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TREASURY DEPARTMENT

UNITED STATES SAVINGS BONDS ISSUED AND REDEEMED THROUGH November 30, 1967
(Dollar amounts in millions - rounded and will not necessarily add to totals)

DESCRIPTION	AMOUNT ISSUED ^{1/}	AMOUNT REDEEMED ^{1/}	AMOUNT OUTSTANDING ^{2/}	% OUTSTANDING OF AMOUNT ISSUED
MATURED				
Series A-1935 thru D-1941 _____	5,003	4,995	8	.16
Series F and G-1941 thru 1952 _____	29,521	29,470	51	.17
Series J and K-1952 thru 1954 _____	2,236	2,216	20	.89
UNMATURED				
Series E ^{3/} :				
1941 _____	1,867	1,633	234	12.53
1942 _____	8,246	7,231	1,014	12.30
1943 _____	13,272	11,670	1,602	12.07
1944 _____	15,473	13,509	1,964	12.69
1945 _____	12,153	10,419	1,734	14.27
1946 _____	5,498	4,522	976	17.75
1947 _____	5,206	4,112	1,093	21.00
1948 _____	5,372	4,143	1,230	22.90
1949 _____	5,298	4,013	1,284	24.24
1950 _____	4,631	3,452	1,179	25.46
1951 _____	4,008	2,988	1,020	25.45
1952 _____	4,199	3,101	1,098	26.15
1953 _____	4,793	3,440	1,353	28.23
1954 _____	4,882	3,419	1,462	29.95
1955 _____	5,083	3,485	1,599	31.46
1956 _____	4,902	3,302	1,600	32.64
1957 _____	4,610	3,004	1,606	34.84
1958 _____	4,481	2,756	1,725	38.50
1959 _____	4,192	2,524	1,668	39.79
1960 _____	4,193	2,402	1,791	42.71
1961 _____	4,220	2,290	1,930	45.73
1962 _____	4,065	2,143	1,922	47.28
1963 _____	4,521	2,198	2,323	51.38
1964 _____	4,410	2,102	2,308	52.34
1965 _____	4,316	1,968	2,348	54.40
1966 _____	4,632	1,780	2,852	61.57
1967 _____	3,228	728	2,500	77.45
Unclassified _____	524	503	22	4.20
Total Series E _____	152,275	108,838	43,437	28.53
Series H (1952 thru May, 1959) ^{3/} _____	5,485	2,895	2,590	47.22
H (June, 1959 thru 1967) _____	6,407	1,141	5,267	82.21
Total Series H _____	11,892	4,036	7,856	66.06
Total Series E and H _____	164,167	112,874	51,293	31.24
Series J and K (1955 thru 1957) _____	1,515	1,220	295 ^{4/}	19.47
All Series { Total matured _____	36,760	36,681	79	.21
{ Total unmatured _____	165,682	114,094	51,588	31.14
{ Grand Total _____	202,441	150,775	51,667	25.52

^{1/} Includes accrued discount.

^{2/} Present redemption value.

^{3/} Option of owner bonds may be held and will earn interest for additional periods after original maturity dates.

^{4/} Includes matured bonds which have not been presented for redemption.

UNITED STATES SAVINGS BONDS ISSUED AND REDEEMED THROUGH December 31, 1967
(Dollar amounts in millions - rounded and will not necessarily add to totals)

DESCRIPTION	AMOUNT ISSUED ^{1/}	AMOUNT REDEEMED ^{1/}	AMOUNT OUTSTANDING ^{2/}	% OUTSTANDING OF AMOUNT ISSUED
MATURED				
Series A-1935 thru D-1941 _____	5,003	4,995	8	.16
Series F and G-1941 thru 1952 _____	29,521	29,470	51	.17
Series J and K-1952 thru _____	3,156	3,089	67	2.12
UNMATURED				
Series E ^{3/} :				
1941 _____	1,869	1,635	235	12.57
1942 _____	8,250	7,237	1,013	12.28
1943 _____	13,276	11,679	1,597	12.03
1944 _____	15,484	13,519	1,964	12.68
1945 _____	12,162	10,428	1,734	14.26
1946 _____	5,502	4,527	974	17.70
1947 _____	5,210	4,119	1,091	20.94
1948 _____	5,377	4,149	1,229	22.86
1949 _____	5,303	4,020	1,283	24.19
1950 _____	4,635	3,158	1,177	25.39
1951 _____	4,012	2,994	1,018	25.37
1952 _____	4,201	3,107	1,094	26.04
1953 _____	4,797	3,447	1,350	28.14
1954 _____	4,886	3,427	1,459	29.86
1955 _____	5,088	3,494	1,594	31.33
1956 _____	4,907	3,312	1,595	32.50
1957 _____	4,613	3,017	1,596	34.60
1958 _____	4,498	2,758	1,720	38.32
1959 _____	4,198	2,533	1,665	39.66
1960 _____	4,201	2,111	1,790	42.61
1961 _____	4,227	2,299	1,929	45.64
1962 _____	4,073	2,152	1,921	47.16
1963 _____	4,529	2,209	2,320	51.23
1964 _____	4,418	2,116	2,302	52.11
1965 _____	4,324	1,985	2,339	54.09
1966 _____	4,642	1,815	2,827	60.90
1967 _____	3,589	849	2,740	76.34
Unclassified _____	499	553	-53	-
Total Series E _____	152,761	109,257	43,504	28.48
Series H (1952 thru May, 1959) ^{3/} _____	5,485	2,932	2,552	46.53
H (June, 1959 thru 1967) _____	6,441	1,145	5,296	82.22
Total Series H _____	11,926	4,077	7,848	65.81
Total Series E and H _____	164,687	113,334	51,352	31.18
Series J and K (1956 thru 1957) _____	595	366	229	38.49
All Series { Total matured _____	37,680	37,554	126	.33
{ Total unmatured _____	165,282	113,701	51,581	31.21
{ Grand Total _____	202,961	151,255	51,707	25.48

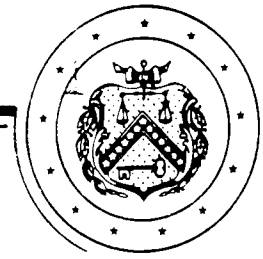
Includes accrued discount.

Current redemption value.

At option of owner bonds may be held and will earn interest for additional periods after original maturity dates.

