

Chapter 4

Building for Future Prosperity

IT IS FITTING and proper, as the preceding Chapter has urged, that we make the extension of prosperity to lagging sectors our peculiar concern at this favorable juncture of the Nation's history. In the measure that we succeed in drawing into the stream of progress the less flourishing parts of the economy, to that extent shall we strengthen the base of future prosperity as well as enhance the general welfare. But as we go about the task of extending the scope of prosperity, it is essential that we never lose sight of the fundamental objective of extending prosperity itself into the future. We must always keep before us two great truths: First, lasting prosperity of the Nation depends far more on what individuals do for themselves than on what the Federal Government does or can do for them. Second, the rate of our economic advance in the years ahead will depend largely on our ability as a people to preserve an environment that rewards individual initiative and encourages enterprise, innovation, and investment.

A Government that earnestly seeks to build for the Nation's long-range prosperity has clear-cut responsibilities. It should administer the public finances with a keen sense of awareness of the impact that the Government's huge operations have on the economy. It should safeguard competition and firmly resist any outcroppings of monopoly. It should encourage home ownership, better homes, and sound neighborhoods. It should lead the States and localities in a mutual endeavor to fill the Nation's vast needs for public facilities on which the growth of the private economy so largely depends. It should foster education, science, technology, and creative research. It should constantly strive to strengthen our ties of trade, investment, and enterprise with other nations of the Free World. And it should improve the defenses of our economy against the threat of both inflation and recession. These objectives are worthy of our best efforts in the year that lies ahead.

I. PRESERVING SOUND FEDERAL FINANCES

Sound management of the Government's fiscal affairs requires the observance of certain fundamental principles. First, the budget should provide adequately for the Nation's security and other urgent needs. Second, all governmental operations should be conducted with prudence and economy.

Third, sufficient revenues should be raised to meet the Government's outlays, if not every individual year, then surely over a term of very few years. Fourth, the cost of government should be distributed fairly among taxpayers. Fifth, revenues should be raised in ways that interfere as little as possible with incentives to work, to venture, or to invest. Sixth, the public debt should be managed so as to contribute to stable economic growth. A brief review of how these principles have recently been applied will help to indicate the fiscal policy that in current circumstances will best serve the Nation's interests.

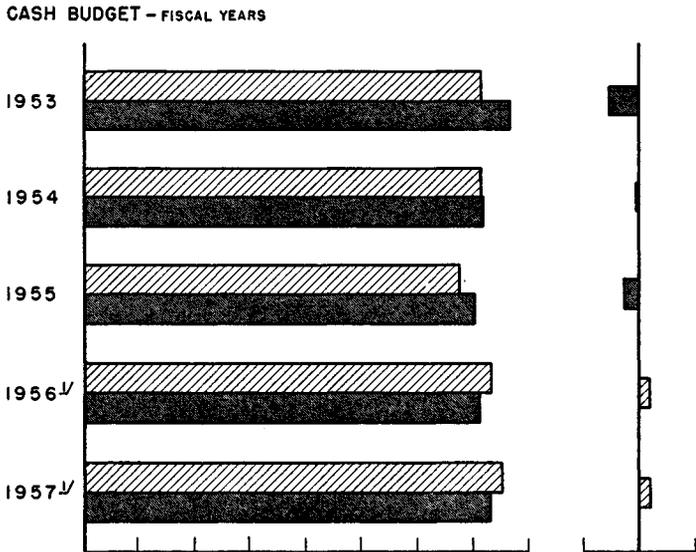
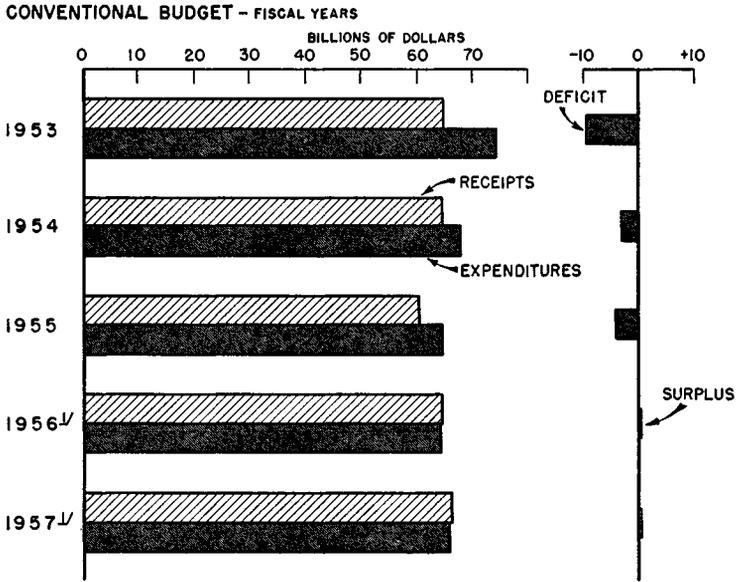
The past three years have been marked by substantial achievements in bringing Federal expenditures and revenues into balance. Budget expenditures were reduced from 74.3 billion dollars in fiscal year 1953 to 64.6 billion in 1955, a drop of 9.7 billion. A slight further reduction is estimated for fiscal year 1956. These economies and a rising national income have made it possible to reduce taxes and yet move decisively toward a balanced budget. In fiscal year 1955 the budgetary deficit amounted to 4.2 billion dollars, compared with a deficit of 9.4 billion in 1953. For the present fiscal year, a balanced administrative budget is in prospect. The showing of the consolidated cash budget, which includes transactions of the various trust funds, will be more favorable still. It may be reasonably expected that the cash budget will register a surplus of over 2 billion dollars for the current fiscal year.

In formulating its fiscal policies, the Administration has given careful consideration to the effects of taxation and governmental finances on the general economy. The record is clear and instructive. In the spring of 1953, when inflation was still a real danger, a Message to the Congress recommended that the excess profits tax, which was then in effect, be extended six months beyond its expiration date of June 30, 1953. The decision to extend this burdensome and unpopular tax was taken because it would have been imprudent to increase the deficit and the public debt under the conditions prevailing at the time. In September 1953, when it became clear that the inflationary threat had passed and that government expenditures were being reduced, the Administration announced that, besides relinquishing the excess profits tax, it would not recommend any postponement of the reduction of individual income taxes scheduled for January 1, 1954.

Early in 1954, when a mild economic contraction was under way, extensive changes in the tax structure were proposed to promote economic growth. The Congress responded by liberalizing depreciation allowances, by extending the period over which business losses could be carried back in computing the income tax, by permitting more liberal treatment of research and development as a current expense, by reducing the double taxation of dividend income, and by lowering excise taxes. In addition, several inequities in the personal income tax were corrected, in line with recommendations. Taken altogether the tax reductions that were carried

CHART 33

Federal Receipts and Expenditures



^{1/} ESTIMATED.

