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Walter Heller's economic leadership within the political realm opened a Pandora's Box for politicians in Washington and for the American public. As Chair of the Council of Economic Advisers (CEA) during the Kennedy administration, Heller was able to introduce Keynesian economics into the political mainstream and oversee the passage of the first federal tax cuts for the purpose of stimulating demand and economic growth. In the process, however, Heller helped remove politicians' historical reservations regarding budget deficits, setting the stage for today's staggering deficit problem.

HELLER'S ECONOMIC PHILOSOPHY

Throughout his professional life, Walter Heller served in various government posts, offering his economic expertise to the political realm. During World War II, the Treasury Department hired Heller as a financial economist. After the war, he worked with the United States military government in Germany. In 1957, the offer of a teaching and research position in economics at the University of Minnesota prompted Heller to end his service to the federal government temporarily. However, from 1961 to 1964, Heller returned to Washington to become one of the most influential chairs in the history of the Council of Economic Advisers (Galbraith 1987, p. 258). Heller decided to return to the University of Minnesota after serving four grueling years in Washington. He was tired and feared he had lost his objectivity within such a wholly political environment (Flash 1965, p. 274; Hargrove & Morley 1984, p. 185).

As a researcher and professor, Heller wrote and lectured extensively on federal, state, and local finance, originating the idea of federal revenue sharing with state and local governments (Pechman 1987, p. 637). Until his death in 1987, he continued to voice his opinions on national economic policy through opinion pieces in *The Wall Street Journal*, serving as a member of its

Board of Contributors. In an obituary published by the Brookings Panel on Economic Activity of which Heller was a founding member, Heller was remembered as "one of the most important and effective economists of the post-World War II period" (Pechman 1987, pp. x-xi).

Walter Heller was a Keynesian. He believed government should assume the responsibility of regulating the business cycle and attaining full-employment through active fiscal policy. Heller contended that the government budget is a useful instrument for regulating aggregate demand. When the economy is below full employment, aggregate demand can be raised, he argued, either by increasing government expenditures or lowering tax rates. Business cycles, he maintained, arise from defects in economic institutions that can be corrected by deliberate action; they should not be regarded as a fact of nature.

In his public service, Heller extolled the merits of what he termed a *balanced economy* over the restrictions of the conventional balanced budget. He stated that:

> The success of fiscal and budget policies cannot be measured only by whether the budget is in the black or in the red. The true test is whether the economy is in balance. Only an economy which is realizing its potential can produce the goods and create the jobs the country needs.
> (Heller in Norton 1977, p. 184)

Heller was not afraid to endorse a budget in the red if it meant the economy would be stimulated to reach its full potential. Combining his skills as an economist and educator, he took this unconventional political idea to those at the top of the fiscal policy machine: the President and the Congress.

Heller defined two types of deficits, Type A and Type B. Type A deficits are caused by the performance gap. The performance gap is the difference between the actual gross national product (GNP) and the potential GNP. Potential GNP is the amount of output the nation would produce if it were functioning at full employment. Type A deficits occur because government revenues decrease as GNP falls below its potential level.[1] Heller called Type A passive deficits (Heller 1976, p. 108). Type B deficits are caused by fiscal policy which increases government expenditures and/or reduces taxes. Heller referred to these as active deficits (1976, p. 108). When the economy produces below its potential GNP, Heller called for an active deficit to return the economy to a smooth path of growth. Although exacerbating the deficit in the short run, Heller argued such a policy would stimulate the economy, increase tax revenues, and, as the economy moved toward full employment, eventually offset the recession-caused deficit (1976, p. 109). Along with prescribing fiscal policy to create a growing economy, Heller advocated an expansionary monetary policy to hold down interest rates and encourage private spending. However, Heller maintained that Type B deficits are not beneficial if the economy is already producing at a full employment level.