~~UNITED STATES SAVINGS BONDS ISSUED AND REDEEMED THROUGH DECEMBER 31, 1967~~

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 1, 1967

FOR IMMEDIATE RELEASE

SECRET SERVICE PROMOTIONS ANNOUNCED

U. S. Secret Service Director, James J. Rowley, today announced the promotion of Rufus W. Youngblood to Deputy Director. This new post is the second highest position in the Secret Service.

Thomas L. Johns, formerly Special Agent in Charge of the Presidential Protective Division, is succeeding Mr. Youngblood as Assistant Director (Protective Forces).

Robert H. Taylor, formerly Deputy Special Agent in Charge of the Presidential Protective Division, is promoted to the position of Deputy Assistant Director (Protective Forces).

Clinton J. Hill, formerly Assistant Special Agent in Charge of the Presidential Protective Division, is promoted to Special Agent in Charge of that Division.

Director Rowley said that these promotions are a final part of the overall recent reorganization of the Secret Service. The purpose of this reorganization is to strengthen and broaden the administrative structure of the Service.

The Deputy Director participates with the Director in supervising the activities of the Secret Service in the discharge of its protective and criminal investigative responsibilities.

Mr. Youngblood was born January 13, 1924 in Macon, Georgia. He served in the U. S. Army Air Force during World War II. He is a graduate of the Georgia Institute of Technology, Atlanta, Georgia, and earned a Bachelor of Industrial Engineering Degree in 1950. Mr. Youngblood was appointed as a Special Agent with the Secret Service in 1951 and has served in the Atlanta and Washington, D. C., field offices and on the Vice Presidential and Presidential Protective Divisions. In 1965 he was promoted to Special Agent in Charge of the Presidential Protective Division and later that year promoted to Assistant Director (Protective Forces). Mr. Youngblood resides in suburban Virginia with his

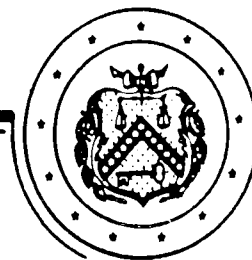
wife, the former Peggy Denham, and three children; daughters - Adele Lois age 11; Rebecca Ann age 6; and son Mark age 17. A married daughter, Joy Youngblood Rumpf, resides in Andover, Massachusetts.

Mr. Johns was born on December 11, 1925, in Birmingham, Alabama. He served as an Aviation Cadet with the U.S. Naval Air Corps during World War II. In 1950 he earned a Bachelor of Science Degree in Law and Business Administration from Howard College in Birmingham. Mr. Johns was appointed to the Secret Service as a Special Agent in 1954 and has served in the Birmingham, Chicago, and Atlanta field offices on the Vice Presidential and Presidential Protective Divisions. He was promoted to Assistant Special Agent in Charge of the Presidential Protective Division in 1965 and in 1966 to Special Agent in Charge of that Division. He resides in suburban Virginia with his wife, the former Nita Jean Parker, with their son Jeff age 17.

Mr. Taylor was born May 16, 1926 in Iola, Kansas. He served in the U.S. Navy during World War II. He received a B.A. Degree in Political Science from Wichita State University in Wichita, Kansas, in 1950 and has attended Memphis State Law School, Memphis, Tennessee. He was appointed to the Secret Service as a Special Agent in 1950 and has served in the Kansas City, Washington, D. C., and Memphis field offices and on the Presidential Protective Division. Before his promotion to Deputy Special Agent in Charge of the Presidential Protective Division in 1966, Mr. Taylor was Special Agent in Charge of the Memphis Field Office. Mr. Taylor resides in suburban Virginia with his wife, the former Loretta Mae Bowman, and their two children, a daughter Karen age 16, and a son Kenneth age 14.

Mr. Hill was born January 4, 1932 in Larimore, North Dakota. In 1954 he graduated from Concordia College, Moorehead, Minnesota, with an A.B. Degree in History. He served in the U.S. Army, Counter Intelligence Corps, from 1954 to 1957. He was appointed as a Special Agent with the Secret Service in 1958. After serving in the Denver Field Office he was transferred in 1959 to the Presidential Protective Division. Mr. Hill resides in suburban Virginia with his wife, the former Gwen Ardeth Brown, and their two sons, Chris age 11 and Corey age 6.

TREASURY DEPARTMENT



WASHINGTON, D.C.

OR RELEASE 6:30 P.M.,
Monday, December 4, 1967.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated September 7, 1967, and the other series to be dated December 7, 1967, which were offered November 29, 1967, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	91-day Treasury bills		:	182-day Treasury bills	
	maturing March 7, 1968		:	maturing June 6, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.746	4.961%	:	97.190	5.558%
Low	98.736	5.000%	:	97.174	5.590%
Average	98.739	4.989%	<u>1/</u> :	97.179	5.580% <u>1/</u>

46% of the amount of 91-day bills bid for at the low price was accepted
 34% of the amount of 182-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 19,161,000	\$ 9,161,000	:	\$ 28,253,000	\$ 7,153,000
New York	1,888,148,000	1,054,068,000	:	1,647,400,000	756,133,000
Philadelphia	37,455,000	12,605,000	:	14,983,000	4,917,000
Cleveland	48,773,000	23,690,000	:	64,010,000	29,390,000
Richmond	20,456,000	17,279,000	:	20,584,000	9,604,000
Atlanta	57,263,000	34,261,000	:	43,433,000	23,323,000
Chicago	247,267,000	135,089,000	:	277,607,000	78,917,000
St. Louis	51,803,000	33,903,000	:	31,812,000	16,442,000
Minneapolis	28,746,000	18,336,000	:	21,328,000	7,868,000
Kansas City	26,729,000	20,487,000	:	13,787,000	11,287,000
Dallas	26,129,000	13,929,000	:	14,174,000	8,874,000
San Francisco	309,780,000	127,320,000	:	238,498,000	46,823,000

TOTALS \$2,761,710,000 \$1,500,128,000 a/ \$2,415,869,000 \$1,000,731,000 b/

- / Includes \$216,041,000 noncompetitive tenders accepted at the average price of 98.739
- / Includes \$133,936,000 noncompetitive tenders accepted at the average price of 97.179
- / These rates are on a bank discount basis. The equivalent coupon issue yields are 5.14% for the 91-day bills, and 5.84 % for the 182-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 4, 1967

FOR IMMEDIATE RELEASE

UNITED STATES FOREIGN GOLD TRANSACTIONS IN 1967

The Treasury announced today that net sales of monetary gold by the United States to foreign countries during the third quarter of 1967 amounted to approximately \$53 million.

