “led the fight in pushing the [tax] plan through Congress.”⁷⁰⁸ Others, by comparison, have argued that his role was insignificant. Reflecting this view, one individual wrote Heller in 1964 offering his congratulations for the eventual passage of the measure, but remarked that while the CEA chairman had “composed” the piece “someone else played [the tune].”⁷⁰⁹ This chapter will show that Heller’s contribution to the legislative process of the tax cut was important but not vital. This was because members of the Treasury spent more time on Capitol Hill working with members of Congress to push the bill forward. However, Heller did apply pressure on lawmakers at certain moments, mustered further evidence in favour of the measure as the legislative process unfolded, and publicly defended the tax programme against its critics.

II

He first did the latter during his JEC appearance on January 28. Here, the University of Michigan’s Gardner Ackley flanked Heller. Ackley was one of two new members of the Council after James Tobin and Kermit Gordon left their posts the previous year. Importantly, the mere presence of the CEA chairman before the JEC demonstrated the extent to which Heller *was* engaged in the legislative process of the tax cut. This was because his predecessors (except for Keyserling) refused to testify in an open manner before congressional committees, seeing themselves as leading “a quiet, data-gathering group of economists.”⁷¹⁰ Heller, by comparison, was determined to transform the CEA into “a top-flight analysis *and* policy center within the

⁷⁰⁷ Cited in *Ibid*, 368.

⁷⁰⁸ Art Pine and John Berry, ‘Economic Advisers Council Loses Clout in Making of Policy,’ *Washington Post*, 6 January 1980. F1. PQHN.

⁷⁰⁹ Agnew H. Bahnson to Heller, 27 February 1964. Heller Papers. Box 47.

administration.”⁷¹¹ Consequently, he regularly appeared before Congress. In short, his advocacy of the tax cut to the JEC demonstrated that he was an active participant in the legislative process.

Harder to ascertain, is the extent to which Heller’s various appearances before Congress in 1963 aided the passage of the tax cut. His JEC appearance on January 28 was hardly successful. In their testimony, Heller and Ackley downplayed the risks that the tax cut posed to prices, the level of debt, and the balance-of-payments. However, what distinguished it from previous Council and administration statements was that they also went into detail about the multiplier effects of the proposal. “Apart from tax reduction,” Heller explained, “one finds no prospect of a sustained rise in demand which might carry the economy within striking distance of its productive potential.”⁷¹²

Using the example of an \$8.5 billion tax cut, Heller and Ackley outlined how a reduction of that size would eliminate the performance gap. They explained that, out of the \$8.5 billion, consumers would spend \$8 billion. This process would be “repeated period after period.”⁷¹³ To meet the rise in demand, production would increase. This would itself create a further \$4 billion of GNP and would boost purchasing power (leading to a further increase in output). This “in turn leads to a further increase of spending of about \$2 billion; another round of about \$1 billion, and so on.”⁷¹⁴ The cumulative effect of these enlargements in GNP would be \$16 billion, which would constitute a consumption multiplier of two. However, the rate of

⁷¹⁰ Johnston, ‘Remembering Minnesota’s Mr. Economics, Walter Heller,’ *MINNPOST*, 29 August 2012. Available at: <https://www.minnpost.com/macro-micro-minnesota/2012/08/remembering-minnesota%E2%80%99s-mr-economics-walter-heller> [Accessed 03/01/2016]

⁷¹¹ Canterbury, *Economics on a New Frontier*, 136. Emphasis in the original.

⁷¹² ‘Statement of Walter W. Heller, Chairman, Accompanied by Gardner Ackley, Member, before the Joint Economic Committee,’ 28 January 1963. POF. Box 75a.

⁷¹³ Ibid.

⁷¹⁴ Ibid.

investment would also accelerate, as businesses would respond to enlarged markets by expanding plant and equipment.⁷¹⁵ After acknowledging that it was difficult to determine what the investment multiplier would be, Heller and Ackley deemed it “reasonable to expect that the combined effects of added consumption and investment can close, or nearly close, the gap between potential and actual output.”⁷¹⁶

This attempt to impress the JEC with the multiplier effects of the tax cut made use of the multiplier-accelerator (M-A) model developed by Paul Samuelson in the late 1930s. According to economist Martin Prachowny, not only was this model outdated, but also the conclusions that Heller and Ackley reached because of deploying it were inaccurate, shortcomings that undermined their efforts to sell the tax cut to the JEC. For Prachowny, Heller and Ackley should have used the IS-LM model, developed by Alvin Hansen and the British economist John Hicks shortly after Samuelson formulated his.⁷¹⁷ Technically more advanced, this would have shown the tax cut’s impact on the rate of interest. This was important because William McChesney Martin told the JEC that interest rates would naturally rise in the wake of the tax cut, thereby “‘crowd[ing] out’ some investment.”⁷¹⁸ If the Council had deployed the IS-LM model, Prachowny has argued, they would have offered a more complete perspective of the tax cut’s impact to the JEC.⁷¹⁹ This would also have enabled them to put pressure on Martin to boost the money supply.⁷²⁰ By not doing so, Heller and Ackley did not deploy one of the best tools available to sell the tax programme to Congress.

Additionally, Prachowny maintained that both Council members did not

⁷¹⁵ Ibid.

⁷¹⁶ Ibid.

⁷¹⁷ Prachowny, *The Kennedy-Johnson Tax Cut*, 52.

⁷¹⁸ Ibid, 65.

⁷¹⁹ Ibid, 65.

⁷²⁰ Ibid, 66.

adequately predict the multiplier effects of the tax cut. This apparently failed to sit well with Senator Paul Douglas, a trained economist and chairman of the JEC. After reading their prepared statement on January 28, Douglas asked Heller and Ackley to explain in more depth how the consumption and investment multipliers worked. After Ackley used a set of charts to do so, Douglas apparently showed that he was “dissatisfied with the Council’s presentation,” not least because he asked the economist Roy Moor to present his own, independent calculations.⁷²¹ Moor’s investment multiplier calculations differed from the Council’s, leading Douglas to indicate that he “wanted more details on the investment response than the Council had provided.”⁷²² Hence, not only did Heller and Ackley make use of an outdated model to justify the tax cut, they also reached the wrong conclusions because of deploying it.

Prachowny’s arguments have several limitations. Firstly, given the fact that Heller deemed it necessary to wrap up the arguments for the tax cut in orthodox language, it is understandable that he did not deploy a more sophisticated Keynesian model to justify it. Doing so would not have changed the minds of the JEC’s fiscal conservatives (a minority on that committee), who either opposed a tax cut or insisted a significant expenditure reduction should accompany such a measure.⁷²³ Douglas did probe Heller and Ackley extensively during their JEC testimony, but suggestions he was unhappy with their answers are wrong. Exemplifying this, the JEC’s report on the administration’s *Economic Report*, most of which was authored by Douglas,

⁷²¹ Ibid, 50.

⁷²² Ibid, 50.

⁷²³ As the CEA later concluded, “‘experience hath shown’ that logic is at best a feeble offset to partisan emotion.” CEA, ‘Joint Economic Committee Report on the 1963 Economic Report,’ 28 March 1963. Attached to Heller, Memorandum for the President, ‘Background for meeting with Senator Paul Douglas tomorrow,’ 28 March 1963. POF. Box 75a.

supported the administration's tax cut proposal.⁷²⁴ Douglas also later dismissed the differences between the Council's multiplier estimates and that of Roy Moor's.⁷²⁵ Therefore, Heller and Ackley had adequate justifications for deploying the model that they did and the differences between theirs and Moor's multiplier estimates did not dissatisfy Douglas to the extent that Prachowny has insisted.

Nevertheless, Heller did make one error in his JEC testimony, which provided critics of the tax cut with an important piece of ammunition. This came in the form of a remark that he made to the Democratic Representative Martha Griffiths of Michigan. After she explained that her constituents opposed the tax cut, Heller responded that it was "quite remarkable that the basic Puritan ethic of the American people should be such that they want to deny themselves tax reduction...because of their fears of deficits, and the additions to the national debt."⁷²⁶ Despite claiming that he "didn't say it in a downgrading way," Heller's attack on the Puritan ethic – values of hard work, frugality, and thrift – equated, in the eyes of some, to an attack on the character of the American people.⁷²⁷ This led John Byrnes of Wisconsin, the ranking Republican member of the Ways and Means Committee, to remark that he "would rather be a Puritan than a Heller."⁷²⁸ The CEA chairman's comment "gave critics of deficit financing an opportunity" to "attack" the tax cut.⁷²⁹ Thus, after the administration devoted so much time to formulating a proposal that was "tailored to meet the acid tests of Congressional legitimation processes," Heller's public

⁷²⁴ CEA, 'Joint Economic Committee Report on the 1963 Economic Report.' It did, however, argue that more of the stimulus should be concentrated in the first year of enactment.

⁷²⁵ n.n., 'Tax Cut Debate 'Accelerates,' *Christian Science Monitor*, 6 February 1963, 7. PQHN.

⁷²⁶ Cited in Rowen, *The Free Enterprisers*, 163-164.

⁷²⁷ Heller and Gordon, Interview with Hackman and Pechman, 67.

⁷²⁸ Heller, Interview in Hargrove and Morley, 209.

⁷²⁹ Solon Simmons, *The Eclipse of Equality: Arguing America on Meet the Press* (Stanford, CA, 2013), 101.

promotion of it got off to a bad start.⁷³⁰

III

The JEC's hearings on the tax cut concluded in early February, after which the Ways and Means Committee considered the measure. Here, the proposal was debated and redrafted until the autumn. Heller had been a long-time acquaintance of the chairman of that committee, Wilbur Mills, having worked with him closely during his wartime stint at the Treasury. However, the CEA chairman did not play a direct role in the negotiations that took place between the administration and the committee.⁷³¹ As a result, Heller spent the period during which the committee considered the tax cut seeking to muster support for it from outside of Congress. This, he hoped, would translate into positive committee action. Crucial to this was an effort to win popular support for the tax cut.

On February 10, Heller appeared on *Meet the Press*, a television show that "subject[ed] national decision makers at the peak of their influence to critical and probing questions [from the nation's top journalists] in front of the mass public."⁷³² Heller told Kennedy that this would provide him with "a good chance to answer some of the dirtiest and most damaging arguments against the tax cut."⁷³³ No sooner did the programme start, however, than Vermont Royster of the *Wall Street Journal* criticised Heller for his remark to the JEC two weeks earlier. "[Y]ou have complained that the American people...aren't smart enough to understand why big deficits financed by inflation aren't good economics...what is wrong with the puritan ethic," Royster

⁷³⁰ Phillip Michael Simpson, 'Macro-Economic Decision-Making: The 1964 and 1968 Revenue Acts,' PhD Thesis, University of Arizona (1971), 145. PQDT.

⁷³¹ They did occasionally meet for lunch from the summer of 1962 onwards, where Heller would stress the merits of the tax cut to Mills, but it appears likely that Mills had more contact with other administration officials in 1963. Heller, Interview with McComb, 21 December 1971, 22. LBJL-OHC.

⁷³² Simons, *The Eclipse of Equality*, 1.

⁷³³ Heller, Memorandum for the President, Untitled, 2 February 1963. POF. Box 75a.

asked Heller.⁷³⁴ In his defence, the CEA chairman argued that he cited the puritan ethic “in an admiring” way, yet the interview did little to help him rectify the gaffe he had made weeks earlier.⁷³⁵ Reflecting this, the “attack on the Puritan ethic did not end there,” not least because “the voice of middle America, Mary Craig, came after Heller” by citing his remark one month later.⁷³⁶

The interrogation Heller received on *Meet the Press* did not deter him from his public campaign. In addition to further appearances on that programme, he appeared on *Eye-Witness*, gave regular speeches across the country, and wrote for the *Saturday Evening Post*.⁷³⁷ Heller’s growing public profile induced *Look* magazine to label him “Mr Tax Cut.”⁷³⁸ As well as using the Council’s pulpit for public education to drum up support for the measure, the CEA chairman worked behind-the-scenes to achieve this too. One way that he did so was by suggesting that the Treasury investigate how the tax cut would improve the finances of America’s state-local governments.⁷³⁹ This proved useful for Kennedy, who was provided with an analysis of how the tax cut could transform the revenues of Illinois, where the president was due to speak in March.⁷⁴⁰ It was also useful for other administration officials. In a speech in Atlanta on March 8, the Assistant Secretary of the Treasury Joseph Barr said that an “extra \$71 million would be added to Georgia’s tax revenues” following enactment of the tax cut.⁷⁴¹ Two months later, Dillon officially released the findings

⁷³⁴ National Broadcasting Company, *Meet the Press: Interview with Dr. Walter Heller*, *Sunday February 10 1963*, 7:5 (Washington DC, 1963), 2-3. Copy in Heller Papers. Box 22.

⁷³⁵ *Ibid*, 3.

⁷³⁶ Simons, *The Eclipse of Equality*, 102.

⁷³⁷ For information on Heller’s various appearances and writings in the media, see Heller, Memorandum for the President, ‘TV Appearances,’ 4 March 1963. POF. Box 75a; and Canterbury, *Economics on a New Frontier*, 127.

⁷³⁸ T. George Harris, ‘Mr Tax Cut,’ *Look*, 27:12, 18 June 1963, 83. Heller Papers. Box 10. UoM.

⁷³⁹ Heller, Memorandum for the President, ‘Illinois Tax Data for Chicago Speech,’ 15 March 1963. POF. Box 75a.

⁷⁴⁰ *Ibid*; ‘Effect of the President’s Tax Program on State and Local Tax Revenues in Illinois,’ 12 March 1963. Attached to *Ibid*.

⁷⁴¹ n.n., ‘U.S. Tax Cut Called a Benefit for State,’ *The Atlanta Constitution*, 8 March 1963, 48. PQHN.

of his department's investigation. This revealed that state and local governments would "get an annual \$2.9 billion revenue bonanza" if Congress enacted Kennedy's proposal, something that Paul Douglas referred to as "heartening."⁷⁴²

In addition to highlighting the potential impact of the tax cut, Heller worked behind-the-scenes to ensure that a favourable transnational comparison received coverage in the press. In 1963, the Conservative government in Britain, responding to that nation's slack economy, proposed a reduction of tax liabilities (notably on personal income) equivalent to \$11.7 billion in a single year.⁷⁴³ To add legitimacy to the president's proposal, Heller sought to highlight how the British were using bold, Keynesian methods. On April 27, the CEA chairman told Kennedy that he had "carefully placed" articles that compared the two tax cuts in the *New York Times*, *Newsweek*, and the Associated Press.⁷⁴⁴ The AP stated, "President Kennedy's fiscal advisers, who had felt pretty daring up to now, are studying the new British budget with goggle eyes."⁷⁴⁵ This was because the Conservative government had proposed "a bigger deficit" in GNP terms than Kennedy did for FY 1964.⁷⁴⁶ "The Kennedy fiscal advisers," it went on to note, were "comforted, and even flattered, that the British people took some lessons from the United States plan for dealing with a slack economy."⁷⁴⁷ What amazed them the most was that "the British public and parliament aren't screaming bloody murder about 'fiscal irresponsibility.'"⁷⁴⁸

As he worked both publicly and privately to muster popular support for the tax cut, Heller had to defend the measure against continuous criticism. These came

⁷⁴² n.n., 'Dillon Predicts State Bonanza if U.S. Tax Cut,' *Los Angeles Times*, 8 May 1963, C9. PQHN.

⁷⁴³ Heller, Memorandum for the President, 'U.K. Budget,' 8 April 1963. Heller Papers. Box 16.

⁷⁴⁴ Heller, Memorandum for the President, 'The U.K. Budget Story,' 27 April 1963. Heller Papers. Box 6.

⁷⁴⁵ Sterling Green, 'Tory Budget Astounds U. S.,' *The Washington Star*, n.d. Attached to Ibid.

⁷⁴⁶ Green, 'Tory Budget Astounds U. S.'

⁷⁴⁷ Ibid.

⁷⁴⁸ Ibid.

from both the left and the right of the political spectrum. Soon after Kennedy announced the tax cut, Leon Keyserling emerged as one of its most vocal opponents. Believing strongly that the “the lower and middle income brackets need more social service, more housing, more medical care, and more aid to education,” the former CEA chairman suggested that increased spending, in addition to tax reduction, offered the best means to drive the economy forward.⁷⁴⁹ Keyserling’s discontent with JFK’s economic policies reached its peak in a speech that personally attacked Heller and Ackley. Not only did he describe their policies as “incompetent, regressive, not socially-minded, and not very courageous,” he implied that his personal cook understood economics better than they did.⁷⁵⁰

Because Keyserling served as an important voice for the AFL-CIO, the ADA, and other left-liberal interest groups, it was essential for Heller to take the sting out of his criticisms. The CEA chairman decided to “cozy up” to his fellow liberal economist in order “to neutralize him.”⁷⁵¹ This he did by arranging a series of meetings between both Keyserling and Kennedy, which provided the former with “a bit of an audience” to “quiet him down.”⁷⁵² Heller and Ackley also told Keyserling that, whilst the Council was sympathetic to his views, it would be impossible to push his expenditure plans through Congress.⁷⁵³ As with Galbraith, Heller and Ackley showed Keyserling that the best way to modernise the public sector would be to cut taxes, as this would eventually provide the revenues needed to build and improve the nation’s schools, hospitals, and roads. Though Heller later said that this amiable

⁷⁴⁹ n.n., ‘Tax Cut Alone Won’t Help, Former Truman Aide Says,’ *Boston Globe*, 11 March 1963, 4. PQHN.

⁷⁵⁰ Ackley, Memorandum for the Files, ‘What I said in St. Louis,’ 27 April 1963. Attached to Heller to Kennedy, 27 April 1963. POF. Box 75a.

⁷⁵¹ Heller and Gordon, Interview with Hackman and Pechman, 72.

⁷⁵² Ibid, 72.

⁷⁵³ Ackley, Memorandum for the Files, ‘What I said in St. Louis.’

approach “never did any good,” certain evidence suggests otherwise.⁷⁵⁴ In May, Keyserling indicated that he would act more cooperatively with the administration.⁷⁵⁵ Reflecting this, Heller drafted a presidential letter to Keyserling on July 24 which explained that the “thrust of your [latest] criticism – so long as it is couched in the generally temperate and responsible terms you have adopted...is good.”⁷⁵⁶

Though Heller helped moderate the criticisms of Keyserling, his efforts to defend the tax bill from its conservative critics proved more challenging. One big issue during this period spurred on those who considered the tax cut fiscally irresponsible: the fact that the economy picked up. This amounted to a blow for Heller because, in the wake of the JEC hearings, Kennedy decided that selling the tax cut on technical grounds alone had not been “a very persuasive argument with Congress.”⁷⁵⁷ As a result, both Heller and Kennedy stressed that there would be a recession if their bill was not passed.⁷⁵⁸ On March 21, however, they dropped this strategy, for the CEA chairman had realised that the economy was performing better than expected. The Council’s GNP forecast for the second quarter of 1963 indicated that output was \$10 billion higher than the first quarter.⁷⁵⁹ Heller expected this to have “two effects on the tax cut discussion.”⁷⁶⁰ In the first case, opponents of the measure would likely adopt the “Tom Curtis Approach,” which Heller named after a conservative Republican congressman from Missouri. This involved saying that a tax cut, or at least a large one, was undesirable because the economy was doing well.⁷⁶¹

⁷⁵⁴ Heller and Gordon, Interview with Hackman and Pechman, 72.

⁷⁵⁵ Keyserling, Memorandum for the President, ‘Questions Raised about My Recent Talks Discussing Your Administration And Its Economic Policies,’ 25 May 1963. WHSFWH. Roll 17.

⁷⁵⁶ Kennedy, ‘Draft Letter for Leon Keyserling’ 24 July 1963. Attached to Heller, Memorandum for the President, Untitled, 24 July 1963. POF. Box 76.

⁷⁵⁷ Heller, Interview in Hargrove and Morley, 210.

⁷⁵⁸ See n.n., ‘Heller Fears Slums Unless Tax is Cut,’ *New York Times*, 9 March 1963, 2. PQHN.

⁷⁵⁹ Heller, Memorandum for the President, ‘The Improved Economic Outlook,’ 21 March 1963. Heller Papers. Box 5.

⁷⁶⁰ Ibid.

⁷⁶¹ Ibid.

Alternatively, proponents of the measure could adopt the “Hale Boggs Approach,” named for the-then Democratic House Majority Whip from Louisiana. This involved stressing that the more prosperous economy would decrease the size of the FY 1964 deficit, thereby making a larger tax cut a possibility.⁷⁶²

The latter was the tactic that Heller urged the administration to adopt. The importance of doing so soon intensified because, partly in response to the better economic picture, the Ways and Means Committee postponed the tax cut’s enactment until October. Worried that this delay meant that the economy would require a more potent stimulus, Heller informed Kennedy that they should use “the Boggs point that a stronger economy means a smaller deficit.”⁷⁶³ In comparison, Dillon opposed speeding up the tax cut in this way. Siding more with proponents of the Tom Curtis Approach, the Treasury Secretary argued that the “present state of the economy gives no excuse for such a suggestion.”⁷⁶⁴ In the end, the administration made no notable attempt to speed up the tax cut’s calendar. Nevertheless, Dillon and Heller did work together to refute the suggestion that the improved economic conditions negated the need for the measure altogether. The Treasury’s report into the tax cut’s probable impact upon state-local finances, for example, “came at a time when doubt” was “being expressed about the need for a federal tax cut.”⁷⁶⁵ Similarly, both worked to mobilise businesspersons to lobby for the measure. In a speech to the Business Council on May 11, Heller “made an eloquent plea for the proposed tax cut.”⁷⁶⁶ The Treasury, by comparison, established a business lobby group, with Henry Ford II as

⁷⁶² Ibid.

⁷⁶³ Heller, Memorandum for the President, ‘Sustaining Recovery through 1964: Preliminary Report,’ 5 April 1963. Heller Papers. Box 6.

⁷⁶⁴ Dillon, Memorandum for the President, ‘Comments on Attached Memorandum from Mr. Heller,’ 5 April 1963. Heller Papers. Box 6.

⁷⁶⁵ n.n., ‘Dillon Predicts State Bonanza if US Tax Cut.’

⁷⁶⁶ See n.n., ‘Business Leaders Mobilize,’ *The Miami News*, 11 May 1963, 2A. Heller Papers. Box 49.

its chair, to support the tax cut in 1963.⁷⁶⁷

As well as mobilising support from business leaders, Heller arranged for “three of the country’s top economists” to circulate a petition in favour of the tax cut.⁷⁶⁸ Not only was this signed by 412 economists across 43 colleges and universities, it refuted the argument of those who supported the Tom Curtis Approach by stating that “‘natural forces’ alone will not eliminate excess unemployment this year or even next.”⁷⁶⁹ Clearly pleased with the response, Heller informed Kennedy that he would “get the most effective distribution” of it.⁷⁷⁰ Nevertheless, even though the CEA chairman succeeded at drumming up elitist support for the tax cut, the legislative process went on at its own pace. In addition to the improved economic picture, this was due to the intense debate generated by the administration’s reform proposals. By June, the Ways and Means committee had virtually stripped the reforms from the tax package altogether, leading Heller to vent his frustration at the president by saying that he had always “opposed cluttering up the 1963 tax cut by inclusion of tax reforms.”⁷⁷¹ What also worried the CEA chairman was that, despite the improved economic outlook, he saw “little assurance that private consumption and investment will keep rising through 1964 without a potent stimulus.”⁷⁷² To compound his problems, the Federal Reserve also showed signs of adopting policies that would hasten this development.

IV

Throughout 1961-62, the Fed had implemented Operation Twist. However,

⁷⁶⁷ Simpson, ‘Macro-Economic Decision-Making,’ 152-153; Heller and Gordon, Interview with Hackman and Pechman, 70-71.

⁷⁶⁸ Heller, Memorandum for the President, Untitled, 25 May 1963. POF. Box 75a.

⁷⁶⁹ Lester Chandler, James Duesenberry, and Robert A. Gordon, ‘The Tax Program of the Kennedy administration,’ Attached to Ibid.

⁷⁷⁰ Heller, Memorandum for the President, Untitled, 16 July 1963. POF. Box 76.

⁷⁷¹ Heller, Memorandum for the President, ‘Personal Note to the President,’ 7 June 1963. POF. Box 76.

⁷⁷² Heller, Memorandum for the President, ‘Assuring Economic Expansion through 1964,’ 13 June 1963. Heller Papers. Box 6.

the balance-of-payments deficit took a turn for the worse early in 1963, largely “as a result of an increase in capital flowing overseas.”⁷⁷³ At the end of May, it stood at \$1.5 billion, up from \$670 million in the first quarter of 1963.⁷⁷⁴ In early April, Heller expressed concern at a “heightened interest in tighter money” on behalf of both the Treasury and the Fed.⁷⁷⁵ This displeased him because such a course of action would slow down the economy before the enactment of the tax cut. Sensing a problem with the payments deficit back in December, the Fed had raised short-term interest rates then. According to Heller, there was no need to do so again. This was especially because the administration had put pressure upon the Canadian government to reduce its interest rates to allow capital to flow back to America.⁷⁷⁶ To reinforce his argument, Heller passed Kennedy the findings of the Brookings Institution’s 1963 preliminary report on the long-term outlook for the payments problem, which warned that raising interest rates would harm the domestic economy.⁷⁷⁷ The CEA chairman also stressed that it was preferable to wait until after the tax cut’s enactment before tightening credit. This was because a slight rise in interest rates would naturally occur if the administration adopted “a truly expansionary fiscal policy.”⁷⁷⁸

Due to Heller’s arguments in early April, the Treasury and the Fed both agreed that it was not desirable to increase short-term interest rates.⁷⁷⁹ No sooner was this consensus reached, than at a meeting on April 18 JFK expressed alarm at being told that the nation’s gold reserves might fall to \$13 billion.⁷⁸⁰ This prompted Martin

⁷⁷³ Davis, ‘Politics of Prosperity,’ 195.

⁷⁷⁴ CEA, ‘Recent Balance of Payments Developments,’ 10 June 1963. Heller Papers. Box 16.

⁷⁷⁵ Heller, Memorandum for the President, ‘Monetary Policy Today – The Uneasy Truce between Domestic and Balance-of-Payments Considerations,’ 6 April 1963. Heller Papers. Box 6.

⁷⁷⁶ Ibid.

⁷⁷⁷ Heller, Memorandum for the President, ‘Summary of the Brookings Report on the US Balance-of-Payments Outlook,’ 5 April 1963. Heller Papers. Box 16.

⁷⁷⁸ Heller, Memorandum for the President, ‘Monetary Policy Today.’

⁷⁷⁹ Davis, ‘Politics of Prosperity,’ 397.

⁷⁸⁰ Sorensen, Memorandum for the Record, ‘Meeting with the President, 18 April 1963, 10:00 A.M., to 12 Noon – Balance of Payments,’ 24 April 1963. Sorensen Papers. Box 40.

to remark that the US could put “deflationary pressure on the economy through monetary policies.”⁷⁸¹ Heller responded by arguing that the “basic goal was not merely to save gold, but to do it in a way that kept domestic expansion going.”⁷⁸² Despite this, the Fed tightened monetary policy in early May, causing the rate on three-month Treasury bills to rise to 3 percent (from 2.9 percent).⁷⁸³ This decision concerned Heller, who feared “that higher short-term rates will now spill over into the long-term market.”⁷⁸⁴ This would lead to less capital availability for mortgages, plant and equipment, and state and local facilities, all of which were integral to the economy’s productive capacity.⁷⁸⁵ Monetary policy needed, he implored, “to be more sensitive to its probable impact on long-term rates.”⁷⁸⁶

The Fed’s decision in May caused a further complication, one that Dillon raised with Kennedy in June. “Any further increase in short-term rates,” the Treasury Secretary warned, “will require a change in the rediscount rate,” the level of interest at which commercial banks drew short-term capital from the central banking system.⁷⁸⁷ This was because certain short-term rates could not “go substantially above the rediscount rate,” which had stayed at 3 percent since November 1960.⁷⁸⁸ Dillon also knew that increasing the discount rate would ease the payments deficit by putting a brake upon the domestic economy. This is another likely reason why such a policy appealed to him. Unsurprisingly, Dillon’s desire to raise the discount rate alarmed Heller. He informed Kennedy that a ½ percent increase favoured by both Martin and the Treasury Secretary would “have the same negative impact on GNP as knocking

⁷⁸¹ Ibid.

⁷⁸² Ibid.

⁷⁸³ Heller, Memorandum for the President, ‘The Fed Tightens the Screw,’ 31 May 1963. Heller Papers. Box 6.

⁷⁸⁴ Ibid.

⁷⁸⁵ Ibid.

⁷⁸⁶ Ibid.

⁷⁸⁷ Dillon, Memorandum for the President, ‘Monetary Policy, the Balance of Payments and Domestic Growth,’ 17 June 1963. POF. Box 90.

\$1½ to \$3 billion off your proposed tax cut.”⁷⁸⁹ True, there would be ways “to ease somewhat the impact” of a discount rate hike. Nevertheless, the CEA chairman stressed that one “inescapable fact remains: the supply of [long-term] funds would be available only at a *higher* price, and at that higher price less of it would be used for expansion of the economy via housing, plant and equipment, municipal construction, and so forth.”⁷⁹⁰ Rather than tighten money, Heller argued, the administration “should simply stick to the path it was already following.”⁷⁹¹

Worried that Kennedy might support a discount rate hike, the CEA chairman told the president that the administration should deploy “a ‘twist’ policy with a vengeance.”⁷⁹² This involved persuading the Fed to buy vigorously in the long-term market to maintain low long-term rates, which would ensure that ample funds would be available to maintain high levels of investment.⁷⁹³ Despite formulating this plan, the CEA chairman preferred there to be no rise in the discount rate altogether. So, he wrote to Kennedy on July 7 to dissuade him from approving this course of action. To prevent an immediate response from the Treasury Secretary, he deliberately ensured that a copy did not reach Dillon.⁷⁹⁴ Calling himself “the professional guardian of the Kennedy expansion,” the CEA chairman stressed that a rise in the discount rate was undesirable.⁷⁹⁵ He also explained that if the discount rate was increased, he had serious misgivings about whether the Fed and the Treasury would comply with any request to pursue a more vigorous Twist policy, especially because, in early 1961,

⁷⁸⁸ Ibid.

⁷⁸⁹ Heller, Memorandum for the President, ‘Assuring Economic Expansion through 1964.’

⁷⁹⁰ Heller, Memorandum for the President, ‘Various Items,’ 20 June 1963. Heller Papers. Box 6. Emphasis in the original.

⁷⁹¹ Davis, ‘Politics of Prosperity,’ 401.

⁷⁹² Heller, Memorandum for the President, ‘Proposed Discount Rate Boost,’ 7 July 1963. Heller Papers. Box 6.

⁷⁹³ Ibid.

⁷⁹⁴ Indeed, Heller attached a cover note to the memo, saying “I am not sending a carbon copy to Doug Dillon!” Heller to Kennedy, 8 July 1963. POF. Box 76.

Heller struggled to persuade both to adopt Operation Twist in the first place.⁷⁹⁶

To bolster his argument, Heller arranged for James Tobin, a specialist on monetary policy, to offer his thoughts on a discount rate hike. Agreeing with Heller that such a policy was unwise, Tobin remarked that it would be difficult to raise short-term rates further and not affect the long-term market, especially as he doubted whether the Fed would pursue the 'Super-Twist' to the extent necessary.⁷⁹⁷ Swayed by Heller's counterattack, Kennedy asked his CEA chairman how he would tackle the payments crisis. This prompted Heller to deny that the payments deficit posed any long-term problem, especially because inflationary forces on the European continent indicated that US exports were likely to rise.⁷⁹⁸ The CEA chairman also reiterated his case that an expanding economy would take care of the nation's trade imbalance, for if "profits rise and investment opportunities expand at home, the attention of investors will shift to the domestic scene."⁷⁹⁹

No sooner did the president's attention sway back in Heller's favour than Dillon re-entered the fray. On July 10, the Treasury Secretary drew Kennedy's attention to "recent market action."⁸⁰⁰ He did this to undermine Heller's argument that a rise in the discount rate would have an undesirable impact upon long-term investments. Because rumours had been circulating about a rise in the discount rate, the Treasury Secretary noted that a "1/4 of 1 percent" increase on the rate of 90-day Government bills had taken place.⁸⁰¹ The "minor influence" of this rate change "on the long-term market," Dillon explained, "was dramatically illustrated by the [very

⁷⁹⁵ Heller, Memorandum for the President, 'Proposed Discount Rate Boost,' 7 July 1963. Heller Papers. Box 6. Attached to Ibid.

⁷⁹⁶ Heller, Memorandum for the President, 'Proposed Discount Rate Boost.'

⁷⁹⁷ Tobin to Kennedy, 1 July 1963. POF. Box 76.

⁷⁹⁸ Heller, Memorandum for the President, 'A Program for the Balance of Payments,' 8 July 1963. Heller Papers. Box 16.

⁷⁹⁹ Ibid.

⁸⁰⁰ Dillon, Memorandum for the President, 'Recent Market Changes in Interest Rates,' 10 July 1963. POF. Box 90.

recent and] successful competitive sale” of “a \$50 million Illinois Bell Telephone Company issue of 40-year bonds.”⁸⁰² This had been “brought to the market at a rate of 4.36 percent and was a prompt sell-out.”⁸⁰³

Undecided about changing the discount rate, JFK called a meeting of the Quadriad on July 15 to solve the matter. Prior to this, Heller emphasised the views of certain European officials to deter JFK from endorsing Dillon’s approach, a technique that had worked well for him in 1962.⁸⁰⁴ However, making use of this transnational comparison did not help Heller this time around, as on July 15 Kennedy sided with Dillon. At that meeting, the Treasury Secretary opened by saying that the payments deficit was developing to the point “where it bordered on a ‘run’ on the dollar.”⁸⁰⁵ Indeed, figures showed that the trade imbalance amounted to \$5 billion (at an annual rate) for the second quarter of 1963.⁸⁰⁶ “An increase in the discount rate and a somewhat smaller rise in the Treasury bill rate,” Dillon concluded, “could save \$500 million in short-term capital outflows.”⁸⁰⁷ This, together with other actions that the president would soon announce, would cut the payments deficit by \$2 billion.⁸⁰⁸ Any rise in the cost of short-term capital would not have an undesirable effect upon the long-term market, Dillon also maintained, not least because of the evidence that he presented to Kennedy five days earlier.⁸⁰⁹

Though Heller questioned the majority of Dillon’s points, Kennedy heeded the advice of his Treasury Secretary on the need for a 0.5 percent rise in the discount

⁸⁰¹ Ibid.

⁸⁰² Ibid.

⁸⁰³ Ibid.

⁸⁰⁴ Heller, Memorandum for the President, ‘Report from Paris, especially on US monetary policies,’ 13 July 1963. Heller Papers. Box 6.

⁸⁰⁵ n.n., ‘Draft Notes on Quadriad Meeting with the President,’ 15 July 1963. Attached to Heller, Memorandum for the President, Untitled, 18 July 1963. Heller Papers. Box 6.

⁸⁰⁶ Ibid.

⁸⁰⁷ Ibid.

⁸⁰⁸ Ibid.

⁸⁰⁹ Ibid.

rate. Still, it is worth noting that Heller's presence at the meeting did ensure that "there was discussion of the possible restrictive effects [of a discount rate hike] upon the U.S. domestic economy."⁸¹⁰ This led to an agreement that the Treasury and the Fed would deploy the 'Super-Twist' policy championed by the CEA chairman.⁸¹¹ Moreover, following the Fed's announcement of the discount rate hike on July 16, Kennedy followed it up two days later with a message that laid out a new set of policies to curb the payments problem. This included a statement that committed his administration to exploring "long-range reform" of the Bretton Woods system, something that the Council had long-favoured.⁸¹²

It is also worth noting that, as the payments situation deteriorated throughout the first half of 1963, talk took place within the administration about the possibility of devaluing the dollar. As early as February 24, for example, Heller forwarded JFK excerpts of a talk by Paul Samuelson, where the MIT economist explained that the US should be prepared to "alter the parity of the dollar" if it were "truly overvalued."⁸¹³ This was also something that Tobin agreed with.⁸¹⁴ As Amy Davis has noted, talk of devaluation in 1963 helped enable Kennedy "to change his mind about international monetary reform," not least because it provided "a fundamentally different context within which to view the issue."⁸¹⁵ This demonstrated that, since 1961, a large shift in the president's views had taken place.⁸¹⁶ When he came to office, Kennedy had feared upsetting the banking and finance community, so he

⁸¹⁰ n.n., 'Draft Summary of Conclusions: Meeting with the President July 15,' 15 July 1963. Heller Papers. Box 6.

⁸¹¹ Ibid.

⁸¹² Kennedy, 'Special Message to the Congress on Balance of Payments,' 18 July 1963. APP; Davis, 'Politics of Prosperity,' 408.

⁸¹³ Heller, Memorandum for the President, 'Paris, Gold, and Samuelson Revisited,' 24 February 1963. Heller Papers. Box 5.

⁸¹⁴ Tobin, Memorandum for the President, 'The Balance of Payments,' 11 October 1963. Attached to Heller to Kennedy, 16 October 1963. POF. Box 76.

⁸¹⁵ Davis, 'Politics of Prosperity,' 417.

⁸¹⁶ Ibid, 427-428.

refused to endorse a strong fiscal stimulus, ruled out any possibility of devaluation, and rejected the Council's various calls for an overhaul of the Bretton Woods system. By the summer of 1963, the president had opened himself up to the latter.⁸¹⁷ Heller thus did not win the battle over the discount rate hike, but he was successful at convincing Kennedy to conduct international monetary policy with less fear of upsetting bankers and financiers. Furthermore, the CEA chairman ensured that the Fed engaged in the 'Super-Twist,' which meant that as monetary policy tightened in the summer of 1963, its impact upon the tax cut would be minimised.

V

After ensuring that the rise in the discount rate would not seriously undermine the tax cut, Heller's focus switched back to securing the enactment of that measure. This had languished in the Ways and Means Committee during both July and August. Indeed, it took from July to September 13 for its members to conclude voting on the tax cut's various provisions.⁸¹⁸ Concerned that the measure was stalling, Heller indirectly attempted to increase the pressure upon its members. In an appearance before the House Banking Committee on July 26, he raised concern about a softening economic picture in 1964, saying that "house construction, automobile sales and business spending for new plant and equipment might all start declining next year, unless a tax reduction was put into effect."⁸¹⁹ The increase in GNP during the spring of 1963, he also said, was "not a boom by any standards," being "scarcely enough "to keep up with an expanding labor force and growing productivity."⁸²⁰

This effort failed to speed up the Ways and Means Committee's consideration

⁸¹⁷ This contrasts with Lee, whose study does not recognise how this signified a major shift in policy. "The Strength of the Currency," 219-220.

⁸¹⁸ Davis, 'Politics of Prosperity,' 439.

⁸¹⁹ n.n., 'Business Outlook Seen 'Uncertain': Heller Testifies on Economy before House Group,' *New York Times*, 26 July 1963, 31. PQHN.

⁸²⁰ Cited in *Ibid*, 31.

of the tax cut. In fact, when that body did eventually approve it, the decision to do so was arguably attributable to the efforts of officials other than Heller. Dillon had made sixty-three trips to Capitol Hill from February to August, for example, and his negotiations with the committee's members played a crucial role in getting the measure out of that body and onto the House floor.⁸²¹ The orthodox language that Heller and Kennedy had used to sell the tax cut did convince certain Democrats on the committee that they could support the measure (and not appear fiscally irresponsible), but its conservative members demanded that expenditures be trimmed.⁸²² In fact, Mills "promised the administration that he could pass the bill within a few months, but only if the president stressed his commitment to expenditure control."⁸²³ This was a particular blow for Heller. In response to the pessimistic forecast for 1964, he had wanted Congress to increase spending while it considered the tax cut.⁸²⁴ Instead, JFK wrote to Mills in August to say that he would keep a tight rein on expenditures if the tax cut was passed, something that proved important to gaining the Ways and Means Committee chairman's full support.⁸²⁵ Thus, Dillon and Kennedy played a more important and direct role than Heller in paving the way for the committee to endorse the tax cut.