SOURCES: TREASURY DEPARTMENT AND BUREAU OF THE BUDGET.

through during 1954 amounted to 7.4 billion dollars on a full-year basis. Allowing for the increase in social security contributions which became effective January 1, 1954, there was still a saving to individuals and businesses of 6.1 billion dollars. This huge reduction in taxes was a powerful aid in bolstering consumer purchasing power and investment incentives at a time when output and employment were tending to decline.

By the end of 1954, the business hesitation that had prevailed at the beginning of the year largely disappeared. Output, employment, and incomes were again rising impressively, but the Federal budget remained out of balance. In these circumstances, as explained earlier in this Report, it was desirable to postpone the reduction in the corporate income tax and in certain excise taxes that was scheduled for April 1, 1955. Congress adopted the Administration's recommendations, and the timely application of this fiscal restraint contributed materially not only to the balanced budget that is now in prospect, but also to the attainment of prosperity without inflation during the year.

The Treasury's management of the public debt has also been carried out with an eye to the needs of the economy. By skillful planning and timing, its debt operations have been coordinated with monetary and fiscal policies and have helped to reinforce them. Despite variations in economic and financial conditions, the Treasury has made good progress in lengthening its outstanding maturities. Since January 1953, the Treasury's marketable debt running for more than five years has been increased by about 9 billion dollars. Simultaneously, the debt maturing or callable within one year has been reduced by 13 billion. As a result of this readjustment of maturities, the Treasury's operations are less exposed to the hazard of market fluctuations. Its needs in turn are less of a disturbing factor in the money market, thus giving the Federal Reserve System greater freedom in monetary operations.

The broad principles that have successfully guided our fiscal policy in recent years should continue to govern our actions. The demands on the Federal budget are very heavy and some of them—notably, the national security programs—are becoming even larger. In addition, new programs are needed to assist agriculture, to aid school construction, to promote development in scattered urban communities that have been experiencing chronic unemployment, to establish a flood indemnity program, and for other essential purposes. Only a higher level of tax revenues in fiscal year 1957, combined with rigid economies in managing governmental operations, will permit a modest enlargement of essential Federal expenditures within the framework of a balanced budget.

Present tax levels are very high and they impose a heavy burden on individuals and business concerns. But in view of existing economic conditions and present budget estimates, an early reduction of taxes cannot now be justified. To add further to our public debt in order to win for ourselves a reduction in taxes, which in the current state of high prosperity

might chiefly serve to raise prices, would be irresponsible. In times like these we should bend our thoughts to the desirability of debt reduction, and not concentrate exclusively on the desirability of tax reduction. Once a budgetary surplus comes definitely into sight and economic conditions continue to be favorable, we should begin reducing our huge public debt. Such an act of fiscal integrity would signify with unmistakable clarity that our democracy is capable of self-discipline. It would add to the confidence that people need to have in their Government, if they are to plan boldly for their own and their children's economic future.

Two measures are recommended for early action by the Congress. First, the reductions in excises and in the corporate income tax that are now scheduled for April 1, 1956 should be postponed again. Second, legislation allowing a temporary increase in the statutory debt limit should be continued. This legislation is needed because of the seasonal disparities between expenditures and income, the limited cash balances with which Treasury operations are now being conducted, and the small gap between the outstanding debt and the temporary statutory limit of 281 billion dollars.

II. FOSTERING COMPETITIVE ENTERPRISE

One of the basic tenets of this Administration is that competitive markets are a more efficient instrument than governmental directives for organizing production and consumption. Another is that a free and competitive economy promotes industrial versatility, innovation, and investment to a greater degree and with more assurance of continuity than can be attained in an intricately regulated or cartelized economy. These fundamental beliefs are deeply rooted in our Nation's history, and they have been confirmed once again by the experience of the last three years. The relative ease and rapidity with which our economy adjusted to the reduction in military expenditures following the end of the Korean conflict, and the vigorous expansion that ensued in 1955, reflect the creative powers of an enterprise system subject to a minimum of restraints and operating in an atmosphere of confidence. The fostering of competitive enterprise, so heavily stressed in the Employment Act, is and must remain one of the leading objectives of policy.

In considering what government can do to maintain competitive markets, it is well to remember that an open economic system is more an expression of the character and will of a people than the result of any specific acts of government. Yet there are ways in which government can usefully contribute to the strengthening of competitive enterprise.

First, and most important, is the maintenance of monetary, fiscal, and housekeeping policies that promote high and rising levels of economic activity. The rate at which new businesses are established is highest when prospects for profit are favorable. Good times also stimulate business

growth, and this is particularly important for small and medium-sized concerns. The widening of economic opportunities which occurs during prosperity is, therefore, a powerful and pervasive encouragement to independent, competitive endeavor. This is illustrated by the experience of the first six months in 1955, when new business formations were 11 percent above the first six months of 1954, while business discontinuances were 7 percent below. The net increase in the business population was 45,000, compared with 11,000 in 1954 and 27,000 in 1953. When the economy is contracting, the shrinking of markets may temporarily intensify business rivalries, but their longer-range effect is to discourage enterprise. The will, no less than the capacity, to compete is weakened by declining business and its harvest of disappointments. Thus, good times do much to strengthen competition; in turn, strong competitive markets are a major force in generating prosperity and distributing its fruits widely.

Second, government can strengthen competitive markets by helping small and medium-sized businesses overcome impediments to their expansion. In our modern economy, with its heavy capital requirements, high taxes, and emphasis on national markets, small concerns are subject to serious handicaps in many lines of endeavor. Yet the continuance of small and medium-sized businesses, and their ability to prosper and grow, are vital to the Nation's welfare. As stated in last year's Economic Report, "our economy is strong and progressive because it contains, in addition to its five million farm enterprises, four million independent centers of business decision—each potentially free to experiment with new ideas, new men, new methods, and new products." When the Government helps smaller concerns to overcome some of the hindrances to their growth, it is acting in the interests of the whole economy.

The Government is now aiding small businesses in numerous ways. The Small Business Administration, which was established to assist them, makes loans—whenever possible in participation with private lenders—for periods that are usually longer than those commonly available from private lending agencies. It provides counsel on technical processes, managerial problems, and new product lines, and helps to channel government contracts to small enterprises. During 1955 significant improvements were made in procurement procedures, so that a larger portion of Federal contracts may go to these enterprises. The maximum size of loans by the Small Business Administration was also raised last year.