The major transactions during the quarter, as shown in Table I, were the purchase of \$19.6 million from Greece by the United States and the sale by the United States of \$76.6 million to the United Kingdom.

The net drain on United States monetary gold stocks in the third quarter due to industrial and artistic demand (net of inflow from new production and scrap) came to \$39 million. This brought the total net outflow of gold from the gold stock of the United States in the third quarter of 1967 to \$92.2 million.

Table II, attached, shows quarterly sales of gold by the United States during 1967 to other countries to enable them to pay the gold portion of their quota increases in the International Monetary Fund. Deposits of like amounts of gold were made by the IMF with the United States to mitigate the effects upon the United States gold stock of the quota increases.

Attachments

TABLE 1

UNITED STATES NET MONETARY GOLD TRANSACTIONS WITH
FOREIGN COUNTRIES AND INTERNATIONAL INSTITUTIONS
January 1 - September 30, 1967

(In millions of dollars at \$35 per fine troy ounce)

Area and Country	First Quarter	Second Quarter	Third Quarter	Total
Western Europe				
Greece	-	-	+19.6	+19.6
Ireland	-0.3	-0.6	-0.4	-1.3
Switzerland	-	-30.0	-	-30.0
Turkey	-16.9	+21.2	-	+4.4
United Kingdom	+3.3	-34.0	-76.6	-107.3
Yugoslavia	<u>-0.7</u>	<u>-0.9</u>	<u>-0.7</u>	<u>-2.2</u>
Total	-14.5	-44.3	-58.1	-116.8
Canada	-	+50.0	-	+50.0
Latin America				
Argentina	-0.4	-0.3	-0.1	-0.8
Brazil	-0.4	-0.3	-0.1	-0.8
Chile	-1.5	-1.5	-	-3.0
Colombia	*	*	-	*
Costa Rica	-0.1	-0.1	-0.1	-0.4
Dominican Republic	-0.1	-0.1	-0.1	-0.4
Ecuador	-	-0.2	-0.6	-0.8
El Salvador	-	-	-2.5	-2.5
Guatemala	*	*	*	-0.1
Haiti	*	-0.1	-0.1	-0.2
Honduras	*	-	-	*
Mexico	-10.0	-	-	-10.0
Nicaragua	-0.1	*	-	-0.1
Peru	+10.0	+15.0	+10.0	+35.0
Surinam	+2.6	-	-	+2.6
Uruguay	<u>*</u>	<u>*</u>	<u>*</u>	<u>-0.1</u>
Total	-0.1	+12.3	+6.2	+18.4
Asia				
Afghanistan	-1.2	-0.1	-0.1	-1.3
Ceylon	-0.1	*	-0.1	-0.2
Indonesia	-1.8	-	-0.2	-2.0
Iran	-1.3	-	-	-1.3
Iraq	-0.1	-0.1	-	-0.2
Pakistan	-0.2	-0.2	-0.2	-0.7
Syria	<u>-0.2</u>	<u>-0.2</u>	<u>-0.2</u>	<u>-0.5</u>
Total	-4.8	-0.6	-0.8	-6.2
Africa				
Burundi	*	*	*	*
Liberia	-0.1	-0.1	-0.1	-0.3
Rwanda	*	*	*	-0.1
Somalia	-0.1	-0.1	-0.1	-0.2
Sudan	-0.1	-0.2	-0.2	-0.5
Tunisia	<u>-0.1</u>	<u>-0.1</u>	<u>-0.1</u>	<u>-0.3</u>
Total	-0.4	-0.5	-0.5	-1.4
Total	-19.8	+17.0	-53.2	-56.1
Domestic Transactions	-29.9	-32.5	-39.0	-101.3
Total Gold Outflow	-49.7	-15.5	-92.2	-157.4

*Under \$50,000.

Figures may not add to totals because of rounding.

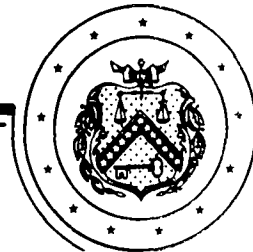
TABLE 2

UNITED STATES MONETARY GOLD TRANSACTIONS
WITH FOREIGN COUNTRIES
MITIGATED THROUGH SPECIAL DEPOSITS BY THE IMF
(Millions of U.S.\$)

January 1 - September 30, 1967

Area and Country	First Quarter	Second Quarter	Third Quarter	Total
<u>Latin America</u>				
Dominican Republic	-0.4	—	—	-0.4
Total	-0.4	—	—	-0.4
<u>Asia</u>				
Iran	-13.7	—	—	-13.7
Lebanon	-0.6	—	—	-0.6
Vietnam	-1.3	—	—	-1.3
Total	-15.6	—	—	-15.6
<u>Africa</u>				
Algeria	—	-0.8	—	-0.8
Cameroon	—	-0.2	—	-0.2
Central African Rep.	—	-0.1	—	-0.1
Chad	—	-0.1	—	-0.1
Congo(Brazzaville)	—	-0.1	—	-0.1
Congo(Kinshasa)	—	-2.4	—	-2.4
Dahomey	—	-0.1	—	-0.1
Gabon	—	-0.1	—	-0.1
Ivory Coast	-0.2	—	—	-0.2
Mauritania	—	-0.1	—	-0.1
Morocco	—	-0.9	—	-0.9
Niger	—	—	-0.1	-0.1
Rwanda	—	-0.2	—	-0.2
Upper Volta	—	-0.1	—	-0.1
Total	-0.2	-5.3	-0.1	-5.5
Total	-16.2	-5.3	-0.1	-21.6
IMF Deposit	+16.2	+5.3	+0.1	+21.6

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 5, 1967

FOR RELEASE P.M.'S
TUESDAY, DECEMBER 5, 1967

VICE PRESIDENT HUMPHREY WILL MEET WITH
INDUSTRY-GOVERNMENT SPECIAL TRAVEL TASK FORCE
AT ORGANIZATION SESSION IN WASHINGTON
JANUARY 16, 1968

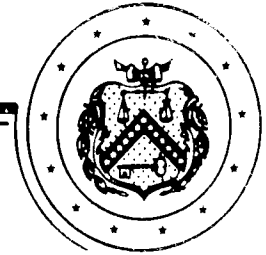
The first meeting of the Industry-Government Special Travel Task Force will be held at the Treasury in Washington on January 16, Robert M. McKinney, Chairman, announced here yesterday. Vice President Hubert H. Humphrey, will meet with the group at its organization session.