Heller's economic philosophy addressed all phases of the economic cycle. He encouraged the use of stimulative fiscal policies during downturns in the business cycle, but he also recognized that the government must enact fiscal restraint during periods of growth, i.e., increase tax rates or decrease government spending. This use of active fiscal policy would smooth-out business cycles, hence creating a balanced economy. Although Keynesian philosophy was dominant among economists during the late 1950s and early 1960s, most politicians did not hold such views (Stein 1990, p. 380). Many politicians believed deficit spending by the government was a source of depression, not a means of achieving full employment. Heller used his teaching skills to convince these politicians to accept an active role for the federal government in steering the economy. Heller believed that "policy makers had to be weaned away from the annually balanced budget and the cyclically balanced budget as policy targets and from actual deficits or surpluses as measures of budget stimulus or restriction" (1976, p. 189). He asserted that it took twenty-five years to convert a Democratic President to these beliefs and ten more to persuade a Republican (Heller 1976, p. 189).

HELLER AND THE "NEW ECONOMICS" IN WASHINGTON

President John Kennedy appointed Heller as Chair of the Council of Economic Advisers in 1961. Heller brought a synthesis of Keynesian and neoclassical economics into the White House. The press dubbed this philosophy the "New Economics" (Tobin & Weidenbaum 1988, p. 5). Dornbusch and Fischer characterize it as "a mix of activism and optimism" (1987, p. 426). Kennedy entered office without an established economic policy agenda beyond a predilection for fiscal conservatism. As the leading economic adviser to the President, Heller played a key role in teaching Kennedy economics and developing Kennedy's economic policies (Tobin and Weidenbaum 1988, p. 6). Kennedy and Heller believed the Employment Act of 1946, which established the Council of Economic Advisers, required the administration to establish targets for maximum employment, production, and purchasing power. Kennedy's was the first administration publicly to specify numerical targets for full employment. It set goals of 4 percent unemployment, 4 percent annual economic growth, and inflation at a low 1 percent (Heller 1982, pp. 237-38). Heller influenced Kennedy to change fiscal policy from "corrective" to "propulsive," i.e., a change from reactive fiscal policy to proactive fiscal policy in order to achieve these economic goals (Pious 1979, p. 296).

During his administration's first months, President Kennedy's fiscal conservatism was not always compatible with the economic policy vision of his CEA Chair. Kennedy had campaigned as a fiscal conservative and entered office endorsing the virtues of a balanced budget. He considered raising taxes to finance the American response to the Berlin Crisis in 1961, but Heller convinced him that such an act would further weaken the sluggish economy (Hargrove and Morley 1984, p. 165). As the recession dragged on, Heller persuaded the President that a balanced economy, one with low unemployment and high growth, was more essential than a balanced budget. This led Kennedy to propose tax cuts as a stimulus for the economy, despite the resulting budget deficit (Flash 1965, p. 271).

Heller obtained direct access to the President for the CEA Chair. According to Hugh Norton, "never before had the Council achieved such influence as a policy-making body and vendor of new ideas" (1973, p. 65). During the one thousand days of Kennedy's presidency, Heller forwarded over 300 economic memos to the Oval Office (Heller 1966, p. 29). Indeed Heller was the front man for Kennedy, advocating policies which were politically risky for Kennedy to support. Once Heller had built sufficient acceptance for an economic policy within the Congress and with the general public, Kennedy could safely express his endorsement (Pious 1979, p. 308).

Heller created a more public role for the CEA Chair than his predecessors had desired. He viewed the opportunity to testify before Congress's Joint Economic Committee as a chance to educate politicians outside of the White House and to voice economic ideas for public consumption (Norton 1977, p. 184). Heller established formal relations with the Secretary of the Treasury and the Budget Director. Termed the "Troika," this group brought the administration's top economic policy makers together to communicate and coordinate. The group was expanded into the "Quadraid" with the addition of the Federal Reserve Chairman, another key player in national economic policy. Heller also maintained relations with nongovernmental groups such as the Brookings Institution, the Committee for Economic Development, the National Planning Association, and the press (Norton 1977, pp. 186, 190). Heller used these many paths of communication to introduce to politicians, pundits, and the public the administration's goal of cutting taxes to boost the economy.