Other governmental programs are helpful to small business firms. The Office of Technical Services in the Department of Commerce disseminates information derived from government and government-sponsored research. It also publishes lists and abstracts of government-owned patents, currently exceeding 5,000 in number, which are available for license on a nonexclusive, royalty-free basis. Several other units in the Department of Commerce provide technical, managerial, marketing, and other aids. While these programs are helpful to the business community generally, they are of special

advantage to small firms, which cannot hire the services of technical, managerial, and financial experts as readily as the larger firms.

The maintenance of healthy, competitive markets requires that Federal policies for promoting economic expansion and for aiding small and medium-sized businesses be supplemented by vigorous measures for preventing monopolistic practices and combinations. One of the clearest lessons of business history is that tendencies toward monopoly are always present in some degree and that constant vigilance is needed to assure ascendancy of competitive conditions. Strict enforcement of the antitrust laws is our primary weapon for thwarting any impairment of competition. In the summer of 1953, the Attorney General appointed a National Committee to Study the Antitrust Laws, composed of leading experts on the subject. The Report of this Committee has served most usefully as a basis for study of needed legislative changes. Two of last year's enactments embody revisions paralleling those suggested by the Committee's Report. One raised maximum penalties under the Sherman Act from \$5,000 to \$50,000; the other gave the Federal Government the right to sue for damages sustained by it as a result of antitrust violations. Further improvements in the antitrust laws are likely to draw heavily on the results of the Committee's deliberations.

Meanwhile, the Department of Justice and the Federal Trade Commission are vigorously enforcing these laws. In 1955 the number of proceedings instituted against corporate mergers was larger than in all previous years since 1950, when the antimerger amendment to the Clayton Act was passed. During the year numerous legal actions against price-fixing and market-sharing practices were successfully carried out. Various orders were issued, prohibiting price discriminations that were unfairly injurious to small competitors. Orders against the practice of exclusive dealing served to open to smaller manufacturers distribution outlets previously closed by dominant competitors. Also, numerous suits dissolving group boycotts helped to keep the channels of trade open to independent entry and action.

Nevertheless, mergers have become more numerous of late and an eye, at once vigilant and discriminating, must be kept on such developments. Many mergers have a solid economic justification and serve the general interest by increasing competition; others have neutral effects; while still others place obstacles in the path of effective competition. Over the years Americans have wisely viewed excessive business concentration, or any other undue concentration of economic power, with uneasiness. To serve the basic American desire for an economy in which business opportunities are increasing and in which economic control is widely diffused, it is desirable to strengthen our antitrust laws and provide larger appropriations for their enforcement.

Toward this end, the following revisions of antitrust legislation are recommended. First, all firms of significant size that are engaging in interstate commerce and plan to merge should be required to give advance

notice of the proposed merger to the antitrust agencies, and to supply the information needed to assess its probable impact on competition. Second, Federal regulation should be extended to all mergers of banking institutions. Combined with the requirement for advance notice, this extension of the law would give the Government an opportunity to prevent mergers that are likely to result in undue restraint of banking competition. Third, Federal approval should be required for the acquisition of banks by holding companies. Fourth, the Clayton Act should be amended to make explicit the Federal Government's authority to take action in merger transactions in which either party is engaged in interstate commerce. Fifth, it should also be amended so as to make the cease-and-desist orders of the Federal Trade Commission final when issued, unless appealed to the Courts. Sixth, when civil rather than criminal proceedings are contemplated, the Attorney General should be empowered to issue a civil investigative demand, compelling the production of documents before the filing of a complaint, and without having to invoke grand jury proceedings.

Finally, the Congress should give serious study to the Report of the Presidential Advisory Committee on Transport Policy and Organization. A fundamental premise of that Report is that the railroad industry no longer has the monopoly power that it had toward the end of the nineteenth century, when the Interstate Commerce Act was passed, but instead largely operates under competitive conditions. The central proposals of the Report therefore seek to diminish the detailed administrative regulations that have grown up over the years, and to give common carriers greater freedom to compete. The time is surely ripe for a re-examination of the intricate regulations of the transportation industry, with a view to opening up the industry to more freely competitive effort. But in framing any legislation, it will be necessary to retain adequate safeguards of the interests of the shipping public and competing carriers.

III. EXTENDING HOME OWNERSHIP AND IMPROVING NEIGHBORHOODS

Additions to the Nation's stock of housing are required by the growth of population, changes in its makeup, migration from rural to urban areas, and gradual deterioration of older homes and apartments. The main-spring of recent residential construction, however, has been the desire for home ownership and the demand for better homes and neighborhoods as essential elements in the higher levels of living that people seek to attain. Progress in these directions has been significantly aided by the Federal Government as well as the States and localities, but it has depended primarily—as it should—on decisions and actions by individual citizens, the building industry, and private financial institutions.

The main objectives of the Administration's housing policies have been to facilitate home ownership, to promote a high and reasonably stable rate of home building, and to improve the quality of existing homes and neighborhoods. These objectives have been carried out through many

instrumentalities, the most important being the program of mortgage loan insurance by the Federal Housing Administration (FHA), the program of mortgage loan guaranty by the Veterans Administration (VA), and programs for slum clearance and urban renewal. In developing these Federal activities the fullest cooperation has been sought of private interests and local governments.

More and better housing is essential to raising the levels of family living. Also, the manner in which home construction and improvement is achieved and the rate at which these activities proceed have a vital bearing on the prosperity and stability of the entire economy. The results of recent experience are gratifying. They appear in the high rate at which new homes have been built, in the spread of home ownership, in the improvement of urban neighborhoods, and in the general avoidance of housing surpluses which can only bring trouble to the building industry and the economy at large.

In the past three years more than 3½ million nonfarm housing units have been built. They embody high standards of comfort, commodiousness, and suitability for healthy, safe, and convenient living. About 50 percent of the new housing units were built under FHA and VA programs. Total expenditures on new home construction, even in terms of constant dollars, have far exceeded those of any earlier three-year period. This achievement of the home building and financing industries gives dramatic proof of what can be accomplished through private enterprise and with private capital.

The spread of home ownership has been likewise remarkable. Before World War II, the percentage of nonfarm dwelling units occupied by the owner reached 46 in 1930 and fell to 41 in 1940. After the war the percentage rose to 53 in 1950 and is now 57 or higher. This achievement is probably unique among highly urbanized, industrial nations. Widespread home ownership yields prized benefits to individual families. It also encourages active interest in civic affairs and pride in community development. A nation in which so many millions of families have growing investments in their homes and neighborhoods is likely to be governed by a high sense of responsibility.