Appointment of Robert G. Pelikan as Executive Director of the Task Force was announced by Mr. McKinney. Mr. Pelikan, on loan from the Office of the Assistant Secretary for International Affairs, has served as Treasury Attache in Rome and Tokyo. An office and staff to deal with matters on the government sector of the Task Force assignment has been established in the Treasury Department, Washington. Matters in the private sector will be handled from the New York office, to be established shortly.

The Presidential Task Force, consisting of leaders in private industry and government, will recommend actions to increase foreign travel to the United States, improving the U.S. balance of payments and helping foreign visitors learn to know the United States and its people. In appointing the Task Force, the President noted that the most satisfactory way to arrest the increasing balance of payments gap resulting from travel was not to limit American travel abroad but rather to stimulate and encourage foreign travel to the United States.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

December 5, 1967

FOR IMMEDIATE RELEASE

TREASURY ANNOUNCES PUBLICATION OF PROGRESS IN MANAGEMENT IMPROVEMENT BOOKLET

The Treasury today announced the publication of "Progress in Management Improvement," a pamphlet illustrating the results of cost reduction and management improvement efforts undertaken by bureaus of the Treasury Department in fiscal year 1967.

Savings under these actions added up to approximately \$145.6 million and 2,600 man-years. This total was reported by the Treasury in a report to the President in September.

Examples of the achievements of the Department listed in the 31-page booklet include:

- (1) Two major changes in tax collection procedures that had the effect of accelerating the collection of revenue and thereby reducing borrowing costs and saving \$80 million.
- (2) Elimination of needless paperwork by the Bureau of Customs that will save an estimated \$341,000 in processing time and costs. In terms of processing, this will mean a reduction of 1,324,000 pieces of paper each year within Customs and 566,000 pieces of paper the public will no longer have to prepare.
- (3) The Bureau of Accounts presorted by ZIP Code, Social Security, and tax refund checks prior to release to the Post Office Department with resulting savings to the Post Office Department of more than \$1 million.

* * * *

(4) The Internal Revenue Service program saved \$16.4 million and 1,641 man-years through management improvements including:

- a. Greater use of GSA vehicles and adoption of a sliding scale reimbursement rate for users of privately owned automobiles. Nearly half a million dollars were saved by encouraging drivers to use GSA vehicles for official travel and, where this was not possible, reimbursing them at a rate comparable to the cost of renting a GSA vehicle. Previously, drivers of privately owned automobiles were reimbursed at a rate of 10 cents per mile as compared with the 7 cents per mile cost of renting a GSA vehicle.
- b. In excess of \$2 million was saved by IRS through constant review of the need for vacant positions. During fiscal years 1966 and 1967, over 300 vacant positions were abolished as a result of this review.
- c. Saving of \$2.3 million resulted from suggestions submitted by IRS employees. This developed from the IRS policy to make maximum use of the employee suggestion program as a tool for improving management effectiveness.

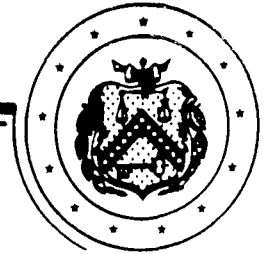
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(5) The Bureau of Engraving and Printing saved \$256,000 by the use of improved equipment and techniques to reduce the average cost of printing currency from \$8.42 to \$8.14 per thousand notes.

(6) The Office of the Treasurer reduced reimbursable costs by more than \$1 million through regulations granting the Federal Reserve banks the authority to verify and destroy certain denominations of unfit Federal Reserve notes.

- (7) The United States Coast Guard, which at the time was a bureau of the Treasury Department, saved nearly \$38 million during fiscal year 1967. The major cost reduction of \$14.6 million resulted from a reorganization of the search and rescue facilities along the East and Gulf coasts which will enable the Coast Guard to provide better service at less cost.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 4, 1967

FOR IMMEDIATE RELEASE

TREASURY SECRETARY FOWLER NAMES WILLIAM B. ANDREWS
AS NEW SAVINGS BONDS CHAIRMAN FOR THE STATE OF MONTANA

William B. Andrews, President of the Union Bank and Trust Company of Helena, Montana, has been appointed by Secretary of the Treasury Henry H. Fowler as volunteer State Chairman for the Savings Bonds Program in Montana. He succeeds A. T. Hibbard, Honorary Chairman of the Board, Union Bank and Trust Company, Helena.

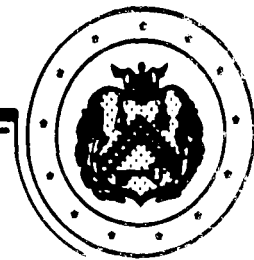
Commenting on Mr. Andrews' appointment, Secretary Fowler said "We feel that the Savings Bonds Program is one of the most important activities in which we are engaged. It not only is an essential feature of our debt management program but also serves to encourage thrift."

Mr. Andrews has served for eight years as Vice State Chairman of the Montana Savings Bonds Committee and has long been associated with the program.

He is a graduate of the University of Montana, majoring in business administration. He served as an officer in the Army during World War II. He entered the banking industry in 1951 and rose to the presidency of one of the largest banks in Montana in 1966. He is a leader in civic activities in his community and is well known and highly regarded in industry throughout Montana.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

December 6, 1967

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing December 14, 1967, in the amount of \$2,400,635,000, as follows:

91-day bills (to maturity date) to be issued December 14, 1967, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated September 14, 1967, and to mature March 14, 1968, originally issued in the amount of \$1,000,527,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated December 14, 1967, and to mature June 13, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Monday, December 11, 1967. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

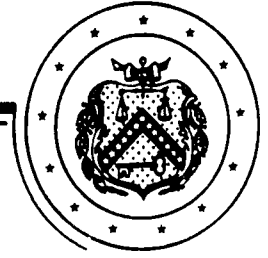
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on December 14, 1967, in cash or other immediately available funds or in a like face amount of Treasury bills maturing December 14, 1967. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 6, 1967

FOR IMMEDIATE RELEASE

TREASURY SECRETARY FOWLER NAMES JAMES W. RAWLES
NEW SAVINGS BONDS CHAIRMAN FOR THE STATE OF VIRGINIA

James W. Rawles, Executive Vice President, State-Planters Bank of Commerce and Trusts, Richmond, Va., was appointed by Secretary of the Treasury Henry H. Fowler as volunteer State Chairman for the Savings Bonds Program in Virginia, effective December 1. He succeeds John H. Randolph, Jr., President, First Federal Savings and Loan Association of Richmond, Va.