When the bill was approved on September 13 (by a vote of 17 to 8), the committee's version did reflect one idea previously championed by the CEA chairman. This was the notion that the improved economic outlook in early 1963 made a larger tax cut a possibility, as the committee recommended an overall

⁸²¹ n.n., 'Public Support Sought for Tax Cut Program,' *Los Angeles Times*, 18 August 1963, F16. PQHN.

⁸²² Simpson, 'Macro-Economic Decision-Making,' 176-177.

⁸²³ Zelizer, *Taxing America*, 201.

⁸²⁴ Heller, Memorandum for the President, 'Fiscal Strategy – Or 1964 Comes First,' 7 August 1963. Heller Papers. Box 6.

⁸²⁵ Simpson, 'Macro-Economic Decision-Making,' 183; Bernstein, *Promises Kept*, 159.

reduction of \$11.1 billion.⁸²⁶ Moreover, certain observers have argued that, by the fall of 1963, the tax cut enjoyed a large amount of popular support, which they attribute to Heller's efforts. Irving Bernstein has said that the "tax bill had become a high-speed locomotive that could not be stopped. The American people strongly favored its passage. The campaign Heller and Kennedy had waged to educate the American public in elementary Keynesian economics had succeeded."⁸²⁷ Heller, too, made this assertion. In 1963, he sent a wealth of public opinion data to Kennedy, which apparently showed that his efforts to generate popular support for the tax cut were paying off. In June, the CEA chairman forwarded JFK a study by the University of Michigan, which claimed that attitudes "toward a tax cut have become more favourable during the last few months."⁸²⁸ On Thursday, October 17, he also sent Kennedy the editorial page of the *Milwaukee Journal*, which argued that the "case for federal tax reduction seldom has been put as convincingly as it was in Milwaukee Tuesday" by Heller.⁸²⁹

Though popular support for the tax cut undoubtedly increased in 1963, the extent to which Heller generated a tidal wave of opinion favourable to the measure is open to debate. In a *New York Times* article on September 8, one journalist claimed, "Public opinion, stimulated for nearly a year by all the black arts of persuasion, has yet to declare itself ringingly on the question of Mr. Kennedy's tax reduction program."⁸³⁰ Though a poll conducted by the *Washington Post* showed that 62 percent of Americans favoured Kennedy's tax cut, the *Times* reported that there was

⁸²⁶ Davis, 'Politics of Prosperity,' 440. Footnote 24.

⁸²⁷ Bernstein, *Guns or Butter*, 35.

⁸²⁸ 'Excerpt From *The Outlook for Consumer Demand*, June 1963, Institute for Social Research, The University of Michigan.' Attached to Heller to Kennedy, 25 June 1963. Heller Papers. Box 6.

⁸²⁹ 'The Case for a Tax Cut,' *Milwaukee Journal*, 16 October 1963, Editorial Page. Attached to Heller, Memorandum for the President, Untitled, 17 October 1963. POF. Box 76.

⁸³⁰ Tom Wicker, 'White House Presses Tax Bill: A Major Effort is Being Made to Garner Strong Public Support,' *New York Times*, 8 September 1963, E8. PQHN.

serious concern within the administration about whether “the public really wants tax reduction, or understands the need for it.”⁸³¹

Shortly before the tax cut approached House enactment, Kennedy deemed it essential to give a major address to boost the appeal of the measure. The president asked Heller to provide him with “human” examples that he could cite in this speech, another point that indicates just how unsure the administration was about the level of popular support that the tax cut enjoyed.⁸³² Delivered by the president on September 18, this emphasised the benefits of the tax cut for all Americans. “Under this bill,” Kennedy declared, “every wage earner in the country will take home more money every week beginning January 1st. Every businessman will pay a lower tax rate. Low income families and small businessmen will get a special tax relief, and the unemployed worker who gets a new job will find his income going up many times.”⁸³³

Hailed by one congressional representative as “the way public education” should “be done,” the fact that the president gave such an address helps to demonstrate that popular support for the tax cut was not as high as some have suggested.⁸³⁴ Even though more Americans did favour the tax cut (a feat that was still remarkable given Eisenhower’s success at convincing the nation that deficits were inflationary), most Republicans in Congress proved resistant to it nonetheless. Indeed, shortly before the House voted on the measure, the Republicans made a move to recommit it. They did so in the hope that they could make its enactment dependant “on the President submitting a budget in January, 1964, which showed fiscal 1964

⁸³¹ Louis Harris, ‘Administration Tax-Cut Measure Continues to Hold Public’s Favor,’ *Washington Post, Times Herald*, 2 December 1963, A2. PQHN; Ibid, E8.

⁸³² Heller and Gordon, Interview with Hackman and Pechman, 53.

⁸³³ Kennedy, ‘Radio and Television Address to the Nation on the Test Ban Treaty and the Tax Reduction Bill,’ 18 September 1963. APP.

⁸³⁴ Heller and Gordon, Interview with Hackman and Pechman, 76.

expenditures below \$97 billion and fiscal 1965 below \$98 billion.”⁸³⁵ Defeated by a vote of 226 to 199, this attempt to modify the tax cut demonstrated that Heller and Kennedy’s efforts to drum up popular support for it had not washed away the notion of fiscal responsibility within Congress.

VI

The House passed the tax bill on September 26 by 271 votes to 155, paving the way for the next stage in the legislative process. This involved gaining the approval of the Senate. In this regard, it was essential to push the tax cut through the Finance Committee, chaired by the Democrat Harry Byrd of Virginia. Byrd “had an unblemished record as a fiscal conservative and regarded the Keynesian tax cut as a dangerous disease.”⁸³⁶ Before turning to Heller’s dealings with Byrd, it is important to note that during the fall of 1963 the CEA chairman fought another battle as well. This involved refuting the argument that the economy’s problems stemmed from structural rather than cyclical factors, something that Heller thought that he had put to rest much earlier in the year.

In June, the CEA chairman informed Kennedy that he had received “an interesting confirmation” of the Council’s argument that the nation’s unemployment problem was predominantly cyclical.⁸³⁷ This came after he enjoyed a positive reception to his remarks in an April debate on the subject at the University of California.⁸³⁸ By October, however, concern reignited about structural unemployment. This followed several remarks made by the Michigan State University economist Charles Killingsworth, who told a congressional committee in September that the economy’s problems were attributable to an insufficiently trained

⁸³⁵ Stein, *The Fiscal Revolution in America*, 448.

⁸³⁶ Bernstein, *Guns or Butter*, 27.

⁸³⁷ Heller, Memorandum for the President, ‘Structural Unemployment Once Again,’ 8 June 1963. POF. Box 76.

and skilled workforce. These comments were “widely quoted by opponents of the Administration’s [tax] bill.”⁸³⁹ In October, Swedish sociologist Gunnar Myrdal added fuel to these flames by publishing a book that Heller criticised for placing too much emphasis on “the structural explanation of our persisting unemployment problem.”⁸⁴⁰

In addition to securing the Finance Committee’s approval of the tax cut, Heller focused in October on refuting the case of the structuralists. In an early October speech before the American Council on Education, the CEA chairman responded to Killingsworth by citing “figures to show that unemployment among the less educated had not risen as much in recent years as unemployment among college graduates.”⁸⁴¹ He provided a further rebuttal to the structuralists in testimony before the Senate Subcommittee on Labor and Public Welfare three weeks later.⁸⁴² Though Killingsworth countered Heller’s various rebuttals, the CEA chairman arguably won the debate. This was evidenced by the fact that, in early November, the *Washington Post* reported that those “who have insisted that the cause of unemployment is primarily structural have adduced very little in the way of solid evidence to buttress their thesis. And the little that has been offered was subjected by Dr. Heller to searching analysis which indicates that it is sorely defective.”⁸⁴³

With the debate about structural unemployment put to rest, Heller focused on pushing the tax cut through the Finance Committee, which started debating the measure on October 15. Shortly after these deliberations began, Byrd realised that the

⁸³⁸ Ibid.

⁸³⁹ Eileen Shanahan, ‘Tax Cut Defended as Jobs Stimulus: Heller Rebutts View it can’t end Problem of Unskilled,’ *New York Times*, 5 October 1963, 44. PQHN.

⁸⁴⁰ Heller, Memorandum for the President, ‘Uncle Gunnar’s New Book, *Challenge to Affluence* (for Oct. 15 release),’ 11 October 1963. POF. Box 76.

⁸⁴¹ Shanahan, ‘Tax Cut Defended as Jobs Stimulus,’ 44.

⁸⁴² ‘Statement of Walter W. Heller, Chairman Accompanied by Gardner Ackley and John P. Lewis, Members of the Council of Economic Advisers, before the Subcommittee on Employment and Manpower of the Senate Committee on Labor and Public Welfare,’ 28 October 1963. POF. Box 76.

⁸⁴³ n.n., ‘Explaining Unemployment,’ *Washington Post, Times Herald*, 2 November 1963, A10. PQHN.

tax bill would pass the Senate.⁸⁴⁴ However, he sought to ensure a gesture of fiscal restraint accompanied the proposal. This meant that he was prepared to wait for the administration to submit its budgetary proposals for FY 1965 before releasing the tax cut.⁸⁴⁵ This would enable him to “put pressure on the administration to hold down the 1965 budget [to under \$100 billion].”⁸⁴⁶ Worried that Byrd’s actions would bog down the tax bill in the Finance Committee, JFK undertook a renewed drive to secure the measure’s passage. It is likely that he instructed Heller and Dillon to highlight the potential of a recession. This made Heller uncomfortable because he preferred to sell the tax cut on technical grounds. He also felt it unlikely that many people would buy this argument (especially given the upturn in the spring).⁸⁴⁷ The CEA chairman further disagreed with the president over whether he should appear before the Finance Committee to personally urge the tax cut’s passage. Presumably because he did not want to further aggravate Byrd with Keynesian ideas, or make a gaffe similar to the one that he made before the JEC, Heller did not want to appear before that body. However, the president ordered him to do so because “the Administration ought to take every chance it had to put its case across.”⁸⁴⁸

Accordingly, Heller appeared before the Finance Committee on November 12. Flanked by Ackley and the Council’s newest member, John P. Lewis of the University of Michigan, the CEA chairman once again laid out the administration’s case for the tax cut. In doing so, he stressed that there would be a recession if that measure was not passed and downplayed the extent to which it would be

⁸⁴⁴ Bernstein, *Guns or Butter*, 27.

⁸⁴⁵ Stein, *The Fiscal Revolution in America*, 451.

⁸⁴⁶ Ibid, 451.

⁸⁴⁷ Heller and Gordon, Interview with Hackman and Pechman, 72, 55.

⁸⁴⁸ Heller, ‘Confidential Notes on Breakfast Briefing with the President, Wednesday, Oct., 9, 1963 (Dictated from notes Oct. 10 1963).’ Heller Papers. Box 6.

inflationary.⁸⁴⁹ Despite agreeing with Kennedy that his testimony would “serve a useful purpose,” Heller’s appearance before the Finance Committee “failed to improve the prospects for a speedup in committee action.”⁸⁵⁰ Indeed, after he delivered the Council’s prepared statement, members of the committee subjected the CEA chairman to a rigorous examination. One member even remarked that his colleagues were “doing a fine job of giving what I think is a wonderful idea of a rough time.”⁸⁵¹

Byrd led the way by stressing that, to pass the tax cut, FY 1965 expenditures should be below \$100 billion. Heller retorted that this would offset the impact of the tax cut.⁸⁵² Another member questioned the CEA chairman over how Kennedy’s measure would produce the “tremendous impetus” that Heller foresaw, especially as it would only average \$110 per person.⁸⁵³ Invoking the example of the British tax cut, Heller highlighted how that measure had underwritten “a rise of 7 percent in [British] industrial production.”⁸⁵⁴ Whilst the CEA chairman impressively defended the tax cut in the face of these probing questions, both the length and the intensity of his interrogation demonstrated that certain members of the Finance Committee were unconvinced of the merits of that measure. After he returned to the White House on the evening of November 12, Heller had not improved the tax cut’s prospects of enactment by the Senate.

VII

⁸⁴⁹ ‘Statement of Walter Heller, Chairman Accompanied By Gardner Ackley and John P. Lewis, Members of the Council of Economic Advisers before the Senate Committee on Finance,’ 12 November 1963. Heller Papers. Box 23.

⁸⁵⁰ Heller, Memorandum for the President, Untitled, 16 October 1963. POF. Box 76; John D. Morris, ‘Heller, in Senate Hearing, Urges Speed on Tax Cut,’ *New York Times*, 13 November 1963, 21. PQHN.

⁸⁵¹ *Revenue Act of 1963, Hearings before the Committee on Finance, United States Senate* 88th Congress: 1st Session, on H. R. 8363, November 12-15, 21, 22, 1963. Part 4 (Washington DC, 1963), 1621.

⁸⁵² *Ibid*, 1589-1594.

⁸⁵³ *Ibid*, 1598.

Ten days after the CEA chairman appeared before the Senate Finance Committee, he boarded a plane with several members of the cabinet for an economic summit in Japan. Shortly after taking off, they received news that Kennedy “had been shot and ‘seriously wounded.’”⁸⁵⁵ Then, news reached them that JFK was dead. “The plane fell into complete grief-stricken silence,” Heller recalled, “for a period that no one can measure by the clock.”⁸⁵⁶ After forging such a close bond with Kennedy since their meeting in Minneapolis in October 1960, it is unimaginable what Heller felt at this moment. The man whom he later referred to as “the best economics student I ever had” was dead, and the CEA chairman would have to work with a new president upon his return.⁸⁵⁷

Still, Heller had achieved much in the lead up to Kennedy’s death. True, the tax cut did face the final hurdle of Senate Finance Committee approval, but this chapter has shown that Heller played an important role in getting it to that critical stage. In January, he helped Kennedy frame the tax cut in a way that appealed to certain members of Congress. Throughout the year, he also refuted concerns that the measure would substantially increase the levels of debt and inflation. He further used both the Council’s pulpit for public education and his own behind-the-scenes manoeuvring to muster support for the measure. In the spring, Heller responded well to the attacks made by Keyserling and adequately refuted the argument that the brighter economic picture negated the need for the tax cut. In July, he ensured that monetary policy did not offset the future impact of that measure. He did not play a role in the negotiations between the administration and the Ways and Means

⁸⁵⁴ Ibid, 1599, 1603.

⁸⁵⁵ Heller, ‘Chronology of Events On Board the Aircraft Carrying the Cabinet Group to Japan on the Day of President Kennedy’s Death,’ 23 November 1963, in Heller, Interview with McComb, 20 February 1970. Appendix. LBJL-OHC.

⁸⁵⁶ Ibid.

⁸⁵⁷ Heller, ‘Let’s Tailor the Policies to Fit the Problems,’ *Challenge*, 16:2 (May/June 1973), 32.

Committee. Heller was also not so successful at drumming up popular support for the tax cut as has been argued. Furthermore, he made an unfortunate gaffe before the JEC in January. Nevertheless, Heller mobilised support for the tax cut from business and academic circles and was successful at refuting the revival of the structural unemployment argument in the fall. By the time of Kennedy's assassination in November 1963, Heller had played an important role in the administration's effort to push the tax cut through Congress. This set the stage for the consolidation of the Keynesian revolution in early 1964.

Chapter Six

A Foot Soldier in the Great Society

After returning to US soil at midnight on November 22, Walter Heller went straight to his office in the Executive Office Building located opposite the White House. There, he prepared a briefing for the new president that he would give the following day. Lyndon B. Johnson was the man sworn in to replace John F. Kennedy. The former Senate Majority Leader from Texas, Johnson had served as JFK's vice-president. Given his roots in the South, much uncertainty surrounded Johnson's succession. As Heller recalled, "There was some fear that he might be quite conservative."⁸⁵⁸ Soon after he took office, LBJ spoke with fellow Texan Robert Anderson (Eisenhower's former Treasury Secretary), undoubtedly doing little to quell such a concern.⁸⁵⁹ Heller also worried that Johnson would seek advice from other economists.⁸⁶⁰ Such a fear was understandable given how the CEA chairman had carefully built up his influence over the previous three years, so much so the tax cut that he championed was close to enactment.

As it turned out, these concerns were unfounded. Johnson, far from being a conservative, appreciated Heller's ideas. The new president viewed the tax cut as essential to his ambitious programme of liberal reform, known as the Great Society. "There are many problems ahead," LBJ remarked early in his presidency, "There is a crying need to eliminate poverty, reduce unemployment, improve education, and to further the goal of civil rights. No piece of legislation can help as much in solving these problems as the tax bill."⁸⁶¹ Heller often stated that the tax cut's primary aim was to offset the economy's chronic slack, but he also maintained that an expanding

⁸⁵⁸ Heller, Interview with McComb, 20 February 1970, 13.

⁸⁵⁹ Heller, Interview with McComb, 21 December 1971, 17.

⁸⁶⁰ Heller, Interview with McComb, 20 February 1970, 16.

economy would make it easier to tackle the nation's fundamental economic and social problems.⁸⁶² As a result, Heller was a central figure in the formulation of the Great Society, a task that he began under President Kennedy. This chapter assesses how Heller worked with LBJ to secure the eventual passage of the tax cut, before exploring what role Heller played in the development of the Great Society. This will include discussion of Heller's role in the origins of the War on Poverty, which began during the Kennedy years. By examining the way in which Heller helped shape the Great Society, this chapter will demonstrate how Keynesian liberalism reached its peak by the mid-1960s, elevating Heller and his economist colleagues to positions of influence unmatched either before or since.

I

In hindsight, Heller had no need to fear that Johnson would shun him for conservative economics. Despite the assertion of Rowland Evans and Robert Novak that the “orthodox attachment to the balanced budget was shared to a surprising degree by Johnson,” the new president “was singularly predisposed toward an economic strategy that focused most squarely on the demand side of the economy.”⁸⁶³ True, Johnson lacked enthusiasm for deficit spending during his tenure as Senate Majority Leader, but his experiences ensured that he would be sympathetic to liberal Keynesianism. Like John Maynard Keynes, Johnson cared deeply for the unemployed, the impoverished, and the underprivileged.⁸⁶⁴ This owed much to his tenure as a schoolteacher on the Mexican border in the late 1920s.⁸⁶⁵ He also served as the administrator of the Texas branch of the National Youth Administration in the

⁸⁶¹ Lyndon B. Johnson, ‘Statement by the President Following Senate Committee Action on the Tax Bill,’ 24 January 1964. APP.

⁸⁶² See Chapter Two of this thesis.

⁸⁶³ Rowland Evans and Robert Novak, *Lyndon B. Johnson: The Exercise of Power* (New York, 1966), 369; Shreve, ‘A Precarious and Uncertain Liberalism,’ 131.

⁸⁶⁴ Shreve, ‘A Precarious and Uncertain Liberalism,’ 9-11.

late 1930s, where he witnessed first-hand the positive impact of public works.⁸⁶⁶ As a Congressman, Johnson was involved in the electrification of rural Texas, which demonstrated to him how public power could aid the poor.⁸⁶⁷ He did preach fiscal responsibility during the 1950s, but Johnson did this to survive politically in an era when “Republicans were beginning to attack liberal legislation more on its cost than its merits.”⁸⁶⁸ Coming from the South, however, he did believe that the government had a duty to promote the wellbeing of businesses alongside that of the poor, so he would see in the growth economics of Walter Heller a way to lift all boats.⁸⁶⁹

It took the efforts of Heller to convert Johnson to growth liberalism. This was something that Heller did from 1961-63.⁸⁷⁰ As the *Washington Post*’s economics commentator Hobart Rowen noted, during this period Heller was in certain respects “closer to Johnson than he was to Kennedy.”⁸⁷¹ Neither was originally part of JFK’s inner circle, so they sat side-by-side at JFK’s morning briefing sessions. There, Heller tutored Johnson in the new economics.⁸⁷² Heller would also share with Johnson certain memoranda that he sent to Kennedy, undoubtedly hoping that this would convert the vice-president to his ideas.⁸⁷³ Additionally, Johnson’s office was in the same building as Heller’s. In fact, Heller approached his “via the main stairwell that opened in front of Johnson’s suites,” which ensured that both men “engaged in numerous informal conversations.”⁸⁷⁴ As Heller educated Kennedy about the virtues of liberal Keynesianism, he acquainted Johnson with his ideas. What is more, LBJ proved adept at grasping them.

⁸⁶⁵ Robert Dallek, *Lyndon Johnson: Portrait of a President* (London, 2005), 15-17.

⁸⁶⁶ *Ibid*, 27-31.

⁸⁶⁷ *Ibid*, 38-39.

⁸⁶⁸ Shreve, ‘A Precarious and Uncertain Liberalism,’ 129-130, 125-126 (quotation 126).

⁸⁶⁹ *Ibid*, 130-131.

⁸⁷⁰ *Ibid*, 160-161.

⁸⁷¹ Cited in *Ibid*, 162.

⁸⁷² Heller, Interview with McComb, 20 February 1970, 3.

⁸⁷³ *Ibid*, 3.

Still, Heller feared Johnson would shun him after the latter assumed the presidency. Accordingly, in the lead up to their first meeting on November 23, Heller wrote Johnson a memo that stressed the urgency of the tax cut. This said that the economy was “in the eleventh quarter of expansion from the recession low point in the first quarter of 1961,” but “the thrust of the tax-cut” remained “essential to lift the economy to, or near, full employment.”⁸⁷⁵ To emphasise the need for the measure, Heller said that “tentative estimates” showed “that *with* the tax cut, GNP will be \$12 billion higher in 1964 than *without*.”⁸⁷⁶ If its passage continued to be delayed by the Senate Finance Committee, the nation might “face a slowdown or even a downturn” towards the end of 1964.⁸⁷⁷ Despite knowing that Senator Harry Byrd would only release the tax cut if the administration submitted budgetary expenditures for FY 1965 under \$100 billion, the CEA chairman informed LBJ that Kennedy had voiced his own preference for a FY 1965 budget “between \$101 and \$102 billion.”⁸⁷⁸ Heller preferred this size because cutting around \$1 – 1½ billion from the FY 1965 budget would offset the stimulus of the tax cut.⁸⁷⁹

Heller repeated these points during his meeting with Johnson in the evening of November 23. To Heller’s relief, both men had “a very satisfactory discussion of issues and of approaches and of the problems of the tax cut,” to the extent that LBJ indicated he “was thoroughly sold on the tax cut idea.”⁸⁸⁰ As the CEA chairman was leaving, the president even pulled him back and said, “Now, I want to say something about all this talk that I’m a conservative who is likely to go back to the Eisenhower

⁸⁷⁴ Shreve, ‘A Precarious and Uncertain Liberalism,’ 162. Footnote 91.

⁸⁷⁵ Heller, Memorandum for the President, ‘Summary Review of the Economic Situation and Pending Issues,’ 23 November 1963. Heller Papers. Box 6.

⁸⁷⁶ *Ibid.* Emphasis in the original.

⁸⁷⁷ *Ibid.*

⁸⁷⁸ *Ibid.*

⁸⁷⁹ See too Heller, Memorandum for the President, ‘A Quick Economic Round-up,’ 23 November 1963. White House Central Files [Henceforth WHCF]. FG 11-2/A. Box 56. LBJL.

⁸⁸⁰ Heller, Interview with McComb, 20 February 1970, 19, 22.

ways or give in to the economy bloc in Congress. It's not so...I'm no budget slasher. I understand that expenditures have to keep on rising to keep pace with the population and help the economy.”⁸⁸¹ Despite this, LBJ indicated that it was politically impossible to pass the tax cut unless the FY 1965 budget was reduced, saying to Heller that he would ““like to have [Treasury Secretary Douglas] Dillon and [Kermit] Gordon [now serving as Budget Director] and myself and perhaps a couple of others have a bull session with you on this.””⁸⁸² They scheduled the meeting for two days later.

Worried that LBJ would slash the FY 1965 budget, prior to this meeting Heller attempted to dissuade the president from doing so. He stressed that cutting the budget would constitute “a real cut,” as “very little of it could be gotten from inter-year switches in outlays, asset sales, changes in government loan financing mechanisms, or other ‘gimmicks.’”⁸⁸³ This meant the economic impact of such a policy would be significant, to the point whereby it would result in a \$5.5 billion loss in GNP within sixteen months.⁸⁸⁴ Not only was this “equivalent to sacrificing between 10 and 15 percent of the expansionary effect” of the tax cut by the fourth quarter of 1964, further delay of the measure would almost certainly tip the economy into a recession by then.⁸⁸⁵ Additionally, Heller argued that the administration could defend a budget of \$101 – 102 billion. As FY 1964 expenditures would be around \$98.5 billion, a \$3 billion increase for FY 1965 “would be little more than half of the average increase in the three Kennedy budgets.”⁸⁸⁶ It would also “be less than the

⁸⁸¹ Heller, ‘Notes on Meeting with President Johnson, 7.40 p.m., Saturday, November 23, 1963.’ Heller Papers. Box 7.

⁸⁸² Heller, Interview with McComb, 20 February 1970, 21.

⁸⁸³ Heller, Memorandum for the President, ‘The general economic effect of holding the FY 1965 budget below \$100 Billion,’ 25 November 1963. Heller Papers. Box 6.

⁸⁸⁴ Ibid.

⁸⁸⁵ Ibid.

⁸⁸⁶ Heller, Memorandum for the President, ‘Case for a \$101-\$102 billion Budget,’ 25 November 1963. WHCF. FG 11-2/A. Box 56. LBJL.

average budget increase in Eisenhower's second term," whilst a budget of \$101 – 102 billion for FY 1965 was smaller than Ike had predicted when he left office.⁸⁸⁷

At the same time as Heller sought to dissuade Johnson from bowing to Byrd's demands, Douglas Dillon argued that to pass the tax cut the president must slash the FY 1965 budget. Shortly before the November 25 meeting, the Treasury Secretary told Johnson it was imperative "to secure Senate action on the tax bill as soon as possible."⁸⁸⁸ This was because the Senate would soon debate the Civil Rights Act, another measure promoted by Kennedy in 1963, thereby holding up the passage of the tax cut.⁸⁸⁹ To secure the Finance Committee's approval of the measure, Dillon explained that the sooner LBJ's "budget expenditure target for fiscal 1965 is in the public domain, the more likely you are to get substantial progress toward early enactment of the tax bill."⁸⁹⁰ He also hoped Johnson would propose "a significantly lower figure" than the one suggested by Heller.⁸⁹¹ Additionally, despite Heller telling Johnson that the increase over FY 1964 would be less than the yearly expenditure increases of the previous three years, the Treasury Secretary indicated that he preferred FY 1965 expenditures to be as close to the FY 1964 level as possible.⁸⁹²

To counter Dillon's influence, Heller persuaded Secretary of Agriculture Orville Freeman and Secretary of Labor Willard Wirtz to urge Johnson not to slash the FY 1965 budget. The CEA chairman followed these efforts up during the meeting on November 25 by arguing that Johnson would alienate key liberal groups, such as the AFL-CIO, if he accepted Byrd's demands.⁸⁹³ The president did not heed Heller's

⁸⁸⁷ Ibid.

⁸⁸⁸ Dillon, Memorandum for the President, 'The Tax Bill,' 25 November 1963. Legislative Background File. Tax Increase [Henceforth LBFTI]. Box 1. LBJL.

⁸⁸⁹ Ibid.

⁸⁹⁰ Ibid.

⁸⁹¹ Ibid.

⁸⁹² Ibid.

⁸⁹³ Ackley, 'Troika Meeting with President Johnson, Monday, 25 November, 1963 (notes by Gardner Ackley, CEA),' 30 November 1963. Heller Papers. Box 7.

advice. Instead, he agreed with Dillon that it would be impossible to enact the tax cut if the budget was above \$100 billion. Aware, too, that it was necessary to get the tax bill to the Senate floor ahead of the Civil Rights Act, Johnson told Heller to call off the lobbying of his “liberal friends.”⁸⁹⁴ Unless Heller agreed to “get the budget down,” Johnson explained, ““you won’t pee one drop.””⁸⁹⁵ The president’s political lesson forced Heller to agree. Conceding defeat, he explained that “if it were a choice between a tax bill right away and \$1-½ billion of expenditures...he’d have to agree that, on economic grounds,” the budget cuts were justified.⁸⁹⁶

Johnson thus persuaded Heller that the political merits of cutting the budget outweighed the economic impact of doing so. Importantly, the extent to which Heller further objected to the expenditure cuts after the meeting on November 25 has been the subject of debate. Allen Matusow suggests Heller continued to object to the budget cuts.⁸⁹⁷ This historian’s argument is lent credence by the fact that, on December 14, the CEA chairman sent the president a memo highlighting how further cuts “could mean the difference between getting below 5 percent unemployment or not getting there [before the 1964 Presidential Election].”⁸⁹⁸ However, David Shreve has disagreed with this assessment, arguing that, following the meeting on November 25, Heller “immediately launched an effort to help Johnson explain the budget cutting exercise to liberals who would oppose it.”⁸⁹⁹ On December 3, the CEA chairman forwarded the president several points that he could make in an upcoming meeting with members of the AFL-CIO, which proved instrumental in “convincing” its

⁸⁹⁴ Ibid.

⁸⁹⁵ Ibid.

⁸⁹⁶ Ibid.

⁸⁹⁷ Matusow, *The Unraveling of America*, 56. For more on this see Shreve, ‘A Precarious and Uncertain Liberalism,’ 205. Footnote 38.

⁸⁹⁸ Heller, Memorandum for the President, ‘The Unemployment Cost of Budget Cutting,’ 14 December 1963. WHCF. FG 11-2/A. Box 56. LBJL.

⁸⁹⁹ Shreve, ‘A Precarious and Uncertain Liberalism,’ 205. Footnote 38.

leaders that cutting the budget was imperative.⁹⁰⁰

Further evidence substantiates Shreve. As opposition to both the tax and budget cuts from liberal Senator Albert Gore of Tennessee reached its peak in early January, Heller told Johnson he had provided the economist Robert Nathan with certain “budget-economic information” that the latter “said he will use” on behalf of the administration.⁹⁰¹ This was important because Nathan could “make the difference between opposition and support [for the tax cut] among very influential liberals.”⁹⁰² The fact that Heller saw fit to shore up liberal support for the tax cut in the wake of the budget cuts demonstrates that the CEA chairman unreservedly favoured cutting the budget following the meeting on November 25. Moreover, one month after that meeting, Johnson decided to slash the FY 1965 budget further, a decision to which Heller did not object.

On December 23, Johnson told Heller that he wanted to cut FY 1965 expenditures by more than \$1.5 billion. This he wanted to do by raising an extra \$1 billion in revenue during that fiscal year.⁹⁰³ Rather than protest this course of action, Heller went back to his office, and, within an hour, found a way that the president could raise an extra \$1 billion. This he did by suggesting that the regular withholding rate – the amount of taxation retained from a person’s pay – should be reduced from 18 percent to 14 percent (instead of 15 percent) a year early (i.e. in 1964). This would “shift the revenues [in FY 1965] enough to produce eight hundred [million dollars] more.”⁹⁰⁴ A reduction of the withholding rate would also offset the reduced stimulus from cutting the FY 1965 budget, as it would mean “an average of \$200 million per

⁹⁰⁰ Ibid, 205.

⁹⁰¹ Heller, Memorandum for the President, ‘Robert Nathan,’ 8 January 1964. WHCF. FG 11-2/A. Box 56. LBJL.

⁹⁰² Ibid.

⁹⁰³ Heller, Interview with McComb, 21 December 1971, 19-21.

month will be put into the private economy.”⁹⁰⁵ Pleased that he had now satisfied the political need of budget cutting “with an economic good,” the CEA chairman asked Kermit Gordon to find an extra \$200 million, which the Budget Director did.⁹⁰⁶ Writing to Johnson later that evening, Heller informed the president that he would have an extra \$1 billion in revenue.⁹⁰⁷ This helped to pave the way for LBJ to “[astonish] everybody by submitting a final [FY 1965] budget [on January 8] that cut spending to only \$97.9 billion,” below that favoured by the House Republicans who attempted to recommit the tax cut back in September.⁹⁰⁸

In addition to helping Johnson find further budget cuts, Heller, in January, shrewdly manipulated the release of economic data to help ensure the Finance Committee’s endorsement of the tax bill. In a telephone call to Jack Valenti, LBJ’s Special Assistant, on January 10, Heller noted that he had received “some rather interesting economic news” and had an idea “how to play it.”⁹⁰⁹ GNP for the fourth quarter of 1963 had come in at \$600 billion (at an annual rate). This not only constituted a “terrific jump” from the previous quarter but also was much higher than the Council had estimated.⁹¹⁰ “*Normally*,” Heller told Valenti and then the president, “I would urge immediate White House release of such good news.”⁹¹¹ However, undoubtedly conscious of the fact that the unexpected increase in economic activity during the previous spring had roused conservative opposition to the tax cut, he

⁹⁰⁴ Ibid, 20; Heller, Memorandum for the President, ‘The Case for Dropping the Withholding Rate to 14%,’ 5 January 1964. WHCF. FG 11-2/A. Box 56. LBJL.

⁹⁰⁵ Heller, Memorandum for the President, ‘The Case for Dropping the Withholding Rate to 14%.’

⁹⁰⁶ Heller, Interview with McComb, 21 December 1971, 21, 20.

⁹⁰⁷ Heller, Memorandum for the President, ‘MORE Revenue in FY 1965,’ 23 December 1963. WHCF. FG 11-2/A. Box 56. LBJL.

⁹⁰⁸ Matusow, *The Unraveling of America*, 56.

⁹⁰⁹ Jack Valenti, Telephone Conversation with Walter Heller, 10 January 1964. Tape: WH6401.11, PNO: 14, Conversation: 1317. Online at the Miller Center Presidential Recordings Website [Henceforth MC]

⁹¹⁰ Ibid.

⁹¹¹ Ibid; Heller, Memorandum for the President, ‘More Good News on GNP,’ 10 January 1964. WHCF. FG 11-2/A. Box 56. LBJL. Emphasis in the original.

counselled that the administration should impose “a rigid clamp on the news till January 20,” when the 1964 *Economic Report* would be released.⁹¹² This was because it was essential “not to give the Senate Finance Committee any excuse for slowing down their action on the tax bill,” something that Valenti and Johnson both agreed with.⁹¹³

As well as shrewdly manipulating the release of this economic data, Heller helped to publicise an economy drive undertaken by LBJ in December and January to firm up conservative support for the tax cut.⁹¹⁴ He also, at the urging of both the president and his advisers, ensured that the press discussed both comparisons with the 1963 British tax cut and other European fiscal policies.⁹¹⁵ Meanwhile, he and Johnson worked closely to persuade supporters of the tax cut to lobby harder for the measure. On January 11, LBJ and Heller met in the White House with members of both the Business and Citizens Committees’ for Tax Reduction. As Valenti told LBJ before the meeting, its purpose was to get the Citizens Committee “to coordinate heavily, in the next two weeks, through contacts with members of the Senate, to get this bill out of [the Finance] Committee and voted on.”⁹¹⁶ Heller and LBJ successfully achieved this goal. Reflecting this, the acting-chairman of the Citizens Committee wrote Heller two days later, explaining that the session “sent all of our members back home resolved to work even harder and to be more vociferous for the tax legislation.”⁹¹⁷

⁹¹² Ibid.

⁹¹³ Ibid.

⁹¹⁴ This was following a telephone conversation between Heller and LBJ on 23 December. See Johnson, Telephone Conversation with Heller, 23 December 1963. Tape: K6312.15, PNO: 1. MC. For an example of Heller publicising the economy drive, see n.n., ‘Defense Cuts to Aid the Poor, Heller Says,’ *Washington Post, Times Herald*, 27 January 1964, A4. PQHN.

⁹¹⁵ Presidential aide Bill Moyers suggested that Heller should emphasise the transnational comparisons in the press. Moyers to Johnson, 18 December 1963. WHCF. Ex F19. Box 55. LBJL. For an example of Heller stressing the transnational comparisons see n.n., ‘The Envious Economists,’ *Wall Street Journal*, 28 January 1964, 10. PQHN.

⁹¹⁶ Valenti, Memorandum for the President, ‘Meeting with Citizens Committee for Tax Reduction and Revision on Thursday, January 9 at 4:00 PM,’ 9 January 1964. LBFTI. Box 1. LBJL.

⁹¹⁷ Allan Cartter to Heller, 13 January 1964. WHSFWH. Roll 86.

Thus, Heller played an important role in the administration's broader attempts to secure the Finance Committee's approval of the tax bill. True, he did not directly engage in the legislative process. However, the CEA chairman's efforts, combined with those of Johnson and other administration members, ensured that the Finance Committee reported out the measure on January 28. Just over a week later, the Senate approved the tax bill, before Johnson signed it into law on February 26. In short, the Revenue Act of 1964 provided \$10 billion of tax reduction over a two-year period. Most of this took place in its first year of enactment and the bill set aside a certain amount for corporations (so that investment expanded alongside consumption). Its passage, during non-recession conditions, signified the triumph of growth liberalism over that of commercial Keynesianism. Whilst Franklin Roosevelt, Harry Truman, and Dwight Eisenhower cautiously deployed deficit spending during their presidencies, it was not until the passage of the 1964 Revenue Act that Keynesian political economy enjoyed its heyday in America. As noted by Heller, this put at the president's "disposal, as nothing else can, the resources needed to achieve great societies at home and grand designs abroad."⁹¹⁸

II

After passage of the tax cut, both Heller and Johnson expected a substantial rise in economic activity. This, they believed, would produce "higher federal revenues [which] would finance" the Great Society.⁹¹⁹ The tax cut *did* prove instrumental to the expansion of the liberal state during the 1960s. Out of the total increase in GNP between 1961 and 1965, only a quarter resulted from cyclical recovery whilst enhanced economic power accounted for the rest.⁹²⁰ Yet, Heller did

⁹¹⁸ Heller, *New Dimensions of Political Economy*, 11.

⁹¹⁹ Joseph Califano, Jr., *The Triumph and Tragedy of Lyndon Johnson: The White House Years* (New York, 2015), 65.

⁹²⁰ Tobin cited in Collins, *More*, 59.

not wait for passage of the tax cut before formulating desirable social programmes. In fact, he played a key role in developing the War on Poverty under Kennedy, something he did out of concern that not everyone would reap the benefits of the tax cut.⁹²¹

Throughout late 1962, John Kenneth Galbraith, Leon Keyserling, and the sociologist Michael Harrington, had all critiqued the tax cut on the grounds that it would by-pass the poor. Therefore, Kennedy asked Heller to give him “facts and figures on...the poverty problem in the United States.”⁹²² In response, Heller noted that, in 1960, 22 percent of the population was impoverished and a significant number remained in such a state, especially minorities, female-headed households, and the elderly.⁹²³ It was clear that the nation had “reduced the share of the population in poverty during all periods of prosperity,” but the tax cut would not alleviate the hardship of those who were most disadvantaged. These people, Heller explained, suffered from structural impediments that prevented them from sharing in improved economic conditions.⁹²⁴

Kennedy had also asked for this information in preparation for an interview in December, where he expected a question about poverty. This question was not asked, but the issue was dramatized in February 1963 when a television documentary “led to the White House receiving over 100 letters expressing concern” about poverty.⁹²⁵ In

⁹²¹ As Morgan noted, “The lack of progressive features” in the tax cut was “unusual in view of the measure’s Democratic paternity. For the large majority of taxpayers in the \$5,000 to \$50,000 income range...the cuts were roughly similar.” Morgan, *Deficit Government*, 94.