Results are also beginning to be realized from the measures taken to encourage home improvements and to rehabilitate parts of our cities and towns that had been allowed to degenerate into slums or near-slums. The Housing Act of 1954, following a recommendation by the President's Advisory Committee on Housing, initiated an urban renewal program under which Federal grants are made to cities and towns for the conservation and rehabilitation of neighborhoods, as well as for slum clearance projects provided under earlier laws. The Federal Government also offers grants to small communities and to metropolitan areas and regions for urban planning. These moves are bearing fruit. Toward the end of 1955, more than 200 urban renewal projects in 165 locations had been approved for final plan-

ning or execution. They will ultimately provide new housing for 70,000 families. City blocks cleared of slums, and construction projects on previously blighted sites, are visible in an increasing number of places.

Also important for the future, as well as for the recent past, are the steps taken in 1954 to make Federal programs for the insurance of housing loans more effective. FHA terms for mortgage insurance on existing properties were liberalized to facilitate the movement of families to better accommodations. Insurance of mortgages on properties in urban renewal areas was permitted in order to hasten redevelopment. The maximum insurable mortgage amounts for owner-occupied, rental, and cooperative housing, which had remained unchanged for years, were finally brought into adjustment with postwar building costs. Funds for home improvement were made more readily available by permitting FHA to insure supplementary loans under an open-end mortgage. Consumer protection was improved by requiring builders who do their financing with Federally underwritten mortgages to deliver warranties to home purchasers. Malpractices under the FHA home repair and modernization program were brought under control by limiting the eligibility for loan insurance to improvements that add to the basic utility of homes, and by requiring lenders to assume 10 percent of any loss on insured loans.

Of late, considerable effort has also been devoted to encouraging the use of private capital where public funds would otherwise be required. A new charter was drawn for the Federal National Mortgage Association (FNMA), which provides for the eventual retirement of its government capital. Steps were taken to restrict the use of FNMA as a primary source of mortgage funds, although its authority to assist special housing programs was continued. A Voluntary Home Mortgage Credit Program was established under the auspices of the Housing and Home Finance Agency. Through this program the flow of private mortgage funds into remote areas and to minority groups is being augmented.

While further progress in promoting extension of home ownership and improvement of urban communities can be expected of existing governmental programs, their effectiveness would be enhanced by certain legislative changes. First, as proposed earlier in this Report, the mortgage insurance program should be amended in the interest of increasing the availability of adequate housing for older persons. Second, in order to serve more effectively the objectives of urban renewal, any community that seeks Federal assistance for public housing should be required to adopt a workable program for the prevention and elimination of slums. To further the same objectives, a public housing program of 35,000 dwelling units for each of the next two years should be authorized. Third, in order to facilitate home improvements, the permissible size of insured repair and modernization loans, which has remained unchanged on the statute books despite the great rise in building costs during the past fifteen years, should be increased. This insurance program has proved very useful in promoting home im-

provements; it is now safeguarded against abuse and should be given permanent status. Finally, the authorization of home mortgage insurance by FHA should be increased and put on a more permanent basis.

IV. ENLARGING PUBLIC ASSETS

All levels of government share a responsibility for providing the public improvements on which the general welfare and the growth of the private economy heavily depend. In projects which clearly involve the national interest and are beyond the economic competence of local bodies, the Federal Government must play a key role. But its part in these essential programs must be performed so as to encourage rather than displace the necessary efforts of State and local agencies.

Public construction has risen sharply since the end of World War II and has been proceeding at a brisk pace in the last few years. When military, atomic energy, and other industrial components of public construction are excluded and adjustments are made for price changes, it appears that the volume of public construction in 1953-55 surpassed any earlier three-year period. New public construction amounted to about 35 billion dollars in these years, with about two-thirds of this total accounted for by State and local governments.

But a great backlog of necessary public works remains. This is largely the consequence of heavy expenditures for our national security during and since World War II, coupled with unexpected population gains. Outlays for public construction during the next few years should be large enough to contribute decisively toward removing this backlog, replacing obsolete facilities, and providing for normal growth. The stock of public facilities must be increased, so that it will be commensurate with the growth of private wealth and the improvement in the level of living of a rapidly increasing population. Deficiencies in essential public works can seriously restrict economic progress. It would be shortsighted to subject our economy to such a hazard.

Among the deficiencies, none is more important for the Nation's future than the shortage of school classrooms, which accumulated partly during the years of depression and war, when school construction was severely curtailed, and partly in the early postwar period, when it failed to keep pace with the growth of the school-age population. In the last few years expenditures on school construction have risen encouragingly, and building is currently proceeding at the record rate of 67,000 schoolrooms per year. However, even at this rate of construction it would take many years to remove the backlog, which is estimated at over 200,000 rooms, since the greater part of the new construction must provide for growth and replacements.

The provision of school buildings has been traditionally a State and local function. It is highly desirable that it remain just that. At the

same time, it has become clear that in the absence of Federal aid, the existing shortage of schoolrooms will long continue in many communities, to the detriment of the entire Nation. If the critical shortage that now exists is to be largely corrected over the next few years, Federal assistance is essential. This conclusion has been reached by many students of school problems, and it has recently been endorsed by the White House Conference on Education, which reflected the results of serious deliberation in earlier meetings of citizens throughout the land. In view of existing needs and circumstances, the Congress is urged to authorize a program of Federal aid for school construction which, over a five-year period, could be expected to stimulate the States and localities to sufficiently greater efforts to remove the accumulated shortage. Specifically, the Congress is requested to authorize Federal matching grants to the States, to be used in districts that are themselves unable to provide urgently needed public school facilities. Loans should also be made available to facilitate school financing, in a manner and under conditions that are set out in the special Message of January 12, 1956. At the end of five years, when it may be expected that school facilities will again be adequate, Federal aid can and should terminate.

Other shortages of educational plant exist at the present time. In particular, there are grave inadequacies in our facilities for medical research and for training the large number of physicians, dentists, and health scientists required by our rapidly growing population. Since private benefactions cannot fully fill the gap, it is recommended that the Congress authorize a five-year program of Federal construction grants to assist medical and dental schools to improve their physical facilities for research and teaching. Also, the Federal loan program for college housing should be continued, but on a basis that will bring forth the large volume of private funds that is necessary to meet growing requirements.

The construction of hospital and related facilities has been substantially augmented in recent years, in part because it has been bolstered by 700 million dollars of Federal grants. These have been made under the Hospital and Medical Facilities Survey and Construction Program, which provides matching grants to the States for the construction of hospitals and related health facilities. This program is being administered with close attention to the needs of low-income groups and rural areas. The Congress is requested to extend the program for an additional two years. Federal insurance of mortgage loans for the construction or improvement of private health facilities is again recommended.