Mr. Rawles is a native of Virginia. He received a Bachelor of Arts degree from the University of Virginia, a Master of Business Administration degree from the Harvard Business School, and a certificate from the Stonier Graduate School of Banking, Rutgers University.

He began his banking career with the J. & W. Seligman and Company of New York in 1930. He joined State-Planters in September 1933. He has served in a number of positions and was elected Executive Vice President in 1966.

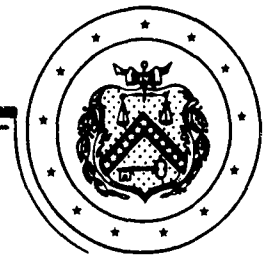
Mr. Rawles is a member of the Association of Reserve City Bankers and has held a number of posts with the Virginia Bankers Association.

He is active in many community activities including the Red Cross, American Cancer Society and the United Givers Fund.

He is a member and former vestryman and treasurer of St. Paul's Episcopal Church.

Mr. Rawles is married to the former Georgina Olivia Marraccini. They have five children.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 7, 1967

FOR IMMEDIATE RELEASE

The Treasury today announced that it has transferred \$475 million in gold from its Treasurer of the United States account to its Exchange Stabilization Fund. The gold will be used to make settlement for the United States' share in support operations in the London gold market in November, to cover sales made recently to central banks which requested the Treasury to convert some of their dollar balances into gold, and, as is customary from time to time, to provide the Exchange Stabilization Fund with additional resources to meet future contingencies.

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TREASURY DEPARTMENT
Washington

REMARKS BY THE HONORABLE MELVIN I. WHITE
DEPUTY ASSISTANT SECRETARY FOR TAX POLICY
UNITED STATES TREASURY DEPARTMENT
BEFORE THE
ANNUAL TAX DINNER OF THE
NEW JERSEY SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS
AT THE BRUNSWICK INN, EAST BRUNSWICK, NEW JERSEY
WEDNESDAY, DECEMBER 6, 1967

Economic Issues in Tax Policy

Essentially good policy making is choosing the best among the possible alternatives. To establish the proper basis for policy, alternative courses of action must be subjected to a two-sided examination: the benefits of each must be identified and the cost calculated. Then the various benefit-cost relationships -- or expressed quantitatively, the benefit-cost ratios -- must be compared with one another so that the optimum action program can be decided upon. Furthermore, the entire examination must be future-oriented, involving forecasts of possible consequences as a result of taking alternative measures.

Economics perhaps more so than other disciplines does develop, I think, sensitivity to, or even affinity for the policy making problem. In economics one is accustomed to think never in absolute, but only in relative terms; gains

are always measured against costs; and the search is always for the optimum, not the perfect solution. History is irrelevant except when it can serve as a basis for appraising the future.

However, the expertise of the economist is limited, and there are not many areas where he can, working entirely within the framework of his own discipline, designate the optimum choice -- especially if you include capability of political enactment as a criterion.

Certainly this is the case in the multi-faceted field of tax policy. Therefore, I am aware that in dealing with the economic aspects of tax policy tonight I am not giving a rounded treatment of the subject. But in speaking to a group as sophisticated in tax matters as this one, it is undoubtedly wise to abide by a basic economic principle and focus these remarks on that phase of the subject where I can at least claim a comparative advantage. Beyond this, I do believe that economics invariably has something important to say about what should be done in tax policy, if not always about what can be done.

I would like then to consider some specific tax policy issues for which an economic examination of the alternatives involved appears to me to be particularly relevant and useful.

Form of the Surcharge

First -- a surprise to no one, I'm sure -- I would like to consider the surcharge. As all of you undoubtedly know the surcharge proposed by the President calls for a tax that on a full year basis would be equal to 10 percent of existing liabilities of individuals and corporations, not 10 percent of income. On average the surcharge would amount to about 1 percent of personal income. Thus a married couple with two dependents, a wage income of \$10,000, and taking typical deductions, would have a tax under present rates of \$1,114. A 10 percent surcharge would amount to \$111, or only slightly more than 1 percent of the family's income.

The surcharge would not apply to low-income families and individuals. The surcharge proposal provides an exemption so that married couples with two dependents and with total earnings of \$5,000 or less, and single people with earnings of less than \$1,900 a year would not be subject to the surcharge. This exemption would cover approximately 16 million

taxpayers. In addition there are, of course, all the families and individuals who would not be subject to the surcharge because they are not subject to tax under present law.

Altogether there are approximately 75 million men, women, and children who would not be touched at all by the surcharge.

The surcharge form is itself, of course, a choice among alternative ways of raising revenue. It is a choice that is easy to administer, requires no change in the definition of the tax base and is easy for the taxpayer to understand. It reflects the generally progressive pattern of our present income tax system, and this is strengthened by the provision for a low-income exemption.

The surcharge form of tax increase is in line with the recommendations concerning tax changes for short-run stabilization of the Subcommittee on Fiscal Policy of the Joint Economic Committee. In the spring of 1966 the Subcommittee held hearings on the subject of tax changes for short-run stabilization. These hearings constituted a thorough and comprehensive investigation of the subject including alternative types of tax measures. The Subcommittee gave a final

endorsement to a uniform percentage addition to (that is a surcharge) or subtraction from, tax liabilities, as being on balance the best type of tax change for purposes of economic stabilization.

Relation to Tax Reform

There are those who, while not disclaiming the need for a tax increase, have advocated the closing of loopholes in our existing tax laws as a possible partial alternative, or adjunct to, the surcharge. However, tax reform measures are not appropriate for meeting the temporary objectives for which the surcharge is so well designed.

Reform measures have the purpose of accomplishing permanent not temporary structural changes in the tax system. They must be appraised in relation to long-range objectives of the tax system. The issues involved are complex and controversial, and protracted Congressional debate about them is only to be expected.

Furthermore, realistically viewed, revenue raising reforms would provide significant revenue only after a considerable lapse of time, and, thus, would not contribute significantly to the fiscal restraint we now need. This reflects not only the

time required for Congressional debate but also the fact that most reforms would involve some phasing in arrangement and period of adjustment by taxpayers that would defer realization of the potential revenue, in some cases, for many years.