⁹²² Heller cited in James Sundquist, ‘Origins of the War on Poverty,’ in Sundquist (ed.) *On Fighting Poverty: Perspectives From Experience* (London, 1969), 7. For JFK’s concerns about Galbraith, Keyserling and Harrington’s critiques see Mark I. Gelfrand, ‘The War on Poverty,’ in Robert Divine (ed.) *Exploring the Johnson Years* (Austin, TS, 1981), 128.

⁹²³ Heller, Memorandum for the President, ‘Selected Facts on Low-Income Population in the U.S.,’ 16 December 1962. POF. Box 63a.

⁹²⁴ Ibid.

⁹²⁵ CEA’s Role in Major Program Areas,’ Administrative History of the Council of Economic Advisers [Henceforth AHCEA], Chapter V, V-ID, Box 1. LBJL.

response, JFK asked Heller “to look into the poverty issue in greater depth.”⁹²⁶ As noted by Carl Brauer, the CEA chairman knew that the critiques of Galbraith, Keyserling, and Harrington could hurt Kennedy politically. Thus, concern “about protecting Kennedy’s left flank on the tax cut” drove Heller to ask Robert Lampman, a CEA staff economist and an expert on poverty, to conduct further research.⁹²⁷ Although Brauer was right that Heller took a closer look at poverty due to this political concern, it is important to note that the CEA chairman did not suddenly shift his interest onto the issue in early 1963. He was aware beforehand that the tax cut’s benefits would not be all-embracing. True, Brauer has pointed out that Heller’s experience as a PhD student at the University of Wisconsin instilled in him a concern “with distributional objectives, with social justice and economic equity,” but he does not acknowledge that as far back as the late 1950s, the CEA chairman understood that faster economic growth would not eradicate poverty.⁹²⁸

This explains why Heller turned to Lampman to study the issue in greater depth. Lampman was also an alumnus of the Wisconsin Economics Department and had conducted a Joint Economic Committee investigation into poverty in the late 1950s. Heller read Lampman’s findings shortly after publication.⁹²⁹ In his study, Lampman concluded that economic growth had reduced the number of people in poverty, but conceded that a faster growth rate would not solve the issue completely.⁹³⁰ Hence, prior to asking Lampman to study the issue more closely in

⁹²⁶ Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 103.

⁹²⁷ Ibid, 119 (quotation), 102-104.

⁹²⁸ Ibid, 103. See too Maris A. Vinovskis, *The Birth of Head Start: Preschool Education Policies in the Kennedy and Johnson Administrations* (Chicago, IL, 2005), 32. For Heller’s understanding of growth and the poverty issue in the late 1950s see Chapter Two of this thesis.

⁹²⁹ Robert Lampman, Interview in Michael Gillette, *Launching the War on Poverty: An Oral History* (New York, 2010), 4.

⁹³⁰ Indeed, he predicted that, based on long-run trends, the poverty rate would only decline by a further 10 percent by 1977-87 (from 20 percent in the late 1950s). See Seymour Martin Lipset, *The First New Nation: The United States in Comparative Perspective* (London, 2003, originally published, 1964), 335.

early 1963, Heller was “well geared up in his own thinking to the things to do after” the tax cut.⁹³¹ In the late 1950s, for example, he had talked about the need to increase output to generate a “fiscal dividend,” which could be used to assist those whom the tax cut would leave untouched.⁹³² Reflecting this, when he later wrote to Lampman to ask his thoughts about a possible antipoverty programme, the CEA chairman said that he was making “a request I’ve had in suspension for some time.”⁹³³ He also knew that the fiscal dividend would not come immediately, so in 1963 he had in mind the idea of “redirect[ing] several hundred million dollars from existing programs into a new antipoverty effort.”⁹³⁴

In his response to Heller’s initial request, Lampman updated the study that he conducted in the late 1950s. He concluded that, from 1956-61, there had been a “drastic slowdown in the rate at which the economy” was taking people out of poverty. Measuring poverty based upon cash income, Lampman found that “the percentage of families with less than \$3000 of total money income (in 1961 dollars)” had only declined by 2 percent (this compared to 10 percent between 1947-56).⁹³⁵ Though Heller attributed this to “the costs of economic slack,” he admitted that the results were “distressing.”⁹³⁶ He indicated, too, that whilst they offered “another dimension of what’s at stake in the proposed tax cut,” there needed to be a greater effort on behalf of the poor.⁹³⁷ Accordingly, he wrote to Lampman on June 3 to

⁹³¹ Lampman, Interview in Gillette, *Launching the War on Poverty*, 5.

⁹³² It seems likely that Heller first used the phrase “fiscal dividend” in the 1960s, but in the 1950s, he often discussed how to use the increased revenues from higher growth. See Chapter Two of this thesis. For Heller’s use of the phrase see Barry Riccio, *Walter Lippmann: Odyssey of a Liberal* (London 1996), 205.

⁹³³ Heller, Memorandum for Lampman, ‘Poverty,’ 3 June 1963. AHCEA, Volume II, Documentary Supplement, Part IV. Box 3. LBJL.

⁹³⁴ Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 108.

⁹³⁵ Heller, Memorandum for the President, ‘Progress and Poverty,’ 1 May 1963. POF. Box 75a.

⁹³⁶ Ibid.

⁹³⁷ Ibid.

request ideas for “a possible Kennedy offensive against poverty.”⁹³⁸

Further developments solidified Heller’s conviction that doing so was politically imperative. Following rumours “that the Republicans were planning an anti-poverty program,” Heller viewed it as essential to prevent the GOP from co-opting a natural issue for the Democrats.⁹³⁹ He also became aware that the labour movement, which had strong ties to Leon Keyserling, regarded the tax cut as a measure for the rich. This was particularly following an early June meeting between the CEA and members of the AFL-CIO. In this, that organisation’s representatives argued that Kennedy had “not shown enough concern about the well-being of the working class and the lower strata of society.”⁹⁴⁰ Clearly anxious that the tax cut would lead to Kennedy losing support from the left, Heller wrote to the president on June 13 to say that there was “a major problem of equity in the distribution of the bounties of your tax cut program.”⁹⁴¹ This concern undoubtedly solidified his desire to formulate a war on poverty in June 1963.

In addition to harbouring political concerns, other factors strengthened Heller’s conviction that it was necessary to do something for the poor. The civil rights demonstrations during the first half of 1963 gave the poverty issue “an additional allure” to him.⁹⁴² As the CEA noted at the time, “much of the bitterness in the dramatic protests of Negroes” was “rooted in their relative economic status,” something exemplified by the 1963 March on Washington’s emphasis on ‘jobs and

⁹³⁸ Heller, Memorandum for Lampman, ‘Poverty.’ For the quotation see Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 102.

⁹³⁹ Sundquist, ‘Origins of the War on Poverty,’ 20.

⁹⁴⁰ Warren Smith to Heller, ‘Luncheon Discussion with Nat Goldfinger and Larry Rogin,’ 7 June 1963. POF. Box 76.

⁹⁴¹ Heller, Memorandum for the President, ‘Assuring Economic Expansion through 1964.’ This was also partly a response to the fact that conservative lobby groups did not take kindly to the administration’s reform proposals that accompanied the tax cut. In fact, they had managed to persuade the Ways and Means Committee to strip or modify many of the reforms that previously had the support of liberal groups, making the reform package less equitable than originally intended.

⁹⁴² Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 105.

freedom.⁹⁴³ Knowing that African Americans suffered disproportionately high levels of poverty, Heller had always opposed discrimination. In fact, he commissioned a CEA study in 1962 to show that its abolition would increase economic growth by 2.5 percent.⁹⁴⁴ However, he was concerned that the inadequate training and education of African Americans would prevent them from taking part in a full-employment economy. This was exemplified by the fact that the CEA's 1962 study showed that, if African Americans attained as much education as whites in a non-discriminatory economy, output could increase by 3.2 percent.⁹⁴⁵ This led Heller to conclude that it was essential to cultivate their development. African American joblessness, he told Kennedy, would likely decrease by half if the economy were at full employment.⁹⁴⁶ The "other half" needed to be "whittled away by particularized attacks on training, discrimination, motivation, health, and so forth."⁹⁴⁷ As the civil rights demonstrations reached their peak in 1963, Heller's commitment to an antipoverty offensive thus increased. As one CEA staff member put it, Heller "saw, literally, the March on Washington and that sure didn't do anything to cool us off on pushing this embryonic program."⁹⁴⁸

Importantly, two scholars have argued that Heller saw in an antipoverty initiative a means to court black voters.⁹⁴⁹ This is unlikely. Instead, the CEA chairman "viewed poverty either as more of a white problem than a black one or as

⁹⁴³ CEA, 'Draft Material on Economic Aspects of the Civil Rights Problem,' 25 July 1963. Records of the Council of Economic Advisers. Roll 6. LBJL.

⁹⁴⁴ CEA, 'Economic Costs of Racial Discrimination in Employment,' 25 September 1962. Office Files of George Reedy. Box 22. LBJL.

⁹⁴⁵ Ibid.

⁹⁴⁶ Heller, Memorandum for the President, 'Various Items,' 20 June 1963. POF. Box 76.

⁹⁴⁷ Ibid.

⁹⁴⁸ Cited in Michael B. Katz, *The Undeserving Poor: America's Enduring Confrontation with Poverty* (New York, 2013), 107.

⁹⁴⁹ See Frances Fox Piven and Richard A. Cloward, *Regulating the Poor: The Functions of Public Welfare* (New York, 1993), 255-282.

one that superseded race.”⁹⁵⁰ Knowing that Kennedy’s support for civil rights legislation in June 1963 would boost the president’s appeal with African Americans, Heller saw a poverty programme as a way of appealing to Southern Democrats distressed with Kennedy’s promotion of the Civil Rights Act. This was because poverty was an issue that particularly beset white people in the South.⁹⁵¹ Reflecting this, when he wrote to Kennedy on June 20 to inform him that Lampman was looking into a possible antipoverty programme, Heller noted that although the “civil rights message covers a lot of the ground” there needed to be “a broader program not linked to race.”⁹⁵² During a meeting with the president in October, Heller also explained that “having mounted a dramatic program for one disadvantaged group (the Negroes), it was both equitable and politically attractive to launch [one] specifically designed to aid other disadvantaged groups.”⁹⁵³ It is further worth noting, as Alice O’Connor has done, that when the CEA did develop the antipoverty programme it was conscious of ensuring the initiative was not viewed as one purely for African Americans (as this would be politically disastrous).⁹⁵⁴ When Lampman replied to Heller on June 10 to outline a possible antipoverty initiative, for example, he “took care to note that nonwhites were *not* to be listed among the groups who proved ‘immune to growth,’” despite the opposite being the case.⁹⁵⁵ This further demonstrates that, though motivated to develop an antipoverty programme by the issue of civil rights, Heller and Kennedy were not interested in using it to appeal to black voters.

Two other factors explain why Heller developed an antipoverty programme in

⁹⁵⁰ Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 105.

⁹⁵¹ Ibid, 105.

⁹⁵² Heller, Memorandum for the President, ‘Various Items.’

⁹⁵³ Heller, ‘Confidential Notes on Meeting with the President,’ 21 October 1963. Heller Papers. Box 6.

⁹⁵⁴ Alice O’Connor, *Poverty Knowledge: Social Science, Social Policy and the Poor in Twentieth-Century US History* (Princeton, NJ, 2001), 154-155. See too Gavin Wright, *Sharing the Prize: The Economics of the Civil Rights Revolution in the American South* (Cambridge, MA, 2013), 240. Wright demonstrates that, in 1964, the Johnson administration was conscious of dissociating the poverty programme with the issue of race.

1963. The first was the fact that, as he promoted and defended the tax cut that year, the CEA chairman grew conscious of the need to appease those who argued that the economy's problems stemmed more from structural rather than cyclical factors. He publicly maintained that a deficiency in overall demand was the chief cause of the economy's slack, but Heller admitted to Kennedy on June 8 that he and the Council "agree – and frequently say – that structural unemployment *is* serious."⁹⁵⁶ This followed comments made in support of the theory by Secretary of Labor Willard Wirtz.⁹⁵⁷ As Charles Killingsworth's arguments gained prominence in October 1963, Heller further viewed a poverty programme "as a kind of compromise with the structuralists."⁹⁵⁸ Reflecting this, the CEA chairman circulated a memo to CEA staff on October 10, which stressed the need to place more emphasis on structural rather than cyclical issues in the 1964 *Economic Report*.⁹⁵⁹ That document subsequently emphasised the need to address both structural unemployment and poverty, which demonstrates just how much the structural critiques of the tax cut influenced Heller's thinking about the latter.⁹⁶⁰

As well as the issue of structural unemployment, another factor prompted Heller's interest in a poverty programme. At some point in 1963, he started to see an attack on poverty as a way to increase federal aid to education, something that he had long championed.⁹⁶¹ As has been mentioned, Heller had estimated that the tax cut would be large enough to close the performance gap, but he believed that it was

⁹⁵⁵ O'Connor, *Poverty Knowledge*, 154-155. Emphasis added.

⁹⁵⁶ Heller, Memorandum for the President, 'Structural Unemployment Once Again.' Emphasis in the original.

⁹⁵⁷ Ibid.

⁹⁵⁸ Lampman, Interview with Michael L. Gillette, 24 May 1984, LBJL-OHC, 24.

⁹⁵⁹ Heller, Memorandum for the Professional Staff, 'Initial Assignments for the 1964 Annual Report,' 10 October 1963. Attached to Heller, Memorandum for the President, Untitled, 10 October 1963. POF. Box 76.

⁹⁶⁰ *The Economic Report of the President, 1964* (Washington DC, 1964), 55-112.

⁹⁶¹ See Holden and Biddle, 'Walter Heller and the Introduction of Human Capital Theory into Education Policy,' 3-4, 5, 27, 32-41.

important to expand the economy's potential alongside its actual rate of output.⁹⁶² Aware that the administration's Investment Tax Credit, Trade Expansion Act, and the 1964 Revenue Act's reductions for corporations, would all help to accomplish this, Heller also attached importance to investment in education. In October 1963, he pointed out that "the advance of knowledge of how to combine resources to achieve greater efficiency in production" had accounted for 36 percent of the growth in output per worker from 1929 to 1957.⁹⁶³ In short, Heller encouraged people "to view education through the lens of human capital theory."⁹⁶⁴

Yet, as he promoted this concept to policymakers in 1961 and 1962, Heller was disappointed at the Kennedy administration's lack of success at securing more investment in education. He asked Rashi Fein, a CEA staff member, to explore ideas for a new education programme in 1963.⁹⁶⁵ In December 1962, Fein informed Heller that it would take a major intervention from the president to convince policymakers to promote aid to education.⁹⁶⁶ It is likely, therefore, that Heller viewed the poverty issue as a means to secure this stronger presidential effort for aid to education.⁹⁶⁷ The fact that he appointed Lampman (a strong proponent of Human-capital theory) and later CEA staff economist Burton Weisbrod to develop the poverty programme lends credence to this suggestion. In his reply to Heller's request for ideas on an antipoverty initiative, Lampman proposed "investing in youth as the best way to fight poverty,"

⁹⁶² See Chapter Two of this thesis.

⁹⁶³ Heller, 'The Commitment to Economic Growth,' Address at the Forty-Sixth Annual Meeting of the American Council of Education, Washington D.C., 4 October 1963. POF. Box 76.

⁹⁶⁴ Holden and Biddle, 'Walter Heller and the Introduction of Human Capital Theory into Education Policy,' 33-34.

⁹⁶⁵ For Heller's decision to ask Fein see n.n., 'Minutes of Cabinet Committee on Economic Growth, 25 September 1962,' 9 October 1962. Heller Papers. Box 11.

⁹⁶⁶ Rashi Fein, Memorandum for Heller, 'The Big Issues in Aid to Education,' 5 December 1962. Heller Papers. Box 6.

⁹⁶⁷ Holden and Biddle, 'Walter Heller and the Introduction of Human Capital Theory into Education Policy,' 49.

which “reflected [the CEA’s] faith in education and human-capital theory.”⁹⁶⁸ Thus, although Heller undoubtedly viewed the poverty issue as a means to appease both the tax cut’s leftist critics, the structuralists, and implicitly aid the cause of civil rights, he also felt that it offered a route to increased economic potential through investment in education.⁹⁶⁹

III

Unsurprisingly, as the Council developed its antipoverty programme in 1963, educational aid to disadvantaged youths eventually emerged as a central theme.⁹⁷⁰ Additionally, Heller and Lampman believed that the poor were trapped in a cycle of poverty, so argued that it was imperative to provide them with more skills, training, healthcare, and nutrition so that they could exploit new job opportunities that would be created by the tax cut.⁹⁷¹ It is also worth noting that, from the outset, Heller and Lampman rejected redistributive policies as a means to solve the issue of poverty: not only would these measures fail to address the causes of the problem, it was also clear they would be unpopular.⁹⁷²

Despite settling upon this broad set of ideas for an antipoverty programme, the initiative lacked a concrete set of policies to tie it together. This made Kennedy nervous about promoting an attack on poverty. Arthur Schlesinger has suggested that, before his assassination, Kennedy decided that an attack on poverty “would be the centrepiece in his 1964 legislative recommendations.”⁹⁷³ The evidence suggests

⁹⁶⁸ Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 107.

⁹⁶⁹ Holden and Biddle, ‘Walter Heller and the Introduction of Human Capital Theory into Education Policy,’ 49.

⁹⁷⁰ James Patterson, *America’s Struggle against Poverty: 1900-1980* (Cambridge, MA, 1981), 136.

⁹⁷¹ Brauer, ‘Kennedy, Johnson, and the War on Poverty,’ 106.

⁹⁷² Lampman, Memorandum for Heller, ‘An Offensive Against Poverty,’ 10 June 1963. AHCEA, Volume II, Documentary Supplement, Part IV. Box 3. LBJL.

⁹⁷³ Schlesinger, *A Thousand Days*, 857. See too Theodore H. Andrews, ‘John F. Kennedy, Lyndon Johnson, and the Politics of Poverty, 1960-1967,’ PhD Thesis, Stanford University (1997), 5, 161-164. PQDT. Andrews suggests that reports on poverty in Appalachia in the fall of 1963 fully convinced JFK to launch a poverty initiative.

otherwise. In a meeting with the president on October 21, Heller noted that whilst it was “perfectly clear that he [Kennedy] is aroused about” the poverty issue, the CEA needed to “really produce a program to fill the bill” if he were “to run with it.”⁹⁷⁴ Likewise, in Heller’s very last meeting with the president, Kennedy again said that he would only do something on the poverty front if the CEA could “get a good program.”⁹⁷⁵ JFK subsequently told Heller to continue his efforts, a comment that the CEA chairman repeated to Lyndon Johnson on November 23.⁹⁷⁶

Johnson responded enthusiastically to this, telling his CEA chairman to “push ahead full-tilt on this project.”⁹⁷⁷ Heller admitted, though, that even after Kennedy’s assassination he did not have “the final answer to an attractive program.”⁹⁷⁸ Another point reflecting this is that, two weeks beforehand, he circulated a memorandum to various departmental heads that asked for suggestions on “imaginative *new* programs” for the antipoverty initiative.⁹⁷⁹ In particular, Heller said that he preferred ideas that maximised “the pride that individuals and communities can take in their own efforts to eradicate poverty,” noting that such an approach would minimise the idea that the poverty programme would be characterised by handouts.⁹⁸⁰ In response, the CEA was overwhelmed with recommendations, to the extent that the Bureau of the Budget helped analyse the suggestions.⁹⁸¹

By this point, Lampman had left the administration and CEA staff economists William Capron and Burton Weisbrod took over the role of firming up the poverty

⁹⁷⁴ Heller, ‘Confidential Notes on Meeting with the President,’ 21 October 1963.

⁹⁷⁵ Heller, ‘Notes on a Quick Meeting with the President and other Leading Members of the Kennedy Family,’ 19 November 1963. Heller Papers. Box 6.

⁹⁷⁶ Ibid.

⁹⁷⁷ Heller, ‘Notes on Meeting with President Johnson, 7.40 p.m., Saturday, November 23, 1963.’

⁹⁷⁸ Ibid.

⁹⁷⁹ Heller, Memorandum for Various Agency Heads, ‘1964 Legislative Programs for ‘Widening Participation in Prosperity’-An Attack on Poverty,’ 5 November 1963. AHCEA, Volume II, Documentary Supplement, Part IV. Box 3. LBJL. Emphasis in the original.

⁹⁸⁰ Ibid.

⁹⁸¹ Vinovskis, *The Birth of Head Start*, 33.

initiative.⁹⁸² They were conscious of the need to tie the programme's key component, namely educational grants for the young poor, into a far more comprehensive package. Therefore, Capron set up a meeting between Heller and David Hackett, who had chaired the President's Committee on Juvenile Delinquency.⁹⁸³ Capron decided to do so because, in response to Heller's earlier memorandum, Hackett suggested the idea of "community action" as a means to unify the administration's poverty effort.⁹⁸⁴ It placed "emphasis on the active participation of community residents in the formulation and administration of [poverty] programs."⁹⁸⁵ This appealed to Heller because it promoted local initiative and took into account the diverse manner in which poverty manifested itself across America.

Enthusiastic about Hackett's proposal, Heller wrote to Theodore Sorensen on December 20 and recommended that "a major 'Attack on Poverty'" be included in LBJ's 1964 legislative programme.⁹⁸⁶ The "major focus" of this would be "on youth," with community action forming its core component.⁹⁸⁷ This would place "major emphasis on the proposal to launch a number of major demonstration projects...each focused on a significant poverty situation."⁹⁸⁸ Heller anticipated launching 10 demonstration projects that would cost \$90 million overall in FY 1965. After the tax cut began to work, he argued that the government could spend an additional \$10 million annually on each demonstration project, meaning a total of \$245 million would be spent on community action programmes in FY 1969.⁹⁸⁹ Separately, Heller wanted educational grants for elementary and secondary education to supplement

⁹⁸² 'CEA's Role in Major Program Areas,' AHCEA, Chapter V, V-3. Box 1. LBJL.

⁹⁸³ William Capron, Interview in Gillette, *Launching the War on Poverty*, 16.

⁹⁸⁴ Ibid, 16. See too David Hackett, Memorandum for Heller, 'Attack on Poverty,' 1 December 1963. Legislative Background File. Economic Opportunity Act. Box 1. LBJL.

⁹⁸⁵ Katz, *The Undeserving Poor*, 120.

⁹⁸⁶ Heller, Memorandum for Sorensen, 'Poverty Program,' 20 December 1963. AHCEA, Volume II, Documentary Supplement, Part IV. Box 3. LBJL.

⁹⁸⁷ Ibid.

⁹⁸⁸ Ibid.

community action, arguing that \$50 million could be earmarked for this in FY 1965.⁹⁹⁰ At the heart of his anti-poverty proposal, then, was both investment in education and the use of community action.

For numerous scholars, this approach was too conservative and ultimately precipitated the implementation of a flawed poverty programme. In early 1964, Sargent Shriver took on the task of pushing the antipoverty programme through Congress and he modified Heller's proposal significantly. Nevertheless, these scholars have argued that when Heller headed the administration's antipoverty effort, the CEA chairman shunned proposals integral to its success. This ensured that Shriver did not consider them. Judith Russell has said that Heller too easily brushed aside the recommendations of Secretary of Labor Willard Wirtz. Both "repeatedly had sharp differences of opinion over the structural explanation of unemployment and consequently over the role and scale that jobs programs should play in the poverty program."⁹⁹¹ Throughout the poverty initiative's gestation, Wirtz "expected fully to use the War on Poverty as a way to get large-scale job creation."⁹⁹² According to Russell, an opportunity to push this through came when Johnson replaced Kennedy. However, Heller's belief that unemployment stemmed primarily from insufficient demand meant that he did not focus on direct job creation, something that could have helped many poverty-stricken and low skilled individuals, especially African Americans.⁹⁹³

Just as Russell argued that Heller too easily brushed aside the suggestions of

⁹⁸⁹ Ibid.

⁹⁹⁰ Ibid.

⁹⁹¹ Judith Russell, *Economics, Bureaucracy, and Race: How Keynesians Misguided the War on Poverty* (New York, 2003), 35.

⁹⁹² Lampman, Interview with Gillette, 21.

⁹⁹³ Russell, *Economics, Bureaucracy, and Race*, 35-36, 38-39. For others who have argued that an active labour market policy should have accompanied the Keynesian macroeconomic policies of the 1960s see Stein, *Running Steel, Running America*, 69-88; and Mucciaroni, *The Political Failure of Employment Policy, 1945-1982*, 6-7, 26-45.

Wirtz, the scholars Maris Vinovskis and Julie Jeffrey contended that the CEA chairman did not fully explore the various educational features that could have gone into the CEA's antipoverty initiative. This especially pertained to those advanced by representatives from the Department of Health, Education and Welfare (HEW).⁹⁹⁴ Vinovskis pointed out that in response to Heller's memorandum in early November, the Secretary of HEW called for greater emphasis to be placed upon education, so much so that he "wanted the new antipoverty initiative" to highlight "special education projects [that he had previously outlined] and recommended a separate bill to achieve these objectives."⁹⁹⁵ However, Heller, Capron, and Weisbrod prioritised the community action idea, a decision that prompted the Assistant Secretary of HEW to comment on December 26 that he was alarmed that educational policies formed such a small part of the poverty programme.⁹⁹⁶ Like Russell, both Vinovskis and Jeffrey argued that Heller unnecessarily minimised important contributions from other administration officials. This meant that Heller's anti-poverty proposal lacked components that Shriver may have regarded integral to its success.

These critiques do not appreciate what was politically possible in late 1963. Despite Russell's contention that there existed a small window of opportunity to promote a large-scale jobs programme, it is highly unlikely that Johnson would have explored this. After all, Heller had already sold him on the tax cut.⁹⁹⁷ Likewise, JFK had faced substantial difficulties promoting increased aid to education, so it is unsurprising that Heller, Capron, and Weisbrod chose not to endorse the HEW proposals. Furthermore, Jeffrey herself admitted that Shriver's bill actually stimulated

⁹⁹⁴ Vinovskis, *The Birth of Head Start*, 44-45; Julie Roy Jeffrey, *Education for Children of the Poor: A Study of the Origins and Implementation of the Elementary and Secondary Education Act of 1965* (Columbia, OH, 1978), 29-52.

⁹⁹⁵ Vinovskis, *The Birth of Head Start*, 33.

⁹⁹⁶ Wilbur Cohen, Memorandum for Sorensen, 'Legislative Program to Attack Poverty,' 26 December 1963. Wilbur Cohen Papers. Box 149. WHS.

“political interest in the kind of educational proposals discussed by Heller’s group.”⁹⁹⁸ Indeed, following Johnson’s landslide re-election in 1964, the ideas that HEW and the Council respectively advanced “appeared in modified but more impressive form as the ESEA [the Elementary and Secondary Education Act of 1965].”⁹⁹⁹ Rather than mishandling the anti-poverty effort, Heller was a key player in the successful drive to promote federal aid to education in the 1960s, having shrewdly used the antipoverty programme to help achieve this objective.¹⁰⁰⁰

Still, once implemented, the poverty programme did suffer from certain limitations. Despite this, Heller always defended it. Demonstrating this, in 1973 he cited a study that found that “nearly 600 community action agencies” had played a “constructive” role in eliminating poverty.¹⁰⁰¹ The programme in Minneapolis, he remarked, was “outstanding.”¹⁰⁰² Yet, as was demonstrated by the sociologist and future Democratic Senator Daniel Patrick Moynihan of New York, many community action programmes were “ill-fated.”¹⁰⁰³ First, the juvenile delinquency projects they were modelled on had “yielded no promising results.”¹⁰⁰⁴ Secondly, many suffered from poor organisation and underfunding, whilst others were marred by conflicts between the various institutions tasked with administering them.¹⁰⁰⁵ It is clear that despite what Heller later argued about community action, this component of the War on Poverty suffered from certain problems.

Nevertheless, the War on Poverty dramatized “the contemporary rediscovery

⁹⁹⁷ This was also because Kennedy failed to secure increased expenditures for public works in 1962.

⁹⁹⁸ Jeffrey, *Education for Children of the Poor*, 28.

⁹⁹⁹ Ibid, 28.

¹⁰⁰⁰ Holden and Biddle, ‘Walter Heller and the Introduction of Human Capital Theory into Education Policy,’ 49-54.

¹⁰⁰¹ Heller, ‘Let’s Tailor the Policies to Fit the Problems,’ 38.

¹⁰⁰² Ibid, 38.

¹⁰⁰³ Daniel Patrick Moynihan, *Maximum Feasible Misunderstanding: Community Action in the War on Poverty* (New York, 1969), xiii.

¹⁰⁰⁴ Matusow, *The Unraveling of America*, 123.

¹⁰⁰⁵ Ibid, 122-123; Moynihan, *Maximum Feasible Misunderstanding*, 131, 136, 144.

of poverty, which might not have happened so rapidly without the involvement of Heller.”¹⁰⁰⁶ This was important, as it “lift[ed] poverty from benign neglect to a place on the public agenda,” which “prepared Congress to accept other programs helping the poor, notably federal aid to education and health insurance for the indigent, or Medicaid, in 1965.”¹⁰⁰⁷ Far from mishandling the Kennedy-Johnson antipoverty effort, Heller played a crucial role in laying the foundations for many of the key liberal reforms of the 1960s. True, the War on Poverty ultimately failed in its goal of total eradication of deprivation, but it constituted a well-intentioned attempt to broadly distribute the fruits of 1960s growth to those who did not benefit directly from the 1964 tax cut.

IV

Ambitious though he may have been in fighting poverty in the early 1960s, this only took Heller temporarily away from his primary aim of creating jobs and securing full employment. With the tax cut passed in February 1964, Heller closely monitored its impact. Though he confidently predicted that it would increase the rate of output, the CEA chairman was initially stunned when, two months after its passage, there was “no quick reflection...[of this] in increased retail sales.”¹⁰⁰⁸ Writing to LBJ on May 11, Heller explained that sales in April had dropped for a second successive month.¹⁰⁰⁹ Fortunately, as further economic data became available from June onwards, the impact of the tax cut became clear. In a memorandum to Johnson on June 2, Heller said that circumstantial evidence undoubtedly showed “the

¹⁰⁰⁶ Patterson, *America's Struggle against Poverty*, 153.

¹⁰⁰⁷ *Ibid.*, 153.

¹⁰⁰⁸ Heller, Interview with McComb, 21 December 1971, 23.

¹⁰⁰⁹ Heller, Memorandum for the President, ‘Economic News Notes,’ 11 May 1964. WHCF. FG 11-2/A. Box 56. LBJL.

economy to be responding well to the tax cut.”¹⁰¹⁰ Business optimism and consumer spending had significantly increased during the first half of 1964, to the point whereby “the Administration’s January forecast of \$623 billion GNP [for the calendar year] *will* be realized or bettered.”¹⁰¹¹ Such an advance, Heller surely anticipated, was bound to yield a healthy fiscal dividend, one that would open up numerous possibilities for liberal reform.

If the jury had been out regarding the tax cut’s impact, to Heller the verdict was much clearer concerning the role that monetary policy should play as the Great Society took shape. Shortly after LBJ endorsed the tax cut in November 1963, the president had avowed his support for continued deployment of the ‘Super-Twist’ (the policy of buying heavily in the long-term market) in a telephone conversation with Heller on December 14.¹⁰¹² Nevertheless, not everyone subscribed to the CEA chairman’s view that long-term interest rates should remain as low as possible. At the turn of the year William McChesney Martin expressed concern that, with the impending enactment of the tax cut, inflation might increase. Reflecting this, Heller wrote to LBJ on December 29 to say that financial observers were “widely predicting that interest rates will rise in 1964,” something that he attributed to comments made by the Fed.¹⁰¹³ “The case for higher interest rates to date,” Heller said, “has been – quite rightly – that they were needed to overcome our balance-of-payments deficit...[yet Fed officials] were beginning to suggest that we need higher interest rates for domestic reasons – to meet a threat of inflation.”¹⁰¹⁴ An alarmed Heller

¹⁰¹⁰ Heller, Memorandum for the President, ‘Economic Impact of the Tax Cut,’ 2 June 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹⁰¹¹ Ibid. Emphasis in the original.

¹⁰¹² Johnson, Telephone Conversation with Heller, 14 December 1963. Tape: K6312.08, PNO: 38. MC.

¹⁰¹³ Heller, Memorandum for the President, ‘The Threat of Tighter Money,’ 29 December 1963. Heller Papers. Box 6.

¹⁰¹⁴ Ibid.

pointed out that “rising interest rates could put a real crimp on our expansion.”¹⁰¹⁵ Accordingly, he urged Johnson to bring forward the next Quadriad meeting.¹⁰¹⁶ He noted, too, that a rate increase in 1964 would undermine LBJ’s attempt to trim the FY 1965 budget, as this would result in higher interest payments on the national debt.¹⁰¹⁷

Johnson shared Heller’s concerns. He called a Quadriad meeting on January 10, during which Heller “argued that the simulative effects of the tax cut should not be killed off by a tightening of monetary policy.”¹⁰¹⁸ This paved the way for Johnson to impress upon Martin the urgency of following the ‘Super-Twist.’¹⁰¹⁹ To shore up Martin’s support after January 10, Heller used the 1964 *Economic Report* to highlight the dangers of higher interest rates.¹⁰²⁰ However, both these moves failed to have any long-term impact, for Martin’s fears of inflation reignited after the tax cut’s enactment. In March, this prompted Heller to express concern that the Fed may increase interest rates.¹⁰²¹ Though another Quadriad session ensured that this did not happen, the CEA chairman continued to worry about Martin’s actions throughout April, May, and June.¹⁰²² This prompted the Council to conduct a major study on price stability to show that excessive demand was not a potential danger.¹⁰²³

Ironically, the impact of the tax cut eventually dissuaded Martin from increasing interest rates. By June, it was clear that the economy was experiencing noninflationary growth. This forced Martin to admit that he had been “just plain

¹⁰¹⁵ Ibid.

¹⁰¹⁶ Ibid;

¹⁰¹⁷ Heller, Memorandum for the President, ‘Tight Money in 1964?’ 5 January 1964. WHCF. Confidential File. FG 11-3 (1963-65). Box 18. LBJL.

¹⁰¹⁸ ‘CEA’s Role in Fiscal Policy,’ AHCEA, Chapter II, II-40. Box 1. LBJL.

¹⁰¹⁹ Bremner, *Chairman of the Fed*. 188.

¹⁰²⁰ Ibid, 189; See too Heller, Memorandum for Jack Valenti, ‘Attached Column on Interest Rates,’ 3 February 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹⁰²¹ Heller, Memorandum for the President, ‘An Itchy Finger on Interest Rates,’ 2 March 1964. WHCF. Confidential File, FG 11-3 (1963-65). Box 18. LBJL.

¹⁰²² Heller, Memoranda for Johnson, ‘Quadriad Meeting 4.45 p.m., Thursday,’ and ‘Your Meeting With Chairman Martin,’ 17 March 1964 and 5 May 1964 respectively. Both in WHCF. FG 11-2/A. Box 56. LBJL.

wrong about how the tax cut would quickly fire up, not to say overheat, the economy.”¹⁰²⁴ During a luncheon meeting with Heller in July, the Fed chairman went as far as saying that he saw “great calm in the money markets.”¹⁰²⁵ As a result, the Central Bank’s policy was “strictly status quo.”¹⁰²⁶ Accordingly, Heller saw fit to call only one meeting of the Quadriad between July and November, a testament that his and Johnson’s efforts, coupled with the tax cut’s impact, convinced Martin to maintain an easy monetary policy.¹⁰²⁷ Martin did raise the discount rate in November by 0.5 percent, but the need to protect the payments deficit after the British increased their discount rate prompted this. Hence, as the tax cut took effect in 1964, Heller helped to ensure that monetary policy would not undermine that measure, an integral task given LBJ “considered a robust, non-inflationary economy so critical” to the Great Society.¹⁰²⁸

As Heller sought to persuade the Fed that the tax cut would not produce excessive demand, he also worked hard to prevent the onset of cost-push inflation. This task was important because, as CEA member John P. Lewis pointed out, cost-push inflation could “generate pressure on the Administration – and tempt the Fed – to attack the problem with restrictive monetary and fiscal policies.”¹⁰²⁹ In April 1963, as the tax cut was making its way through Congress, Heller had played an essential role in averting a second steel crisis.¹⁰³⁰ During 1964 the automobile industry posed the biggest threat to the administration’s wage-price guideposts. At a December 1963

¹⁰²³ CEA, ‘The Outlook for Price Stability in 1964,’ 8 July 1964. AHCEA, Volume II, Documentary Supplement, Part I. Box 1. LBJL.

¹⁰²⁴ Heller, Memorandum for the President, ‘Meeting with Bill Martin Yesterday,’ 17 July 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹⁰²⁵ Ibid.

¹⁰²⁶ Ibid.

¹⁰²⁷ Bremner, *Chairman of the Fed*, 183.

¹⁰²⁸ Califano Jr., *The Triumph and Tragedy of Lyndon Johnson*, 65.

¹⁰²⁹ Lewis, Memorandum for Heller, ‘Price-Wage Policy for 1964,’ 10 December 1963. AHCEA, Volume II, Documentary Supplement, Part II. Box 1. LBJL.

meeting Walter Reuther, head of the United Automobile Workers, informed Heller “that the UAW is going for a whopping wage increase” in its negotiations with automobile manufacturers the following summer.¹⁰³¹ Such a move, Heller warned LBJ, “would give a big shove to the wage-price [guideposts],” something Reuther was aware of.¹⁰³² It was thus imperative to convince Reuther to moderate the UAW’s wage demands.

What is also important about this incident, according to David Shreve, is that it undercuts the assessment that Johnson was indifferent to inflation during his presidency. On the contrary, with “fiscal and monetary policies geared toward full employment in 1964,” Shreve has noted, “Johnson latched onto the guidepost concept [to avert price rises].”¹⁰³³ These actions “represented the revolutionary side of the New Economics.”¹⁰³⁴ Agreeing with Heller that it was important to convince automobile workers to moderate their wage demands, Johnson issued a strong endorsement of the guideposts in the 1964 *Economic Report*.¹⁰³⁵ He also asked Heller, Defence Secretary Robert McNamara (a former Ford executive), and Willard Wirtz to work out how the administration should respond to Reuther’s statement. This resulted in the CEA chairman travelling “to [the] Ford headquarters to collect data” on March 23, before meeting with Reuther once again on April 9.¹⁰³⁶ “The upshot of the administration’s information gathering efforts,” Shreve noted, “was that

¹⁰³⁰ For Heller’s activities on this score see his and Gordon’s Interview with Hackman and Pechman, 39-42.

¹⁰³¹ Heller, Memorandum for the President, ‘Prices and Wages in 1964,’ 6 December 1963. Office Files of George Reedy. Box 22. LBJL.

¹⁰³² Ibid.

¹⁰³³ Shreve, ‘Lyndon Johnson and the Keynesian Revolution: The Struggle for Full Employment and Price Stability,’ in Mitchell B. Lerner and Shreve (ed.) *Looking Back at LBJ: White House Politics in a New Light* (Lawrence, KS, 2005), 181, 194 (quotation).

¹⁰³⁴ Shreve, ‘A Precarious and Uncertain Liberalism,’ 248.

¹⁰³⁵ *The Economic Report of the President, 1964*, 11.

¹⁰³⁶ Shreve, ‘A Precarious and Uncertain Liberalism,’ 250.

adherence to the guidepost principle suggested an auto industry price cut.”¹⁰³⁷ This, Heller deduced, would convince Reuther to reduce the UAW’s wage demands.