The importance of completely modernizing the Interstate Highway System, which links together the principal cities by 40,000 miles of road, is so clear and so widely recognized that it requires no elaboration in this Report. The country urgently needs an integrated network of safe, controlled-access highways to relieve existing congestion and to provide for the expected growth of motor vehicle traffic. A modernized interstate

system would also help to strengthen the Nation's defenses and to reduce the toll of human life exacted each year in highway accidents. The Congress is again urged to consider and to provide for the full modernization of the Interstate Highway System. It was suggested last year that this vast road program be financed by an independent authority created by the Congress, and that interest and amortization on the highway debt be paid out of the excess—which may be expected to increase—of Federal revenues from present gasoline and lubricating oil taxes over current Federal grants-in-aid for roads. If this financing plan is not satisfactory to the Congress, a sound alternative not involving budget deficits should be devised. Since the need for improved highway facilities is becoming more and more pressing, the whole interstate system should be authorized as one project, to be completed in about ten years.

By the nature of the projects involved, the Federal Government must play a key role in the conservation and development of water resources. In 1953-55, over 2 billion dollars of Federal funds were expended for the construction of facilities of this type. Recent legislative and administrative actions have strengthened both public and private activities in the sphere of water resource conservation and development. The St. Lawrence Seaway was authorized in 1954, after many years of discussion. In the same year, the conservation of soil and water resources was advanced by allowing outlays made by farmers on water projects to be treated as a current expense for tax purposes, by expanding the provision of governmental loans for such projects, and by establishing a cooperative program with State and local agencies for the construction of small dams and related works. The Report of the President's Advisory Committee on Water Resources Policy has recently been transmitted to the Congress. This report sets forth a comprehensive policy for the conservation and development of the Nation's water resources. It stresses the need for greater uniformity in the evaluation of projects, their authorization, and their cost-sharing provisions, as well as close and continuous collaboration with local groups. In due course, legislative proposals will be submitted to implement the recommendations of this Committee.

In the conservation and development of water resources, including power, the Federal Government should continue to advance the partnership principle, as exemplified by projects such as John Day, Markham Ferry, and Cougar. It should continue to encourage leadership from local sources, whether private or public, and assume an active role only where it has some particular competence—that is, where the projects are especially complex or large, where interstate conflicts are involved, or where there is a clear impact on the national interest. The Upper Colorado River project, which is vital to several States and which involves generation of power, irrigation, municipal water supply, flood control, and other functions, is an outstanding example of the type of project that the Federal Government

should undertake. Recommendations concerning this project and other needed developments of water resources are presented in the Budget Message.

The increasing scarcity of water makes it mandatory that its waste be prevented. Pollution of streams and lakes is a flagrant example of waste. Hence, the extension and strengthening of the Water Pollution Control Act are again urged.

Expenditures on atomic energy construction have in recent years accounted for a significant part of total Federal construction expenditures. In 1953-55 they amounted to 2.7 billion dollars. They are now tapering off with the completion of important projects. Private investment, while still modest, is being accelerated under the stimulus of the Atomic Energy Act of 1954. In the spirit of this law, the Atomic Energy Commission has given technical and financial assistance to development of private atomic power plants, has invited private participation in the supplying of atomic energy materials and services, has provided access to technical information, and has released its patents without royalty. This cooperation of government and industry is bringing the goal of competitively priced atomic electric power closer to realization.

The limitation of Federal efforts to their proper sphere in the construction of public assets will require the States and localities to continue assuming heavy responsibilities for public works. There can be little doubt that the great majority of them have both the economic and financial capability of doing so. In some cases, however, State constitutions or State and local statutes which currently restrict borrowing may need to be revised. Smaller communities seeking to raise capital for public improvements would also be aided by a revision of the Federal tax laws, such as was recommended last year, to allow a regulated investment company, holding the bulk of its assets in the form of tax-exempt securities, to pass through to its shareholders the tax-exempt status of the income received on such securities.

V. IMPROVING SKILLS AND TECHNOLOGY

The swift pace of scientific knowledge brings both new opportunities and new responsibilities. What we as a people do, or fail to do, to improve skills, to train specialists in the sciences and in engineering and other applied fields, and to add to scientific and technical knowledge will have a vital bearing on our national security and on the level of living of future generations.

The problem of improving skills and building new knowledge has several aspects. The provision of adequate physical facilities for training and research is one of them. Progress in this direction is being made by the present high rate of construction of facilities and will be hastened by the Federal programs that have been recommended above. Another basic aspect of the problem—adding to the supply of trained personnel to staff

the physical facilities—presents greater difficulties. As pointed out in a special Message to the Congress in February 1955, the shortage of teachers, while less obvious than the shortage of classrooms, is the more serious. Shortages of personnel exist also in various branches of scientific research and development and in numerous technical specialties.

Primary responsibility for meeting the critical shortage of teachers rests with educational institutions, the States, and local communities. All practicable steps should be taken by them to attract suitably trained individuals to the teaching profession. In this connection, special attention should be given to the need for better high school instruction in science and mathematics. The supply of scientific and engineering manpower, so vital to our military security and future prosperity, depends to a large degree on the availability and quality of such instruction. Physics and chemistry are not taught at all in many high schools, and in many others the teaching of these subjects is seriously deficient. The experimental program of supplementary training for teachers in science, mathematics, and engineering, which the National Science Foundation has under way, should help to raise the quality of instruction in these subjects. An enlarged appropriation for this purpose is needed.

Private and public institutions of higher learning are the means through which we must overcome the shortages of personnel in engineering, medicine, scientific research, and other areas. The newly recommended program for adding to the physical facilities for research and training in medicine and dentistry, which has already been noted, will help to meet certain of these needs. Other activities of the Federal Government to encourage higher education should also be strengthened, notably the program of research grants and graduate fellowships administered by the National Science Foundation, the program of research and training supported by the Atomic Energy Commission, and the various programs of the Department of Health, Education, and Welfare for training nurses, for medical research, and for research on air and water pollution.

These programs, important as they are, should not obscure the need for balanced expansion of our liberal arts colleges, universities, and technical institutes. The increased need for advanced training and the prospective growth of student enrollments pose difficult and far-reaching problems, which should be thoroughly explored by the Office of Education together with private and public institutions of higher learning. A distinguished group of educators and citizens will soon be appointed to consider, through study and conferences, the immediate and long-range efforts which must be made to reach appropriate solutions to the problems facing our colleges and universities.

The future improvement of our level of living, no less than our military security, is heavily dependent on research in the basic sciences and technology. Our willingness to invest huge sums for this purpose is one of the outstanding reasons for the pre-eminence of American science and industry.

extend employment in new directions, increase its amount, and add abundantly to its fruits. Although adjustments for some individuals are made necessary by technological changes, they can usually be carried out with little difficulty when the oscillations of the business cycle are kept under reasonably good control. The need of a strong system of unemployment insurance to ease personal adjustments is stressed later in this Report.