Heller found the public receptive to a policy that promised to move the country from its highest unemployment rates since World War II. Many also believed federal tax rates were too high. First the public and then Congress accepted the fiscal expansion proposed by Heller, even though it meant a budget deficit (Stein 1990, p. 373). Indeed politicians began to see deficits as a necessary fiscal tool to benefit the economy, and the debt as a more or less benign side-effect.

Beginning in 1962, the CEA under Heller developed and built support for a tax reduction program, influenced the reduction amount, and gained approval of a budget deficit as a trade-off for full employment. Heller called for a tax reduction totaling $13.5 billion. The proposed reduction decreased individual income tax rates from the range of 20-91 percent to 14-65 percent and corporate tax rates from 52 percent to 47 percent. The proposal underwent minor changes as it was pushed through the legislative process. The final result, the Revenue Act of 1964, cut tax revenues by $12 billion, reduced individual income tax rates to the 14-70 percent range and the corporate tax rate to 48 percent (*Congressional Quarterly* Feb. 28, 1964, pp. 387-95). Nelson Polsby called the tax cut, "the frankest, best-publicized, and most explicitly didactic approach of Keynesian economics ever undertaken by the federal government" (1986, pp. 33-4).

Edward Flash, in his book on the role of the Council of Economic Advisers during its first twenty years, asserts that the CEA under Heller was highly influential because of the faltering economic recovery in 1962, the willingness of Kennedy to learn from and work with modern economists, the Council's conciliatory relationship with Treasury Secretary Douglas Dillon, and the highly qualified staff at the CEA which was "in harmony with its time" (1965, pp. 273-74). James Anderson credits the CEA's influence during the 1960s to its willingness to become active in the politics of policy and its monopoly of economics staff, expertise, and information within Washington (1986, p. 91). Heller and the CEA were in harmony with the President and his administration, and were able to influence their views on economics as well.

Heller continued to serve as the CEA Chair while Lyndon Johnson completed Kennedy's term. During that time he began the development of Johnson's Great Society programs as a manifestation of Johnson's and his own belief that government should provide economic opportunities for low-skilled workers and a respectable income for those who are unable to earn it themselves (Pechman 1987, p. x). Heller resigned from the CEA in November, 1964. However, Johnson continued to call on Heller for economic advice throughout his years as President (Anderson, J. 1986, p. 94).

SUCCESS AND FAILURE OF THE "NEW ECONOMICS"

The economic ideas Heller brought to Washington have been credited with the nation's continuous economic growth from 1961 to 1969 (Dornbusch & Fischer 1987, p. 431). In 1982, Heller asserted that his New Economics had been correct, noting that by July 1965, the unemployment rate had fallen to 4.4 percent while inflation remained at 1.5 percent. He also credited the 17 percent rise in GNP during the two years following the tax cut to Kennedy's expansionary fiscal policy (Heller 1982, p. 246). In 1966, Heller asserted that Presidents Kennedy and Johnson were the first "modern economists" in the White House. He meant they were free of the beliefs that government deficits create inflation, that increased government spending is the source of depression, and that a government debt is an immoral burden on our grandchildren (Heller 1966, pp. 36-7).

However, as the "New Economics" spread throughout Washington, key features of its implementation tended to be ignored. Indeed Heller's fiscal policies have been blamed for the rising inflation of the late 1960s and the 1970s (Dornbusch & Fischer 1987, p. 431). Heller recognized that if the fiscal and monetary policies of the New Economics reacted only to recessions and not to inflation, these policies would be discredited within the academic world and would be dangerous for the economy. An economic theory which allowed for budget deficits during recessions but did not call for surpluses during economic booms would be politically expedient, but economically irresponsible. Unfortunately, once the belief that budget deficits could be beneficial was accepted in Washington, political realities made attaining fiscal restraint much more difficult. Politicians found it harder to sell tax increases to their constituents than to sell and vote for tax cuts.