Following six months of negotiations, such an agreement never materialised, as automobile producers believed that price cuts would put their profit margins in jeopardy. Judging that it would take an intervention by LBJ to convince the producers to cut prices, Heller urged him on June 4 to speak personally with the head of General Motors. Johnson refused on grounds that he did not feel that such a plan would work.¹⁰³⁸ As a result, on September 12 UAW announced annual wage increases of 4.7 percent, which “knocked a giant hole in the credibility of the wage-price guidelines.”¹⁰³⁹ Despite this, Heller told Johnson that while there would be “some cost-push pressure on prices,” he was confident that “rising productivity, growing plant and manpower capacity, sharp competition – and an administration that keeps business and labour well aware of their responsibilities – add up to a prospect for maintaining a good, though not perfect, record on the price and cost front.”¹⁰⁴⁰ Furthermore, despite the president’s reluctance to intervene personally in the automobile settlement, the lead up to the incident did show his determination to keep inflation under control. It also impelled him to enforce the guideposts in 1965, both of which help show that Johnson took inflation seriously.¹⁰⁴¹

Despite Heller’s failure to influence the wage-price dispute, the pressure that he placed upon Martin, coupled with the good economic picture, both ensured that the Fed refrained from engaging in restrictive policies because of the automobile settlement. In fact, such was the pace at which the economy had picked up by the

¹⁰³⁷ Ibid, 250.

¹⁰³⁸ Johnson, Telephone Conversation with Heller, 4 June 1964. Tape: WH6406.02, PNO: 13, Conversation: 3627. MC.

¹⁰³⁹ Bremner, *Chairman of the Fed*, 193.

¹⁰⁴⁰ Heller, Memorandum for the President, ‘The Outlook for Price Stability in 1964,’ 8 October 1964. Heller Papers. Box 6.

second half of 1964, the CEA chairman began to press a new and innovative policy upon Johnson. This, Heller said, would “get funds to the State and local units where much of the Great Society must be built.”¹⁰⁴² Some context is necessary to understand this policy. By the summer of 1964, Heller had grown concerned about the possibility of “renewed ‘fiscal drag.’”¹⁰⁴³ The federal tax system was “so powerful,” he pointed out, that despite cutting taxes it would annually generate “about 6 billion dollars more revenue than it did in the year before.”¹⁰⁴⁴ Unless the US “match[ed] that \$6 billion of cash ‘take’ from the public with \$6 billion of federal cash ‘outflow’ to the public,” he warned, “we gradually begin to tighten the fiscal brakes.”¹⁰⁴⁵ Heller explained that there were several ways to offset this. The government could either increase spending, cut taxes, or automatically “route more funds to State and local governments.”¹⁰⁴⁶

For several reasons, Heller preferred the final option. Firstly, he had always expressed concern about the growing financial pressures upon state-local governments.¹⁰⁴⁷ Unsurprisingly, he was alarmed by 1964 that the states were “facing ever-growing and urgent demands for public services.”¹⁰⁴⁸ Secondly, Heller’s experience developing the withholding taxation system during World War II had demonstrated to him “the power of setting things up to work automatically,” which is another reason why ‘revenue-sharing’ appealed to him.¹⁰⁴⁹ Additionally, Heller saw in revenue-sharing a way to bolster the Great Society: not only would it enable the

¹⁰⁴¹ Shreve, ‘A Precarious and Uncertain Liberalism,’ 253-254.

¹⁰⁴² Heller, Memorandum for the President, ‘Goldwater’s Latest Fiscal ‘Me-Too,’ 18 September 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹⁰⁴³ n.n., ‘No More Depressions? Interview with the President’s Economic Adviser,’ *US News & World Report*, 29 June 1964, 59. WHCF. FG 11-2/A. Box 56. LBJL.

¹⁰⁴⁴ *Ibid.*, 59.

¹⁰⁴⁵ *Ibid.*, 59.

¹⁰⁴⁶ *Ibid.*, 59.

¹⁰⁴⁷ See Chapter Two of this thesis.

¹⁰⁴⁸ n.n., ‘No More Depressions,’ 59.

¹⁰⁴⁹ Johnston, Interview with the Author.

government to distribute funds more efficiently to local units, a large portion of the money “would be used to pay for social welfare and educational programs.”¹⁰⁵⁰

Inspired by the economic, practical, and social benefits of revenue-sharing, Heller urged Johnson on May 12 to “do more to reconcile” both “the fiscal squeeze on State-local governments” and “the huge and growing tax revenues of the federal government.”¹⁰⁵¹ Knowing that economic arguments alone would not entirely persuade the president, he pointed out that it would “be [a] mighty attractive” programme for taxpayers, who would be saved from making increased contributions towards state-local finances.¹⁰⁵² He also knew that, having enacted the tax cut and launched the War on Poverty in early 1964, LBJ was “on the prowl for new initiatives.”¹⁰⁵³ Since revenue-sharing would undercut Republican ‘big government’ attacks against the Democrats, the CEA chairman viewed it as a potentially important issue for Johnson’s re-election.¹⁰⁵⁴

In his memorandum to LBJ on May 12, Heller asked for “a green light” to “push ahead with more specific approaches and proposals [for revenue-sharing].”¹⁰⁵⁵ Enthusiastic about the idea, LBJ gave permission to go ahead. Therefore, the CEA chairman asked the Brookings economist Joseph Pechman, an expert on public finance, to develop a plan. In his response two weeks later, Pechman outlined a proposal where the states would be sent back “2 percentage points of the individual

¹⁰⁵⁰ Sobel, *The Worldly Economists*, 139. It is worth noting that Heller viewed the grants as having no-strings-attached, but given the fact that state-local finances were under increasing pressure due, in large part, to education and welfare expenses, the CEA chairman understood that state governments would likely spend the grants on education and welfare.

¹⁰⁵¹ Heller, Memorandum for the President, ‘Federal Relief for State-Local Taxpayers?’ 12 May 1964. WHCF. FG 11-2/A. Box 56. LBJL. Emphasis in the original.

¹⁰⁵² Ibid.

¹⁰⁵³ Heller, Interview in Hargrove and Morley, 213.

¹⁰⁵⁴ Evans and Novak, *Lyndon B. Johnson*, 501.

¹⁰⁵⁵ Heller, Memorandum for the President, ‘Federal Relief for State-Local Taxpayers?’

and corporate income taxes” on an annual basis.¹⁰⁵⁶ Importantly, such a proposal would have an equalizing effect, since the funds would be based on “[each] state’s expenditures for state and local activities,” as well as “the ratio of the state’s per capita income to the national average.”¹⁰⁵⁷ Though the plan would incentivise “states and local governments to increase their expenditures,” the total amount given to them would only match 10 percent of their outlays.¹⁰⁵⁸ This ensured it provided no “invitation to profligacy.”¹⁰⁵⁹ Because it would be difficult to administer the money centrally, Pechman recommended a Trust Fund oversee the dispersal of funds.¹⁰⁶⁰

Impressed with Pechman’s response, Heller at once sent it to Johnson. One day later, he provided the president with further data outlining the pressing need for revenue-sharing.¹⁰⁶¹ Undoubtedly concerned by these figures, Johnson heeded a suggestion by Heller to establish a secret task force headed by Pechman, which would formulate a more concrete revenue-sharing proposal. “The principal reason for secrecy in this case,” two scholars have noted, “was to inhibit the organization of early opposition to [the revenue-sharing plan].”¹⁰⁶²

Not long after establishing the task force, however, revenue-sharing was “caught up in presidential politics.”¹⁰⁶³ As a result, Johnson refused to embrace it. The chain of events that precipitated this was set in motion when Barry Goldwater, the Republican candidate for the 1964 election, outlined his own revenue-sharing initiative that summer. In response, Heller urged Johnson to “unveil our approach to the problem,” noting that Goldwater’s plan contained numerous problems that LBJ

¹⁰⁵⁶ Pechman, ‘A Method of Sharing Federal Revenues with the States,’ 26 May 1964. Attached to Pechman to Heller, 26 May 1964. Gordon Papers. Box 36.

¹⁰⁵⁷ Ibid.

¹⁰⁵⁸ Ibid.

¹⁰⁵⁹ Ibid.

¹⁰⁶⁰ Ibid.

¹⁰⁶¹ Heller, Memorandum for the President, ‘Growth of Federal Versus State-Local Taxes, Debt and Spending,’ 27 May 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹⁰⁶² Welborn and Burkhead, *Intergovernmental Relations in the American Administrative State*, 167.

could exploit.¹⁰⁶⁴ One was that the Republican programme was less equitable than Pechman's because it proposed to distribute funds based on the amount originally contributed by each state, thereby providing the larger states with a disproportionate share.¹⁰⁶⁵ Goldwater also proposed to abolish the existing system of programmatic grants in return for the implementation of his proposal. This, Heller said, would enable the administration to court the support of numerous interest groups whose members benefited from those schemes.¹⁰⁶⁶

Though Johnson, in light of Goldwater's proposal, was "particularly interested in having a plan that would distribute funds on a more equitable basis," he refused to publicly discuss revenue-sharing throughout September and October.¹⁰⁶⁷ Instead, he simply acknowledged that his administration was exploring the possibility of improving federal, state, and local economic relations.¹⁰⁶⁸ Heller grew concerned that the president would miss an opportunity to exploit the issue in the run up to the election, a point that he raised with presidential aide Walter Jenkins in October. Thinking that, after doing so, Jenkins went on to secure "an oral commitment" from LBJ that endorsed revenue-sharing, Heller leaked details of the Pechman Task Force to the press.¹⁰⁶⁹ Though he made it clear that Johnson had not "signed onto the specifics of this plan," the *New York Times* subsequently carried a story saying that the president had.¹⁰⁷⁰ This subjected the idea "to premature attack from pressure groups" and "mortally wounded it."¹⁰⁷¹

Heller's leak angered the president. Johnson said that he had not given Jenkins

¹⁰⁶³ Ibid, 167.

¹⁰⁶⁴ Heller, Memorandum for the President, 'Goldwater's Latest Fiscal 'Me-Too.'

¹⁰⁶⁵ Ibid.

¹⁰⁶⁶ Ibid.

¹⁰⁶⁷ Heller, Interview in Hargrove and Morley, 213-214.

¹⁰⁶⁸ Ibid, 213-214.

¹⁰⁶⁹ Ibid, 214.

¹⁰⁷⁰ Ibid, 214.

¹⁰⁷¹ Evans and Novak, *Lyndon B. Johnson*, 501.

permission to fix his name to the Pechman Task Force.¹⁰⁷² Whilst a certain amount of blame for this lay with Jenkins, Heller, too, was guilty of misjudgement. As far back as July 11, the president reprimanded Heller for discussing revenue-sharing with the press. This warning came after LBJ read an article in a national newspaper that quoted Heller as saying Johnson was considering revenue-sharing. “God, Walter, this is dynamite politically,” LBJ said, “[I’m] trying to be economical and the headline is ‘Johnson Trying to Make Up His Mind About What The Hell To Do With \$18 billion’...I don’t want to get committed to an act until I’ve seen and looked at it and then you can make it public when I embrace it.”¹⁰⁷³ Given the clarity with which LBJ made this point back in July, Heller should have gone to the president directly for an endorsement in October. He did try to salvage the situation by insisting that there had been “*a very good reception*” to Pechman’s proposals.¹⁰⁷⁴ However, Johnson unsurprisingly took the decision to “put the Heller[-Pechman] Plan in a remote filing cabinet to be forgotten for a long and indefinite period.”¹⁰⁷⁵ Heller’s misjudgement was in large part responsible for Johnson’s refusal to make revenue-sharing a central feature of the Great Society.¹⁰⁷⁶

V

Shortly after this, Heller sent Johnson his letter of resignation. He would be leaving “the world’s best-job-for-an-economist” after November’s Presidential

¹⁰⁷² Heller, Interview in Hargrove and Morley, 213-214.

¹⁰⁷³ Johnson, Telephone Conversation with Heller, 11 July 1964. Tape: WH6407.07, Conversation: 4219. MC.

¹⁰⁷⁴ Heller, Memorandum for the President, ‘Federal Revenues for the States,’ 30 October 1964. WHCF. FG 11-2/A. Box 56. LBJL. Emphasis in the original.

¹⁰⁷⁵ Evans and Novak, *Lyndon B. Johnson*, 501.

¹⁰⁷⁶ This did not stop him, however, from continuing to argue for revenue-sharing in the 1960s, though Johnson remained unimpressed. See Heller, Memorandum for the President, ‘That Blankety-Blank Revenue-Sharing Plan,’ 16 December 1966. Name File H. [Walter W. Heller] [Henceforth NFHWH]. Box 219. LBJL; and Heller, Memorandum for the President, ‘The ‘Heller Plan,’ 26 July 1965. Heller Papers. Box 15.

Election.¹⁰⁷⁷ This came as no surprise to the president, whom the CEA chairman had told as far back as February that he would leave in November.¹⁰⁷⁸ Even though their relationship was strained over the revenue-sharing issue, Heller informed LBJ that it was “going to be mighty tough to leave your side.”¹⁰⁷⁹ He assured him that he would “be at your beck and call” back in Minnesota.¹⁰⁸⁰ Three reasons, Heller later remarked, compelled him to leave. Firstly, when he accepted the post in December 1960, Heller wanted to serve only three years. Reflecting this, he had sent his family back to Minnesota before Kennedy’s assassination, but agreed to stay on at Johnson’s request.¹⁰⁸¹ Secondly, his wife’s health (which was better suited to Minnesota’s weather) and the fact that he had taken out a loan of approximately \$15,000-\$20,000 to cover the cut in pay that he took when he became CEA chairman, both necessitated Heller’s return to his more lucrative academic job in a better climate.¹⁰⁸² Heller also felt that if he “wanted to maintain essentially an academic career” then he “ought to go back,” or else he feared becoming a hostage to the political environment.¹⁰⁸³

Not mentioned by Heller in his resignation letter to Johnson (or retrospectively), is that he may have left the White House after growing concerned about the possible economic impact of America’s increased involvement in Vietnam. “My Dad said to me,” Eric Heller recalled, “that ‘Guns and Butter is what Johnson wants and it’s going to cause a horrible problem down the road in the economy and I don’t want to be seen as part of it.’ That was the ultimate reason he left.”¹⁰⁸⁴ Certain evidence supports this assertion. Following the Gulf of Tonkin incident on August 2,

¹⁰⁷⁷ Heller, Memorandum for the President, Untitled, 30 October 1964. NFHWH. Box 219. LBJL.

¹⁰⁷⁸ Heller, Interview with McComb, 21 December 1971, 24.

¹⁰⁷⁹ Heller, Memorandum for the President, Untitled, 30 October 1964.

¹⁰⁸⁰ Ibid.

¹⁰⁸¹ Heller, Interview with McComb, 21 December 1971, 57.

¹⁰⁸² Ibid, 57, 59.

¹⁰⁸³ Ibid, 58.

¹⁰⁸⁴ Eric Heller, Interview with the Author.

Heller told Gardner Ackley and John P. Lewis that although no one had asked the Council “to make a round-up of the possible economic impact of the Viet Nam flare up, I don’t think it would be a good idea to be caught flat-footed if things [do] flare up.”¹⁰⁸⁵ This was because commodity prices had increased.¹⁰⁸⁶ So concerned was Heller about the potential economic impact of Vietnam at this point, he told Ackley and Lewis “to keep close track of spot prices, commodity features, etc.” and made a move to become a member of the National Security Council.¹⁰⁸⁷ It is not entirely clear whether Heller’s concerns about the economic impact of Vietnam impelled him to leave the LBJ administration. Significantly, he urged expansionary policies upon Johnson immediately after leaving the White House (something that the next chapter will demonstrate). Nevertheless, Heller’s concern about the potential economic impact of Vietnam in the summer of 1964 proved prescient. This was especially the case given the key role played by that conflict in undermining the legitimacy of Keynesian liberalism, right after it reached the zenith of its influence during Heller’s CEA chairmanship.

Before turning to Heller’s response to this development, it is essential to reflect upon his final year in the White House. His crowning achievement was undoubtedly the passage of the 1964 Revenue Act, which consolidated the Keynesian revolution in America. Heller played an important role in securing the eventual passage of that measure. At the same time, he was central to the development of the War on Poverty, an initiative that began under Kennedy. He further made certain that, as Johnson’s Great Society took shape in 1964, monetary policy did not hamper its development. In fact, Johnson told his vice-president Hubert Humphrey that Martin

¹⁰⁸⁵ Heller, Memorandum for Ackley and Lewis, ‘Economic Impact of Viet Nam,’ 7 August 1964. Records of the Council of Economic Advisers, Roll 9. LBJL.

¹⁰⁸⁶ Ibid.

would have changed Fed policy “half a dozen times” had it not been for Heller.¹⁰⁸⁸ Meanwhile, as fiscal drag became a concern in the summer of 1964, Heller tried to convince LBJ to channel funds back to the states. Whilst Johnson rejected this plan, partly because of Heller’s misguided leak, a review of Heller’s activities in 1963-64 demonstrates that he was a central figure in the development of the Great Society. It is unsurprising that Johnson called Heller one of his three “most valuable” advisers at the end of 1964.¹⁰⁸⁹ It also demonstrates why LBJ relied upon Heller after the latter left the White House, for the former regarded the Minnesotan’s counsel as indispensable once Vietnam threatened to unravel all that both men had created.

¹⁰⁸⁷ Ibid; Heller, Memorandum for Jack Valenti, ‘National Security Council Activity,’ 7 August 1964. Heller Papers. Box 3.

¹⁰⁸⁸ Johnson, Telephone Conversation with Humphrey, 5 November 1964. Tape: WH6411.09, PNO: 07, Conversation: 6244. MC.

Chapter Seven

Guns, Butter, and Milton Friedman

Two years after he left his post as CEA chairman, Walter Heller boasted, “Economics has come of age in the 1960’s. Two Presidents have recognized and drawn on modern economics as a source of national strength and Presidential power.”¹⁰⁹⁰ Such exuberance confirmed that Heller and his contemporaries *were* enjoying their heyday during the mid-1960s thanks to the results of the 1964 Revenue Act. In September 1965, the CEA’s Arthur Okun proclaimed that every dollar of tax reduction had produced 1.82 dollars of spending in 1964-65.¹⁰⁹¹ Resultantly, real GNP grew by 5.5 percent and 6.3 percent respectively, unemployment fell to 4.1 percent (with inflation running low) and the performance gap closed.¹⁰⁹² These conditions facilitated the consolidation of the Great Society, which expanded rapidly in the mid-1960s. Heller had much to celebrate after leaving the White House, jesting in 1966 that the tax cut had raised the prestige of economists more than it had the level of GNP.¹⁰⁹³ Outside the economics profession, too, came positive appraisals of the new economics. In 1966, the *New Yorker* published a cartoon of an upper middle-class couple reading the news in their living room, with the wife saying to her husband that, although she did not know of Walter Heller, she was thankful he was a presidential adviser.¹⁰⁹⁴

Of course, Heller was no longer part of the Johnson administration. Yet, he continued to advise Lyndon Johnson as Keynesian liberalism reached its peak in the mid-1960s. To his surprise, Heller discovered that managing an economy operating at

¹⁰⁸⁹ Ibid. The other two advisers were Robert McNamara and Dean Rusk.

¹⁰⁹⁰ Heller, *New Dimensions of Political Economy*, 1.

¹⁰⁹¹ Okun, ‘Measuring the Impact of the 1964 Tax Reduction,’ Remarks before the American Statistical Association, Philadelphia, 10 September 1965. Heller Papers. Box 4. JFKL.

¹⁰⁹² Morgan, *Deficit Government*, 95.

¹⁰⁹³ Heller, ‘The Future of Our Fiscal System,’ *The Journal of Business*, 38:3 (Jul. 1965), 235.

¹⁰⁹⁴ This was reprinted in Robert Smith, ‘His Ideas Shaped 2 Presidents,’ *The Minneapolis Tribune*, 20 November 1966. Copy in Heller Papers. Box 10. UoM.

full employment posed more of a challenge than fixing one beset by chronic slack. In 1967, Heller confidently asserted that Keynesian advisers had at their disposal the means to “fine-tune” a full employment economy in order to stifle inflationary pressures.¹⁰⁹⁵ At this very moment, the Vietnam War disproved his words. Then, Heller and his colleagues had to address the first serious intellectual challenge to the legitimacy of the new economics. This came in the form of monetarist theory, which gained credence in the 1960s thanks to the University of Chicago’s Milton Friedman. Accordingly, this chapter assesses the role of Heller during the initial stages of Keynesianism’s eclipse in the mid-to-late 1960s. It challenges the conventional perspective that Johnson was mostly responsible for this, positing instead that Heller and others deserve a sizable portion of the blame. It will also examine how well Heller responded to Friedman’s rise to prominence.

I

When Heller left the CEA in November 1964, the expansion from the tax cut looked likely to peter out after mid-1965. This deeply concerned him. Writing to Johnson as far back as July 24, 1964, Heller had explained that while the economy would continue expanding up to early 1965 he was unable to “see where the steam needed for further expansion in late 1965 and 1966” was “going to come from.”¹⁰⁹⁶ Both “business and academic economists” increasingly saw “a slowdown or even a downturn after mid-1965.”¹⁰⁹⁷ As a result, Heller argued for the removal of excise taxes, notably on gasoline and alcohol, implemented by Franklin Roosevelt in 1933.¹⁰⁹⁸ Enacted as temporary measures to help balance the budget, these had

¹⁰⁹⁵ Heller and Milton Friedman, *Monetary vs. Fiscal Policy* (New York, 1969), 34.

¹⁰⁹⁶ Heller, Memorandum for the President, ‘What the Trained Eye Begins to See Beyond Mid-1965,’ 25 July 1964. Gordon Papers. Box 36.

¹⁰⁹⁷ *Ibid.*

¹⁰⁹⁸ *Ibid.*; Heller, Memorandum for the President, ‘Excise Tax Repeal and the Platform: Secretary Dillon’s Memorandum of July 23,’ 30 July 1964. Gordon Papers. Box 36.

remained in place for the next thirty-one years. Due to his fears that the expansion would slow down in mid-1965, Heller was “strong for getting rid of them.”¹⁰⁹⁹ In September, he followed up his July memoranda with statistical evidence that proved the need for these tax cuts, telling Johnson that if the US was operating at “4 percent unemployment the economy could produce \$20 to \$25 billion a year more.”¹¹⁰⁰

Fearing the danger that lay ahead, Johnson agreed to ask Congress in January 1965 to repeal FDR’s excise taxes. However, an October review of the president’s projected FY 1966 expenditures compelled Heller to stress the need for further expansionary measures. Conscious that most of the stimulus from the 1964 tax cut came in its first year, Heller predicted a “continued good advance through early 1965 with gains in GNP of \$10 billion per quarter,” but “smaller gains thereafter of \$7 billion per quarter.”¹¹⁰¹ This “would not keep pace with [the economy’s expanding] potential,” so “unemployment would edge above 5% by year-end.”¹¹⁰² Heller thus noted Johnson’s “recent promise of an excise tax cut” was only “one step toward a fiscal stimulus for FY 1966.”¹¹⁰³ He recommended “increased government expenditures, further tax cuts, or some combination of the two.”¹¹⁰⁴ The Fed’s decision to increase the discount rate in November enhanced the importance of doing so. As Heller told Johnson, “In the face of a higher discount rate...our best bet to sustain prosperity in 1965-66 lies in the excise tax cuts, [and other measures]...even if this means a FY 1966 deficit in the general range of the FY 1965 deficit.”¹¹⁰⁵

¹⁰⁹⁹ Heller, Interview with McComb, 21 December 1971, 40.

¹¹⁰⁰ Heller, Memorandum for the President, ‘Economic Round Up,’ 24 September 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹¹⁰¹ Heller, Memorandum for the President, ‘Economic Outlook for 1965: The August Troika Revisited,’ 6 October 1964. WHCF. FG 11-2/A. Box 56. LBJL.

¹¹⁰² Ibid. These were conclusions reached two months previously, but Heller explained in this memo that he saw hardly any need to alter them in October.

¹¹⁰³ Ibid.

¹¹⁰⁴ Ibid. For the quotation see ‘CEA’s Role in Fiscal Policy,’ AHCEA, Chapter II, II-11, Box 1. LBJL.

¹¹⁰⁵ Heller, Memorandum for the President, ‘Various Items,’ 10 December 1964. WHCF. PE 2. Box 8. LBJL.

Gardner Ackley, who replaced Heller as CEA chairman, shared these concerns. In a memorandum to Johnson on March 3, 1965, Ackley expressed alarm that the jobless rate had edged up.¹¹⁰⁶ Heller thus told Johnson that it was imperative to get “the most good out of the excise tax cuts” and advised the president to urge the business community to pass them “through to the consumer in the form of price cuts.”¹¹⁰⁷ This was something that Johnson did, for when he signed into law \$4.2 billion of excise tax cuts on June 22 he “called on ‘every manufacturer and every retailer in this country’ to pass on the full amount of the excise cut to consumers.”¹¹⁰⁸ In spite of this, further factors made Heller and Ackley argue for more stimuli. Increases in payroll taxes, for example, were due to go into effect in early 1966.¹¹⁰⁹ Looking ahead, Ackley urged “a big second instalment” of excise tax cuts on January 1 1966, whilst Heller and LBJ “began to discuss whether we shouldn’t have some sort of a little income tax cut at the bottom of the scale...if the quivers in the economy turned into a softness, and again, a growing gap.”¹¹¹⁰

As it turned out, Johnson’s decision to send combat troops to Vietnam in the summer of 1965 provided the stimulus that Heller and Ackley craved. Before examining their reaction to this effect, it is important to note that Heller’s decision to urge expansionary policies upon Johnson from November 1964 through to the summer of 1965 undercuts the assertion that he left the Johnson administration because he could foresee both LBJ’s decision to fight in Vietnam and the inflationary impact that it would have. Had Heller anticipated Johnson’s Americanisation of the

¹¹⁰⁶ Ackley, Memorandum for the President, ‘Economic News Notes,’ 3 March 1965. Heller Papers. Box 6. JFKL.

¹¹⁰⁷ Heller, Memorandum for the President, ‘Getting the Most Good Out of the Excise Tax Cuts,’ 13 January 1965. Heller Papers. Box 6. JFKL.

¹¹⁰⁸ Thomas J. Foley, ‘Excise Cuts Take Effect Today,’ *Los Angeles Times*, 22 June 1965, 1. PQHN.

¹¹⁰⁹ Ackley, Memorandum for the President, ‘Thinking Ahead on Economic Problems,’ 5 May 1965. Heller Papers. Box 15. JFKL.

¹¹¹⁰ Ackley, Memorandum for the President, ‘Excise Tax Reduction,’ 11 May 1965. Heller Papers. Box 15. JFKL; Heller, Interview with McComb, 21 December 1971, 41.

Vietnam War, he would not have pressed the president to undertake expansionary economic measures. LBJ's decision to send troops to Vietnam also pleased Heller and Ackley, especially as projected expenditures indicated that there would only be a "moderate" build-up of the armed forces.¹¹¹¹ "We are certainly not saying that a Vietnam crisis is just what the doctor ordered for the American economy," Ackley wrote, "But on a coldly objective analysis, the over-all effects are most likely to be favourable to our prosperity."¹¹¹²

Heller agreed with this assessment. Admittedly, he was more cautious than Ackley about the potential danger of Vietnam. In September 1965, he forwarded Johnson a newsletter that he penned for the National City Bank of Minneapolis (NCBM), a new institution whose board Heller joined after leaving the CEA. In his newsletter, the Minnesotan explained that there "is little doubt that it [Vietnam] will be a substantial and growing factor in the economic outlook for months to come."¹¹¹³ If that conflict caused a \$3 – 5 billion increase in federal purchases by the end of 1966, the "added stimulus could be readily absorbed by the economy."¹¹¹⁴ A \$6 – 9 billion increase would "pretty well use up the economy's margin of unused and new resources," whilst \$10 – 15 billion "might disrupt our good record on prices and call for anti-inflationary action." This included a tax increase.¹¹¹⁵

Heller's more cautious tone proved prescient: during the fall of 1965 he could see "that the economy was getting a very considerable stimulus," not least because prices edged up.¹¹¹⁶ Writing to presidential aide Jack Valenti, Heller warned that the

¹¹¹¹ Ackley, Memorandum for the President, 'Economic Aspects of Vietnam,' 30 July 1965. WHCF. FG 11-3. Box 57. LBJL.

¹¹¹² Ibid.

¹¹¹³ Heller, 'The Economic Outlook,' *National City Bank of Minneapolis* [Henceforth *NCBM*], 1 September 1965. Attached to Heller to Johnson, 8 September 1965. WHCF. BE 5. Box 23. LBJL.

¹¹¹⁴ Ibid.

¹¹¹⁵ Ibid.

¹¹¹⁶ Heller, Interview with McComb, 21 December 1971, 42.

“rapid buildup for Vietnam is coming on top of an economy that has been expanding for five years. It may well be reaching the point where a temporary tax boost is a sensible thing to do to keep total demand in balance with total supply.”¹¹¹⁷ Others agreed. William McChesney Martin, for example, increased the discount rate in December 1965, after which LBJ had Heller flown down to his Texas ranch to discuss how to respond. There, Johnson, Heller and others had “a marathon discussion of economic policy,” during which Johnson proposed rescinding the excise tax cuts that he had just passed.¹¹¹⁸ Heller opposed doing so, telling Johnson “those excise tax things we just got rid of were such miserable and illogical taxes.”¹¹¹⁹ Though he said that it might be a good idea to rescind some of them early in 1966 (advice that Johnson heeded), Heller explained that what the economy “really need[s] is a surtax [of around 10 percent] on the individual income.”¹¹²⁰ Such a measure would require taxpayers to pay an extra ten cents on every dollar taxed. Ackley agreed, telling Johnson that if expenditures for the FY 1967 budget reached \$110 - \$115 billion then a tax surcharge would be imperative.¹¹²¹

Johnson refused to follow this advice. He reasoned that a surcharge would be tantamount to requesting a war tax, something that LBJ feared because conservatives in Congress would respond by demanding a sizeable cutback in Great Society expenditures.¹¹²² By this point, the president and Defence Secretary Robert McNamara had decided to hide the true costs of the war from both Congress and the CEA, in the belief that they could pursue both guns and butter without a tax

¹¹¹⁷ Heller to Valenti, 29 December 1965. NFHWH. Box 219. LBJL.

¹¹¹⁸ Heller, Interview with McComb, 21 December 1971, 42 (quotation), 43.

¹¹¹⁹ Ibid, 43.

¹¹²⁰ Ibid, 44.

¹¹²¹ Ackley, Memorandum for the President, ‘Policy Implications of the Budget,’ 17 December 1965. Gardner Ackley Papers. Reel 14. LBJL.

¹¹²² Morgan, *Deficit Government*, 110.

increase.¹¹²³ Reflecting this, Johnson's Budget Message of January 1966 estimated that Vietnam would cost just \$10.3 billion, projected a total level of expenditures for FY 1967 of just over \$112.8 billion, and indicated that the war would end by July 1967.¹¹²⁴ For some observers, LBJ's refusal to heed Heller and Ackley's call for a tax increase was the result of presidential manipulation and deceit, which ultimately opened the inflationary floodgates.¹¹²⁵ Others have advanced a different interpretation. For David Shreve, Johnson scholars have "transmitted an all too simple story of 'guns and butter,' short-sighted manipulation, and incipient inflation."¹¹²⁶ Shreve has demonstrated that Johnson vigorously sought to impose the wage-price guidelines – developed during Heller's CEA chairmanship – to keep cost-push inflation in check as the war expanded.¹¹²⁷ Donald Kettl, too, has argued that those who advised LBJ deserve much of the blame for the failure to keep inflation in check. These individuals proved "uneven in their support for a tax increase" or suggested "guns and butter did not seem like incompatible choices."¹¹²⁸

Heller was one such person. Writing to Johnson on December 12, he told the president that he "might be weary of arguments for keeping the Great Society growing – modestly, but growing – even if Vietnam costs reach \$10 to \$15 billion a year and require a tax increase. But I hope that the hardheaded economic and fiscal

¹¹²³ Matusow, *The Unraveling of America*, 160.

¹¹²⁴ Johnson, 'Annual Budget Message to the Congress, Fiscal Year 1967,' 24 January 1966. APP.

¹¹²⁵ See David Halberstam, 'How the Economy Went Haywire,' *The Atlantic Monthly*, 230:000003 (Sept. 1972), 56. PQC; Rowen, *Self-Inflicted Wounds: From LBJ's Guns and Butter to Reagan's Voodoo Economics* (New York, 1994), 3-21; Doris Kearns, *Lyndon Johnson and the American Dream* (New York, 1976), 296; Matusow, *The Unraveling of America*, 153-179; and Bruce Schulman, *Lyndon Johnson and American Liberalism: A Brief Biography with Documents* (New York, 1995), 157-158.

¹¹²⁶ Shreve, 'Lyndon Johnson and the Keynesian Revolution,' 181.

¹¹²⁷ Ibid, 181-201; and Shreve, 'A Precarious and Uncertain Liberalism,' 243-294.

¹¹²⁸ Donald F. Kettl, 'The Economic Education of Lyndon Johnson: Guns, Butter, and Taxes,' in Robert Divine (ed.) *The Johnson Years, Volume Two, Vietnam, the Environment, and Science* (Lawrence, KS, 1987), 55.

case for moving ahead isn't getting lost."¹¹²⁹ For Heller, it was imperative not to sacrifice the Great Society for a tax increase. In fact, the former could expand whilst Johnson sought the latter. "A billion or two next year could spell the difference between progress and stagnation of the Great Society...That billion or two is peanuts when compared with GNP, previous tax cuts, and the recent rise in personal income and profits."¹¹³⁰ Aware that this entailed asking for a slightly larger tax increase than he anticipated earlier in the year, Heller argued that "Well-heeled private citizens and businesses – cashing in on government-sparked prosperity – can afford the costs of Vietnam far better than the bare-bones budgets of our programs for the poor, the Negro, the unskilled, and the undereducated."¹¹³¹ For Heller, guns and butter *were* compatible goals. Even though the Minnesotan favoured a tax increase, his suggestion that increased spending on the Great Society could concurrently take place alongside Vietnam surely would have played no small role in solidifying Johnson's desire not to sacrifice "the woman" that he loved for "that bitch of a war."¹¹³²

II

Despite calling upon Johnson in late 1965 to provide more funds for the Great Society, over the next few months Heller argued that the president should prioritise deflationary measures. In another newsletter for the NCBM on January 1, 1966, the former CEA chairman expressed alarm at reports that, since the summer of 1965, "a rise of \$10 to \$15 billion in federal purchases" had taken place.¹¹³³ This meant that "even the most heroic budget-cutting efforts" would be unable to "keep the fiscal

¹¹²⁹ Heller, Memorandum for the President, 'What Price Great Society?' 21 December 1965. WHCF. Confidential File. WE/MC. Box 98. LBJL.

¹¹³⁰ *Ibid.*

¹¹³¹ *Ibid.*

¹¹³² Johnson cited in Lawrence Eldridge, *Chronicles of a Two-Front War: Civil Rights and Vietnam in the African American Press* (London, 2011), 18

¹¹³³ Heller, 'The Economic Outlook for 1966,' *NCBM*, 1 January 1966. Heller Papers. Box 8. UoM.

[year] 1967 administrative budget from rising into the \$110–\$115 billion range.”¹¹³⁴ He suggested a tax increase was imperative.¹¹³⁵ Worried at the scale of spending on Vietnam, Heller told Johnson on February 13 that he was “even more concerned than I was in December about mounting price pressures.”¹¹³⁶ Senior figures at International Milling – a firm that Heller advised – were “full of talk about...price tension.”¹¹³⁷ This was especially as certain supplies were “up 3 ½%” compared with a year ago.¹¹³⁸ Business inventories had also been piling up, whilst there was “more of a price-push psychology in business...than we’ve had in a long time.”¹¹³⁹ Moves to restrain both demand and investment were imperative, so in addition to a surcharge Heller suggested “credit guidelines and selected credit restraints should be considered.”¹¹⁴⁰

Ackley disagreed. Despite acknowledging that a tax increase was desirable, the CEA chairman did not “see much to be said for credit guidelines and selective credit restraints.”¹¹⁴¹ The former were “likely to be harder on small businesses and on housing than rationing through higher interest rates.”¹¹⁴² The latter would also need to apply to business loans when “no one” had “figured out how to apply such selective restraints to anything except housing loans and consumer credit.”¹¹⁴³ Despite favouring a tax increase, Ackley also told Johnson it was important “that we are not ourselves carried away by all the inflationary talk.”¹¹⁴⁴ At a meeting with the Business Council the week beforehand, one member had explained that their buyers

¹¹³⁴ Ibid.

¹¹³⁵ Ibid.

¹¹³⁶ Heller, Memorandum for the President, ‘Various,’ 13 February 1966. NFHWH. Box 219. LBJL.

¹¹³⁷ Ibid.

¹¹³⁸ Ibid.

¹¹³⁹ Ibid.

¹¹⁴⁰ Ibid.

¹¹⁴¹ Ackley, Memorandum for the President, ‘Attached Memo from Walter Heller,’ 22 February 1966. WHCF. FI. Box 1. LBJL.

¹¹⁴² Ibid.

¹¹⁴³ Ibid.

were “anticipating only a 1% price increase this year on their whole line.”¹¹⁴⁵ Not only did Heller arguably see the inflationary threat as more of a concern than Ackley in early 1966, the CEA chairman did not favour certain policies that Heller pressed upon Johnson. Heller acknowledged this when he wrote to the *New York Times* in May to downplay the differences between himself and Ackley.¹¹⁴⁶ Such a lack of accord between both advisers clearly lends credence to Kettl’s argument that their divergences prevented Johnson from dealing more effectively with the inflationary build-up of Vietnam.

If the jury had been out on both the impending threat of rising prices and the need to implement credit guidelines and restraints, the verdict was much clearer to both Heller and Ackley on suspending the 1962 Investment Tax Credit. Just twelve days after he warned Johnson that his fears of inflation had increased, Heller forwarded the president a speech that he delivered on February 23. In it, the Minnesotan stressed that the “current level of investment is generating capacity increases at a 7% annual rate.”¹¹⁴⁷ This was “welcome muscle for a Vietnam economy, but an unsustainable source of excess capacity under normal growth conditions.”¹¹⁴⁸ Accordingly, measures that could “selectively dampen investment today and postpone it to a post-Vietnam tomorrow...[would] make good sense.”¹¹⁴⁹ Central to such an effort was temporary suspension of the Investment Tax Credit, a

¹¹⁴⁴ Ibid.

¹¹⁴⁵ Ibid.

¹¹⁴⁶ Heller, Letter to the *New York Times*. Reprinted in the *Minneapolis Tribune*, 13 May 1966. Copy in Heller Papers. Box 10. UoM.

¹¹⁴⁷ Heller, ‘Using Fiscal (and Monetary) Policies to Further Employment Act Objectives,’ Remarks at the Employment Act Symposium, 23 February 1966. Attached to Heller, Memorandum for the President, ‘Speeches,’ 25 February 1966. NFHWH. Box 219. LBJL.

¹¹⁴⁸ Ibid.

¹¹⁴⁹ Ibid.

move seconded by both Ackley and the former Budget Director Kermit Gordon.¹¹⁵⁰

Whilst the Keynesians pressed this action upon Johnson, Douglas Dillon's replacement as Treasury Secretary, Henry Fowler, voiced his opposition. Writing to Fowler on March 9, Heller put forward the case for suspending the Investment Tax Credit. He argued that this would provide "a sharper instrument than either tighter money or higher corporate income taxes in getting to the bottom of economic overheating."¹¹⁵¹ Heller also explained that "the amount of responsible readiness in the business community to take some anti-inflationary medicine" was remarkable, having cited individuals from some of the corporations that he advised.¹¹⁵² Fowler proved unwilling to move. He argued that investment in plant and machinery still needed "to be encouraged to promote overall competitive efficiency, increased productivity to justify increased wages, and the additional capacity that is the best answer to shortages."¹¹⁵³ Suspending the measure would also do little to prevent inflation, as it "would produce a small yield...and thus contribute very little to achieving a budgetary surplus."¹¹⁵⁴

Taken aback by Fowler's opposition, Heller met with the House Ways and Means Committee chairman, Wilbur Mills, on August 19. Here, he recommended suspension of the Investment Tax Credit. Reporting to Johnson, Heller explained that he and Mills had "a good give-and-take discussion" about the measure and stated that Mills accepted that repealing it "would be effective in slowing down investment."¹¹⁵⁵

¹¹⁵⁰ Ibid; Ackley, Memorandum for the President, 'An Immediate Tax Program,' 9 August 1966. WHCF. FI 9. Box 55. LBJL; and Gordon, Memorandum for the President, 'Secretary Fowler's Memorandum on a Tax Increase Program,' 22 August 1966. WHCF. FI 11. Box 56. LBJL.