VI. PROMOTING THE INTERNATIONAL FLOW OF GOODS AND CAPITAL

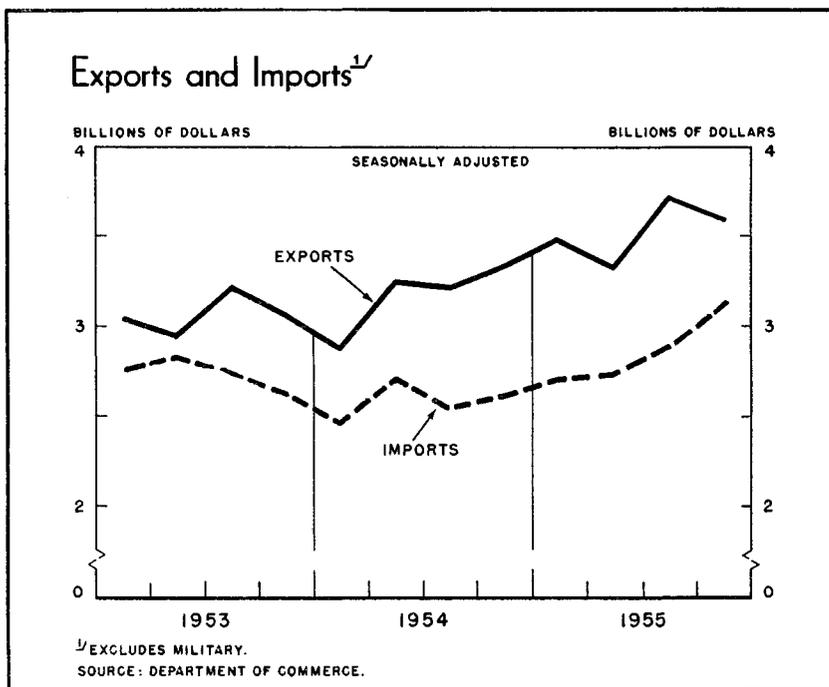
The orderly growth of our economy exerts a strongly favorable influence throughout the world. In turn, economic developments abroad are of profound importance to us. Recent experience illustrates this interdependence. By 1953 the nations of the Free World had achieved sufficient economic strength to be able to absorb the adverse reactions from the mild contraction that got under way in the United States that year. Not only that, but they continued buying from us on a scale that helped to check our economic decline and to speed renewed expansion. In turn, the resumed rise of our imports toward the end of 1954, reinforced by a heavy outflow of private capital, helped to sustain economic expansion in other parts of the Free World and thereby stimulated further expansion in our own exports during the past year.

It is clear that our long-term interests are well served by expansion of the international flow of goods, capital, enterprise, and technology. Sound policies to promote these ends will powerfully advance our national security and economic welfare, and help to build a stronger and more unified community of free nations.

Current restrictions on the flow of goods and capital hamper enterprise and limit the real income of consumers both here and abroad. Despite the progress in trade liberalization achieved in recent years, restrictions are still numerous and widespread. Reduction of these barriers requires both direct action on our part and cooperation with other nations. Our proper and necessary course was outlined in a special Message of March 1954, following the report of the Commission on Foreign Economic Policy. The Congress responded with important legislation in 1954 and 1955, but additional action is urgently needed.

The Trade Agreements Extension Act of 1955 has continued for another three years, with certain modifications, the authority initially granted in 1934 by the Reciprocal Trade Agreements Act. The 1955 Act grants new powers to the President to lower tariffs on a reciprocal and selective basis. Individual tariff rates may be reduced by 5 percent per year for three years, and rates that are in excess of 50 percent ad valorem may be reduced by annual stages to that level. Experience has shown that the "escape clause" and "peril point" provisions of the Act, which are designed to protect domestic industries against serious injury from duty reductions, are broadly

CHART 35



consistent with our basic policy of trade liberalization. Experience has also shown that efforts to expand world trade are most effective when tariff reductions are negotiated on a reciprocal, multilateral basis. Under the authority of the Trade Agreements Act, selective reductions in tariffs on thousands of items have been made during the past twenty years, and they have helped materially to enlarge our exports as well as imports. The 1955 Act has paved the way for a new series of tariff negotiations, which opened at Geneva on January 18, 1956.

The chief instrument through which the United States has for eight years cooperated with other countries of the Free World in reducing trade barriers is the General Agreement on Tariffs and Trade (GATT). Negotiations under the GATT are more effective than bilateral negotiations. They have won for us tariff concessions on items accounting for about 50 percent of the value of our exports. Moreover, through consultations with other GATT members, we have secured the abolition of discriminatory restrictions on our exports of such important items as coal, apples, cigarettes, lumber, potatoes, textiles, automobiles, tobacco, petroleum, wool, and motion pictures. Several European countries have removed all discriminatory restrictions against dollar trade.

To correct certain shortcomings in the working rules and administrative machinery of GATT, which have been recognized for some time, the 34

GATT members completed in March 1955 a revision of the basic Agreement and proposed an administrative agency—the Organization for Trade Cooperation (OTC). Membership in the OTC would enlarge the advantages the United States already enjoys under the GATT. It would also give assurance to the rest of the Free World of our continuing interest in expanding the international flow of goods and capital. Early passage of legislation authorizing our membership in the Organization for Trade Cooperation is of high importance.

Customs regulations are capable of creating barriers to international trade, no less serious than the customs duties themselves. Delays and inconvenience arising from customs regulations have been reduced in the past two years, and the Treasury Department is continuing to review its procedures with a view to simplifying them. Congressional action, however, is needed to facilitate further progress. The basic purpose of the Customs Simplification Bill of 1955, which the House passed in the first session of the 84th Congress, is to diminish uncertainties and delays by simplifying the present system of customs valuation. Modifications of this bill have been suggested to avoid unintended reductions in individual duties that would result from the proposed change in valuation procedures. Early enactment of such a suitably revised bill will constitute a significant advance in our foreign economic policy.

The need for simplifying our tariff rate structure, which the Commission on Foreign Economic Policy had emphasized, was recognized by the Congress in the Customs Simplification Acts of 1953 and 1954. As directed by the latter Act, the Tariff Commission is studying present commodity classifications and rate structures. Legislation will be needed in due course to authorize revisions of our tariff classification schedules. In the meantime, other restraints on international commerce, those arising under the Buy-American Act of 1933, were modified by an Executive Order of December 1954, which has resulted in the removal of a great deal of uncertainty for foreign bidders who seek government contracts.

The field of foreign investment also offers opportunities to encourage economic activity and trade on a world scale. A larger outflow of American capital would benefit both ourselves and other economies. By helping to develop the resources of friendly countries, it would enlarge and diversify the supply of materials on which we can draw. At the same time, it would enable less developed countries to achieve higher rates of economic growth and to become more active partners in the trade of the Free World. To the greatest extent possible, the funds for foreign investment should come from private sources. When private capital moves abroad, it is often accompanied by the export of technical, managerial, and financial skills. Such benefits cannot be realized as effectively through government loans.