This is not by any means to say, however, that tax reform is unimportant, or that it is not a high priority item in the tax policy outlook. On the contrary, tax reform proposals for permanent revision of the laws are under intensive preparation in the Treasury. The President has said that tax reforms will be forwarded to the Congress for the deliberate study, debate, and action they require during the session next year.

Alternatives to a Tax Increase

Accepting that the surcharge is the best form of tax increase, there is still, of course, the question of whether any tax increase at all is justified in present circumstances. Put another way, would not the nation be better off with the alternative of a substantially larger Federal deficit?

We are all aware I'm sure that still another alternative has been proposed -- namely, to cut Federal non-defense

expenditures so drastically that the surcharge will not be needed. Some carefully worked out budget cutting at this time is desirable, and a formula for doing so was presented to the Ways and Means Committee by Secretary Henry H. Fowler and by Director Charles L. Schultze of the Budget Bureau. But it is neither feasible nor desirable to cut expenditures in the drastic amount that would be necessary to obviate the need for the surcharge. Responsible expenditure cut-backs and the tax increase are what is needed; it is not a matter of choice of one or the other.

The tax increase program proposed by the Administration, including the speed-up on corporate tax payments and deferral of excises, would yield \$7.4 billion in fiscal year 1968. Viewed against the nearly \$800 billion level of our Gross National Product, the fiscal year tax yield figure may not indeed, appear significant. But in judging the economic impact it must first of all be kept in mind that once the tax increase program is fully in effect it will raise Federal revenues at an annual rate of about \$12 billion. Then, due to the

multiplier effect, the tax increase could diminish the annual rate of the GNP by considerably more than \$12 billion within a few quarters -- conservatively as much as \$15 billion.

Next, in the present circumstances the tax increase and its GNP effects should not be viewed against the level of GNP but against the growth we might anticipate from hereon with and without the tax increase, compared to the growth the economy can stand without becoming unbalanced and inflationary.

Chairman Gardner Ackley of the Council of Economic Advisers and others have indicated that the economy can tolerate without undue strain a growth in GNP of between \$50-\$60 billion. A growth of \$15 billion -- 25%-30% -- more than this, which might occur in the absence of the tax increase, is not compatible with a balanced economy and non-inflationary rise in prices.

Again, the tax increase must be put in the proper perspective in order to appreciate its importance for the money and credit markets. As Secretary Henry H. Fowler pointed out in his statement before the Ways and Means Committee last Wednesday, November 29, a key question is what the Federal sector's net

demands will be in the January-June 1968 period, and beyond. With a program of rigorous fiscal restraint, it would be possible to make a seasonal repayment to the market of between \$2 to \$5 billion during the January-June period of 1968. Without the tax increase, it would be necessary to make a net demand on the credit market in this period of \$5-\$6 billion or more, depending on how successfully the expenditure side of the budget was restrained. By comparison, in the January-June period of 1967 the Federal sector supplied \$11 billion to the credit market. Thus without the tax increase the swing in Federal credit demands from the first half of fiscal 1967 to the first half of fiscal 1968 might amount to \$17 billion or more.

A figure of \$17 billion may also not appear large in relation to an \$800 billion GNP. But that is not the relevant comparison. Rather the swing in Federal credit demand must be related to the annual flow of credit through the credit markets, which amounts to around \$70 billion annually. Against this total flow of \$70 billion, a change in one sector of \$17 billion does loom very large indeed.

In the absence of the tax increase program, then, the deficit and the borrowing, or credit, needs of the Federal Government -- which would be large even with the surcharge -- would assume outsized proportions which would have consequences for money and credit markets, interest rates, prices, and the general economy.

Effects Without a Tax Increase

I cannot predict the exact magnitude of these consequences. But it does not take much imagination, based on past experience and the teachings of economics to suggest realistic possibilities.

Interest rates could rise. The cost of meeting the Federal Government's credit needs would probably rise, but those needs would, nevertheless, be met. So probably would the needs of large corporations. But one cannot expect that bank credit would expand sufficiently to accommodate all demands. The monetary authorities will want to appraise total demands carefully and accommodate only with reluctance a larger aggregate volume. Undoubtedly as the net result of enlarged Federal credit demands and Federal Reserve action, there would be monetary restraint. Therefore, credit demands

would go unsatisfied and perhaps other demands met only at exorbitantly high rates. As was clear from our experience in 1966, monetary restraint can have a powerful dampening influence on the economy. But the major victim was, and undoubtedly would be again, the homebuilding industry. State and local governments would also be pinched, as would smaller business firms.

Whether or not the surcharge is imposed, it is likely that prices will rise. But without the surcharge prices will rise more and faster. How much more, again, cannot be predicted exactly. But all those low-income families and individuals who would not be touched by the surcharge would clearly stand to lose if there is an additional price rise because of not imposing the surcharge. Beyond this, however, many families and individuals -- and surprisingly far up the income scale -- might very well fare better with the surcharge than without it, in the simple direct sense that the surcharge would amount to less than the loss of purchasing power through the inflationary rise in prices that might occur without the surcharge.

I realize that I am speaking about future consequences rather than about what is observable right now -- although there is much to observe that points toward the necessity of fiscal restraint. This is the way it should be. There are lags in the effects of fiscal policy measures, and these measures are not 100 percent flexible in the sense that they can be reversed quickly and frequently. Therefore, we cannot wait until we are already in an inflationary situation to act. Action must be taken before hand, and therefore, whether willingly or unwillingly, implicitly or explicitly, we are bound to rely on forecasts when policy decisions are made.

I could go on with more detailed examination of the possible implications of not imposing the surcharge. But if I did it would only reinforce what is implied in what I have already said: namely, that in the clearest light that analysis, prudent judgment, and evidence can provide, the surcharge proposal does appear to meet the rigorous, and only really relevant, test of being the best of the alternative courses of action open to us.