¹¹⁵¹ Heller, Memorandum for Fowler, 'The Investment Credit,' 9 March 1966. WHCF. BE 5-2. Box 31. LBJL.

¹¹⁵² Ibid.

¹¹⁵³ Fowler, Memorandum for the President, 'Tax Increase Program Effective Alternative Dates: October 1, 1966, January 1 and March 1 1967,' 16 August 1966. LBFTI. Box 1. LBJL.

¹¹⁵⁴ Ibid.

¹¹⁵⁵ Heller, Memorandum for the President, 'Conversation with Wilbur Mills, August 19,' 20 August 1966. WHCF. Ex BE 5. Box 24. LBJL.

Spurred on by this, as well as by the lobbying of Ackley, Gordon, and the new Budget Director Charles Schultze, LBJ asked Congress for temporary suspension of the Investment Tax Credit on September 8, having sought Heller's advice on the wording of his request.¹¹⁵⁶

Despite overcoming Fowler's opposition to the Investment Tax Credit's suspension, Heller and Ackley's main priority remained convincing the president to promote a tax increase. This was something that Fowler had ruled out in a February appearance before the Joint Economic Committee.¹¹⁵⁷ The Treasury Secretary did endorse such a measure by the summer, but the fact that he was not in accord with Heller and Ackley in early 1966 further substantiates Kettl's argument that indecision amongst LBJ's advisers prevented Johnson from tackling inflation more effectively. Determined to press his case despite the lack of consensus, Heller made numerous speeches in favour of a tax increase throughout early-to-mid-1966.¹¹⁵⁸ Johnson remained unmoved. In addition to his fear that Congress would demand a cutback in Great Society expenditures, one factor further deterred the president. This was that, following its discount rate decision in December, the Fed engineered a credit crunch in mid-1966 due to Martin's fears of inflation. This action raised the possibility that a tax surcharge might tip the economy into a recession.¹¹⁵⁹

Heller and Ackley argued that, even with the Fed's decision, "the great strength of private investment demand was threatening the stability of financial

¹¹⁵⁶ Johnson, 'Special Message to Congress on Fiscal Policy,' 8 September 1966. APP; n.n., 'Points Made or Approved by the President (9:00 a.m. conversation with WWH on 09/06/66),' n.d. LBFTI. Box 2. LBJL.

¹¹⁵⁷ See Rowen, 'Fowler: 'No Tax Boost Now,' *Washington Post, Times Herald*, 4 February 1966. D5. Copy in Consolidated Personal Papers of Walter W. Heller et al [Henceforth Heller Papers]. Box 12. LBJL.

¹¹⁵⁸ See Heller, 'The 'New Economics' in the United States and Its Implications for Thrift,' Remarks before the Eighth International Savings Bank Congress, New York City, 2 May 1966. Heller Papers. Box 8. UoM; n.n., 'Nation's New Economics Faces Its Severest Test,' *St Paul Pioneer Press*, 30 May 1966. Heller Papers. Box 10. UoM; and John Schweitzer, 'U Economist Favors Tax boost for Vietnam War,' *St Paul Pioneer Press*, 12 May 1966. Heller Papers. Box 10. UoM.

markets.”¹¹⁶⁰ To convince Johnson to press ahead with a tax surcharge, Heller broached the subject during his August 19 meeting with Wilbur Mills. In doing so, he was attempting to demonstrate that a surcharge was politically feasible. Heller reported that the Ways and Means chairman “said flatly, ‘I can pass a tax bill.’”¹¹⁶¹ In exchange, Mills required the administration to cut expenditures, for he believed that “Congress had lost control of general-revenue spending after Johnson had [expanded the Great Society].”¹¹⁶² He also needed to “be persuaded that the economy” was “not going to cool off, primarily because of tight money.”¹¹⁶³ Accordingly, Heller reassured Mills that “plant and equipment investment would be the last to be hit by tight money,” meaning that there would continue to be inflationary pressures.¹¹⁶⁴ He also provided Mills with a copy of his latest newsletter for the NCBM, arguing that GNP was rising “by about \$14 billion” per quarter in 1966.¹¹⁶⁵ In response, Mills reiterated that he wanted the administration to cut back its expenditures and disputed whether Heller’s figures pointed to a strong inflationary build-up ahead.¹¹⁶⁶ Clearly, Mills did not come out explicitly in favour of a tax surcharge by the end of the meeting. Yet, Heller told both Ackley and Johnson that the chairman was “ready to go” and even suggested that the administration should call “the Ways and Means Committee back in November to get a tax bill ready.”¹¹⁶⁷ Such was Heller’s confidence in Mills’ readiness to pass a surcharge, that he told Democratic Senator

¹¹⁵⁹ ‘CEA’s Role in Fiscal Policy,’ AHCEA, Chapter II, II-17, Box 1. LBJL.

¹¹⁶⁰ Ibid.

¹¹⁶¹ Heller, Memorandum for the President, ‘Conversation with Wilbur Mills, August 19.’

¹¹⁶² Ibid; Zelizer, *Taxing America*, 260-261 (quotation 261).

¹¹⁶³ Heller, Memorandum for the President, ‘Conversation with Wilbur Mills, August 19.’

¹¹⁶⁴ Ibid.

¹¹⁶⁵ Ibid.

¹¹⁶⁶ Ibid.

¹¹⁶⁷ See Heller, Memorandum for Ackley, ‘Comments on the Fowler Tax Proposal,’ 22 August 1966. WHCF. FI 11. Box 56. LBJL.

Walter Mondale of Minnesota “the signs are favourable at the moment.”¹¹⁶⁸

Heller’s confidence turned out to be misplaced. In a meeting with two administration officials the same day he met with Heller, Mills said that he was “fearful of the economic impact of a general tax increase.”¹¹⁶⁹ His own economic counsellor Norman Ture, of the National Bureau of Economic Research, was adamant the Fed credit crunch meant that the economy faced “immediate danger of recession far more than the danger of inflation.”¹¹⁷⁰ So, just as Heller was telling LBJ that a tax surcharge was politically feasible, other advisers were saying the opposite to the president. It is undoubtedly clear that Johnson was hiding the true costs of the war at this point. However, it is also obvious that the lack of accord amongst those advising him contributed to the president’s reluctance to propose a tax surcharge to dampen down demand.

Another example adds cogency to this point: by the fall of 1966, Heller and others grew unsure about the need for a surcharge. The Investment Tax Credit had been suspended just after the Fed had engineered that summer’s credit crunch, so the “remainder of 1966 and particularly the first half of 1967 began to be less bullish than earlier.”¹¹⁷¹ This meant that the “need for immediate, sizeable fiscal restraint was no longer viewed as urgent.”¹¹⁷² Reflecting this, Heller wrote to Johnson on November 23 to say that the tax surcharge *was* still required. However, he stated that this was more so to rebalance the economy than to dampen demand directly. At “the risk of sounding like a man with a solution in search of a problem,” Heller wrote, he continued to favour a surcharge because it would enable the Fed to cut interest

¹¹⁶⁸ Heller to Walter Mondale, 8 September 1966. Walter Mondale Papers [Henceforth Mondale Papers]. Senatorial Papers, 1949-2008. Issue Files, 1966-67. Box 153.K.9.2F. MHS.

¹¹⁶⁹ Larry O’Brien and Henry H. Wilson, Jr., Memorandum for the President, Untitled, 19 August 1966. LBFTI. Box 1. LBJL.

¹¹⁷⁰ Ibid.

¹¹⁷¹ ‘CEA’s Role in Fiscal Policy,’ AHCEA. Chapter II, II-18. Box 1. LBJL.

rates.¹¹⁷³ This would “put our lopsided economy back on an even keel” and enable the US to “withdraw the resources to fight the war in a more balanced and equitable way.”¹¹⁷⁴ Easier credit would boost both the housing industry and small businesses, whilst increasing taxes would restrain personal consumption and business investment.¹¹⁷⁵ This meant that it would be possible to finance the war with “after-tax wages and profits.”¹¹⁷⁶ Such a strategy would further put the economy “in better shape to make the economic adjustment when Vietnam demands ebb, because it will give” Johnson “an added tax weapon that can be brought into play fast to stimulate the economy when Vietnam ends.”¹¹⁷⁷ Such a move would “appeal to a wide spectrum of voters on grounds that it will support our men in Vietnam,” as well as open up the prospect of a tax cut just before the 1968 Presidential Election.¹¹⁷⁸

Agreeing with Heller on the desirability of easier credit and a tighter budget, Ackley also urged this combination upon Johnson.¹¹⁷⁹ In contrast, the president’s “appointees to the Federal Reserve Board believed that the economy had been slowed down enough and opposed a tax increase.”¹¹⁸⁰ Leon Keyserling also wrote LBJ in early December expressing doubt about the necessity of a surcharge.¹¹⁸¹ The question over whether that measure was immediately necessary at the end of 1966 was unclear. To make matters worse, those in favour of a surtax advanced different reasons for one. Reflecting this, Heller again wrote Johnson on December 14, this time outlining

¹¹⁷² Ibid.

¹¹⁷³ Heller, Memorandum for the President, ‘Boost Taxes, Cut Interest Rates,’ 23 November 1966. WHCF. BE 5. Box 24. LBJL.

¹¹⁷⁴ Ibid.

¹¹⁷⁵ Ibid.

¹¹⁷⁶ Ibid.

¹¹⁷⁷ Ibid.

¹¹⁷⁸ Ibid.

¹¹⁷⁹ Ackley, Memorandum for the President, ‘Further Thoughts on the State of the Economy,’ 8 November 1966. WHCF. BE 5. Box 24. LBJL.

¹¹⁸⁰ Kettl, ‘The Economic Education of Lyndon Johnson,’ 65.

¹¹⁸¹ Ackley, Memorandum for the President, ‘Leon Keyserling,’ 3 December 1966. WHCF. FI 11. Box 56. LBJL.

five divergent views advanced in support of a surcharge.¹¹⁸² Once more, he argued that such a measure was important “to improve the policy mix” rather than to dampen demand directly.¹¹⁸³ He also maintained that it would do much “to protect the programs that are essential to progress in American life and meet the urgent problems of the poor, the Negro, and the cities.”¹¹⁸⁴

This demonstrates that Heller continued to believe in the compatibility of guns and butter. He even stressed that, because the economy would be “producing an \$800 billion GNP within a year, surely we can afford a \$25 to \$30 billion war in Vietnam side-by-side with advances in vital programs to help the underdog and make life worth living.”¹¹⁸⁵ So, not only was Heller no longer arguing for a tax surcharge as a means to directly offset imminent inflationary pressures, he continued to encourage Johnson not to sacrifice the Great Society in favour of funding Vietnam. Coupled with the lack of accord amongst those advising Johnson, it is no wonder the Minnesotan told LBJ that his “special hope” was that the president would get “Divine guidance on the question of a 1967 tax increase” in the New Year.¹¹⁸⁶ It is clear, the reasons behind the president’s eventual decision to request a tax increase “were far more complicated than the argument that Johnson lied to protect both Vietnam and the Great Society.”¹¹⁸⁷

III

Though Heller toned down his advocacy of a surcharge in late 1966, once he completed a forecast of the economic picture for the whole of 1967 he became

¹¹⁸² Heller, Memorandum for the President, ‘The Tax Increase Issues Today,’ 14 December 1966. WHCF. FI 11. Box 56. LBJL.

¹¹⁸³ Ibid.

¹¹⁸⁴ Ibid.

¹¹⁸⁵ Ibid.

¹¹⁸⁶ Heller, Memorandum for the President, ‘Merry Christmas!’ 23 December 1966. WHCF. FI 11. Box 56. LBJL.

¹¹⁸⁷ Kettl, ‘The Economic Education of Lyndon Johnson,’ 72.

convinced that one would be necessary. In his NCBM newsletter in December 1966 – which he forwarded to Johnson – the Minnesotan urged the president to promote a tax increase in January but not implement it in the first half of the year.¹¹⁸⁸ Heller instead wanted it to come into effect “in the second half” of 1967, when he was “quite sure that the economy would be moving up again.”¹¹⁸⁹ In the meantime, Johnson would have to safeguard the economy from stalling. Ignoring the fact that it took just over a year to pass the 1964 tax cut, Heller told the Joint Economic Committee, “Quick and fine-tuning of economic policy must be the order of the year in which we expect first an ebb and then a flow in the tide of economic advance.”¹¹⁹⁰ Despite the previous lack of accord within Johnson’s administration, Ackley and Schultze also reached this conclusion.¹¹⁹¹ In his FY 1968 Budget Message, LBJ thus proposed a modest stimulus for the first part of the year and set aside a surcharge for the second half to avert inflationary pressures.¹¹⁹² Consequently, Heller, Johnson, and others called for the reinstatement of the Investment Tax Credit, not least because they underestimated how efficiently the Fed’s tight money policies of the previous summer had slowed down the economy.¹¹⁹³

To their relief, Congress swiftly re-enacted this measure. Coupled with a more relaxed monetary policy in early 1967, this provided the economy with a sufficient stimulus. Heller wrote to Johnson on July 11, saying, “unless a lot of us are wrong on

¹¹⁸⁸ Heller, Memorandum for the President. ‘Happy New Year!’ 21 December 1966. NFHWH. Box 219. LBJL. Though the newsletter in question is not attached to this particular document (which is a copy of the original), the memo itself tells Johnson that “the sum-up on page 4 [of the newsletter] may interest you, especially the proposed July 1 effective date if a tax increase is recommended.”

¹¹⁸⁹ Heller, Interview with McComb, 21 December 1971, 45.

¹¹⁹⁰ Heller, ‘Statement before the Joint Economic Committee,’ 15 February 1967. Heller Papers. Box 8. UoM.

¹¹⁹¹ Heller, Interview with McComb, 21 December 1971, 45-46.

¹¹⁹² Johnson, ‘Annual Budget Message to the Congress, Fiscal Year 1968,’ 24 January 1967. APP.

¹¹⁹³ Heller, ‘Statement before the Joint Economic Committee,’ 15 February 1967; Louis Dombrowski, ‘Restore Tax Credit,’ *Chicago Tribune*, 10 March 1967, 1. PQHN.

our GNP forecasts for next winter, we should soon ease up on the accelerator.”¹¹⁹⁴ A 6 – 10 percent surcharge on personal income taxes was required in late 1967, to preempt any inflationary developments likely to occur.¹¹⁹⁵ Such a policy would also be desirable if the Fed continued to ease monetary policy, for this would improve the fiscal-monetary mix.¹¹⁹⁶ Ackley, Schultze, and Fowler also favoured implementing the surcharge. Johnson, however, needed further persuasion. In this, Heller apparently played an important role. Just as the president contemplated whether to ask for a surcharge, he invited the Minnesotan to have lunch with him and the German Chancellor Ludwig Erhard, whom Heller worked with during his post-war stint as Chief of Internal Finance in West Germany. This gave Heller “a marvellous vehicle” to influence the president.¹¹⁹⁷ “I did it through the things I was telling Erhard,” he recalled, “because in the process I was trying to get [my case] across to Johnson.”¹¹⁹⁸ As a result, Johnson issued a Special Message to Congress on August 3. This warned that the deficit for FY 1968 would hit \$28.7 billion without a tax increase (compared with deficits of \$3.7 billion and \$8.6 billion for FYs 1966 and 1967). Should this happen, there would be “ruinous inflation.”¹¹⁹⁹ A combination of around \$4 billion in expenditure restraint and a temporary 10 percent surcharge on individual income taxes on October 1, 1967, was the president’s response.

Even before Johnson endorsed the surcharge, Wilbur Mills argued that it would be difficult to pass. Such a measure, he explained, “had no appeal to him.”¹²⁰⁰ Four months prior to Johnson’s message, Mills delivered a damning indictment of the

¹¹⁹⁴ Heller, Memorandum for the President, ‘Accelerator Versus Brakes,’ 11 July 1967. WHCF. FI. Box 2. LBJL.

¹¹⁹⁵ *Ibid.*

¹¹⁹⁶ *Ibid.*

¹¹⁹⁷ Heller, Interview with McComb, 21 December 1971, 46.

¹¹⁹⁸ *Ibid.*, 46.

¹¹⁹⁹ Johnson, ‘Special Message to Congress: The State of the Budget and the Economy,’ 3 August 1967. APP.

¹²⁰⁰ Bernstein, *Guns or Butter*, 370.

administration's tax policy. Dismayed with what he regarded as the "disruptive effect of frequent tax changes" pushed by the Keynesians – something exemplified by the quick suspension and re-enactment of the Investment Tax Credit – Mills questioned "the ability of the administration economists to discern short-term movements in the economy and make the right tax prescriptions."¹²⁰¹ To make matters worse, Heller told Walter Mondale that two "off-base guys" who "have control of the editorial pages of both the *New York Times* and *The Washington Post*" had "the ear of Wilbur Mills."¹²⁰² This was because their "only consistent theme these days is, no matter what the new economists do, they're wrong."¹²⁰³ Even if Mills were to consider a tax surcharge, he had also said that he wanted a large reduction in domestic spending to accompany one.¹²⁰⁴

Seeking to win Mills around to Johnson's position, Heller and Brookings economist Joseph Pechman penned coordinated letters to the Ways and Means chairman straight after Johnson issued his Special Message.¹²⁰⁵ In his, Heller stressed that the tax increase was "an economically prudent and politically responsible step to take."¹²⁰⁶ Invoking the example of the Korean War, Heller reminded Mills of "the responsible and courageous leadership role played by the Joint Economic Committee and the House Ways and Means Committee in 1950-51 in raising taxes."¹²⁰⁷ He further noted that, as inflation would become more of a danger in 1968, it was wise

¹²⁰¹ Paul G. Edwards, "'67 Tax Boost Unlikely, Mills, Byrnes Indicate,' *Washington Post, Times Herald*, 27 April 1967, A10. Heller Papers. Box 12. LBJL.

¹²⁰² Heller to Mondale, 31 May 1967. Mondale Papers. Senatorial Papers, 1949-2008. Issue Files, 1966-67. Box 153.K.9.2F. MHS.

¹²⁰³ Ibid. See too Heller, Interview with McComb, 21 December 1971, 47-48.

¹²⁰⁴ Though the main reason for this was that Mills wanted to rein in spending on the Great Society, he also felt that union pressure on businesses to increase wages helped cause inflation (as businesses raised prices in response to this). He therefore preferred decreased spending as an anti-inflationary weapon. Unlike a tax increase, this "would remove money from the economy without squeezing personal and corporate income." Zelizer, *Taxing America*, 268.

¹²⁰⁵ Pechman to Wilbur Mills, 4 August 1967. Heller Papers. Box 12. LBJL.

¹²⁰⁶ Heller to Mills, 4 August 1967. Heller Papers. Box 12. LBJL.

¹²⁰⁷ Ibid.

for fiscal rather than monetary policy to take the necessary pre-emptive action.¹²⁰⁸ Another credit crunch, for example, would be disastrous for the housing industry and small businesses.¹²⁰⁹ A big deficit for FY 1968 would also “represent unsound economic policy and budgetary policy [given the fact that the economy was at full capacity],” whilst the rising level of GNP in late 1967 meant that the economy could “take the tax increase in its stride.”¹²¹⁰ In an attack obviously aimed at Norman Ture, Heller explained that those “who [earlier] forecast a recession or prolonged doldrums have already been proved wrong,” whereas the Keynesians were “being proved right.”¹²¹¹ It was thus imperative to follow his advice, or the economy would be worse off.

In an attempt both to expose Mills to other journalists and to convince him not to hold Johnson to ransom over Great Society expenditures, Heller attached to this letter an excerpt from the editorial page of the *Minneapolis Tribune*. This argued that the 1967 race riots offered a “compelling” reason not to scale back domestic spending.¹²¹² “The nation cannot afford to cut back on its spending for education, poverty and job training programs, all vitally needed to eliminate the underlying causes of violence and unrest.”¹²¹³ Although presidential aide Joseph Califano Jr., hailed Heller’s letter as both a “first-rate job” and “a great help,” Mills remained unmoved.¹²¹⁴ Having developed a reputation for not endorsing a proposal unless he was sure that it had plenty of support, Mills wanted to tread lightly on the surcharge. In fact, he believed that “both Ways and Means and the House would vote it

¹²⁰⁸ Ibid.

¹²⁰⁹ Ibid.

¹²¹⁰ Ibid.

¹²¹¹ Ibid.

¹²¹² ‘No Choice But to Raise Federal Taxes,’ *Minneapolis Tribune*, 4 August 1967, Editorial Page. Attached to Ibid.

¹²¹³ Ibid.

¹²¹⁴ Califano Jr., to Heller, 8 August 1967. Heller Papers. Box 12. LBJL.

down.”¹²¹⁵ Despite the fact that Mills opened hearings on the tax increase on August 12, the progress of the bill went very slow, putting the October date of enactment in severe doubt. Mills was also “very chary of economic forecasts” and felt that Johnson did not provide definitive proof that the economy would overheat in 1968.¹²¹⁶

With the tax surcharge becalmed, Heller engaged in a robust effort to muster support for its advancement. Along with Pechman and George Bach of Stanford University, he organised a petition seeking support for the surcharge from a wide range of professional economists. After amassing over 300 signatures, this was sent to Mills and the Louisiana Senator Russell B. Long, chairman of the Senate Finance Committee. With “government expenditures rising rapidly,” it warned, “growth of total demand” threatened “to exceed the capacity of the economy to increase total output.”¹²¹⁷ Thus, a tax increase would forestall “a new round of inflation.”¹²¹⁸ The petition further explained that, “given the projected size of military outlays,” cuts “in federal civilian programs” would be futile “to avert the need for a tax increase.”¹²¹⁹ Such cuts also amounted to “poor – indeed, dangerous – social policy in the light of the conditions of millions of our citizens living in the ghettos of our cities.”¹²²⁰ This last statement was particularly important, not least because Mills soon made it clear that he would hold up the surcharge until he and LBJ agreed upon “a specification of budget cuts” likely to be “much larger” than the president wanted.¹²²¹

In addition to organising this petition, Heller used his September 20

¹²¹⁵ Bernstein, *Guns or Butter*, 370.

¹²¹⁶ Heller, Interview with McComb, 21 December 1971, 22.

¹²¹⁷ ‘Economists Statement,’ Congressional Record – Senate, 11 September 1967, S12768, S2769; Pechman to Long, and Pechman to Mills, both 19 September 1967. All Heller Papers. Box 12. LBJL.

¹²¹⁸ ‘Economists Statement.’

¹²¹⁹ Ibid.

¹²²⁰ Ibid.

¹²²¹ Schultze, Memorandum for the President, ‘Wilbur Mills and the Tax Bill,’ 16 September 1967. LBFTI. Box 4. LBJL.

newsletter for the NCBM to drum up popular support for the surcharge.¹²²² Using what one observer described as “strong words,” the former CEA chairman warned that inflation could jump well above its 1967 level of 3 percent by 1968 without preventative action.¹²²³ Continuing to believe that guns and butter were compatible, Heller argued that waging “the good fight against inflation and the ghettos, side by side with the war in Vietnam” was possible.¹²²⁴ This was because, once the surtax had been enacted, there could be an overhaul of the taxation system in order to generate additional revenues for spending on the Great Society.¹²²⁵ Again, Heller’s efforts failed to achieve the desired effect. The fiscally conservative Senator William Proxmire of Wisconsin dismissed the petition on the basis that just 2 ½ percent of the American Economic Association’s whole membership signed it.¹²²⁶ Similarly, one member of the public wrote to the *St Paul Dispatch* at the end of September to criticise Heller’s prediction that the FY 1968 budget would be inflationary. He reminded its readers that, in 1962, Heller made an error forecasting a surplus for FY 1963.¹²²⁷ These critical approaches were, to Heller’s dismay, reflected in the actions of the Ways and Means Committee. On October 3, it voted 20 to 5 to lay aside the surtax until LBJ and Mills reached an agreement on domestic expenditure restraint.¹²²⁸

Whilst he tried in vain to pressure congressional conservatives to endorse the surtax, Heller was successful at boosting that measure’s appeal amongst key liberals in Congress, albeit after October 3. The latter appreciated the economic case for the

¹²²² Heller, ‘Economic Outlook and Policy,’ *NCBM*, 20 September 1967. Heller Papers. Box 8. UoM.

¹²²³ Ibid; John Cunniff, ‘Heller, Former Presidential Aide, Urges Tax Increase,’ *Seattle Times*, 20 September 1967. Heller Papers. Box 12. LBJL.

¹²²⁴ Heller, ‘Economic Outlook and Policy,’ 20 September 1967.

¹²²⁵ Ibid.

¹²²⁶ Congressional Record – Senate, 11 September 1967, S12768.

¹²²⁷ Walter C. Peters, ‘Beware of Heller’s Dogmas,’ Letter to the Editor, *St Paul Dispatch*, 25 September 1967. Heller Papers. Box 12. LBJL.

¹²²⁸ Bernstein, *Guns or Butter*, 370.

surcharge, but wanted to use it as a vehicle to achieve comprehensive reform of the taxation system. Heller sympathised with this aim, but argued that a protracted struggle to overhaul the tax structure should not hold up the surcharge.¹²²⁹ Accordingly, in a letter to Johnson on September 16, Heller explained that he was writing to a number of prominent liberals in Congress on the need to prioritise the surtax.¹²³⁰ He was also in conversation with Representative Donald Fraser of Minnesota about the possibility of having “a session with the Democratic Study Group [DSG]” to make this argument.¹²³¹ Walter Mondale also wanted Heller to brief sceptical Democrats in the Senate.¹²³² These efforts came to a head on October 10, when Heller had separate engagements on Capitol Hill with 50 members of the DSG, 50 House staff members, 16 Democratic Senators, and the press.¹²³³ Calling himself “an unpaid lobbyist” who was there at his “own expense and no-one’s request” (a statement that, retrospectively, Heller admitted was not true), the Minnesotan made a robust effort to increase liberal support for the surcharge.¹²³⁴

Quoting material from a speech that he delivered to the Economic Club of Detroit, Heller stressed that loophole closing was a “laudable undertaking” but there would be “months and months of Congressional deliberations.”¹²³⁵ After highlighting how the attempt at tax reform in 1963 held up the passage of the 1964 Revenue Act, Heller argued that it was “self-defeating to confuse loophole closing, an equity move

¹²²⁹ Heller, Memorandum for the President, ‘Arguments to Persuade Liberals on the Tax Bill (especially those who say ‘let’s close loopholes instead’),’ 11 September 1967. Heller Papers. Box 12. LBJL.

¹²³⁰ Heller, Memorandum for the President, Untitled, 16 September 1967. WHCF. BE 5. Box 25. LBJL.

¹²³¹ Ibid.

¹²³² Heller, Memorandum for the President, ‘Plugging for the Tax Increase,’ 6 October 1967. LBFTI. Box 5. LBJL.

¹²³³ Heller, Memorandum for the President, ‘Report from the Hill,’ 12 October 1967. LBFTI. Box 5. LBJL.

¹²³⁴ Richard P. Kleeman, ‘Heller Supports Johnson’s 10 Pct. Tax Surcharge,’ *Minneapolis Tribune*, 11 October 1967. Attached to Ibid. For Heller’s admission that he was there partly on Johnson’s request see Heller, Interview with McComb, 21 December 1971, 47.

that won't produce revenue until 1969, with the surtax."¹²³⁶ In closing, he made the argument that "the surtax will serve" the "liberal purposes [of the Democrats] might well," not least because it was "strongly progressive."¹²³⁷ It would also ensure that the Democrats could "afford the very domestic programs they, as liberals, regard as essential."¹²³⁸ This was because "the alternative of higher prices and higher interest rates" would "hit the little fellow hardest."¹²³⁹

Following his meetings with both the House staff members and the Senators, Heller reported that he "got the pleasing comment that a number of doubters on the surtax had been convinced."¹²⁴⁰ Reflecting this, Mondale congratulated Heller "on a magnificent performance" and promised to insert the Economic Club of Detroit speech into the *Congressional Record*.¹²⁴¹ With regard to his appearance before the DSG members, Heller said that it was "hard to know how many were converted."¹²⁴² However, a note from Fraser on October 17 showed that many were. Not only did Fraser say that the DSG thought Heller made his "case well and they'll go along [with the surtax]," he described Heller's appearance as "one of the most effective things I've seen done here on Capitol Hill."¹²⁴³

In addition to his efforts on October 10, Heller gave four speeches across America to drum up support for the tax increase.¹²⁴⁴ He also penned an article for the *Washington Post* that attacked Mills' suggestion that the administration should wait

¹²³⁵ Heller, 'The Economy: Whither Now,' Excerpts from Detroit Economic Club Speech, 2 October 1967. Attached to Heller, Memorandum for the President, 'Plugging for the Tax Increase.'

¹²³⁶ Heller, Memorandum for the President, 'Supplementary Report on Meeting with the DSG,' 12 October 1967. LBFTI. Box 5. LBJL.

¹²³⁷ Ibid.

¹²³⁸ Ibid.

¹²³⁹ Ibid.

¹²⁴⁰ Heller, Memorandum for the President, 'Report from the Hill.'

¹²⁴¹ Mondale to Heller, 11 October 1967. Heller Papers. Box 12. LBJL; and Mondale to Heller, 17 October 1967. Mondale Papers. Senatorial Papers, 1949-2008. Issue Files, 1966-67. Box 153.K.9.2F. MHS.

¹²⁴² Heller, Memorandum for the President, 'Supplementary Report on Meeting with the DSG.'

¹²⁴³ Donald Fraser to Heller, 17 October 1967. Heller Papers. Box 12. LBJL.

for prices to increase in 1968 before enacting the surcharge.¹²⁴⁵ Along with his hard work throughout September, these attempts to increase support for the surcharge were reminiscent of Heller's efforts to boost the appeal of the 1964 Revenue Act as it made its way through Congress. Still, neither Heller's nor the LBJ administration's actions broke the deadlock. The British decision to devalue the pound in November proved more decisive. This prompted concerns among foreign dollar holders that the US would do the same to protect its own currency, causing another run on gold. As one historian noted, "Johnson now believed that passage of the tax surcharge was essential to reassure foreign bankers that the United States had the will and the ability to keep inflation under control."¹²⁴⁶ Consequently, the president was willing to accept Mills' most important demand to achieve this: the need to curtail domestic expenditures.

This alarmed Heller. He accepted, like Johnson, that the pound's devaluation made passage of the surtax essential. In fact, he introduced the president to a French-born Wall Street banker who offered to assist the administration in urging sceptical congressional representatives to pass the measure.¹²⁴⁷ At the same time, the Minnesotan told the president on November 22 "the local news dispatch of something like a \$7 billion spending cut in exchange for the full surtax sent a chill down my spine."¹²⁴⁸ Slowing down "progress of the Great Society programs, would be a mighty high price to pay to get the full surtax."¹²⁴⁹ If Johnson did have to find \$7

¹²⁴⁴ For Heller's discussion of this see Heller to Califano Jr., 24 October 1967. Heller Papers. Box 12. LBJL.

¹²⁴⁵ Heller, 'Surtax Decision Must Be Based on a Forecast, Heller Believes,' *Washington Post, Times Herald*, 15 October 1967, G1. PQHN.

¹²⁴⁶ Morgan, *Deficit Government*, 112.

¹²⁴⁷ Heller, Memorandum for the President, 'Various Personal and Fiscal Items,' 22 November 1967. NFHWH. Box 219. LBJL.

¹²⁴⁸ Ibid.

¹²⁴⁹ Ibid.

billion in cuts, it would be important to scale back “things, not people.”¹²⁵⁰ This meant targeting federal construction projects, highway programmes, agricultural measures, and funding for supersonic transport development.¹²⁵¹

Following six months of protracted wrangling, Johnson cut \$6 billion in domestic spending to secure the passage of the surtax. Enacted in June 1968, this measure came into being too late to affect the-then record FY 1968 deficit of \$25.1 billion (2.8 percent of GDP). However, it helped generate a \$3.2 billion surplus for FY 1969 (0.3 percent of GDP).¹²⁵² This worried Heller, who predicted that such a swing from red to black would produce a downturn in late 1968.¹²⁵³ To his surprise, a slowdown failed to materialise, partly because the temporary nature of the surcharge did little to affect the long-term income expectations of consumers.¹²⁵⁴ Instead, a 4 percent inflation rate beset the economy at the end of 1968, prompting Heller to tell Johnson that he had egg on his face.¹²⁵⁵ If only the president had called for a tax increase in 1966, he and other Keynesians lamented, there would be little inflation.¹²⁵⁶ Instead, businesspersons interpreted the Vietnam escalation “to mean that good times would roll on.”¹²⁵⁷ Therefore, throughout 1966-67 they went “on an investment binge,” setting America along the path of inflation.¹²⁵⁸ Not only did this undermine the validity of Keynesian economics, it legitimised the arguments of Milton Friedman. He had forecast inflation for late 1968, saying that the Keynesians

¹²⁵⁰ Ibid.

¹²⁵¹ Ibid.

¹²⁵² Extra social insurance tax revenue was also important to this.

¹²⁵³ See Heller, Memorandum for the President, Untitled, 8 September 1968. NFHWH. Box 219. LBJL.

¹²⁵⁴ Morgan, *Deficit Government*, 113.

¹²⁵⁵ Ibid, 114; Heller, Memorandum for the President, Untitled, 31 December 1968. NFHWH. Box 219. LBJL.

¹²⁵⁶ Matusow, *The Unraveling of America*, 161-162; Heller, ‘President Johnson and the Economy,’ in James MacGregor Burns (ed.) *To Heal and to Build: The Programs of President Lyndon B. Johnson* (London, 1968), 159.

¹²⁵⁷ Matusow, *The Unraveling of America*, 161-162.

¹²⁵⁸ Ibid, 161-162.

neglected how quickly the money supply increased during the 1960s. The fact that Friedman's forecast proved consistent with events provided Keynesianism with its first intellectual challenge. This prompted Heller to engage the Chicago economist in various exchanges in the late 1960s.

IV

Friedman was born in Brooklyn, New York, in 1912. He was, as the historian Robert Sobel has observed, "the most important critic of the new economics."¹²⁵⁹ To understand why Friedman afforded the money supply so much importance by 1968, it is important to appreciate his belief that government actions destabilised the economy: if left alone, the private sector would grow at a steady pace.¹²⁶⁰ A champion of the free market, Friedman's identification with classical ideas took shape when he studied at the University of Chicago, an institution that he joined during the 1930s. Whereas Keynesian ideas captivated Heller at this time, Friedman came under the influence of Frank Knight, Henry Simons, and Jacob Viner, all leading critics of Roosevelt's New Deal.¹²⁶¹ After moving to Columbia to complete his PhD, Friedman worked in and out of government. There, he developed a dislike for bureaucracy, believing it to be inefficient.¹²⁶² Before graduating in 1946, Friedman worked as an economics instructor at the University of Wisconsin and (during the war) as a statistical economist for the Tax Research Division of the US Treasury. In both instances, he and Heller interacted. Not only did Heller campaign to have Friedman appointed to the Wisconsin Faculty, he "protested when anti-semitism and personal resentments kept MF [Milton Friedman] from being offered a more prominent

¹²⁵⁹ Sobel, *The Worldly Economists*, 144.

¹²⁶⁰ Matusow, *The Unraveling of America*, 162.

¹²⁶¹ Sobel, *The Worldly Economists*, 149-150.

¹²⁶² *Ibid.*, 151-152.

position.”¹²⁶³ When both men joined the Treasury during the war years, Heller worked as one of Friedman’s assistants.¹²⁶⁴

They struck up a friendship that survived divergent beliefs. Writing to Heller in 1949, Friedman criticised the CED’s decision to incorporate discretionary monetary policy into the stabilizing budget policy, indicating that this would create instability because policymakers could not forecast correctly.¹²⁶⁵ This prompted Heller – a consultant to the CED – to reply that stable tax rates and discretionary monetary policies *could* work in tandem.¹²⁶⁶ As both men established themselves in their respective economics departments during the 1950s – Heller in Minnesota and Friedman in Chicago – it became clear that each of them had different ideas about how the economy should be managed. Whilst Heller championed greater use of discretionary fiscal measures, Friedman favoured use of monetary policy to stabilise the economy. Studying under Simons, Knight, and Viner had exposed him to their work on the quantity theory of money.¹²⁶⁷ Attracted, too, by the fact that monetary policy entailed less government interference in the economy compared with discretionary fiscal measures, much of Friedman’s work in the post-war years involved creating a monetary policy formula that adhered to his belief in small government.

This culminated in Friedman championing the significance of the money supply. In 1963, he published *A Monetary History of the United States*, a monograph that built on previous works offering “a strong defense of the quantity theory of

¹²⁶³ Samuelson to John Thorkelson, 7 July 1987. James Tobin Papers [Henceforth Tobin Papers]. Box 25. Manuscripts and Archives. Yale University Library [Henceforth YUL]. See too Walter P. Heller to Tobin, 21 August 1990. Tobin Papers. Box 25. YUL.

¹²⁶⁴ Sobel, *The Worldly Economists*, 154.

¹²⁶⁵ Friedman to Heller, 22 February 1949. Milton Friedman Papers [Henceforth Friedman Papers]. Box 28. Hoover Institution Archives [Henceforth HIA]

¹²⁶⁶ Heller to Friedman, 25 February 1949. Friedman Papers. Box 28. HIA.

¹²⁶⁷ Sobel, *The Worldly Economists*, 164.

money.”¹²⁶⁸ Arguing that shifts in the money supply constituted the most important factor in understanding the business cycle, Friedman went as far as arguing that the Fed helped cause the Great Depression by allowing the money supply to shrink by a third between 1929 and 1933.¹²⁶⁹ For Friedman, “money possessed a unique power to throw smoothly running economies out of gear.”¹²⁷⁰ People would always strive to retain a certain amount of income as savings, so if the Fed increased the money supply people would spend any excess to restore their balances, thereby producing inflation.¹²⁷¹ Accordingly, he “believed that if only the Fed would permit the money supply to grow at about the same rate as output, without starts and stops, the main source of instability would be eliminated and so would the main excuse for government intervention.”¹²⁷²

Promoting an appealing alternative for many who deplored the new economics, Friedman “missed few opportunities in the late 1960s to contrast what he saw as the lurching behaviour of the Federal Reserve with the apparent consistency...of his rules-based approach.”¹²⁷³ In doing so, he made the argument that the 1964 Revenue Act had virtually no impact upon the economy. Instead, he maintained that the inflation that plagued Heller and the Keynesians in the late 1960s traced its roots back to a substantial rise in the money supply between August 1962 and August 1965.¹²⁷⁴ That accounted for the increase in GNP during this period. Moreover, because Heller, Ackley, and others had concerned themselves primarily with interest rates, Friedman chastised them for not realising that the money supply

¹²⁶⁸ Ibid, 167.

¹²⁶⁹ Friedman and Anna Schwartz, *A Monetary History of the United States, 1867-1960* (Princeton, NJ, 1963), 299-332.

¹²⁷⁰ Matusow, *The Unraveling of America*, 162.

¹²⁷¹ Ibid, 163.

¹²⁷² Ibid, 163.

¹²⁷³ Angus Burgin, *The Great Persuasion: Reinventing Free Markets since the Depression* (Cambridge, MA, 2012), 179.