When the Vietnam War increased federal expenditures and accelerated economic growth, Heller recognized it was time to enact the other side of New Economics, i.e., fiscal restraint to slow a runaway economy. Johnson, however, was reluctant to sanction a rise in taxes which Heller, Gardner Ackley and Arthur Okun, Heller's successors on the CEA, were advocating. The President feared the public would view higher taxes as another reason to oppose the Vietnam War (Jacobs 1986, pp. 70-1). It took until mid-1968 before tax increases were enacted, too late to stop the rising inflation (Heller 1982, p. 247).

HELLER'S AMBIGUOUS LEGACY

Heller's positive contribution as Chair of the Council of Economic Advisers was the important role he developed for economics and economists in national economic policy formation. Since Heller's time, the availability of economic expertise has grown within the political world. Economic concerns became integral to political decision-making as Congress and the President recognized the key role which the state of the economy plays in their electoral success (Tufte 1978, p. 9). Economic experts, however, must still compete with the political realities faced by politicians in perpetual campaigns for reelection. Economic theory, in this context, may easily be supplanted by electoral concerns. Heller encountered opposition in his initial attempt to cut taxes to stimulate the economy in 1962 because many politicians feared the reactions the resulting decrease in revenues and consequent budget deficit would draw from their constituents. Heller was successful because he presented a logical justification for a deficit, educating the general public along with the politicians.

Regrettably, the dominant economic advisory voice established for the CEA Chair under Heller did not continue much beyond the decade of the 1960s. Norton asserts that the influence of the CEA steadily increased from 1946 until 1971 (1977, p. 22). However, during the Nixon, Ford and Carter administrations, other agencies were developed within the executive branch which competed with the CEA, such as the Council of Economic Policy, the Council on International Economic Policy, the Domestic Council, the Economic Policy Board, and the Economic Policy Group, as well as an expanded policy-making role for the Office of Budget and Management (Pious 1979, p. 249; Hart 1987, p. 57). Another reason for the CEA's decline was the formation of economic advisory units within existing executive branch agencies, decreasing their demand for CEA advice (Anderson, J. 1986, p. 100). During the Reagan administration, for example, CEA Chair Murray Weidenbaum discovered that the CEA was left out of the inner loop of policymaking. After eighteen months, he resigned (Zwicker 1989, p. 264). Two months later, Martin S. Feldstein was named Chair. Feldstein became distressed by the rising budget deficits under the Reagan administration, and he did not hesitate to speak publicly against the federal government's spending policies. A breakdown of the relationship between the CEA and the President occurred and Feldstein's resignation ensued (Zwicker 1989, p. 264). This left the Council of Economic Advisers in a precarious position; the Reagan administration even considered abolishing the CEA. However, after seven months, Reagan appointed Beryl W. Sprinkel as CEA Chair. At this low point, CEA influence was restricted to providing limited advice, analysis, and data (Zwicker 1989, p. 265). Michael J. Boskin served as CEA Chair under President George Bush. In the midst of the 1990-92 recession Boskin suggested that Bush propose tax cuts to spur the economy, but other members of the administration convinced the President that the economy would recover by itself (Jacobson 1992, p. 162). The CEA remained weak.

Unlike Heller, CEA Chair Laura D'Andrea Tyson did not assume a public role as President Bill Clinton's economic policy spokesperson. In the Clinton administration, the CEA's voice is diluted by the presence of the National Economic Council. Indeed, Clinton may promote Tyson to head the National Economic Council, signifying how the current administration presently ranks the two economic advisory organizations (*The Wall Street Journal* 1995, A1). The CEA Chair has not regained the influence Heller built for the position, and Heller's legacy of a dominant and public role for the CEA Chair in economic policy-making remains diminished.