It is highly desirable, as stressed in last year's Economic Report, that we "encourage investment in all countries whose desire to speed their economic development has led them to create a hospitable climate for business invest-

ment.” The recommendations made in that Report, with respect to the taxation of corporate income from foreign sources, have not yet been acted on by the Congress. Legislation on these proposals, which can have a significant influence on foreign investment, is again requested. Also, the lending authority of the Export-Import Bank should be extended beyond June 30, 1958. This would enable the Bank—which has actively encouraged the outflow of private capital by its loan participation, credit guarantees, and loan supplements to private venture capital—to finance projects that call for advances over a period longer than two years.

The United States has recently taken steps to participate in the International Finance Corporation (IFC), which is to be affiliated with the International Bank for Reconstruction and Development. The IFC will begin operations as soon as at least 30 countries, out of the 44 member countries of the Bank that have indicated an intention to join, have together subscribed 75 million dollars. The IFC will make loans to supplement venture capital going into productive private enterprises abroad, particularly in the less developed areas of the world, and it will also help to find experienced management where needed. The new institution is expected to expand investment abroad by its own lending and also by helping to create an investment climate in foreign countries that will be more attractive to their own citizens as well as those of other nations.

The rate of economic progress is bound to play a vital role in the struggle between the principles of freedom and those of regimentation in the poorer and less developed areas of the Free World. Our economic development and technical cooperation programs for raising living standards in these areas are proving helpful and should be moderately expanded, with special emphasis on activities that encourage local private enterprise and the inflow of private capital from abroad. The Mutual Security Program, of which these economic programs are a part, must be continued. High though our expenditures on national security are, they would be vastly higher if we did not have strong allies.

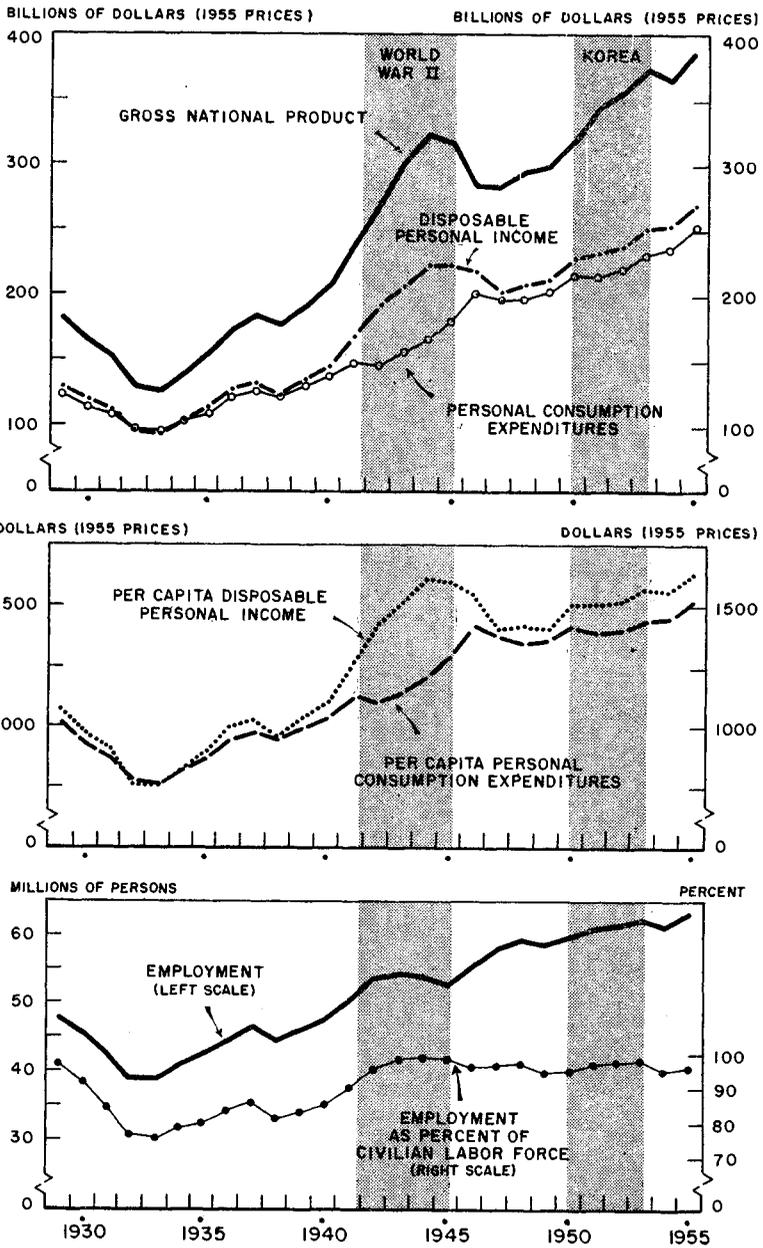
The United States can take pride in the progress that has been achieved in cooperation with other countries in enlarging the mutually advantageous flow of goods, capital, technology, and enterprise within the Free World community. Continuance of this trend will build an international environment that is increasingly favorable to the maintenance of peace and the extension of prosperity.

VII. INCREASING THE STABILITY OF OUR EXPANDING ECONOMY

Economic improvement, whether by our own actions or in cooperation with other nations of the Free World, is always subject to the risk of interruption by business fluctuations. The mere fact that they have been kept under good control in recent years is not an adequate basis for concluding that the business cycle has been ironed out, or that we need be concerned no longer about the possibility of running into a sizable recession or inflation. The

CHART 36

Indicators of Prosperity



SOURCES: DEPARTMENT OF COMMERCE AND COUNCIL OF ECONOMIC ADVISERS.

need for poise and foresight on the part of business, labor, and government is undiminished. As we build for the Nation's future prosperity, we must strive to promote not only a well-balanced growth of the economy, but also a relatively stable rate of growth. Although our defenses against recession and inflation are much stronger than a generation ago, we should try to make them still stronger.

By helping to maintain buying power at a time when payrolls diminish, our Federal-State Unemployment Insurance System constitutes a first line of defense against a possible recession. Remarkable advances in this insurance system have been achieved during the past two years. In 1954 its coverage was broadened by the Congress to include civilian employees of the Federal Government and the employees of many small firms. Uninterrupted payment of benefits by States whose reserve funds become low was practically assured by the establishment of a special Federal loan fund. Steps were taken to equalize the tax impact of the System on new and old firms, thereby removing a barrier to the establishment and early growth of new enterprises. These Federal actions have been supplemented by the States. In these two years, 33 States, besides the District of Columbia, raised the amounts that may be paid weekly to unemployed men and women covered by the insurance system. Eight States and the District of Columbia lengthened the duration of the period for which unemployment benefits may be paid, and four States extended coverage to firms with fewer employees than the minimum set by Federal law.