¹²⁷⁴ Matusow, *The Unraveling of America*, 164.

subsequently grew by more than 6 percent between June 1965 and May 1966, which brought the economy to full employment.¹²⁷⁵ After engineering the credit crunch in the summer of 1966, the Fed increased the money supply again, by both 8.2 percent between January and September 1967 and by 8.5 percent from April to December 1968.¹²⁷⁶ In the process, it unleashed inflation. Whilst Heller predicted a downturn by the end of 1968, Friedman's assertion that a continuous rise in prices would plague the economy proved right.

This precipitated a fierce debate between both men. Deploring Heller's belief that it was possible to fine-tune a full employment economy, Friedman famously stated that inflation was "always and everywhere a monetary phenomenon."¹²⁷⁷ He argued that the tax surcharge failed to curtail inflation because it reduced government borrowing from the central banking system, thereby freeing up funds for private borrowers to spend.¹²⁷⁸ In response, Heller indicated that his focus upon interest rates certainly distracted him from the significance of the money supply: "The question is *not* whether money matters – we all grant that."¹²⁷⁹ At the same time, he argued that there were several issues with Friedman's approach that caused the Chicago man to overstate the money supply's significance. First, Friedman never specified which money supply variable gave the best indication of inflationary and deflationary trends. "Last spring," Heller told Friedman in early 1969, "M1 (the money stock) was all the rage...But when that slowed down, most of the alarmists switched horses to M2 (money plus time deposits), which quite conveniently began rising sharply."¹²⁸⁰

¹²⁷⁵ Ibid, 165.

¹²⁷⁶ Ibid, 170-173.

¹²⁷⁷ Cited in Ibid, 164.

¹²⁷⁸ Ibid, 174. He also stressed that, over the long term, it was impossible to push unemployment below its "natural rate" without aggravating inflation. This contradicted Heller's idea that it was possible to maintain a 4 percent jobless rate through fiscal expansion and still maintain price stability. Ibid, 177.

¹²⁷⁹ Heller and Friedman, *Monetary vs. Fiscal Policy*, 16. Emphasis in the original.

¹²⁸⁰ Ibid, 20. See, too, Heller to Friedman, 18 October 1976. Friedman Papers. Box 28. HIA. Heller made his critique, discussed in the main body of text, at a time when there were simple measures of

Heller also asserted that interest rates were far more important than Friedman suggested. In 1948, the money supply tightened, yet the US was “swamped with liquidity” because interest rates remained low.¹²⁸¹

What also did not add up was how Friedman accounted for his claim of both a long and variable average lag between alterations in the money supply and changes in the rate of output. Heller argued Friedman’s lack of evidence in both these respects quite clearly demonstrated that “the level of economic activity, or total demand for the nation’s output, is influenced by variables other than the stock of money,” including the 1964 Revenue Act.¹²⁸² Accordingly, Heller said that Friedman did not find “anything like a near-perfect correlation – a rigid link – between money and economic activity.”¹²⁸³ The only evidence suggesting that Friedman had done so was that money velocity – the rate at which money exchanged hands in the economy – rose by 28 percent between 1960 and 1968. However, if velocity was the same in 1968 as it was for 1960, GNP should have been \$675 billion, not \$860 billion. The money supply, Heller concluded, could not produce such a difference, which showed other factors determined both velocity and output.¹²⁸⁴ True, Friedman had demonstrated that economists should give more attention to changes in the money supply, but Heller and James Tobin pointed out that implementing a “fixed-throttle money-supply rule” would be destabilising. Indeed, it would be impossible to adjust fiscal policy and interest rates to offset unforeseen economic problems.¹²⁸⁵ As a former staff economist on the Heller CEA also put it, Friedman based his argument

money. Economists conceived various redefinitions in the 1970s and 1980s because the measurement of the money supply became more complex. This made it even more challenging for monetarists to pinpoint which money supply variable accurately reflected inflationary and deflationary trends, something that Heller alluded to in this 1976 letter.

¹²⁸¹ Heller and Friedman, *Monetary vs. Fiscal Policy*, 20.

¹²⁸² *Ibid.*, 24.

¹²⁸³ *Ibid.*, 22.

¹²⁸⁴ *Ibid.*, 22.

for a fixed money supply rule on his assertion that government activism bred instability, which ignored the fact that “changes in business policy” did the same.¹²⁸⁶

In addition to the various critiques advanced by the Keynesians, David Shreve has pointed out that, in formulating his thesis, Friedman assumed “that the nation’s stock of money was determined only from the supply side, that is through the actions of the Federal Reserve.”¹²⁸⁷ Throughout the 1960s, though, private banks and non-bank corporations “acted to increase the nation’s supply of money without prodding from the Federal Reserve.”¹²⁸⁸ This demonstrated that Friedman had oversimplified his analysis. As to his suggestion that the 1964 tax cut did nothing to create the expansion of the 1960s, Heller argued “that however you sliced it, consumption spending, up by an average of \$4.4 billion per quarter in the three quarters proceeding the tax cut, jumped ahead by \$8.4 billion per quarter in the three quarters following the tax cut.”¹²⁸⁹ Demand-induced fiscal policy, therefore, was the most important element behind the 1960s expansion. The fact that Friedman failed to amass any concrete evidence to link the prosperity of that decade to the increase in the money supply shows that he failed to refute this point sufficiently.

Given these various limitations, it is unsurprising that soon after Friedman rose to prominence the performance of the economy failed to conform to his expectations. Having forecast inflation in the last half of 1969, Friedman argued that this would turn into a sharp recession in 1970 as the Fed responded by reducing the money supply to almost zero. That failed to materialise, though output did

¹²⁸⁵ Ibid, 26; Tobin, *The New Economics*, 72-73; Heller, ‘President Johnson and the Economy,’ 156-157.

¹²⁸⁶ Barbara Bergmann to Lester Taylor, 1 May 1970. Heller Papers. Box 6. UoM.

¹²⁸⁷ Shreve, ‘A Precarious and Uncertain Liberalism,’ 219.

¹²⁸⁸ Ibid, 219-220 (quotation 219.)

¹²⁸⁹ Cited in Ibid, 232.

decrease.¹²⁹⁰ As Heller also pointed out, the Fed then responded to that downturn by adopting Friedman's approach, as it set a target of expanding the money supply at 2 – 3 percent for 1970.¹²⁹¹ Halfway through that year it then revised that figure upwards to 5 percent, mainly because the economy remained sluggish.¹²⁹² Such a switch in policy clearly showed “that [adhering to] a given rate of growth of the money supply” was “a difficult and elusive target.”¹²⁹³ However, convinced that its policy could work, the Fed continued to increase the money supply further, to such an extent that in the first quarter of 1971 the money stock (M1, demand deposits, plus currency) rose by 7 – 8 percent, having grown 6 ½ percent over the previous 12 months. The economy remained stagnant, prompting Heller to remark, “in 15 months of experience with its heavier emphasis on the money supply, the Fed has found little support for the general proposition that money supply creates its own demand.”¹²⁹⁴

As the 1970s unfolded and inflation worsened, further evidence discredited Friedman, which Heller used to good effect. In a 1979 article for the *Wall Street Journal* (a publication to which Heller regularly contributed in the 1970s), he wrote that inflation was clearly embedded in “external forces largely beyond the reach of monetary policy,” especially given the domestic impact of the global increases in food and oil prices during the 1970s.¹²⁹⁵ To the extent that a reduction in the money supply was capable of subduing inflation, Heller indicated that the impact of external shocks needed to be absent and said that such a strategy could have “unconscionable

¹²⁹⁰ Heller, ‘The U.S. Economic Outlook,’ *NCBM*, 29 September 1970. Heller Papers. Box 10. UoM.

¹²⁹¹ *Ibid.*

¹²⁹² *Ibid.*

¹²⁹³ *Ibid.* Indeed, the monetarist experiment in the early 1980s further demonstrated this point. For insightful analysis see Morgan, ‘Monetary Metamorphosis: The Volcker Fed and Inflation,’ *Journal of Policy History*, 24:4 (2012), 545-571.

¹²⁹⁴ Heller, ‘Vigorous Recovery Without Inflation: Can We Do It?’ Excerpts from Remarks before the Detroit Economic Club, Michigan, 5 April 1971. Heller Papers. Box 10. UoM.

¹²⁹⁵ Heller, ‘The Realities of Inflation,’ *Wall Street Journal*, 19 January 1979, 10. PQHN. He also made this point in a debate with Friedman in 1978. See, ‘Milton Friedman: Why Economists Disagree.’ Available at: <https://www.youtube.com/watch?v=kG8iXMaZTXE> [Accessed 07/31/2016]

costs in jobs and output,” so much so it could produce a ““deep, deep, depression.”¹²⁹⁶ Clearly, there were painless ways to arrest this issue, and, by this point, Friedman was not advancing his arguments as cogently as he had done beforehand.¹²⁹⁷ Thus, Heller responded robustly to the prominence of monetarist theory in the late 1960s and 1970s, despite the fact that the eclipse of Keynesianism had already begun.

V

Indeed, the rise of Friedman came on top of the Keynesians’ failure to fine-tune the economy in the mid-to-late 1960s. In addition, just as monetarism experienced problems during the 1970s, the Keynesians struggled to defend their doctrine due to the unprecedented phenomenon of stagflation. The next chapter will explore Heller’s response to this problem. Before doing so, it is essential to reflect upon his role in the beginning of Keynesianism’s eclipse. What is clear is that, despite the confidence with which he initially approached the second half of the 1960s, the Minnesotan overestimated how easy it would be to manage an economy operating at full employment. In fact, he later admitted that his use of the phrase “fine-tuning” was just as embarrassing as his “puritan ethic” remark of 1963.¹²⁹⁸ It is also clear that, despite the assertions of certain Johnson scholars, Heller, Ackley, and others deserve part of the blame for letting the inflationary genie out of the bottle.

Heller did this by both encouraging Johnson to view Vietnam and the Great Society as compatible and by not coordinating his recommendations more effectively with other advisers. If he had better communicated his ideas and not worried about expanding the Great Society, LBJ may have abandoned his desire not to sacrifice the latter for a tax increase at an earlier date. Once Johnson did request that measure, Heller was useful in his attempts to convince both the public and members of

¹²⁹⁶ Heller, ‘The Realities of Inflation.’

Congress that the surtax was a necessity. Still, the British devaluation of the pound in November 1967 played the most important role in forging a compromise to pass it. Heller also responded in an effective manner to the rise of Friedman. This point is worth making, not least because it disputes Allen Matusow's argument that the Keynesians did not react well to the revival of monetarism in the late 1960s.¹²⁹⁹ Heller also moderated "his views to incorporate an [enhanced] appreciation of the importance of monetary policy," something that the next chapter will demonstrate.¹³⁰⁰

The eclipse of Keynesianism thus started to take place by the time Friedman came to prominence. This meant that the Keynesian liberalism espoused by Heller also started to alter. As this chapter has shown, an important shift took place when Heller emphasised the preservation of Great Society programmes over their expansion. This occurred after Johnson reduced domestic spending to secure passage of the surcharge, which reflected a broader shift in liberal circles away from quantitative and towards qualitative liberalism in the late 1960s and early 1970s.¹³⁰¹ As Robert Collins has noted, "growth liberalism's combination of growth-inducing tax cuts, an escalating war in Vietnam, and increased social spending at home had overstrained economic institutions and capabilities."¹³⁰² This gave rise to liberal (and conservative) discontent. In 1973, even Heller admitted that the "great rise in GNP in recent decades – especially in the 1960's, when real income per family (in constant dollars) rose nearly forty percent – has not brought about the personal gratification, the better life, [and] the remedies of social injustices that should have come with such

¹²⁹⁷ Johnston, Interview with the Author.

¹²⁹⁸ Cited in Spulber, *Managing the American Economy from Roosevelt to Reagan*, 79.

¹²⁹⁹ Matusow, *The Unraveling of America*, 153-180.

¹³⁰⁰ Sobel, *The Worldly Economists*, 143.

¹³⁰¹ Importantly, the \$6 billion in cuts that Johnson requested did not come about in full, but the reduction constituted a significant amount.

¹³⁰² Collins, *More*, 68.

material advances.”¹³⁰³

In response to growth’s perceived excesses, certain liberals placed “a new emphasis on the pursuit of quality in American life.”¹³⁰⁴ Heller, for example, discussed the need to rein in the environmental havoc caused by the pursuit of growth, saying that it was important to “make growth cleaner, more benign, [and] more enjoyable.”¹³⁰⁵ The rise of the New Politics movement also reflected this renewed focus upon qualitative liberalism. New Politics liberals fused concerns about improving the quality of life with those of both the anti-war and rights-based movements of the late 1960s.¹³⁰⁶ Seeking to return the Democrats to the left of the political spectrum, the liberalism of the New Politics movement found ultimate expression in George McGovern’s unsuccessful 1972 presidential campaign, which called for a “liberalism of entitlement.”¹³⁰⁷ Influenced by Keynesian adviser John Kenneth Galbraith, McGovern ran on a platform to implement a universal income funded by both a \$22 billion tax increase on the wealthy and a \$32 billion cutback in defence spending.¹³⁰⁸ Heller did not go as far as endorsing the New Politics movement. However, he did shift towards a qualitative perspective during the late 1960s and early 1970s. He admitted, “great wealth – the greatest any nation has ever known – has not been translated into a great society.”¹³⁰⁹ This is important to understanding how Heller adapted his views during the economic and political turmoil of the 1970s and 1980s.

¹³⁰³ Heller, *Economic Growth and Environmental Quality: Collision or Co-Existence?* (Morristown, NJ, 1973), 1.

¹³⁰⁴ Collins, *More*, 62.

¹³⁰⁵ Heller, *Economic Growth and Environmental Quality*, 17.

¹³⁰⁶ Kenneth S. Baer, *Reinventing Democrats: The Politics of Liberalism from Reagan to Clinton* (Lawrence, KS, 2000), 19.

¹³⁰⁷ Davies cited in *Ibid*, 24-25.

¹³⁰⁸ Kamen, ‘Old Liberals, New Politics,’ 319.

¹³⁰⁹ Heller, *Economic Growth and Environmental Quality*, 1.

Chapter Eight

A Keynesian in the Wilderness

At the 1974 annual meeting of the American Economic Association, Walter Heller delivered the plenary address. With the economy beset by both stagnation and inflation, a phenomenon known as stagflation, Heller wanted to highlight what was “right with economics.”¹³¹⁰ However, he admitted that economists had been “caught” with their “parameters down,” having failed to foresee the miserable conditions of the 1970s.¹³¹¹ For the Keynesians, stagflation amounted to a large blow. As one historian noted, stagflation “undermined the utility of fiscal policy,” helping cause what Herbert Stein described as its “disintegration.”¹³¹² Inflation averaged 9.3 percent from 1973-80, whilst unemployment averaged 5.5 percent from 1970-75 and 7 percent from 1975-80.¹³¹³ Against this backdrop, Presidents Richard Nixon (1969-74), Gerald Ford (1974-77) and Jimmy Carter (1977-81) struggled to solve the nation’s problems, veering back and forth between expansionary and restrictive fiscal measures. The disintegration of fiscal policy allowed monetary policy to usurp it. It also paved the way for the revival of supply-side economics, which Republican Ronald Reagan (1981-89) embraced prior to his election in 1980.

With Keynesianism pushed out of the limelight, Heller asserted that it was “[still] valid.”¹³¹⁴ In contrast, one congressional aide writing in a highly conservative magazine claimed Heller could not “accept how completely today’s economic world

¹³¹⁰ Heller, ‘What’s Right With Economics?’ *American Economic Review*, 65:1 (Mar. 1975), 1-26.

¹³¹¹ *Ibid*, 15. Heller originally made this remark a year earlier, before repeating it here (something he alluded to in this speech).

¹³¹² Morgan, *The Age of Deficits*, 37; Stein, *On the Other Hand...Essays on Economics, Economists, and Politics* (Washington DC, 1995), 157. By “disintegration,” Stein was referring to the fact that fiscal policy had become unable to adhere to a given rule, such as either an annually balanced budget or a cyclically balanced budget at high employment.

¹³¹³ Morgan, *Deficit Government*, 116.

¹³¹⁴ Harold G. Shane, ‘Stagflation! A Talk with Economist Walter Heller,’ *The Phi Delta Kappan International*, 56:7 (Mar. 1975), 475.

contradicts his Ivory Tower theories.”¹³¹⁵ Echoing this, economists Robert Lucas and Thomas Sargent argued in 1979 that Keynesianism no longer had any “value in guiding policy.”¹³¹⁶ Most historians have reached a similar conclusion. In doing so, they have cited either the unpopular Keynesianism of New Politics liberals or the ideas of traditional New Deal-Great Society liberals. The latter advocated Keynesian policies described as “outmoded, irrelevant, and intellectually bankrupt.”¹³¹⁷ Speaking about Senators Hubert Humphrey of Minnesota and Edward Kennedy of Massachusetts, Sean Wilentz claimed they “seemed to have run out of steam; it was more apt to look back at the glory days of yore than to propose coherent policies for the present and future.”¹³¹⁸

In contrast, this chapter assesses Heller’s responses to both stagflation and Reaganomics, arguing that post-1960s Keynesian liberalism was more vibrant than assumed. It builds upon recent scholarship by Scott Kamen and Patrick Andelic, both of whom have demonstrated that a group of “neoliberals” emerged in the 1970s Democratic Party to adapt it to new conditions.¹³¹⁹ These individuals included Senators Gary Hart of Colorado and Paul Tsongas of Massachusetts, who “moved to the right of their New Politics predecessors and the Democratic establishment on matters of economic policy.”¹³²⁰ This chapter shows that Heller occupied similar ground, to the point whereby he anticipated Bill Clinton’s New Democrat approach to

¹³¹⁵ Bently T. Elliot, ‘Walter Heller: Inflation Fighter or Worn-Out Keynesian?’ *Human Events*, 38:43 (Oct. 1978), 12 (quotation), 19. PQHN.

¹³¹⁶ Robert Lucas and Thomas Sargent, ‘After Keynesian Macroeconomics,’ *Federal Reserve Bank of Minneapolis Quarterly Review*, 3:2 (Spr. 1979), 2.

¹³¹⁷ Morgan, ‘Liberalism and Inflation in the 1970s,’ Paper delivered at the Policy History Association Conference, Richmond, Virginia. June 2012. Author’s copy. Morgan does not subscribe to the orthodox view described above. His quote in the above paragraph merely describes it.

¹³¹⁸ Cited in Ibid. For examples of other historians who make this argument see Phillips-Fein, *Invisible Hands*, 167; Jefferson Cowie, *Stayin’ Alive: The 1970s and the Last Days of the Working Class* (New York, 2012), 262, 265; Sandbrook, *Mad as Hell*, 290; Stein, *Pivotal Decade: How the United States Traded Factories For Finance in the Seventies* (New Haven, CT, 2010), 190; and James Reichley, *Conservatives in an Age of Change* (Washington DC, 1981), 404.

¹³¹⁹ Andelic, ‘Donkey Work’; Kamen, ‘Old Liberals, New Politics.’

economic policy by the end of the 1980s. In doing so, the chapter demonstrates that the New Democrats did not simply emerge out of the failure of New Politics liberalism. Instead, liberals like Heller, who traced their roots back to New Deal-Great Society liberalism, helped lay the groundwork for Clinton's presidency.

I

Traditional liberals approached stagflation with the belief that unemployment surpassed inflation as the greater of the two problems.¹³²¹ At the beginning of the 1970s, in contrast, Heller described inflation as “the number one *economic* policy problem.”¹³²² Richard Nixon, having inherited a Vietnam-inflated economy in January 1969, extended Lyndon Johnson's tax surcharge for an extra twelve months (reducing it to 5 percent in the final half of that period). The Fed, meanwhile, engineered a credit crunch, which brought the economy to a halt by 1970. Nixon's CEA chairman Paul McCracken described this combination of fiscal control and monetary restraint as “gradualism.”¹³²³ The importance that it afforded monetary policy demonstrated that, to an extent, Nixon and his advisers sympathised with Milton Friedman's ideas (with McCracken describing his views as “Friedmanesque” rather than “Friedmanite”).¹³²⁴ Heller, too, broadly approved of tackling inflation in this way, thereby demonstrating the enhanced importance he attached to the money supply.¹³²⁵ Despite Nixon's use of gradualism, inflation hovered above 5 percent at the beginning of 1970, a phenomenon that Heller earlier confessed to being “struck

¹³²⁰ Kamen, ‘Old Liberals, New Politics,’ 317.

¹³²¹ Morgan, ‘Liberalism and Inflation in the 1970s.’

¹³²² Heller, ‘The Economic Goals and Policies of the Nixon Administration: An Analysis,’ Remarks before the Business Week Conference on Money and Corporation, New York City, 8 December 1969. Heller Papers. Box 8. UoM. Emphasis in the original [Henceforth GPNA]

¹³²³ Matusow, *Nixon's Economy: Booms, Busts, Dollars and Votes* (Lawrence, KS, 1998), 15-16.

¹³²⁴ *Ibid.*, 15.

¹³²⁵ GPNA.

by.”¹³²⁶ Because Nixon’s macroeconomic strategy failed to curb inflation, Heller argued there were “other plausible, feasible, and reasonable things that could be done.”¹³²⁷ Therefore, he suggested that Nixon should focus his policies at a microeconomic level, particularly in terms of reducing inflationary pressures on the supply-side of the economy.¹³²⁸

This demonstrated that Heller had a sound grasp of America’s economic problems. True, the Vietnam War initially sparked inflation, but a host of supply-side factors converged at the beginning of the 1970s to make the issue more troublesome. Arguably, the most important was “the big wage increases that workers were demanding and getting.”¹³²⁹ During Vietnam, unions “had signed long-term contracts locking workers into wages that failed to keep pace with prices.”¹³³⁰ The expiration of these contracts at the start of the 1970s caused unions to lobby for “automatic cost-of-living salary increases pegged to increases in the Consumer Price Index.”¹³³¹ This forced businesses to increase prices in line with inflation. In response, Heller suggested that Nixon should implement wage-price guideposts.¹³³² Liberal economist Arthur Okun, too, pressed such a policy upon Nixon, telling the president in late 1969 that certain prices had only risen by 1 percent in 1968 (when an incomes policy had been in effect).¹³³³ Additionally, Gardner Ackley, John Kenneth Galbraith, Paul Samuelson, and Fed Chairman William McChesney Martin called for revival of the wage-price guideposts of the 1960s, but Nixon was unmoved.¹³³⁴

¹³²⁶ The inflation figure is from Heller, ‘The U.S. Economic Outlook for 1970,’ *NCBM*, 9 January 1970. Heller Papers. Box 10. UoM. For the quote see Heller, ‘The Economic Outlook,’ *NCBM*, 27 September 1969. Heller Papers. Box 10. UoM.

¹³²⁷ GPNA.

¹³²⁸ Ibid.

¹³²⁹ Matusow, *Nixon’s Economy*, 63.

¹³³⁰ Ibid, 64.

¹³³¹ Morgan, *Beyond the Liberal Consensus*, 91-92.

¹³³² GPNA; Heller, ‘The US Economic Outlook,’ 29 September 1970.

¹³³³ Shreve, ‘A Precarious and Uncertain Liberalism,’ 402.

¹³³⁴ Ibid, 404.

Despite Nixon's initial refusal to implement an incomes policy, international considerations eventually compelled him to do so. By mid-1971, the Bretton Woods system was on the brink of collapse. The number of dollars held by foreigners dwarfed US gold reserves. Added to this, the US had a shrinking proportion of the world's trade and fixed exchange rates offered no help for this, as they underwrote a strong dollar to the detriment of US exports.¹³³⁵ Clearly, the dollar was overvalued and when, in 1971, the US ran its first merchandise trade deficit since 1893, this precipitated a new run on gold.¹³³⁶ To stem this, Nixon suspended dollar-gold convertibility in the summer of 1971, as a prelude to axing the system of fixed exchange rates altogether in 1973. To reassure foreigners that such an action would not boost inflation (through the dollar's subsequent devaluation) the president imposed the first peacetime freeze on wages and prices.¹³³⁷ Heller opposed this on the grounds that controls limited economic freedom, created distortions in the allocation of resources (because they prevented markets from operating naturally), and invited a rise in black market activity.¹³³⁸ Nevertheless, even he praised Nixon for undertaking "bold initiatives" to "cope with the three-ply crisis of a faltering recovery, of a vicious price-wage spiral, and a teetering dollar."¹³³⁹

With an incomes policy enacted, Nixon abandoned gradualism. This, too, was something that Heller supported. Whilst the Consumer Price Index (CPI) had risen by 5.9 percent in 1970 (compared with 5.4 percent in 1969), unemployment increased from 3.5 percent to 5 percent in 1969-70.¹³⁴⁰ "Given the background of excessively

¹³³⁵ Matusow, *Nixon's Economy*, 126-128.

¹³³⁶ Morgan, *Deficit Government*, 120.

¹³³⁷ Shreve, 'A Precarious and Uncertain Liberalism,' 410.

¹³³⁸ Heller, 'Mark Scheme for PA211 Final Exam,' 8 June 1970. Heller Papers. Box 4. UoM.

¹³³⁹ Heller, 'Corrected Transcript of Remarks on President Nixon's New Economic Policy,' Testimony to the JEC, 19 August 1971. Heller Papers. Box 10. UoM.

¹³⁴⁰ Heller, 'The US Economic Outlook for 1971,' *NCBM*, 7 January 1971. Heller Papers. Box 10. UoM.

tight money and customary lags in budgetary policy,” Heller explained, “it was appropriate for Federal Reserve policy to serve as a first line of offense as policy turned from restriction to expansion in 1970-71.”¹³⁴¹ However, fiscal stimulus should accompany this, he added.¹³⁴² Following the advice of his own economic counsellors, Nixon agreed. He had already put considerable pressure upon his long-time associate and former Eisenhower CEA chairman Arthur Burns, who replaced Martin as Fed chairman in January 1970, to loosen credit.¹³⁴³ Nixon then ran deficits of \$23 billion and \$23.3 billion (2.1 percent and 1.9 percent of GDP) for FYs 1971-72, actions accompanied by him saying, “I am now a Keynesian in economics.”¹³⁴⁴ David Shreve has argued that Nixon’s economic policies mostly eschewed the use of 1960s Keynesianism, a development that essentially confirmed the doctrine’s eclipse in the early 1970s. This was not least because the president failed to make use of Lyndon Johnson’s wage-price guideposts to keep inflation in check.¹³⁴⁵ Yet, this assessment largely ignored the president’s expansionary deficits in FYs 1971-72, which provided the economy with a large Keynesian stimulus. Others have suggested that Nixon deliberately pumped up the economy to secure his re-election, an action that ultimately unleashed double-digit inflation.¹³⁴⁶ However, Allen Matusow has demonstrated that “policymakers in 1972 misread the economy.”¹³⁴⁷ They essentially “gunned the motor,” not realising that the economy had expanded enough in 1971.¹³⁴⁸ Heller, too, was guilty of this miscalculation, a point that suggests that Nixon and his

¹³⁴¹ Ibid.

¹³⁴² Ibid; Heller, ‘Vigorous Recovery Without Renewed Inflation.’

¹³⁴³ Wyatt C. Wells, *Economist in an Uncertain World: Arthur F. Burns and the Federal Reserve, 1970-78* (New York, 1994), 60-65; and Robert H. Ferrell, *Inside the Nixon Administration: The Secret Diary of Arthur Burns, 1969-1974* (Lawrence, KS, 2010), 37-40.

¹³⁴⁴ Morgan, *Deficit Government*, 120.

¹³⁴⁵ Shreve, ‘A Precarious and Uncertain Liberalism,’ 387-448.

¹³⁴⁶ Morgan, *Deficit Government*, 120.

¹³⁴⁷ Matusow, *Nixon’s Economy*, 185.

¹³⁴⁸ Ibid, 185.

advisers were not alone in underestimating the impact of such a policy change.¹³⁴⁹

Even though Heller broadly agreed with gradualism, the end of Bretton Woods, the expansionary policies in 1971-72, and the imposition of a wage-price freeze in the summer of 1971, he argued that it was essential to develop “a set of carefully thought out wage-price tranquilizers.”¹³⁵⁰ With Nixon under public pressure to replace the freeze with permanent controls in the fall of 1971, Heller said there was “not a moment to lose...in getting labor, business, and public representatives in this country to hammer out some kind of social compact” for wage-price guideposts.¹³⁵¹ He reiterated this point in an appearance on *Meet the Press* in October 1971, where he urged the administration not to “clamp on direct controls.”¹³⁵² Galbraith, Okun, and Ackley also made this argument, but Nixon ignored the liberal economists.¹³⁵³ Instead, the president followed up his wage-price freeze by implementing controls in the fall of 1971, believing that doing so would keep inflation in check. “The administration’s theory,” Nixon’s CEA member Herbert Stein said, “was that the inflation was being propelled by expectations and by long-term wage contracts rather than by current pressure of demand.”¹³⁵⁴ Therefore, Nixon enacted Phase II of his controls experiment, which involved the administration enforcing respective wage and price increases of 5.5 percent and 3 percent.¹³⁵⁵ To Heller’s surprise, Phase II worked.¹³⁵⁶

Despite this, Heller wanted enactment of wage-price guidelines. He also emphasised the importance of not abandoning Phase II quickly. The “large and rising

¹³⁴⁹ Heller, ‘The Economic Outlook,’ *NCBM*, 5 October 1972. Heller Papers. Box 10. UoM.

¹³⁵⁰ Heller, ‘Corrected Transcript of Remarks on President Nixon’s New Economic Policy.’

¹³⁵¹ Heller, ‘The US Economic Outlook for 1971,’ 7 January 1971; *Ibid* (quotation).

¹³⁵² Cited in Shreve, ‘A Precarious and Uncertain Liberalism,’ 409.

¹³⁵³ *Ibid*, 409.

¹³⁵⁴ Stein, *Presidential Economics*, 182.

¹³⁵⁵ Rowen, *Self-Inflicted Wounds*, 72.

¹³⁵⁶ *Ibid*, 73. Heller, ‘The Economic Outlook,’ 5 October 1972.

full employment Federal deficit in fiscal 1973,” he warned in October 1972, “plus a 7 percent to 8 percent rise in the money supply in calendar 1972 are generating plenty of steam in the economic boiler.”¹³⁵⁷ Hence, anything but a smooth transition from controls to guideposts would “seriously jeopardize the progress that has been made in checking inflation.”¹³⁵⁸ This opinion proved correct. After Nixon won re-election in November 1972, he quickly abandoned his wage-price controls. In January 1973, what Heller described as “a semi voluntary and haphazard” programme called Phase III replaced Phase II.¹³⁵⁹ This relaxed the existing controls that were in place. After inflation subsequently shot up, Nixon implemented another temporary freeze before abandoning his controls experiment in 1974.¹³⁶⁰ These actions amounted to what Keynesian Alan Blinder described as “a masterpiece of ill timing.”¹³⁶¹ Under Freeze I and the first half of Phase II, the CPI rose by only 2.9 percent (compared with 3.8 percent from December 1970 to August 1971).¹³⁶² The haphazard transition to decontrol came as both rocketing food prices (caused by crop failures abroad) and substantial rises in energy costs (due to the Arab Oil Embargo of 1973-74) beset the economy. Together, these developments pushed the CPI up by 8.8 percent in 1973 and by 12.2 percent in 1974.¹³⁶³ Nixon was not alone in failing to foresee these supply shocks, but he “helped fan the inflationary fires” by decontrolling the expanding economy so quickly.¹³⁶⁴

II

With prices soaring in 1973-74, Heller called for further supply-side actions to

¹³⁵⁷ Heller, ‘The Economic Outlook,’ 5 October 1972.

¹³⁵⁸ Ibid.

¹³⁵⁹ Cited in Rowen, *Self-Inflicted Wounds*, 73.

¹³⁶⁰ Ibid, 81-84.

¹³⁶¹ Alan Blinder, *Economic Policy and the Great Stagflation* (London, 1979), 132.

¹³⁶² Rowen, *Self-Inflicted Wounds*, 79.

¹³⁶³ Morgan, *Deficit Government*, 122.

¹³⁶⁴ Blinder, *Economic Policy and the Great Stagflation*, 132.

bring this problem under control. Notably, the Minnesotan had stressed the need for such policies before the onset of double-digit inflation. In December 1969, Heller emphasised the need to exploit the economy's more globalised position to bring inflation down. In particular, he argued that boosting import quotas offered a way to accomplish this. This policy, he said, would cut prices by producing "more effective competition of imported goods with domestic goods."¹³⁶⁵ Nixon had failed to boost quotas on imported meat in 1969. This did nothing to reduce the growing CPI (caused by surges in meat prices), which substantiated Heller's argument.¹³⁶⁶ Additionally, Heller argued that removing red tape in the transportation sector would be an effective supply-side response to inflation. "[I]ntermodal competition...can do much of what regulations rooted in a long-gone age of transportation monopoly have been doing in setting transportation prices."¹³⁶⁷

Aside from the anti-inflationary potential that he saw in these supply-side measures, the fact that free trade and deregulation were broadly deemed Republican Party policies made Heller's espousal of both stand out.¹³⁶⁸ True, deregulation did emerge as a key issue for traditional Democrats during the mid-1970s. Edward Kennedy conducted hearings into deregulation as chairman of the Senate Subcommittee on Administrative Practises and Procedure. Yet, Kennedy focused primarily upon breaking the "'cosy triangle' relationship between the regulated industry, congressional committee overseers, and the federal agency implementing the regulations."¹³⁶⁹ Heller, by contrast, viewed deregulation primarily as a means to offset the titanic costs associated with such measures. In this, he had more in common with the conservative economist and future Reagan CEA chairman Murray

¹³⁶⁵ GPNA.

¹³⁶⁶ Matusow, *Nixon's Economy*, 65.

¹³⁶⁷ GPNA.

¹³⁶⁸ Sobel, *The Worldly Economists*, 214.

Weidenbaum, who predicted that the costs of regulations amounted to \$100 billion a year in the late 1970s.¹³⁷⁰ His positioning on deregulation also mirrored that of the neoliberals, who “were more open to market-oriented solutions in public policy and had a larger affinity for business” than did traditional liberals.¹³⁷¹ Similarly, Heller’s emphasis on free trade aligned him with politicians like Hart and Tsongas but put him at odds with organised labour, who favoured protectionist policies to safeguard America’s “old-line industries as steel, autos, electrical appliances, and sectors of the textile industry.”¹³⁷²

As inflation hit double-digits in 1974, Heller’s position to the right of traditional Democrats grew clearer. In September of that year, Heller was one of numerous economists called to Washington to brief Gerald Ford. Worried about inflation, Ford asked his visitors how to solve it. Heller once again called for the reduction of tariffs and deregulation, but he also strongly urged repeal of the Davis-Bacon Act.¹³⁷³ Enacted during the 1930s, Davis-Bacon allowed the federal government to set minimum wage rates on federally financed construction projects.¹³⁷⁴ By the 1970s, many argued that this was causing wages in the construction industry to skyrocket, “to the point where they no longer represent *average* rates but are simply *union scales*, imported from great distances.”¹³⁷⁵ This added to the costs of construction projects and drove up prices, so much so that Davis-Bacon was supposedly raising construction costs by several hundred million

¹³⁶⁹ Morgan, ‘Liberalism and Inflation in the 1970s.’

¹³⁷⁰ Phillips-Fein, *Invisible Hands*, 176.

¹³⁷¹ Baer, *Reinventing Democrats*, 33.

¹³⁷² Michael Kramer, ‘Where Does Hart Stand?’ *New York Magazine*, 9 April 1984, 30 [google books]; Matusow, *Nixon’s Economy*, 119 (quotation).

¹³⁷³ n.n., *The Economists Conference on Inflation, September 5 1974 and September 23 1974* (Washington DC, 1974), 74-76; Heller, ‘An Open Letter to President Ford,’ *Wall Street Journal*, 12 August 1974, 8. PQHN. In the former, Heller implicitly made reference to Davis-Bacon with his “sacred cows” remark.

¹³⁷⁴ Martha Derthick and Paul J. Quirk, *The Politics of Deregulation* (Washington DC, 1985), 219.

dollars per year.¹³⁷⁶ As construction was the nation's largest industry, there were serious concerns that its expanding costs "would spill over into the rest of the price level."¹³⁷⁷ Recognising this, Nixon briefly suspended Davis-Bacon in February 1971, but Heller advised Ford to repeal the measure completely.¹³⁷⁸

According to Hubert Humphrey, Heller's advice "stirred up a hornets' nest" amongst traditional liberals, who criticised him for denouncing a measure designed to protect workers' wages.¹³⁷⁹ Andrew J. Biemiller, Director of the AFL-CIO's Department of Legislation, described Heller's comments as "just incredible."¹³⁸⁰ Yet, Davis-Bacon was not the only piece of traditional liberal legislation that Heller wanted repealed, as he claimed that other "very sacred political cows need to be slaughtered."¹³⁸¹ Chief among them was the Anti-Price Discrimination Act of 1936 (otherwise known as the Robinson-Patman Act).¹³⁸² Implemented to curtail anticompetitive pricing, this made producers sell their stock at the same cost to both small businesses and chain stores. By the 1970s, many argued this also underpinned inflation as chain stores sold their products at artificially high prices. Heller argued that it was appealing to repeal Robinson-Patman, as it "directly support[s] or boost[s] costs and prices."¹³⁸³ Ford did ask the Justice Department to study whether repeal would be effective, but the House Small Business Committee mounted effective opposition to this. Still, the fact that Heller wanted to repeal Robinson-Patman

¹³⁷⁵ Allan C. Brownfield, 'Taxpayer's Dollars Wasted by Davis-Bacon,' *Human Events*, 36:7, 14 February 1976, 8. Emphasis in the original. PQHN.

¹³⁷⁶ Derthick and Quirk, *The Politics of Deregulation*, 219.

¹³⁷⁷ Stein, *Presidential Economics*, 152.

¹³⁷⁸ Matusow, *Nixon's Economy*, 95; Heller, 'An Open Letter to President Ford.'

¹³⁷⁹ Humphrey to Heller, 14 October 1974. Hubert Humphrey Papers [Henceforth Humphrey Papers]. Senatorial Files, 1971-78. Correspondence Files-Legislative, 1974. Box 3. MHS.

¹³⁸⁰ Andrew J Biemiller to Humphrey, 3 October 1974. Attached to Ibid.

¹³⁸¹ Heller, 'The Battle Against U.S. Inflation,' Edited Transcript of Remarks before the International Monetary Conference for the American Bankers Association, Hot Springs, Virginia, 19 May 1970. Heller Papers. Box 8. UoM.

¹³⁸² Heller, 'The US Economic Outlook for 1970,' 9 January 1970.

¹³⁸³ Ibid.

demonstrated that he was willing to fight inflation by sacrificing what many liberals regarded as “the Magna Charta of small business.”¹³⁸⁴

Even though repeal of Robinson-Patman did not take place, Ford rescinded a host of other fair-trade regulations in December 1975.¹³⁸⁵ Again, these measures traced their roots back to the 1930s and Heller supported Ford’s actions. Five years earlier, for example, he claimed that eradicating fair trade legislation “would result in [a] 0.3 percent reduction of the consumer price index.”¹³⁸⁶ Additionally, the Walsh-Healey Public Contracts Act of 1936 was another piece of New Deal legislation that Heller wanted repealed.¹³⁸⁷ This gave the federal government the power to set minimum wages and overtime pay for contractors who sold it a certain amount of supplies, materials, and equipment. Devised to prop up wages during the Great Depression, Heller viewed this as another law that made “government an accomplice in many cost and price-propping actions.”¹³⁸⁸ As in the case of Davis-Bacon, repeal of Walsh-Healey did not take place. Still, whilst some scholars have been critical of traditional liberals for seeking New Deal-era solutions to combat stagflation, Heller quite clearly sought the repeal of certain policies that traced their roots back to the 1930s.¹³⁸⁹ This demonstrates that he adapted his views in a way that was more in line with the neoliberals of the 1970s. It further shows that he recognised the need to modify his thinking to take into account the more inflationary climate of that decade.