Tax Credits and Incentives

Turning now to another aspect of tax policy, the use of tax credits and tax incentives has an eternally popular appeal as a method of achieving specific policy goals. One quickly learns at the Treasury that the flow of claimants for such use of the tax system is enormous and endless. In a recent statement before the Senate Finance Committee on the bill introduced by Senator Robert Kennedy to provide tax incentives for the construction and rehabilitation of low-income housing, Under Secretary Joseph W. Barr gave an indication of the variety of tax incentive bills that have been introduced into Congress. He listed bills to provide:

- A tax credit for tuition and expenses of higher education.
- A tax credit to encourage contributions to higher education.
- A tax credit to encourage worker training.
- A tax credit to encourage industrial pollution control.
- A tax credit to encourage airport development.
- A tax credit for underground transmission lines.

- A tax credit for exports.
- A tax credit for freight cars.
- A tax credit for gold mining.
- A tax credit to encourage hiring older workers.

And this was only a partial list.

Now, in general, a tax credit, or tax deduction, costs public funds just as surely as does an expenditure program. However, they are not generally subject to as careful appraisal as are expenditures since budgets are reviewed annually, tax law only rarely. Thus, the use of tax credits and deductions makes difficult the continuous rational calculation of the efficiency with which our resources are being used for public purposes.

Concern for this consequence of credits, deductions and other tax benefits recently prompted Assistant Secretary Stanley S. Surrey to advance a novel and very interesting suggestion relating to the Federal Budget. Namely, that the possibility should be explored of describing in the Federal Budget the expenditure equivalents of the various tax benefit provisions.

While tax incentives may accomplish some desirable results, in every case the question must be raised as to whether there are alternative ways of accomplishing these results at lower cost. Included in this cost is the erosion of the tax base that goes beyond the one particular credit that is proposed. It is a simple fact of life that no one proposal for use of a credit or deduction can be evaluated in isolation. It inevitably becomes a precedent that will weaken resistance to others. The proliferation of deductions, credits and preferences, increases inequity, multiplies opportunities for tax avoidance, and, in narrowing the tax base, causes the level of tax rates to be higher than they otherwise would be. The Treasury official must always include a heavy "cost add-on" reflecting this precedent effect when weighing cost against benefits of a specific proposal. Finally, the goal of a particular tax credit or deduction, laudable though it may be in its own right, must be evaluated against the aims of other laudable programs that also require public funds.

These general points about the role of tax incentives can be illustrated by considering some of the specific areas where such incentives have been proposed.

Tax Incentives for Low-Income Housing

Tax incentives have been advocated to induce investment in low-income housing in slum areas. This advocacy does not imply that the present tax law is disadvantageous to real investment in general or specifically to investment in low-income housing. Present law provisions offer opportunity for converting ordinary income into capital gain. For several categories of building investment we are aware of the fact that a common operating procedure is for an investor to acquire or construct a building on a relatively small equity and hold it for a period of 8 to 10 years, and then sell it. During his period of ownership depreciation deductions allowed for tax purposes are sufficiently high to offset most of the cash throw-off, and perhaps even create a loss which can be used to offset taxable income from other sources. The gain from the sale of the building at the end of the period is then taxed mostly at the preferential capital gains rate.

On the other hand, it must be recognized that buildings are not eligible for the investment credit nor have depreciation guidelines been established for them. One cannot really say then, a priori, whether on balance the tax system favors or disfavors real estate investment.

Rather the problem is seen to be that low- and moderate-income families cannot afford to pay rents that will, at prevailing levels of building and construction costs, provide sufficient profit to induce the construction of an adequate volume of low-income housing. The purpose of the tax incentive proposals then is to help close the gap between what low-income tenants can afford to pay and the net return required from housing projects by investors. The tax proposals include tax credits and especially fast write-off of capital costs.

Immediately it may be worth noting that the equivalent of any tax incentive proposal can be provided by some form of government expenditure or loan program. Allowing a taxpayer to speed up depreciation deductions by taking, say, 20 percent of the cost in the first year permits a corporate taxpayer to reduce tax payments by 48 percent of this deduction in that year, and requires a commensurate increase in tax payments at a future

time over what would have been paid in the absence of the special depreciation deduction. This benefit can be matched by providing an interest-free loan equal to the tax saving from the depreciation deduction, to be repaid at a later date.

A tax credit equal to X percent of the cost of the investment can be matched by a direct payment equal to the same X percent. Alternatively a comparison can be made in the opposite direction: the stream of benefits to an investor from an annual rent supplement program could be duplicated by a program of annual tax credits.

Thus the tax incentive approach has alternatives for providing investor inducements. How does its impact differ from the alternatives?

One obvious difference is that the tax approach does not provide inducement to the individual or corporation having limited income from other sources and therefore unable to make full use of tax incentives. A direct payment could provide benefits even where the housing project was the investor's sole activity.

The tax benefit from a rapid depreciation deduction varies with the income and tax brackets of the investor. The benefit from a dollar of depreciation deduction can range from as high as 70 cents for the top bracket taxpayer to as low as 14 cents for a low-income investor. This incidentally implies a reversal in the pattern of rewards from what is provided by a free market response to a condition of shortage. Under the free market a shortage results in uniformly higher prices to all suppliers of shortage items increasing the income they earn for their services and the services of their capital. Then the progressive tax implies that the rich supplier keeps after tax only 30 cents of the dollar of additional income while the low-income investor would retain 86 cents on the dollar.

The provision of tax incentives as I have already mentioned, costs public funds. In this case the funds would be transferred from the rest of the community to investors in low-income housing. The transfer would be the price paid to attract investors' capital. Questions may be raised as to whether there are alternative ways of attracting the needed capital at lower cost. Guaranteed loan programs similar to those already in being, but perhaps on a more liberal scale,

should be examined as an alternative. Guarantees of various sorts might do much to remove some of the special risks that deter investment in low-income areas, reducing perhaps the required rate of return. Debt capital is likely to be cheaper to attract than equity capital. The argument for the latter is that it is necessary to assure high quality entrepreneurship in "packaging" projects, and high quality management of the constructed project. But it is not clear how large an equity ratio is needed to fulfill this function.

Manpower Training Incentives

Manpower training is another area, I think, where there is general agreement that programs should be expanded beyond their present scope. Such expansion would have the objectives of alleviating skill shortages, increasing the employability of disadvantaged workers, facilitating the re-employment of workers displaced by technological change and generally improving the skills and productivity of the labor force.

Fundamentally, the justification for a subsidy to private industry to train workers is that, due to labor turn-over,

the individual firm under-invests in worker training, because the benefit from the training will not be returned to the firm but will go to other employers when the worker shifts his job.