Taken together, these changes represent the greatest improvement in the Unemployment Insurance System since its inception. Nevertheless, there is need for further progress. The last two Economic Reports have suggested that the States increase benefits so that the great majority of covered workers will be eligible for payments that at least equal half their regular earnings; that the States which have not yet done so, lengthen the term of benefits to 26 weeks for every person who qualifies for any benefit and remains unemployed that long; that employees of State and local governments be given the protection of unemployment insurance; and that employees of very small firms, which are still excluded from the unemployment insurance system in many States, be accorded this protection. Although very encouraging strides have recently been made toward these goals, they have not yet been realized. The States are again urged to persevere in the task of improvement, so that the stabilizing influence of the Unemployment Insurance System on personal incomes may be enhanced.

To promote stable economic growth, it would also be desirable to increase the influence that the Federal Government can exercise on consumer credit. The development of consumer instalment financing has been, on the whole, highly beneficial to our economy. By its means the homes of many millions of American families have been enriched on a scale that would otherwise have proved impossible. The soundness of this type of credit has been repeatedly tested and found excellent. Nevertheless, instalment credit

sometimes accentuates swings in the buying of automobiles, furniture, television sets, and other consumer durables, thereby exposing the rest of the economy to the hazard of widened fluctuations. In view of the increasing importance of the durable consumer goods industries in our economy and their marked tendency to fluctuate, consideration should be given to restoring the Government's power to regulate the terms of consumer instalment credit.

The Board of Governors of the Federal Reserve System regulated the terms of consumer credit during 1941-47 and again in 1948-49 under an Executive Order of the President. The Defense Production Act provided temporary authority to reinstate these controls in 1950, but this power was withdrawn by the amendments to that Act approved June 30, 1952. Experience during the recent past suggests that the authority to set, if and as circumstances may require, minimum downpayments and maximum maturities on instalment credit for the purchase of consumer durables would be a useful adjunct to other stabilizing measures. Its availability as a stand-by measure, to be used only when the economic situation demands it and under proper administrative safeguards, would increase the Government's ability to fulfill its responsibilities under the Employment Act. Although present conditions do not call for the use of such authority to regulate the terms of instalment credit, this is a good time for the Congress and the Executive Branch to study the problem.

The authority of the Federal Government to influence the use of credit in the purchase or improvement of homes is already fairly broad, but it would be useful to extend it in two directions. First, greater flexibility should be introduced in the terms on which the secondary market facilities of the Federal National Mortgage Association (FNMA) can be used by the home building and home financing industries. At the present time, mortgages may be sold to FNMA under its secondary market program only on the condition that the seller acquire the Association's stock in an amount equal to at least 3 percent of the value of the mortgages sold. The Board of Directors of FNMA should be authorized to set this stock purchase requirement at or above 1 percent, on the basis of conditions in the housing market and in the economy generally. By reducing the permissible stock purchase requirement, the liquidity provided by FNMA to the home mortgage market could be more effectively increased, if the economic situation required it.

Second, the National Housing Act should be amended to allow the Federal Housing Administration to insure home repair and modernization loans with maturities as long as 5 years. The maximum maturity for insured loans of this type is now 3 years, having been at this level since the 1930's. An extension of the maximum limit to 5 years, with discretion granted to the Federal Housing Commissioner to vary the maximum maturity in the light of economic conditions, would permit a liberalization of terms if and when some stimulation of the construction industry becomes desirable.

The introduction in 1934 of insurance for bank deposits and for share accounts in savings and loan associations has greatly strengthened the capacity of our economy to resist possible cumulative effects of any recessionary development. The extension of insurance to the share accounts of credit unions would be a useful step in the same direction. These cooperative institutions have been growing rapidly. By mid-1955 over 7.5 million people had about 2.5 billion dollars invested in credit union shares. The loss of any appreciable part of these savings would work severe hardships on individuals of limited means. As suggested in last year's Economic Report, the Congress should consider the desirability of establishing a self-supporting Federal program of share-account insurance for credit unions. If such a system were established, it would be essential to maintain the proper safeguards, limitations, and supervision that go with an insurance system.

Finally, as has long been recognized, the adjustment of public works expenditure can be helpful in achieving a stable rate of economic growth. For this reason the Administration began concerning itself with the systematic planning of public works early in 1953. For a time this activity was centered in the Council of Economic Advisers. Later, to give the planning work added emphasis and to enlarge its scope, a unit was established in the White House Office under a Special Assistant to the President to coordinate public works planning. The inventory of the status of Federal plans for public works, which was initiated nearly three years ago, is now maintained on an annual basis. A survey of the status of State and local plans for public works has been completed, and it is expected that similar surveys will be made biennially. Recognizing the need for a reserve of "ready-to-go" projects, the Congress last year increased the provision for interest-free loans to States and municipalities for public works planning. Still another forward step would be taken if both the Executive agencies and the Congress became accustomed, in connection with every bill on public construction, to consider the possible need for flexibility in public works programming.

VIII. THE CREATIVE POWER OF A FREE ECONOMY

The broad purpose of the recommendations in the foregoing sections of this Report has been to develop, in the language of the Employment Act, "national economic policies to foster and promote free competitive enterprise, to avoid economic fluctuations or to diminish the effects thereof," and "to promote maximum employment, production, and purchasing power." These recommendations largely concern the activities and policies of the Federal Government. But important as these activities and policies are, we must never lose sight of the fundamental truth expressed at the beginning of this chapter, namely, that the lasting prosperity of our Nation depends far more on what individuals do for themselves than on what the Federal Government does or can do for them.

When many millions of men and women bring about general economic improvement largely through their own actions, they do more than create prosperity in their day. They also strengthen the moral roots of the industry, the enterprise, and the resourcefulness from which still greater prosperity and well-being will spring in the future. That is the basic reason why a Nation that enjoys a high degree of economic freedom typically generates its own growth, why it keeps creating new technologies, new products, new markets, new enterprises, new jobs, larger incomes, and better living. That is why we are still in the midst of a technological revolution in agriculture, communications, and power, of which there was only a glimmer a generation ago. That is why we may look forward with confidence to the continued growth of our economy.

Foresight has helped our Nation make great strides in recent years toward a balanced and sustained prosperity. We have succeeded in expanding the scope of free enterprise, and yet increased the sense of security that people need in a highly industrialized age. Great opportunities for economic progress lie ahead. The recommendations of this Report will prove helpful to the American people in pursuing them.