III

What also reflected this was that, by the mid-1970s, Heller was calling for

¹³⁸⁴ Jonathan J. Bean, *Beyond the Broker State: Federal Policies Toward Small Business, 1936-1961* (Chapel Hill, NC, 1996), 62.

¹³⁸⁵ Shanahan, ‘Fair Trade’ Laws Coming to an End,’ *New York Times*, 13 December 1975, 57. PQHN.

¹³⁸⁶ GPNA.

¹³⁸⁷ Heller, ‘The US Economic Outlook for 1970,’ 9 January 1970.

¹³⁸⁸ Heller, ‘An Open Letter to President Ford.’

¹³⁸⁹ See Cowie’s chapter, labelled “The New Deal that Never Happened,” in *Stayin’ Alive*, 261-313.

even more supply-side actions to overcome inflation. In response to the oil and food price shocks of 1973-74, Heller argued for the “building up of buffer stocks of strategic raw materials in slack times to throw into the speculative breach during the next commodity squeeze.”¹³⁹⁰ He previously urged the Nixon administration to increase stockpiles of sources of supply and in 1976, he told the Joint Economic Committee that increased stockpiles of oil and food “ought to be a basic ingredient of stabilization policy.”¹³⁹¹ Policymakers would have done well to heed this advice, for OPEC increased oil prices again in 1979, an incident that triggered double-digit inflation. As noted by Hobart Rowen, Jimmy Carter adopted a “do-nothing” position toward this, as he was hampered by the fact that the “emergency stockpile of oil that had been authorized at the time of the first oil shock had not been built.”¹³⁹² Clearly, Heller had recognised the extent to which America’s growing dependency upon imports posed inflationary dangers by the mid-1970s. He also argued that economic policy needed to be better able to “spot bottlenecks and shortages in the making,” recommending that an “expert staff should monitor such key industries as aluminium, steel, papers and chemicals” to facilitate this.¹³⁹³

Whilst he called for better mechanisms to both monitor and react to supply shocks, Heller emphasised the need for productivity-enhancing measures. In 1977, he told his Introductory Economics class that “the advance in productivity” was the nation’s “greatest single long-run defense against inflation,” as it would “satisfy labor’s and businesses’ income claims without having to boost prices to do it.”¹³⁹⁴ Such thinking was important because the rate of productivity declined rapidly in the

¹³⁹⁰ Heller, ‘Statement before the Joint Economic Committee National Conference on Full Employment,’ 19 March 1976. Heller Papers. Box 10. UoM.

¹³⁹¹ GPNA; Ibid.

¹³⁹² Rowen, *Self-Inflicted Wounds*, 195.

¹³⁹³ Heller, ‘The Battle Against Inflation,’ *Wall Street Journal*, 6 April 1977, 18. PQHN.

¹³⁹⁴ Heller, ‘Notes on Econ 1-001 for February 17, 1977.’ Heller Papers. Box 7. UoM.

1970s. Japanese and European industries were outperforming their US rivals. After increasing at an average annual rate of 3.3 percent from 1947-65, productivity declined to a 1.5 percent annual rate from 1966-75. It then reduced to 0.2 percent from 1976-80.¹³⁹⁵ Most liberal economists were slow to spot this. Charles Schultze, who served as Jimmy Carter's CEA chairman, grasped the seriousness of the productivity decline only in late 1979.¹³⁹⁶ In contrast, Heller appreciated the need to boost productivity much earlier.

A key factor that alerted him to this was the “shifts in the structure of the labor force” taking place by the 1970s.¹³⁹⁷ A greater proportion of women, minorities, and young people had entered it. These individuals did not have the same levels of training and skills as previous entrants into the labour market. They also dropped out of it more frequently. In 1976, Heller called for the government to cut “down the intolerable disparities [in skills] between blacks and whites, men and women, [and] teenagers and middle ages,” mainly through increased education and training.¹³⁹⁸ In this, Heller once again had much in common with the neoliberals, who favoured “strategic public investment in areas like research and education” to generate economic expansion.¹³⁹⁹ Writing in the late 1990s, political scientist John Sloan argued that measures to train and equip the inexperienced workforce would have done much to boost productivity and thereby help alleviate inflation in the 1970s.¹⁴⁰⁰ The fact that Heller placed emphasis upon doing so much earlier than most economists did was, therefore, prescient.

¹³⁹⁵ Morgan, *Beyond the Liberal Consensus*, 90.

¹³⁹⁶ Morgan, *The Age of Deficits*, 59-60.

¹³⁹⁷ Heller, ‘Notes on Econ 1-001 for February 17, 1977.’

¹³⁹⁸ Heller, ‘Statement before the Joint Economic Committee National Conference on Full Employment.’ He offered these remarks as a solution to overcoming stagnation, but it is likely, given the above discussion, that Heller was well aware of the anti-inflationary merits of such an approach.

¹³⁹⁹ Eva Bertram, *The Workfare State: Public Assistance Politics from the New Deal to the New Democrats* (Philadelphia, PA, 2015), 167.

¹⁴⁰⁰ Sloan, *The Reagan Effect: Economics and Presidential Leadership* (Lawrence, KS, 1999), 231.

Likewise, Heller's calls for deregulation proved significant. Ford and Carter both deregulated airlines and trucking in the mid-to-late 1970s, which led to a decline of prices in the transportation sector.¹⁴⁰¹ Meanwhile, Heller revised the way in which he wanted the government to implement wage-price guideposts. This became important because, during the Ford and Carter years, cost-push inflation continued to be problematic. The impact of the 1973-74 food and oil price shocks both forced unions to lobby harder for cost-of-living wage increases, which businesses passed onto consumers in the form of higher prices.¹⁴⁰² Against this backdrop, Heller and Okun risked "the ire of George Meany," head of the AFL-CIO.¹⁴⁰³ At Ford's inflation summit in September 1974, they urged the president to implement "some sort of 'circuit breaker' or 'social compact' that would interrupt the new wage-price spiral."¹⁴⁰⁴ In doing so, they echoed the arguments of Schultze and Brookings economist George Perry, who suggested that convincing labour to "quit trying to recover 'lost' wages...in exchange for tax cuts" constituted a way to accomplish this.¹⁴⁰⁵ Ford, on the advice of his CEA chairman Alan Greenspan, rejected this idea on the basis that it was too unconventional.¹⁴⁰⁶

Despite this, Heller, Okun, Perry and other liberals pushed this policy upon Carter. Carter took office with the initial aim of stimulating the economy, but he soon opted to prioritise anti-inflationary measures. To combat cost-push inflation, Carter first favoured "simple persuasion to convince labor and business to cooperate voluntarily in moderating price and cost increases without specific guidelines."¹⁴⁰⁷

¹⁴⁰¹ Morgan, 'Liberalism and inflation in the 1970s.'

¹⁴⁰² Morgan, *Deficit Government*, 117.

¹⁴⁰³ Rowen, *Self-Inflicted Wounds*, 109.

¹⁴⁰⁴ *Ibid*, 109.

¹⁴⁰⁵ *Ibid*, 109.

¹⁴⁰⁶ *Ibid*, 109.

¹⁴⁰⁷ Carl Biven, *Jimmy Carter's Economy: Policy in an Age of Limits* (Chapel Hill, NC, 2002), 130.

His first major anti-inflation initiative in April 1977 served as evidence of this.¹⁴⁰⁸ Yet, Carter soon resorted to deploying a stronger incomes policy, which he coupled with an emphasis upon budgetary restraint. Thanks to a new round of external food price shocks and union lobbying, the CPI shot up by 6.5 percent and inflation by 7.7 percent in 1978 and 1979 respectively.¹⁴⁰⁹ In the face of this, Carter's FY 1980 budget plan, announced in October 1978, stressed the need to halve the deficit.¹⁴¹⁰ Additionally, he responded to Okun's advice by promoting "a voluntary 'social contract' to limit wage increases to less than 6 percent and prices to less than 4 percent, with \$15 billion offered as tax rebates for employers and employees who would go along."¹⁴¹¹

Known as "wage insurance," Heller lobbied hard for Carter's proposal. In a January 1979 letter to Al Ullman, Chairman of the House Ways and Means Committee, Heller, Okun and several liberals called for "early enactment of the wage insurance part of President Carter's anti-inflationary program."¹⁴¹² They said that it was understandable "why workers might be reluctant to comply with the wage standards unless there is some safeguard, some landing net, to ensure those who sign up that they will not be penalized."¹⁴¹³ It was also imperative to ensure that businesses adhered to the government's price standards, so Heller favoured tax incentives for those who complied.¹⁴¹⁴ Importantly, Heller's support for wage insurance offers another lens onto his position to the right of traditional liberals in the 1970s: a decade earlier, Heller helped Kennedy and Johnson use the jawbone to

¹⁴⁰⁸ Ibid, 132-133.

¹⁴⁰⁹ Ibid, 191.

¹⁴¹⁰ Morgan, *The Age of Deficits*, 60.

¹⁴¹¹ Rowen, *Self-Inflicted Wounds*, 184; Pine, 'Wage-Price Guidelines Contain a Tax Rebate,' *Washington Post*, 25 October 1978, A1. PQHN.

¹⁴¹² Heller et al to Al Ullman. 23 January 1979. Heller Papers. Box 10. UoM.

¹⁴¹³ Ibid.

¹⁴¹⁴ Heller 'Economic Policy for Inflation: Shadow, Substance, and Statistics,' Draft Article for The America Adventure: A Statistical Odyssey, 1 July 1980. Heller Papers. Box 9. UoM.

enforce their wage-price guidelines. Yet, the emphasis that he placed upon wage insurance in the 1970s – at a time when many traditional liberals favoured controls – highlighted a new interest at blending “the goals of wage-price controls with the methods of the market.”¹⁴¹⁵

IV

With supply-side measures forming Heller’s primary remedy for inflation in the 1970s, the Minnesotan stressed the need to combat this problem in a way that had minimal social consequences. In December 1969, Heller expressed concern over the unemployment costs of gradualism, citing the fact that decreases in the money supply during that year had resulted in a significant loss of jobs.¹⁴¹⁶ When Ford sought to conquer inflation through the imposition of a tax surcharge in late 1974, Heller pleaded with the president to formulate “a compassionate anti-inflation program” that would consist of “generous unemployment benefits, food stamps and housing allowances.”¹⁴¹⁷ Unsurprisingly, Heller did not neglect the use of traditional macroeconomic measures during the 1970s. In fact, in response to the most severe recession since the Great Depression in 1974-75, Heller argued that carefully designed Keynesian policies could help to overcome the economy’s stagnation.

The recession had its roots in the food and oil price shocks of 1973-74. Both produced double-digit inflation that pushed taxpayers into higher brackets. This helped to shift the full employment budget from a deficit of \$12 billion in calendar 1972 to a surplus of \$3 billion in calendar 1973, sucking purchasing power from the economy.¹⁴¹⁸ At the same time, Arthur Burns engineered a sharp reversal in the

¹⁴¹⁵ Blinder, *Hard Heads, Soft Hearts: Tough-Minded Economics for a Just Society* (Reading, MA, 1987), 58.

¹⁴¹⁶ GPNA.

¹⁴¹⁷ Heller, ‘An Open Letter to President Ford.’

¹⁴¹⁸ Morgan, *Deficit Government*, 122.

money supply from expansion in 1972 to restriction in 1973-74.¹⁴¹⁹ As it became clear that the economy was likely to head into recession, Heller explained in late 1973 that “economic need and political advantage will shift the emphasis from tax increases to tax cuts in the coming year.”¹⁴²⁰ Importantly, Heller insisted that expansionary policies would not make inflation worse. As he put it, inflation “[is] nourished not by excess demand but primarily by a variety of cost factors beyond the reach of fiscal and monetary management.”¹⁴²¹ The “great bulk of the stimulus of a prompt tax cut,” he wrote in 1974, “would express itself not in higher prices but in higher output, jobs and income.”¹⁴²² At the same time, Heller urged Burns to expand the money supply at a 7 – 9 percent annual rate.¹⁴²³ With inflation thus caused by supply-side factors, Heller advanced the case that traditional macroeconomic measures could overcome stagnation.

Though he clearly believed that Keynesian stimulus policies could revive the economy, Heller did not go as far as endorsing the centrepiece of traditional liberal efforts to tackle stagnation during the 1970s. This came in the form of the Full Employment and Balanced Growth Act (known as the Humphrey-Hawkins bill). Both Hubert Humphrey and the Californian Representative Augustus Hawkins proposed this in the mid-1970s. Seen by some as “the last product of the New Deal thought,” this attempted to rewrite the 1946 Employment Act by directing the federal government to ensure “full” instead of “maximum” employment.¹⁴²⁴ In doing so, its proponents also placed emphasis on structural economic measures, believing that the

¹⁴¹⁹ Wells, *Economist in an Uncertain World*, 111-114.

¹⁴²⁰ Heller, ‘The U.S. Economic Outlook,’ *NCBM*, 5 October 1973. Heller Papers. Box 10. UoM.

¹⁴²¹ Heller, ‘Excerpts from ‘How Severe the Economic and Energy Crunch,’’ Address before the Independent Bankers Association of America, Dallas, Texas, 22 March 1974. Heller Papers. Box 10. UoM.

¹⁴²² *Ibid.*

¹⁴²³ Heller and George Perry, ‘The U.S. Economic Outlook for 1974,’ *NCBM*, 8 January 1974. Heller Papers. Box 10. UoM.

¹⁴²⁴ Cited in Spulber, *Managing the American Economy from Roosevelt to Reagan*, 100.

stagnation of the 1970s was partly attributable to declining industries and regions.¹⁴²⁵

In short, the Humphrey-Hawkins bill called for guaranteed full employment, the federal government to fund employment of last resort to help facilitate this, and increased aid for depressed areas.¹⁴²⁶

Heller sympathised with these aims, but he shared the concerns of Schultze and Galbraith that the bill would be inflationary. Indeed, its drafters barely considered the bill's inflationary consequences because they sought support from key liberal groups, such as the Black Caucus and the AFL-CIO, who prioritised boosting jobs in the 1970s.¹⁴²⁷ Writing in July 1976 to Brockman Adams of Washington, Chairman of the House Budget Committee, Heller stated that Humphrey-Hawkins needed to “undergo considerable further modification” if it were “to serve the ends of full employment and non-inflationary growth.”¹⁴²⁸ This placed Heller “[on the opposite side to] the Black Caucus, [the] AFL-CIO, and [Humphrey's adviser] Leon Keyserling,” all of whom played a role in drafting the measure.¹⁴²⁹

Reflecting this, Keyserling wrote Heller in October 1976 to persuade him to boost his support for Humphrey-Hawkins, saying that its “anti-inflation provisions” had “been strengthened in many ways.”¹⁴³⁰ Humphrey, too, sought to persuade Heller of the revised draft's merits.¹⁴³¹ However, the economist was unmoved. Despite its anti-inflationary revisions, Heller contended that the bill lacked necessary “escape valves” that could be switched on “if one were to face a 1973-74 type of

¹⁴²⁵ Ibid, 100.

¹⁴²⁶ Andelic, ‘Donkey Work,’ 150-151.

¹⁴²⁷ Humphrey made this clear to Heller on 6 August 1976. Humphrey Papers. Senatorial Files, 1971-78. Correspondence Files-Legislative, 1976. Box 2. MHS.

¹⁴²⁸ Heller to Brockman Adams, 21 July 1976. Attached to Ibid.

¹⁴²⁹ Heller, ‘Notes on PA 8-204 Class,’ 6 May 1976. Heller Papers. Box 5. UoM.

¹⁴³⁰ Keyserling to Heller, 22 October 1976. Leon Keyserling Papers. Speech and Article File, 1923-1989. Box 44. Harry Truman Presidential Library.

¹⁴³¹ Humphrey to Heller, 6 August 1976.

inflation.”¹⁴³² He also preferred to stimulate the economy with a tax cut, telling Humphrey in January 1977 that a “rebate-like tax cut” of the sort proposed by Jimmy Carter in his 1976 presidential campaign made good sense.¹⁴³³ Prior to its enactment in 1978, opponents of the Humphrey-Hawkins bill succeeded in emasculating it of its key employment provisions. In retrospect, some scholars have praised the measure as an enlightened attempt to combine New Deal-Great Society liberalism with the entitlement liberalism of the New Politics movement.¹⁴³⁴ This, however, ignores the fact that the measure would have been inflationary. Instead, others have more aptly described Humphrey-Hawkins as a futile attempt to apply traditional liberal ideas to the problems of the 1970s.¹⁴³⁵ To extend such a criticism to Heller would be misleading, as he never embraced the Humphrey-Hawkins Act.

Not convinced that Humphrey-Hawkins offered the best route to prosperity, Heller put onus on fighting stagnation with a tax cut from the mid-1970s. The 1974-75 recession, he pointed out, had produced a large amount of slack, to the point whereby the economy was running “12 percent below its potential” in late 1975.¹⁴³⁶ This meant that the economy could be stimulated without inducing inflation. Thus, Heller wrote in favour of Ford’s \$25 billion tax cut in 1975 and praised the Democrats for seeking to impose further spending measures and another tax cut on Ford’s FY 1977 budget, saying that “the Keynesian prescription of stimulating aggregate demand can work rather well.”¹⁴³⁷ In May 1976, he also met with Ford and

¹⁴³² Heller, ‘Notes on PA 8-204 Class.’

¹⁴³³ Heller to Humphrey, 3 January 1977. Humphrey Papers. Senatorial Files, 1971-78. Correspondence Files-Legislative, 1977-78. Box 2. MHS.

¹⁴³⁴ Andelic, ‘Donkey Work,’ 135-165; Weir, *Politics and Jobs*, 132-140; Morgan, ‘Liberalism and Inflation in the 1970s.’

¹⁴³⁵ Cowie, *Stayin’ Alive*, 269; Sandbrook, *Mad as Hell*, 290; Biven, *Jimmy Carter’s Economy*, 33.

¹⁴³⁶ Heller and Perry, ‘The U.S. Economic Outlook,’ *NCBM*, 15 October 1975. Heller Papers. Box 10. UoM.

¹⁴³⁷ Sobel, *The Worldly Economists*, 142; Heller, ‘Statement before the Joint Economic Committee National Conference on Full Employment’ (quotation); n.n., ‘Heller Urges Rise in Ford’s Budget,’ *New York Times*, 12 April 1976, 25. PQHN.

unsuccessfully made the case for expansionary policies.¹⁴³⁸

Following Ford's departure from the White House, Heller was equally unsuccessful in pressing such measures upon Carter. In December 1976, Carter's transition team consulted Heller on the best way to incorporate Carter's pledged tax rebate into a 1977 stimulus package.¹⁴³⁹ Yet, when the president announced his \$31 billion programme early that year, Heller described it as "unduly modest."¹⁴⁴⁰ Carter then scrapped the \$8.2 billion rebate, before placing emphasis upon austerity in his budgets for FYs 1980-81.¹⁴⁴¹ For Heller, this was the wrong weapon of choice to combat inflation, primarily because supply-side factors were behind the rise in prices. Research by Otto Eckstein and Christopher Probyn in 1981 substantiated this point. They calculated that if every Jimmy Carter budget had been in balance, inflation in 1980 would have been 9.4 percent instead of 10.1 percent.¹⁴⁴²

Instead, Heller wanted an innovative tax cut to tackle both inflation and stagnation simultaneously. With the economy beset by slack, bracket-creep inflation, supply-shocks, and cost-push pressures, Heller called for a \$35 billion tax cut in 1977. In particular, he stated that reductions in payroll taxes were desirable.¹⁴⁴³ "Nothing more directly relieves pressure on prices than an across-the-board cut in the cost of production. And nothing more effectively does this than a cut in employer payroll taxes" (which would also boost purchasing power).¹⁴⁴⁴ Knowing that it was equally imperative to induce both employers and workers to reduce their wage and price demands, Heller explained that payroll tax cuts would help to accomplish these

¹⁴³⁸ Heller, 'Notes on PA 8-204,' 27 May 1976. Heller Papers. Box 5. UoM.

¹⁴³⁹ Harold Chucker, 'Carter Economic Policies Cause Discomfort,' *Minneapolis Star*, 13 May 1977. Heller Papers. Box 10. UoM.

¹⁴⁴⁰ Cited in Biven, *Jimmy Carter's Economy*, 72.

¹⁴⁴¹ Morgan, *The Age of Deficits*, 60, 68.

¹⁴⁴² Eckstein and Christopher Probyn, 'Do Budget Deficits Matter?' *Data Resources US Review*, (Dec. 1981). Cited in Morgan, 'Liberalism and Inflation in the 1970s.'

¹⁴⁴³ Heller, 'An Engine for 'Disinflation,' *Wall Street Journal*, 22 December 1977, 8. PQHN.

¹⁴⁴⁴ Ibid.

objectives. This policy became particularly appealing following the second oil price hike in 1979, which not only increased bracket-creep inflation but also added to the fiscal drag on spending in the economy. Sensing that an economic downturn was imminent, Heller visited Carter in July and recommended that a “carefully crafted tax cut can couple the restoration of purchasing power with reductions in cost and price pressures.”¹⁴⁴⁵ It would also “buttress” the president’s wage insurance programme, as well as “boost business incentives.”¹⁴⁴⁶

As Heller had anticipated, the impact of the energy crisis helped to produce a recession. Also important to this was Carter’s decision in August 1979 to appoint Paul Volcker as chair of the Fed. An inflation-hawk, Volcker implemented credit restraints and adopted the strategy of money supply control to bring inflation down, which ensured that monetary policy tightened from 1979-80.¹⁴⁴⁷ Writing to Carter in January 1980, Heller explained that a tax cut was imperative to “offset some of the crushing impact of the mounting fiscal squeeze, the tightening oil noose, and super-tight money.”¹⁴⁴⁸ It would also help to alleviate inflation. Specifically, Heller argued for \$20 billion in payroll tax cuts, \$5 billion in accelerated depreciation, and \$5 billion in real wage insurance.¹⁴⁴⁹ He also criticised Edward Kennedy for championing the use of controls, arguing such policies limited economic freedom and

¹⁴⁴⁵ Heller, Memorandum for Jimmy Carter, ‘Fighting Inflation and Recession with a Tax Cut,’ 25 July 1979. Office of Staff Secretary; Presidential Files; Folder: 8/2/79; Container 126. Jimmy Carter Presidential Library [Henceforth JCL]

¹⁴⁴⁶ Heller, Memorandum for Carter, ‘Inflation, Wage-Price Restraint, and Anti-Inflation Tax Cuts,’ 25 July 1979. Office of Staff Secretary; Presidential Files; Folder: 8/2/79; Container 126. JCL.

¹⁴⁴⁷ Morgan, ‘Monetary Metamorphosis,’ 551-555.

¹⁴⁴⁸ Heller, Memorandum for Carter, ‘The Current Case for a Federal Tax Cut,’ 3 January 1980. Office of Staff Secretary. Presidential Files. Folder 1/9/80 [2]; Container 145. JCL.

¹⁴⁴⁹ Ibid. It is also worth pointing out that, to combat the oil crisis in 1979, Heller showed support for Carter’s attempt to decontrol oil prices, to help bring down energy costs. See Heller, Memorandum for Carter, ‘Inflation, Wage-Price Restraint, and Anti-Inflation Tax Cuts.’ This flew in the face of the recommendations of numerous liberals, who rejected decontrol in the 1970s. See Derthick and Quirk, *The Politics of Deregulation*, 211.

would do little to prevent supply shocks.¹⁴⁵⁰ Despite the fact that Brookings economist George Perry, Arthur Okun, and other liberals supported a tax cut, Carter prioritised fiscal restraint throughout 1980.¹⁴⁵¹ Unsurprisingly, the poor economic conditions that ensued played no small role in his defeat to Ronald Reagan in that year's Presidential Election.¹⁴⁵²

Before analysing Heller's response to Reaganomics, it is worth stating that it is wrong to describe his remedies for stagflation as irrelevant. What is clear is that he learned from the mistakes of the late 1960s by placing emphasis upon structural reforms on the supply-side of the economy. He positioned himself to the right of traditional liberals, particularly by arguing for deregulation, higher import quotas, and repeal of certain New Deal-era policies. He clearly saw an opportunity in the globalisation of the economy to relieve inflationary pressures. At the same time, to overcome both stagnation and inflation, Heller prudently argued for carefully structured and well-timed fiscal and monetary policies. These were logical suggestions given the fact Nixon, Ford, and Carter were each forced into making a U-turn when their policies to cure one side of the stagflation coin only made the other side worse. This demonstrated that the standard way of looking at macroeconomics in the 1970s assumed that it was difficult to address supply and demand issues at the same time. Heller, by comparison, not only suggested policies to tackle both simultaneously, he had also modified his thinking to take into account the more inflationary economy of the 1970s. He was right to place emphasis on using supply-

¹⁴⁵⁰ David Warsh, 'Kennedy Freeze Chills Specialists,' *Boston Globe*, 30 January 1980, 32; Heller, 'Walter Heller: The Case for Wage-Price Controls...', *Wall Street Journal*, 27 February 1980, 22. Both PQHN.

¹⁴⁵¹ See Stuart Eizenstat, Memorandum for Carter, 'Results of Consultations with Private Economists and Businessmen,' 25 July 1979. Office of Staff Secretary; Presidential Files; Folder: 7/26/79; Container 125. JCL.

¹⁴⁵² See Bruce Schulman, 'Slouching Towards the Supply Side: Jimmy Carter and the New American Political Economy,' in Gary Fink and Hugh Davis Graham (eds.) *The Carter Presidency: Policy Choices in the Post-New Deal Era* (Lawrence, KS, 1998), 51.

side solutions to tackle this problem, not least because the most authoritative quantitative analyses of inflation in the 1970s have shown that supply-side issues mostly caused it.¹⁴⁵³

V

Reagan's election confirmed the "collapse of the old Keynesian order," heralding in a more conservative approach to economic policy.¹⁴⁵⁴ Central to this was Reagan's advocacy of a form of supply-side economics different to that championed by Heller. This gained credence in the late 1970s thanks to the Republican Representative Jack Kemp of New York. Believing that government interference destabilised the economy, Kemp championed tax reduction to overcome stagflation. In doing so, he "developed a new supply-side rationale" to justify this.¹⁴⁵⁵ Rejecting Keynesian ideas that consumption drove economic growth, Kemp placed emphasis upon increasing production. He maintained that tax cuts for wealthy individuals would incentivise them to work, save, and invest. This would conquer unemployment *and* inflation by boosting both actual and potential output.¹⁴⁵⁶ Kemp further argued it was imperative to reduce the amount of marginal taxation that wealthy individuals paid and said such tax cuts would generate increased revenues, to the point whereby they would pay for themselves.¹⁴⁵⁷ To justify this, he drew on the ideas of University of Southern California economist Arthur Laffer, who had formulated a diagram that purported to "show how tax changes can suppress or unleash incentives to work and

¹⁴⁵³ J. Bradford De Long, 'America's Peacetime Inflation: The 1970s,' in Christina and David Romer (eds.) *Reducing Inflation: Motivation and Strategy* (Chicago, IL, 1997), 247-280; Romer and Romer, 'The Evolution of Economic Understanding and Postwar Stabilization Policy,' in Romer and Romer (eds.), *Reducing Inflation*, 11-78. The author is grateful to Louis Johnston for drawing his attention to these sources.

¹⁴⁵⁴ Collins, *Transforming America: Politics and Culture in the Reagan Years* (New York, 2007), 59.

¹⁴⁵⁵ *Ibid*, 61.

¹⁴⁵⁶ *Ibid*, 61, 63-64.

¹⁴⁵⁷ *Ibid*, 63-64.

invest and hence affect tax revenues.”¹⁴⁵⁸ At a certain point, Laffer argued, taxes not only discouraged individuals from working, but lower taxes generated more revenue by stimulating a greater desire to work, save, and invest.¹⁴⁵⁹

Championed, too, by the *Wall Street Journal*’s Jude Wanniski, supply-side economics manifested itself in the Kemp-Roth tax cut of 1977, which called for personal income taxes to be reduced by 30 percent over three years.¹⁴⁶⁰ A forerunner to Ronald Reagan’s 1981 tax cut, the proponents of Kemp-Roth invoked the 1964 Revenue Act to justify their measure.¹⁴⁶¹ In doing so, they implied its architects had been supply-side economists. Several scholars have regurgitated this argument. Writing in 1988, Howard Winant claimed the “first attempt to develop a comprehensive economic policy based on supply-side concepts took place during the Kennedy administration. The fruit of this policy initiative was the Revenue Act of 1964.”¹⁴⁶²

Brian Domitrovic, too, has argued Kennedy and Heller implemented the ideas of Robert Mundell, one of the leading pioneers of supply-side theory.¹⁴⁶³ In 1961, Mundell argued the best way to stimulate a stagnant economy was through high interest rates and a loose fiscal policy.¹⁴⁶⁴ The former would attract foreign capital and prevent inflation, whilst the latter would spur growth through its incentive effects.¹⁴⁶⁵ In essence, Kennedy, Heller, and Johnson supposedly applied Mundell’s

¹⁴⁵⁸ Heller, Memorandum for Congressmen Butler Derrick and Timothy Wirth, ‘Questions Relating to the Kemp Tax Cut Bill,’ 26 June 1978. Heller Papers. Box 5. UoM.

¹⁴⁵⁹ Ibid.

¹⁴⁶⁰ Collins, *Transforming America*, 61.

¹⁴⁶¹ As Heller pointed out, the supply-siders said that the 1964 tax cut worked “by quickly expanding supply through its benign effect on incentives.” Cited in Heller, Memorandum for Congressmen Derrick and Wirth, ‘Questions Relating to the Kemp Tax Cut Bill.’

¹⁴⁶² Howard Winant, *Stalemate: Political Economic Origins of Supply-Side Policy* (New York, 1988), xi.

¹⁴⁶³ Brian Domitrovic, *Econoclasts: The Rebels Who Sparked the Supply-side Revolution and Restored American Prosperity* (Wilmington, DE, 2009), 64-73.

¹⁴⁶⁴ Ibid, 68.

¹⁴⁶⁵ Ibid, 68.

policy mix by both implementing the Investment Tax Credit of 1962 and reducing the top rate of taxation from 91 percent to 70 percent in 1964.¹⁴⁶⁶ At the same time, the federal funds rate (a short-term interest rate) tripled in four years in the early 1960s, producing the tight money policy Mundell championed.¹⁴⁶⁷ According to Domitrovic, the 1962 and 1964 Revenue Acts “were consistent with the policy-recommendation that Mundell had made [in 1961],” meaning the expansion of the 1960s was the result of supply-side policies.¹⁴⁶⁸

Such an assertion is erroneous, not least because Heller went to painstaking efforts to refute it throughout both the late 1970s and the early 1980s. Writing in 1982, the Minnesotan acknowledged that policymakers *did* implement various supply-side policies in the early 1960s, which ensured that potential expanded alongside actual output.¹⁴⁶⁹ These included the 1962 Investment Tax Credit, the liberalisation of depreciation allowances, the implementation of Operation Twist, and worker retraining initiatives.¹⁴⁷⁰ It was clear, Heller maintained, that the 1964 Revenue Act offset a deficiency in demand, which was caused by “the overburden of taxes.”¹⁴⁷¹ True, dropping the top individual taxation rate did “strengthen the incentives for investment,” but the multiplier analysis that Heller outlined to justify the tax cut clearly demonstrated that it was Keynesian.¹⁴⁷² It showed that, in each of the twelve years prior to enactment of the 1964 tax cut, consumers had spent “close to 93 percent of their available after-tax incomes,” which they would look to restore

¹⁴⁶⁶ Ibid, 71.

¹⁴⁶⁷ Ibid, 73.

¹⁴⁶⁸ Ibid, 71. Domitrovic has regurgitated this argument in recent publications, in which he now claims Treasury Secretary Douglas Dillon sold Kennedy the 1964 tax cut (on supply-side grounds) and downplays the role of Heller. See Domitrovic and Lawrence Kudlow, *JFK and the Reagan Revolution: A Secret History of American Prosperity* (New York, 2016); and Domitrovic, ‘Does Government Intervention Retard or Foster Economic Growth? The Case of Postwar Prosperity,’ *Journal of Policy History*, 29:2 (2017), 289-304.

¹⁴⁶⁹ Heller, ‘Kennedy Economics Revisited,’ 240.

¹⁴⁷⁰ Ibid, 240.

¹⁴⁷¹ Ibid, 243.

following the measure's passage.¹⁴⁷³ The resulting increase in consumption made them capable of generating a multiplier to close the performance gap.

As Heller pointed out to two Congressmen in June 1978, if the 1964 tax cut had worked by expanding incentives – as Kemp and his followers claimed – then a “big jump in trend productivity increases and in the growth in GNP potential” should have taken place.¹⁴⁷⁴ Yet, “no sudden bulge in productivity and potential” had been “found by any close student of the subject.”¹⁴⁷⁵ This was important because the economist Norman Ture estimated that the Kemp-Roth tax cut would “boost GNP by \$170 billion, capital investment by \$113 billion (over 30 percent in real terms in one year), and jobs by 2 million – thus boosting revenues above pre-tax cut levels.”¹⁴⁷⁶ Yet, the fact that these estimates amounted to a supply-side bulge “[many times as big] as the 1964 tax cut produced” demonstrated that there was “no basis in either the 1964 tax cut or any other modern tax cut for Ture’s prediction.”¹⁴⁷⁷ To the extent that there was historical evidence to justify the supply-siders claims, Heller rubbished comparisons that they made with the tax cuts passed by the Republican Party during the 1920s. “At a time when a relative handful of Americans paid income taxes and Federal spending was less than 5 percent of GNP...we are asked to believe that Federal income tax reduction powered the growth of GNP from \$70 billion in 1921 to \$103 billion in 1929.”¹⁴⁷⁸

Heller also strongly refuted contrasts made between the Kemp-Roth tax bill and the 1948 tax cut implemented in West Germany, which supply-siders further

¹⁴⁷² Ibid, 246.

¹⁴⁷³ ‘Statement of Walter Heller, Chairman Accompanied By Gardner Ackley and John P. Lewis, Members of the Council of Economic Advisers before the Senate Committee on Finance,’ 12 November 1963.

¹⁴⁷⁴ Heller, Memorandum for Derrick and Wirth, ‘Questions Relating to the Kemp Tax Cut Bill.’

¹⁴⁷⁵ Ibid. For more on this see Shreve, ‘Lyndon Johnson and the Keynesian Revolution,’ 189.

¹⁴⁷⁶ Heller, Memorandum for Derrick and Wirth, ‘Questions Relating to the Kemp Tax Cut Bill.’

¹⁴⁷⁷ Ibid.

¹⁴⁷⁸ Ibid.

invoked to justify their approach. Heller served as Chief of Internal Finance for the American Military Government in West Germany when this tax cut was written. He pointed out that currency reform, the removal of wage-price controls, the impact of the Marshall Plan, and the overhaul of the German tax structure, all played just as important roles in underpinning West German economic growth than did the 1948 tax cut.¹⁴⁷⁹ Additionally, Heller criticised the supply-siders for failing to refute the arguments of Brookings economist Edward Denison, whose research disputed Laffer's assertion that changes in taxation rates would encourage people to work, save, and invest. Denison discovered "that U.S. gross private domestic saving" had "been virtually invariant year-in and year-out in the face of high taxes, low taxes, or virtually no taxes," remaining "at roughly 16 percent of GNP for about a century."¹⁴⁸⁰ Furthermore, how was it, Heller argued, that the Kemp-Roth bill could "lead to such an upsurge in the work ethic when a considerably larger average increase in real take-home pay in the decade of the 1960s (mostly as a result of substantial economic growth)" generated no upsurge close to what Kemp-Roth was supposed to generate?¹⁴⁸¹

One critique of Keynesian economists in the 1970s and the early 1980s is that they "did not take the supply-siders seriously."¹⁴⁸² The conservative doctrine's proponents tended to be outsiders within the academy and advanced their ideas from the pages of the *Wall Street Journal*.¹⁴⁸³ According to Robert Collins, the Keynesians thus dismissed the supply-siders as "less a valid school of conservative economic thought than a 'cult' or 'sect,'" with Carter economist Lawrence Klein saying, "if

¹⁴⁷⁹ Ibid.

¹⁴⁸⁰ Ibid.

¹⁴⁸¹ Ibid.

¹⁴⁸² Johnston, Interview with the Author.

¹⁴⁸³ Ibid.

there were Nuremberg trials for economists, supply-siders would be in the dock.”¹⁴⁸⁴ Heller, too, found himself criticised for underestimating the supply-siders, notably in a *Human Events* article published in 1978.¹⁴⁸⁵ The fact that the Keynesians underestimated their rivals was thus a mistake, as it enabled the Republicans to emerge as the party of new ideas by the late 1970s. Still, it would be unfair to level this critique at Heller, for he *did* respond robustly to the rise of supply-side economics.

VI

Despite this, supply-side ideas underpinned the Economic Recovery and Tax Act (ERTA) promoted by Ronald Reagan in 1981. For conservatives who lionise Reagan, this piece of legislation and the economic policies that went with it moved the economy out of its 1970s malaise and into a new era of growth.¹⁴⁸⁶ Expressing this sentiment, the journalist Robert Bartley credited Reagan for engineering “seven fat years” of prosperity.¹⁴⁸⁷ Certain evidence supports this assertion. Firstly, Reagan publicly endorsed Volcker’s strategy of money supply control throughout the early 1980s, which brought inflation down to tolerable levels.¹⁴⁸⁸ Added to this, Reagan’s tax cuts did help to generate economic growth.¹⁴⁸⁹ Yet, those who have praised Reaganomics have ignored the negative consequences of Reagan’s supply-side policies, several of which Heller drew attention to throughout the 1980s.

The ERTA reflected the influence of Treasury Secretary Donald Regan and Budget Director David Stockman. Signed into law on August 13, it cut top marginal

¹⁴⁸⁴ Collins, *Transforming America*, 66.

¹⁴⁸⁵ Elliot, ‘Walter Heller,’ 12.

¹⁴⁸⁶ See Sloan, ‘The Economic Costs of Reagan Mythology,’ in Kyle Longley et al (eds.) *Deconstructing Reagan: Conservative Mythology and America’s Fortieth President* (London, 2015), 41-70.

¹⁴⁸⁷ Robert Bartley, *The Seven Fat Years and How to Do it Again* (New York, 1992).

¹⁴⁸⁸ Morgan, ‘Monetary Metamorphosis,’ 556-561.

¹⁴⁸⁹ Collins, *Transforming America*, 88.

tax rates from 70 to 50 percent and reduced income taxes by 23 percent over three years.¹⁴⁹⁰ Accompanying this was the Omnibus Budget Reconciliation Act, which “retrenched over 200 domestic programs at projected savings of \$35.2 billion in FY 1982 and \$140 billion over three years.”¹⁴⁹¹ Reagan also substantially increased defence spending. In short, he claimed that his economic programme would incentivise production, stimulate growth, and eventually yield a balanced budget by FY 1984.¹⁴⁹²

Heller pointed out a key problem in the president’s thinking. Essentially “everything would have to break right” for Reagan’s policies to produce a balanced budget.¹⁴⁹³ This included Reagan’s “rosy” assumption that the economy would grow at a 4.4 percent annual rate from 1982-86. Unsurprisingly, the Fed torpedoed this, as Volcker’s tight money strategy caused output to contract by 2 percent, producing a deep recession in 1981-82.¹⁴⁹⁴ In the face of this, Heller spoke in favour of Reagan’s FY 1982-83 deficits of \$78.9 billion and \$127.9 billion (3.9 percent and 5.9 percent of GDP), calling them the president’s “secret [Keynesian] weapon.”¹⁴⁹⁵ However, Heller and other liberals argued that serious structural deficiencies beset Reagan’s fiscal programme. The most important was that its “expansionary fiscal menu of tax cuts and defense boosts” would “outstrip budget cuts by \$100 billion a year by 1984.”¹⁴⁹⁶ Stockman had sought to paper over this with a “magic asterisk” in the FY 1981 budget plan, which explained that he would make a large amount of unspecified future savings.¹⁴⁹⁷ Yet, with output unlikely to grow at 4.4 percent per year and future

¹⁴⁹⁰ Morgan, *The Age of Deficits*, 85.