Since the 1960s, politicians have approved budget shortfalls regardless of the strength or weakness of the economy, ignoring Heller's admonition to run surpluses when the economy is strong. Paul McCracken, CEA Chair for President Nixon from 1969 to 1971, has contended that throughout the fifty years from the 1940s to the 1990s, the "always-balanced-budget philosophy" has been discarded for "compensatory-fiscal-policy wisdom" (1983, p. 87). In fact, since 1964, the budget has been balanced only once, in 1969 (Anderson, G. 1986, p. 13). Throughout the 1970s, Congress and the successive Republican and Democratic presidents approved budget deficits despite the period of economic growth from 1972-1974. Again during the terms of Presidents Ronald Reagan and George Bush, budget deficits continued and the federal debt rose above the three trillion dollar level while the economy experienced the longest peacetime expansion since World War II. Heller expressed chagrin at the mounting red ink during the 1980s in his *Wall Street Journal* opinion pieces, but his concerns were not heeded (Heller 1982, p. 22).

Today, budget deficits continue, but they cannot be justified as creating Heller's balanced economy. Instead, today's deficits exemplify politicians' lack of fiscal restraint as they consider their prospects for the next election. Economics is held hostage to the politics of Washington. As a result, federal government deficits continue to grow and the national debt has surpassed $4.8 trillion (*CNN* March 5, 1995). Currently, we hear politicians say that the debt is burdening our grandchildren, yet these same politicians refuse to end their habits of deficit spending. One could argue that Washington policymakers have forgotten part of Heller's message, which was to reduce deficits during boom times. On the other hand, some might contend that Heller's philosophy removed politicians' fears of deficit spending and unintentionally opened the door to out-of-control deficits.

The 1994 elections ushered in a monumental change in Washington: a Republican majority in Congress for the first time in forty years. House Republicans have become the majority party supporting a "Contract With America" that advocates, among many other economic proposals, a balanced budget amendment to the Constitution. This may reflect either a radical change by Washington politicians, or an unleashing of a view suppressed in the minority for the last thirty years. James Tobin has asserted that conservatives maintained attachment to budget-balancing (Tobin 1987, p. 48). The incoming House Budget Committee Chairman John Kasich promises a plan to balance the federal budget within seven years (Calmes & Rogers 1994, B4). In contrast, President Clinton's Treasury Secretary Robert Rubin insists that a balanced budget amendment would hurt the economy because it would limit the government's ability to use discretionary fiscal policy (Jan. 15, 1995). If a balanced budget amendment to the Constitution is passed, not only will this end the freedom of Washington politicians to ignore the second half of Heller's philosophy (contraction of deficits during economic booms), it will prohibit Washington economists and politicians from enacting the first half (expansions of deficits during recessions). Active fiscal policy advocated by Heller would come to an end with the 104th Congress.

Walter Heller's ambiguous legacy lies in his strengthening of the role of the Council of Economic Advisers in national policy-making and the introduction of active Keynesian fiscal policy into American politics. It is ironic that while the demand for the expertise of professional economists within government has grown, the role of the CEA has diminished since the days of Heller. During his public service as Chair of the Council of Economic Advisers, Heller introduced those in government to the tools of an active fiscal policy. He contended that Washington advanced from "the bad old days of the annually balanced budget objectives" toward the use of active fiscal policy to reach a balanced economy (Heller 1976, p. 190). However, the belief that Washington can create this balanced economy leads the public to blame politicians for economic downturns which may be, despite Keynes's and Heller's beliefs, beyond the government's control. This belief leads to an unsubstantiated placing of blame and a feeling that the economy is dependent on the government, when in reality, the government is dependent on the economy. Heller equipped politicians with a tool they could use to attempt to "fix" the economy. However, the public has come to believe that the humble "mechanics" in Washington are now the masterful "engineers" creating the product. In selling to politicians and the public the idea that government can beneficially manipulate the economy and in removing politicians' taboo against budget deficits Heller opened a Pandora's box which has yet to be closed.

NOTE

1 In the 1980s, Isabel Sawhill estimated that each one percent rise in unemployment causes a $27 billion Type A federal deficit (1982, p. 53).

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