¹⁴⁹¹ Ibid, 84.

¹⁴⁹² Sloan, ‘The Economic Costs of Reagan Mythology,’ 52.

¹⁴⁹³ Heller, ‘Supply-Side Follies of 1981,’ *Wall Street Journal*, 12 June 1981, 20. PQHN.

¹⁴⁹⁴ Morgan, *The Age of Deficits*, 85.

¹⁴⁹⁵ Heller, ‘The Unavoidable Issue,’ *Wall Street Journal*, 26 October 1984, 30. PQHN.

¹⁴⁹⁶ Heller, ‘Supply-Side Follies of 1981.’

¹⁴⁹⁷ Morgan, *The Age of Deficits*, 88.

tax cuts, expenditure cuts, and military spending planned by Reagan, Heller wrote in late 1981 that there was “a real time bomb in the Reagan program.”¹⁴⁹⁸ The president’s “reckless tax cuts [and military spending]...pose huge deficits for 1984 and beyond.”¹⁴⁹⁹

Despite supply-sider Martin Feldstein’s retort that Reagan’s plan “should be given time,” Heller called upon the president to “slow the tax cuts and the defense buildup.”¹⁵⁰⁰ Stockman unsuccessfully tried to get Reagan to agree to military cutbacks, before switching his attention to reducing social security spending. This proved unsuccessful, so, in 1981-82, the Budget Director tried to convince the president to delay the second and third instalments of his tax cuts, but Reagan refused.¹⁵⁰¹ With output set to grow at less than 4.4 percent from 1981-84, the fears Heller expressed in late 1981 came true. The deficit hit \$212.3 billion and \$221.2 billion in FYs 1985-86 (5 percent and 4.9 percent of GDP). Automatic indexing of tax rates to inflation in 1985 also triggered this, but Reagan’s tax cuts and defence boosts played a key role.

As Reagan’s deficits hit such figures, the president stunned liberals by signalling “his toleration of [them].”¹⁵⁰² Several claimed that the president had deliberately employed large deficits to defund the welfare state.¹⁵⁰³ Heller, too, made this suggestion.¹⁵⁰⁴ However, this accusation was exaggerated: Reagan sincerely believed in the supply-side idea that incentive-boosting tax cuts would pay for

¹⁴⁹⁸ n.n., ‘Will Reaganomics Work? Five Views,’ *US News and World Report*, 28 December 1981, 72. Heller Papers. Box 10. UoM.

¹⁴⁹⁹ Ibid, 72.

¹⁵⁰⁰ Ibid, 71-72; Heller, ‘A Way Out of the Nation’s Economic Trap,’ *Wall Street Journal*, 25 February 1982, 26. PQHN.

¹⁵⁰¹ Morgan, *Reagan: American Icon* (London, 2016), 180, 185-186.

¹⁵⁰² Morgan, *The Age of Deficits*, 91.

¹⁵⁰³ Ibid, 91-92.

¹⁵⁰⁴ Heller, ‘The Deficit: What do we do Now?’ *Wall Street Journal*, 27 September 1982, 22. PQHN.

themselves, so these deficits surprised him.¹⁵⁰⁵ Liberals, however, did have cause to be alarmed at the relationship between the deficit and the welfare state, not least because the president slashed child nutrition programmes, food stamps, aid to the states, and Medicaid to reduce the former, helping deepen inequality. Writing in 1987, Heller expressed alarm at this, pointing out that the poverty rate had jumped from 11.7 percent in 1979 to 14.4 percent in 1984.¹⁵⁰⁶

Whilst Heller rightly blamed Reagan's deficits for helping deepen inequality, historians Judith Stein and Greta Krippner have also attributed it to the decline of manufacturing, a trend that most economists were slow to appreciate in the 1980s. According to them, the deregulation of the financial sector, first initiated by Carter and then consolidated by Reagan, opened up financial markets to capital, which enabled the latter to flow away from productive investment and into the financial sector. To make matters worse, Volcker kept real interest rates (interest rates minus inflation) high to fund Reagan's deficits in the 1980s, as this attracted foreign capital. This strategy underwrote a strong dollar which served to decrease the competitiveness of US manufacturers. Moreover, as the newly deregulated financial sector was the place where this capital went, manufacturing declined further.¹⁵⁰⁷ Heller did not appreciate the significance of the rise of finance, so he was unaware of this deeper, underlying trend that worsened inequality during the 1980s.

Nevertheless, Heller pointed towards other problems associated with Reagan's deficits. Most concerning was the level of debt that they generated. Writing in 1984, Heller rightly predicted that the US would become the world's largest debtor nation

¹⁵⁰⁵ For more on this issue see Collins, *Transforming America*, 79-81.

¹⁵⁰⁶ 'Before Parting, Heller Left Advice on Avoiding Reagan Disaster,' *St Paul Dispatch*, 18 June 1987. Reprinted from January 1987 edition of the *Humphrey Institute News*. Heller Papers. Box 10. UoM.

¹⁵⁰⁷ Stein, *Pivotal Decade*, 206, 267-269; Greta Krippner, *Capitalizing on Crisis: The Political Origins of the Rise of Finance* (London, 2011), 15, 22, 52, 141-142.

by the late 1980s.¹⁵⁰⁸ To the extent that the US could tackle the mounting deficit through robust growth, Heller rubbished Reagan's new "rosy" assumption that the economy would grow at an annual rate of 4 percent until 1989, not least because Congressional Budget Office predictions contradicted this.¹⁵⁰⁹ Instead, Heller urged Reagan to "confront the deficit in a straightforward and responsible way" by increasing taxes.¹⁵¹⁰ In addition to the budget deficit, Heller raised concerns about another deficit that was growing throughout the 1980s. This was the trade deficit, which was expanding because the influx of foreign capital caused the value of the dollar to appreciate, encouraging Americans to buy goods from abroad.¹⁵¹¹ Again, the warnings of Heller and others concerning the growing trade and budget deficits, as well as the level of debt, went unheeded, something that caused serious long-term problems.

In addition to criticising the long-term implications of Reagan's fiscal policies, Heller pointed out throughout the 1980s that the president's economic programme failed to stimulate productivity significantly.¹⁵¹² Contrary to supply-side claims that tax cuts for the rich would spur investment, productivity grew at just a 1.1 percent annual rate during that decade.¹⁵¹³ According to Heller, the government's domestic borrowing partly caused this, primarily because this kept real interest rates high and thereby crowded out money from the private economy.¹⁵¹⁴ However, the capital that poured into the country during the 1980s actually offset the crowding out

¹⁵⁰⁸ Heller, 'The Unavoidable Issue.'

¹⁵⁰⁹ Ibid.

¹⁵¹⁰ Heller, Pechman et al, *Tax Policy: New Directions and Possibilities* (Washington DC, 1984), 3.

¹⁵¹¹ Ibid, 4.

¹⁵¹² Heller, 'Year to Reach for Economic Stars,' *Wall Street Journal*, 28 February 1986, 24. PQHN; Heller, 'The Latest Productivity Puzzle,' Script for the Nightly Business Report, PBS, 20 March 1985. Heller Papers. Box 8. UoM.

¹⁵¹³ Sloan, *The Reagan Effect*, 232.

¹⁵¹⁴ Heller and Perry, 'U.S. Economic Policy and Outlook,' *NCBM*, 15 February 1985. Heller Papers. Box 8. UoM.

effect of the government's domestic borrowing.¹⁵¹⁵ Moreover, this capital helped to produce a host of corporate mergers, as conglomerates sought to create "more innovative, wealth-creating enterprises."¹⁵¹⁶ Because borrowing funded these changes, American businesses chose to save costs by either downsizing their workforces or by moving production abroad, both of which undermined productivity growth. Heller made virtually no mention of this in the 1980s, which again showed that he underestimated the impact of the economy's shift towards finance.

Still, he drew attention to other factors that contributed to the lack of productivity under Reagan. One was the fact that Reagan's tax cuts failed to stimulate investment, with the yearly "economic growth of 4.1 percent in 1983-1988" largely caused by "aggregate demand catching up with potential GNP after a serious recession."¹⁵¹⁷ Secondly, the substantial deficits run by Reagan created a "huge black hole" that "siphoned" private savings from the economy.¹⁵¹⁸ Traditionally, the US had been a low-saving nation, but "the public dissaving represented by the Reagan deficits offset much of the private saving that did take place."¹⁵¹⁹ By 1986, Heller thus commented that the US had its "lowest national savings and investment rates in half a century," which had restricted the growth of productivity.¹⁵²⁰ Additionally, Heller stated that the 1980s witnessed virtually no "investment in human capital," especially in the form of "education, training, health, [and] nutrition."¹⁵²¹

With these points in mind, Heller argued in 1987 that the next president should "push for an adjustment of our structural policies, applying the classical

¹⁵¹⁵ Krippner, *Capitalizing on Crisis*, 97.

¹⁵¹⁶ Morgan, *Reagan*, 258.

¹⁵¹⁷ Heller, 'Year to Reach for Economic Stars'; Morgan, *The Age of Deficits*, 119 (quotation).

¹⁵¹⁸ Heller, 'Year to Reach for Economic Stars.'

¹⁵¹⁹ Morgan, *The Age of Deficits*, 121.

¹⁵²⁰ Heller, 'Year to Reach for Economic Stars.'

¹⁵²¹ Heller, 'Supply-Side Follies of 1981' (quotation); Heller, 'Before Parting, Heller Left Advice on Avoiding Reagan Disaster.'

supply-side precepts designed to boost productive capacity and productivity.”¹⁵²² Central to this was a combination of fiscal restraint, monetary relaxation, and increased investment in human beings, infrastructure, research, and innovation.¹⁵²³ In this, Heller was pre-empting the economic strategy championed by Bill Clinton during the 1990s. True, Clinton failed to enact a major public investment strategy, but he did deem investment in human capital crucial to equip American workers for the high-tech economy of the 1990s.¹⁵²⁴ By calling for this policy at the end of the 1980s, Heller was at the forefront of New Democrat thinking on this issue.

Heller’s emphasis upon both monetary relaxation and fiscal restraint also foreshadowed Clinton’s economic programme. Throughout the 1980s, Heller expressed alarm at the way in which Reagan’s deficits produced inflationary concerns in the financial community.¹⁵²⁵ This was another reason why the Fed kept real interest rates high, leading Heller to argue that deficit reduction was necessary.¹⁵²⁶ In this, Heller’s ideas aligned with the new generation of Keynesians such as Alan Blinder and Paul Krugman, who emerged in the 1980s.¹⁵²⁷ His ideas also mirrored scholars at the Brookings Institution, whose Panel on Economic Activity he regularly attended in the 1980s.¹⁵²⁸ These individuals included future Clinton Budget Director Alice Rivlin, who placed emphasis upon the active use of monetary policy alongside fiscal restraint.¹⁵²⁹ Rivlin’s influence helped prompt Clinton to propose a deficit reduction

¹⁵²² Heller, ‘Before Parting, Heller Left Advice on Avoiding Reagan Disaster.’

¹⁵²³ Ibid.

¹⁵²⁴ See Morgan, ‘A New Democrat’s New Economics,’ in White (ed.) *The Presidency of Bill Clinton: The Legacy of a New Domestic and Foreign Policy* (London, 2012), 66-67.

¹⁵²⁵ Heller, ‘Before Parting, Heller Left Advice on Avoiding Reagan Disaster’; Heller, ‘The Unavoidable Issue.’

¹⁵²⁶ Heller, Pechman et al, *Tax Policy*, 8.

¹⁵²⁷ Krugman, *Peddling Prosperity: Economic Sense and Nonsense in an Age of Diminished Expectations* (London, 1994), 215, 283; Blinder and Janet Yellen, *The Fabulous Decade: Macroeconomic Lessons from the 1990s* (New York, 2004), 81-82.

¹⁵²⁸ Pechman, ‘Walter Heller,’ viii.

¹⁵²⁹ Alice Rivlin, *Reviving the American Dream: The Economy, the States and the Federal Government* (Washington DC, 1992), 7-8, 17, 81, 114, 179.

plan that played no small role in allowing the Fed to lower interest rates in the mid-1990s.¹⁵³⁰ As Blinder and Janet Yellen later noted, this strategy created “a pro-investment macroeconomic climate” that underwrote the economic success of Clinton’s premiership.¹⁵³¹ Far from advancing outdated prescriptions to revitalise the economy, Heller had adapted his views prudently by the late 1980s.

VII

Walter Heller’s responses to both stagflation and Reaganomics did not conform to the traditional view that Keynesian liberalism paled into irrelevance during the 1970s and 1980s. Instead, Heller developed a well-reasoned approach to stagflation, championing supply-side solutions whilst calling for carefully structured macroeconomic measures. Heller’s response to the rise of supply-side economics in the late 1970s also deserves credit, as he took this school of thought seriously. He also responded well to the flaws associated with Reagan’s economic policies, eventually recognising that increased training, fiscal restraint, and a relaxed monetary policy would revive the economy’s fortunes. In this, he anticipated the approach advanced by the New Democrats during the 1990s, whilst his move to the right of traditional Democrats in the 1970s mirrored that of the neoliberals. His positioning was also akin to the transformation of the Democratic Party under Jimmy Carter, who shifted the party’s focus towards both fiscal restraint and a greater appreciation of monetary policy.¹⁵³² By the end of the 1980s, Keynesians like Heller certainly had much to offer in terms of guiding policy.

¹⁵³⁰ Addison Wiggin, ‘An Interview with Alice Rivlin,’ *Daily Reckoning*, 11 December 2008. Available at: <https://dailyreckoning.com/an-interview-with-alice-rivlin/> [accessed 01/23/2017]; Morgan, *The Age of Deficits*, 166-168.

¹⁵³¹ Blinder and Yellen, *The Fabulous Decade*, 81-83.

Conclusion

Aside from his love for economics, Walter Heller had two other passions. Though he lived next to the University of Minnesota's golf course, neither of these was golf. Instead, the first was wood chopping, a task that Heller would do on evenings and weekends.¹⁵³³ His second hobby was clam digging, which Heller pursued at his holiday home in Puget Sound, Washington, a property that he and his wife built in the late 1960s.¹⁵³⁴ Set on fourteen acres of land, with a fifty-foot beach, Heller and his wife spent three months a year at this location during the 1980s.¹⁵³⁵ In July 1985, following both her long battle with lupus and a more recent one with cancer, Emily Heller passed away. She and Walter had met at the University of Wisconsin, where both obtained their PhDs in the early 1940s (Emily's was in physiology). Thereafter, Emily sacrificed her career to support that of her husband's, whilst courageously fighting illness and raising their three children.¹⁵³⁶ Her death brought a huge amount of heartache to Heller, who responded by increasing his already-heavy work schedule.¹⁵³⁷

Despite this, Heller found time to visit the holiday home that he and Emily built. No doubt, it gave him comfort in his time of grief. It was there, on June 15, 1987, while he was "digging out a channel from his beloved lagoon to the sea," that Heller suffered a heart attack.¹⁵³⁸ Various attempts to revive him all failed. Unsurprisingly, an outpouring of grief followed Heller's passing. At a memorial

¹⁵³² See Schulman, 'Slouching Towards the Supply Side,' 51-72.

¹⁵³³ Dave Thomas, 'Walter Heller: Economics Teacher to U.S. Presidents, U Undergrads,' No Publication [Henceforth n.p.] 3 April 1979. Heller Papers. Box 10. UoM.

¹⁵³⁴ Judy Vick, 'My Advisor is Walter Heller, And Heller Says...', *Twin Cities*, December 1981. Heller Papers. Box 10. UoM.

¹⁵³⁵ Ibid.

¹⁵³⁶ Ibid.

¹⁵³⁷ Susan Klemond, 'Heller Retires, Reflects on Career,' n.p. 1 June 1986. Heller Papers. Box 10. UoM. Indeed, despite retiring from the University of Minnesota at the end of the 1987 academic year, Heller remained committed to teaching introductory economics at that institution.

¹⁵³⁸ Walter P. Heller to Tobin, 21 August 1990.

service held at Minnesota's Willey Hall (where Heller lectured introductory economics throughout his career) family, friends, and colleagues gathered to pay their respects. Among the eulogists, James Tobin assessed Heller's tenure as CEA chairman, claiming "great things were done" under his leadership.¹⁵³⁹ Walter Mondale praised Heller for using Keynesian ideas to advance liberal causes. "Economics, as taught by Walter was never the 'dismal science'...it had a purpose, to help people, to expand opportunity, to enlarge justice, and to care for the most vulnerable."¹⁵⁴⁰

Obituaries portrayed Heller as one of the most influential and effective political economists of modern times.¹⁵⁴¹ His long-time associate Joseph Pechman, reflecting on why Heller had been such an important figure in twentieth century US history, described him as "an outstanding economist, an innovator in economic and social policies, an inspiring leader, and a marvellous human being."¹⁵⁴² Yet, despite this moment when scholars, journalists, and politicians reflected upon Heller's career, historians later paid very little attention to it. When he left the CEA in 1964, one American told Heller that his accomplishments would "forever be a part of our economic history."¹⁵⁴³ However, as the economist Louis Johnston recently commented, the historical community has curiously understudied Heller.¹⁵⁴⁴ As mentioned at the beginning of this dissertation, studies of public policy in the 1960s

¹⁵³⁹ Tobin, 'Walter Heller's Council,' Remarks at the University of Minnesota, 26 June 1987. Tobin Papers. Box 25. YUL.

¹⁵⁴⁰ Mondale, 'Eulogy, Walter Heller,' 26 June 1987. Mondale Papers. Political & Campaign Files, 1934-2004. Sound & Visual Recordings File. Box 153.L.2.12f. MHS.

¹⁵⁴¹ See, for example, Carol Byrne and Mike Meyers, 'He Made His Mark as a Transition Belt Between Academic Economics and the World of Public Policy,' *Minneapolis Star*, 17 June 1987. 1A. PQHN; Leonard Silk, 'Fruits of Economist Walter Heller Should Not be Forgotten,' *Journal Record*, 26 June 1987. PQHN; n.n., 'Heller, Economist and Presidential Adviser, Dies,' *Baltimore Sun*, 17 June 1987, 10A. PQHN; and Oswald Johnston, 'Economist Heller Dies,' *Los Angeles Times*, 17 June 1987, 4. PQHN.

¹⁵⁴² Pechman, 'Walter Heller, 1957-1987,' viii.

¹⁵⁴³ Donald C. Cook to Heller, 11 January 1965. Heller Papers. Box 15. JFKL.

¹⁵⁴⁴ Johnston, Interview with the Author.

treated Heller as a secondary actor. This study is an effort to fill that void. As it has shown, Walter Heller was one of the most significant economists and presidential advisers of modern times.

By rediscovering Heller's career, this thesis has mapped the rise, ascendancy, and eclipse of Keynesian political economy in the United States. This sets it apart from existing historical surveys of that doctrine, which have only taken the narrative up to the mid-1960s. This dissertation has further shown how Keynesian ideas intersected with liberal politics. It has illustrated how both merged during the 1930s and has demonstrated how social Keynesianism morphed into growth liberalism. In contrast to the claims of Robert Collins and Herbert Stein, this study has rejected the idea that liberals wholeheartedly embraced the commercial Keynesianism formulated by the post-war business community. Instead, it has demonstrated how many adopted growth liberalism, showing, too, that they played a pivotal role in fashioning the post-war ascendancy of American Keynesianism. In doing so, this thesis has highlighted how liberal and business iterations of Keynesianism did not conform to the idea of a consensus.

This dissertation has also helped show that Keynesian liberalism remained resilient in the 1970s and 1980s, often portrayed as decades of conservatism. Following the onset of inflation and the impact of the rights revolutions in the mid-to-late 1960s, liberals adapted their Keynesian ideas in diverse ways. While some embraced the redistributive Keynesianism espoused by the New Politics movement, Heller continued to recognise the importance of growth. At the same time, he tempered his commitment to expansion with a greater focus upon the quality of life. He also showed a determination to protect, rather than expand, the liberal programmes of the 1960s. Whilst traditional liberals continued to advocate Keynesian

ideas to promote full employment and growth in the 1970s, Heller, Arthur Okun, and others aligned themselves more with neoliberals such as Gary Hart and Paul Tsongas during that decade. These individuals recognised the need to combine traditional Keynesian ideas with a greater emphasis upon anti-inflationary initiatives, including supply-side policies and market-orientated solutions. When the deficit spiralled in the 1980s, the New Democrats and Keynesians like Heller, Alan Blinder, Paul Krugman, and Alice Rivlin shifted emphasis onto deficit reduction, monetary relaxation, and investment in human capital.

The policies that Heller and these individuals advocated, during the 1970s and 1980s, were sensible efforts to adapt to the problems of those decades. Issues such as inflation, debt, and insufficient public investment were important, and Heller recognised that economic growth alone could not solve them. This led him, Okun, and others to adopt a more cautious and pragmatic Keynesianism, but he and Okun never abandoned their fundamental belief in utilising economic management for the greater good. Unlike Hart and Tsongas, who were both criticised for neglecting the underprivileged in the 1970s, Heller and Okun continued to believe that government had a role in shaping demand, utilising fiscal deficits, and engaging in public investment to create a more equal society that would spread the fruits of growth as widely as possible. By demonstrating that their economic liberalism remained vibrant during the 1970s and 1980s, this thesis has helped show that American politics and political economy did not shift totally to the right after the mid-1960s. Because it has also illustrated that liberal Keynesian ideas up to the 1960s were more potent than traditionally assumed, this study has built upon recent scholarship showing that liberalism was a much stronger force in post-war American politics than scholars have appreciated.

By using Heller as its lens, this study has mapped the history of Keynesian liberalism in the United States. Though it has praised him throughout, it has not shied away from voicing criticism of Heller. His advocacy of community action in the War on Poverty, the way that he sought to press revenue-sharing upon LBJ, and the role that he played in the beginning of Keynesianism's mid-to-late 1960s eclipse, were all mistakes. Nevertheless, this thesis' overall interpretation of Heller is positive. Because of this, it has built upon the early positive appraisals made of him by those who first assessed his CEA chairmanship. In comparison with the existing literature, this thesis has also showed that Heller encouraged Kennedy to endorse a tax cut before most historians assume. It has proven, too, that Heller responded more effectively to the rise of both monetarism and supply-side economics than scholars have credited the Keynesians for doing.

I

Given the favourable interpretation of Heller advanced here, it is worth considering what made him such a good political economist. Firstly, Heller had an admirable level of persistence, which helped him convince both Kennedy and Johnson to promote the 1964 Revenue Act. At times, Heller's persistence did not pay off (particularly in terms of how he promoted revenue-sharing), but overall it served him well. Combined with his ability to understand and connect with people, Heller was also persistent without being overbearing. Despite having never met JFK before October 1960, he and Kennedy quickly established a strong rapport. Regardless of the difference in style between JFK and LBJ, Heller worked very effectively with the latter. Heller's persistence, combined with his charming personality, helped underwrite his success as a political economist. Indeed, he knew both his mind and his place, which suited him to working in an advisory capacity.

Added to this, Heller had a unique ability to translate complex economic ideas into clear and understandable terms. This led *Time* to label him the “Demystifier of the Dismal Science.”¹⁵⁴⁵ According to Mondale, Heller “could make the complex seem simple and make the simple feel complex,” whether through drawing transnational comparisons to highlight the merits of a tax cut in 1962, or using carefully chosen metaphors in his writings.¹⁵⁴⁶ This skill not only served Heller well in his dealings with politicians, it also enabled him to educate the American people. Though this thesis has shown that Heller was not particularly successful at selling the 1964 Revenue Act to the public in 1963, he did, at various points in his career, do much to help the public better understand economics. For example, he appeared on *Meet the Press* far more than any other economist did.¹⁵⁴⁷ He also regularly appeared in the public arena to explain economics in the 1970s and 1980s (Paul Samuelson was the only Keynesian to rival Heller in this regard).¹⁵⁴⁸ Unlike John Kenneth Galbraith, who wrote ‘big picture’ economic syntheses that reached popular audiences, Heller talked about the details of economic policy.

The fact that he combined his academic life with stints in public service certainly aided Heller’s ability to convey economics in a clear manner. It was also the result of his non-theoretical approach. Because he concerned himself with how economics worked in practice, this made him especially good at explaining his ideas to either an elite or a popular audience. Still, Heller never won the Nobel Prize in economics that usually goes to theoreticians. However, Heller did “more to bring an

¹⁵⁴⁵ George Church and Bernard Baumohl, ‘Demystifier of the Dismal Science, Walter Heller: 1915-1987,’ *Time*, 129:26 (Jun. 1987), 46. EBSCO.

¹⁵⁴⁶ Mondale, ‘Eulogy, Walter Heller.’

¹⁵⁴⁷ Rowen, ‘Comments at Memorial Service for Walter Heller,’ 26 June 1987. Tobin Papers. Box 25. YUL.

¹⁵⁴⁸ Sobel, *The Worldly Economists*, 141.

understanding of economics to the public than any economist of modern times.”¹⁵⁴⁹ Given this, coupled with both his effectiveness as a presidential adviser and his success at briefly installing liberal Keynesianism as the reigning orthodoxy in the early 1960s, Heller, rather than Alvin Hansen, deserves the title of the ‘American Keynes.’¹⁵⁵⁰

Whilst his ability to convey complex economic ideas in an accessible way was one of Heller’s most notable skills, his greatest asset was his pragmatism. Unlike Leon Keyserling and John Kenneth Galbraith, whose policy prescriptions stayed unchanged throughout their careers, Heller adapted his views to pursue liberal ends. Though he preferred to increase expenditures to close the performance gap in the late 1950s, he recognised that a tax cut was the politically workable route to take. He also showed a remarkable degree of flexibility in the 1970s, for he changed his views during that decade. “If ideas Walter held were contradicted by evolving evidence,” Alan Greenspan once remarked, “he was quick to change.”¹⁵⁵¹ Heller’s pragmatic approach to economic policy, combined with his dogged tenacity, his charm, his political ability, and his aptitude to convey economics in a clear manner, all helped underwrite his success as a political economist. At the same time, Heller “was so much greater than the sum of his separate skills.”¹⁵⁵² According to Pechman, he “joined high competence in all the dimensions of leadership with compassion, good judgment, and hard work, to leave a more indelible mark on the place of economics in American life than any other economist of his generation.”¹⁵⁵³

¹⁵⁴⁹ Rowen, ‘Comments at Memorial Service for Walter Heller.’ For more on this see Ackley, ‘Providing Economic Advice to Government,’ in Pechman and Simler, *Economics in the Public Service*, 221; and Okun, *The Political Economy of Prosperity*, 45.

¹⁵⁵⁰ See Chapter One of this thesis.

¹⁵⁵¹ Peter Kilborn, ‘Walter Heller, 71, Economic Advisor in the 60’s, Dead,’ *New York Times*, 17 June 1987, A1. PQHN.

¹⁵⁵² Pechman, ‘Walter Heller,’ viii-xi.

¹⁵⁵³ *Ibid*, xi.

All of this begs the question of what current policymakers and economists can learn from Heller. Some might consider his former student Louis Johnston a less than impartial source, but he has offered an important insight here. Firstly, if they want to have a greater influence upon policy, economists would do well to ensure that they translate their ideas into clear and understandable terms.¹⁵⁵⁴ Whilst doing so, economists should also be careful not to be “shrill about it.” Certain economists sometimes lose the high ground in economic debates by going “after people by name instead of keeping things on the plain of ‘wrong policy.’” Heller, by contrast, refused to engage in personal politics. True, Heller did get excited when debating his adversaries, but he also showed them respect. The way that he agitated against the antisemitism shown towards Milton Friedman in the early 1940s showed this. Heller’s career also highlights how “simple models have a lot of virtues.” Certain economists and policymakers “seem to think that you can’t do anything, and you can’t get any insight, unless you have a lot of equations and data.” Heller “never needed to show off that way,” an approach which America “could really use now.”

These points illuminate the importance of education to the making of economic policy. Unlike Ronald Reagan’s tax cut of 1981, or George Bush’s tax cuts of 2001 and 2003, the policies that Heller championed throughout his career resulted from cogent, well explained, technical analysis rather than pure dogma. Speaking about the 1964 Revenue Act, one businessperson told Heller that it had shown “how good economic theory can be translated into empirically useable political economy.”¹⁵⁵⁵ With the US now beset by both a structural and a trade deficit as well as a swelling level of public indebtedness, policymakers and economists would do well to base their recommendations upon sound, technical analysis, much like Heller.

¹⁵⁵⁴ Johnston, Interview with the Author.

This is particularly important given the polarised political climate that has emerged since the 1990s, the rise of soundbite politics, and the fact that, since the 1980s, the CEA has declined as an agency of influence within the executive branch of government.

II

The beginning of this thesis mentioned how certain individuals have recently revived Keynesianism, seeing in the doctrine a means to make the US economy stronger. Donald Trump's recent ascension to the presidency has led to suggestions that his investment plans may amount to a Keynesian stimulus.¹⁵⁵⁶ Although Trump's programme will likely provide the economy with a good short-term spurt, most observers believe that it will produce negative long-term consequences (including increased levels of debt and economic inequality).¹⁵⁵⁷ Sufficient investment in human capital, healthcare, nutrition, childcare, and research will also need to accompany this, in order to reduce inequality and facilitate the development of high-tech industries.¹⁵⁵⁸ Others have argued that a dose of Keynesianism is not the correct solution for the US economy now, not least because the jobless level is at 4.6 percent, effectively the rate defined as full employment.¹⁵⁵⁹

Nevertheless, a consensus is forming around the need for a new round of Keynesian stimulus. Over the past seven years, US economic growth has averaged just 2 percent per year, which, according to Keynesian Larry Summers, is only

¹⁵⁵⁵ Alfred Morgan to Heller, 4 May 1964. Heller Papers. Box 49. JFKL.

¹⁵⁵⁶ See, for example, Noah Smith, 'Even Trump believes that Keynes got it right,' *Salt Lake Tribune*, 19 November 2016. PQC.

¹⁵⁵⁷ Larry Elliot, 'Keynesian Economics: Is It Time for the Theory to Rise from the Dead,' *The Guardian*, 11 December 2016. Available at: <https://www.theguardian.com/business/2016/dec/11/keynesian-economics-is-it-time-for-the-theory-to-rise-from-the-dead> [Accessed 12/29/2016]

¹⁵⁵⁸ Obama, 'The Way Ahead,' *The Economist*, 8 October 2016, 23 – 26. Author's copy.

¹⁵⁵⁹ Steven Pearlstein, 'Republicans are finally willing to spend on the Economy – at the exact wrong time,' *Washington Post*, 12 December 2016. Available at:

attributable to the fact the economy has put idle resources back to work.¹⁵⁶⁰ More worrying is that both the labour force and the rate of productivity are each set to grow at just 0.5 percent annually over the next five years. This means that economic output will increase at a yearly rate of only 1 percent.¹⁵⁶¹ “At the very least,” one commentator has explained, “the dismal forecast calls for the government to prepare for another bout of fiscal stimulus.”¹⁵⁶² Others agree. The OECD recently called for all advanced economies to engage in aggressive macroeconomic policies, warning that the global economy was in a “low-growth trap.”¹⁵⁶³ Its chief economist predicted that “fiscal initiatives” could “catalyse economic activity,” pushing the global growth rate up to 3.5 percent per year by 2018 (compared with the current forecast of 3 percent).¹⁵⁶⁴

The case for using fiscal policy to stimulate the economy is also strong given the combination of austerity and monetary easing, which has characterised US economic policy since 2013, has done much harm. Recently, the International Monetary Fund admitted that it underestimated how much the economy would contract under austerity (having previously championed such policies).¹⁵⁶⁵ Similarly,

https://www.washingtonpost.com/news/wonk/wp/2016/12/12/republicans-are-finally-willing-to-spend-on-the-economy-at-the-exact-wrong-time/?utm_term=.11b51f91f394 [accessed 12/29/2016]

¹⁵⁶⁰ Eduardo Porter, ‘Why the US Economy Continues to Stagnate,’ *International New York Times*, 18 May 2016, 16. PQC.

¹⁵⁶¹ Ibid, 16. Economic historian Robert Gordon has also raised concerns about future productivity growth and has questioned whether IT-driven innovations could spur 21st century economies forward in the same way innovations did so in the 19th and 20th centuries. See *The Rise and Fall of American Growth* (Princeton, NJ, 2016).

¹⁵⁶² Ibid, 16.

¹⁵⁶³ Ben Chu, ‘OECD pushes for global Keynesian fiscal stimulus to spring low-growth trap,’ *The Independent*, 28 November 2016. Available at: <http://www.independent.co.uk/news/business/news/oecd-global-keynesian-fiscal-stimulus-catherine-mann-donald-trump-a7443251.html> [accessed 12/29/2016]

¹⁵⁶⁴ Cited in Ibid. For similar views see International Monetary Fund, ‘Fiscal Policies for Innovation and Growth,’ *Fiscal Monitor*, April 2016. Available at: <https://www.imf.org/external/pubs/ft/fm/2016/01/pdf/fmc2.pdf> [Accessed 12/31/2016]; and Blinder, ‘Fiscal Policy Reconsidered,’ *The Hamilton Project*. Available at: http://www.hamiltonproject.org/assets/files/blinder_stabilizers_policy_proposal.pdf [accessed 12/21/2016]

¹⁵⁶⁵ n.n., ‘Where Does the Buck Stop,’ *The Economist*, 13 August 2016, 420, 55. PQC.

Larry Summers and Antonio Fatas have argued that austerity “has substantially reduced growth, leading to levels of public debt that are higher than they would have been had enthusiastic stimulus been used to revive growth.”¹⁵⁶⁶ The fact that austerity has not worked surely adds cogency to the case for renewed fiscal stimulus. Similarly, monetary policy has not spurred economic activity, as investors have remained nervous at the prospect of borrowing in the wake of the financial crisis. With interest rates also at record lows and the Fed committed to expanding the money supply via quantitative easing, the only weapon available to promote stimulus is fiscal policy.¹⁵⁶⁷

This is exactly what Keynes argued in *The General Theory*. He explained that, if monetary policy did not lift “animal spirits,” the government needed to step in with public investment.¹⁵⁶⁸ Unsurprisingly, with the US economy’s current rate of growth so sluggish, several academics have spoken in favour of fiscal stimulus. This is interesting because, since the 1990s, Keynesians developed economic models in which “fiscal policy was all but neutered.”¹⁵⁶⁹ Instead, they placed responsibility upon central banks to “do the heavy lifting.”¹⁵⁷⁰ However, with monetary policy now unable to do so macroeconomists have “written down models in which Keynesian stimulus works fine.”¹⁵⁷¹ Reflecting this, Barack Obama’s CEA chairman Jason

¹⁵⁶⁶ Ibid, 55.

¹⁵⁶⁷ See Jason Furman, ‘The New View of Fiscal Policy and Its Application,’ Paper Delivered at the Global Implications of Europe’s Redesign Conference, 5 October 2016, New York. Available at: https://www.whitehouse.gov/sites/default/files/page/files/20161005_furman_suerf_fiscal_policy_cea.pdf [accessed 12/31/2016]. See too Blinder, ‘Fiscal Policy Reconsidered.’

¹⁵⁶⁸ Larry Elliot, ‘Keynesian Economics.’

¹⁵⁶⁹ n.n., ‘Where Does the Buck Stop,’ 55. For examples, see Blinder and Yellen, *The Fabulous Decade*; and Greg Mankiw and Laurence Ball, ‘What Do Budget Deficits Do,’ Kansas City Federal Reserve Board Economic Policy Symposium – Jackson Hole, 1995. Available at: <https://www.kansascityfed.org/publicat/sympos/1995/pdf/%20s95manki.pdf> [accessed 12/31/2016]

¹⁵⁷⁰ n.n., ‘Where Does the Buck Stop,’ 55.

¹⁵⁷¹ Smith, ‘Even Trump believes that Keynes got it right.’ For examples see DeLong and Lawrence Summers, ‘Fiscal Policy in a Depressed Economy,’ *Brookings Papers on Economic Activity*, 43:1 (2012). Available at: http://larrysummers.com/wp-content/uploads/2012/10/2012_spring_BPEA_delongsummers.pdf [accessed 12/31/2016]; and Blinder, ‘Fiscal Policy Reconsidered.’

Furman has defended this “‘New View’ favoring more activist fiscal policy,” whilst current Fed chairwoman Janet Yellen gave a speech in October 2016 which echoed “recent calls for aggregate demand management that is both more active and of greater magnitude.”¹⁵⁷²

Should fiscal stimulus take place, both policymakers and economists would do well to look back at the rise and decline of Keynesianism in America. Of course, Keynesianism could be more difficult to implement in current conditions. The growth of programme-orientated budgeting in the wake of Keynesianism’s eclipse in the 1970s, coupled with the rise of the entitlement state since the late 1960s, have both weakened fiscal policy.¹⁵⁷³ With the economy beset by both near permanent deficits and record levels of debt, it might be unwise to implement Keynesian policies. Keynesian economists also no longer enjoy the influence that they had during Walter Heller’s day.

Nevertheless, it would be instructive to explore how both policymakers and economists previously implemented Keynesianism. This will provide a model of how to sell Keynesian ideas in particular and economic ideas in general, illustrating what policies worked best in certain conditions.¹⁵⁷⁴ True, there are historical differences to consider when comparing 1960s economic policy to the twenty-first century, not least the fact that America’s position within the global economy is relatively weaker today.¹⁵⁷⁵ Even so, Heller’s “operating style” provides “a case study of an unusually

¹⁵⁷² Martin Sandbu, ‘The Return of Keynesianism,’ *Financial Times* (online), 24 October 2016. PQC.

¹⁵⁷³ Morgan, ‘Reply to Brian Domitrovic,’ *Journal of Policy History*, 23:3 (2011), 444-445.

¹⁵⁷⁴ As to the concerns raised in the paragraph above about the contemporary effectiveness of fiscal policy, it is worth noting that recent research has undermined these. True, programme-orientated budgeting and entitlement spending have weakened the flexibility of fiscal policy, but current research demonstrates that fiscal policy still has considerable potential to generate a multiplier effect. Moreover, though debt is a big problem for the US economy, there is still enough “fiscal space” to enact expansionary policies. See Furman, ‘The New View of Fiscal Policy and Its Application.’

¹⁵⁷⁵ Ruchir Sharma, ‘The Boom was a Blip: Getting Used to Slow Growth,’ *Foreign Affairs*, 96:3 (May/June 2017), 104-114. EBSCO.

successful practice of economic policy entrepreneurship.”¹⁵⁷⁶ This is something recognised in a recent blogpost by economic historian Beatrice Cherrier.¹⁵⁷⁷ Cherrier has credited Heller’s carefully crafted memoranda with educating Kennedy and Johnson and has drawn attention to how his successful engagement in bureaucratic politics convinced administration officials of his approach. This thesis has also mapped Heller’s operating style and has illuminated his success in creating a post-war economic framework to advance liberal objectives. Though the growth rates of the 1960s are almost impossible to envisage for the American economy today, this thesis’ examination of how Heller and other Keynesians adapted the ‘dismal science’ for liberal political aims offers an important lesson to progressive economists today, who are fighting for jobs, equal opportunity, and economic equity in the age of Trump.

¹⁵⁷⁶ Robert H. Nelson, ‘The Economics Profession and the Making of Public Policy,’ *Journal of Economic Literature*, 25:1 (Mar. 1987), 66.

¹⁵⁷⁷ Beatrice Cherrier, ‘How Not to Screw Up Your Economic Expertise: Lessons from the Kennedy Tax Cut Grandmaster, Walter Heller,’ 20 February 2017. Available at: <https://beatricecherrier.wordpress.com/2017/02/20/how-not-to-screw-up-your-economic-expertise-lessons-from-the-kennedy-tax-cut-grandmaster-walter-heller/> [Accessed 05/10/2017]

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