To improve on the solution provided by the market and induce additional investment in training, it has been proposed that a tax credit for manpower training be allowed to industry. This has been viewed as a particularly apt approach, since it would appear to put investment in human capital on a par with investment in physical assets, to which the 7 percent investment credit applies.

However, there are serious defects with this approach. In the first place it might be noted that insofar as tax treatment is concerned investment in manpower training is not now necessarily disadvantaged compared to physical investment, even after allowing for the investment credit. The reason for this is that outlays for training are treated as current expense for tax purposes. This is equivalent to permitting instant, 100 percent depreciation, and it is sufficiently more favorable than double declining balance or sum of the

years digits methods of depreciation to more than offset the investment credit.

Further, the investment credit was readily integrated into the regular administration of the income tax since the essential determinations involved in its application are part and parcel of administering depreciation on capital equipment. Manpower training credit, on the other hand, requires new factual determinations, judgments and application of criteria that are not a normal part of tax administration nor readily adapted to it.

The tax credit approach does not appear an efficient device for alleviating specific occupational shortages, which are concentrated in a few sectors of the economy and in public service areas (medical, educational, and welfare occupations) which would not be affected by the credit. For firms that do have labor shortages the effect of the credit is quite uncertain: many firms are too small to conduct training programs effectively, and many large firms in capital goods and defense industries are limited in their engagement in training by uncertainty as to output which the credit would

not overcome. The help the credit might give to the disadvantaged is likely to be very limited: most workers who would be trained would be those already employed and relatively well educated, and the disadvantaged probably need pre-job training before they can benefit from on-the-job training.

All this is not to say that industry should not be assisted in expanding training. Rather, it is to say that the tax incentive device is not the proper tool. Alternative approaches would be more effective.

Pollution Control

A similar line of reasoning applies to pollution control. Again a problem arises because the market does not produce the desired solution. In this case it is due to the fact that a cost item, rather than a benefit, accrues to other than the originating firm. Thus, the firm tends to under-invest in methods that will reduce this cost.

There is, of course, an economic viewpoint that the cost of pollution -- or of averting pollution -- ought to be borne entirely by the industry and its customers. This viewpoint leads to such proposals as imposing a charge on effluents set sufficiently high to induce their curtailment to acceptable levels, which would come about as a result of adopting methods

that diminish effluents or as a result of curtailing industry output in response to higher costs and prices, or both.

But setting such an approach aside and accepting public responsibility for meeting some portion of the costs of pollution control, the question is whether tax allowance is the proper way to do it. A tax allowance is likely to be inefficient. It tends to be geared to meeting the cost of pollution control only when it is done by treating effluents at the end of the production process. But there apparently are numerous other possible technical means of cutting down on pollution at other stages in the production process which would be reflected in higher operating costs (low sulphur fuels for power plants; better quality control in production; alkalize acid waste and dump it rather than build a plant to remove it). It would be difficult to devise equivalent tax allowances when these means are adopted. Not all pollution is equally significant and it would be preferable to have a method of cost-sharing that could be varied so that the sharing might be greater, say, for high density communities with many sources of pollution than for low density communities with few pollution sources. And tax incentives vary in their impact on firms: pollution does frequently arise from firms that operate at little or no profit,

perhaps for purposes of recovering sunk capital, and, therefore, would not be responsive to tax incentives, while relatively small benefits would be derived from tax deductions by small firms subject to lower marginal rates.

All three of these areas -- low-income housing, manpower training, pollution control -- as well as many others involve socially desirable objectives although individuals would differ about priorities. If the tax system were used for such programs, one wonders how often the programs would be re-examined to evaluate effectiveness and to reappraise their priorities. Finally, if we were to travel freely down the tax incentive route the Treasury Department would soon be making crucial decisions in almost all matters of economic policy. I can assure you that the prospect of such an empire is not really an appealing one to the Treasury Department.

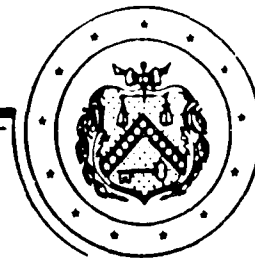
Federal Assistance to States and Localities

Finally, and briefly, a policy issue that very much requires examination of alternatives is that of Federal assistance to state and local governments. Many alternatives have been advanced as to the method to be followed. These include:

substantial Federal tax credits for state income taxes; Federal assumption of a larger share of welfare costs (either directly or through such devices as guaranteed income or negative income tax); expanded urban programs with adequate funding of the Model Cities program and more flexibility provided through an urban development fund which merges different grant programs; and general support grants with a wide range of proposed formulas for distributing funds to states and to localities. On the basis of our present knowledge and analysis, it seems to me premature to try to make a choice at this time. All of these alternatives involve difficult problems of implementation. We are faced today with heavy demands on our fiscal resources. But also in the post-Vietnam period any proposed method of aid involving substantial sums will have to, in the final analysis, also be placed against alternative claims for Federal expenditures and tax reduction.

But, then, the import of what I have been saying this evening is that all uses of Federal funds -- in the form of tax preferences, expenditure or debt reduction -- should be subject to a similar comparative analysis and evaluation. The economist's role in this task is not, of course, exclusive, but it is now and will, I think, become increasingly important.

TREASURY DEPARTMENT



WASHINGTON, D.C.

RE RELEASE 6:30 P.M.,
 Monday, December 11, 1967.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated September 14, 1967, and the other series to be dated December 14, 1967, which were offered on December 11, 1967, were opened at the Federal Reserve Banks today. Tenders were invited for \$500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	91-day Treasury bills maturing March 14, 1968		:	182-day Treasury bills maturing June 13, 1968	
	Price	Approx. Equiv. Annual Rate		Price	Approx. Equiv. Annual Rate
High	98.758 <u>a/</u>	4.913%	:	97.238 <u>b/</u>	5.463%
Low	98.746	4.961%	:	97.215	5.509%
Average	98.751	4.941% <u>1/</u>	:	97.223	5.493% <u>1/</u>

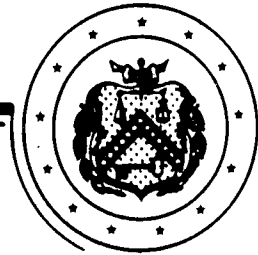
a/ Excepting 2 tenders totaling \$62,000; b/ Excepting 1 tender of \$975,000
 57% of the amount of 91-day bills bid for at the low price was accepted
 38% of the amount of 182-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 20,020,000	\$ 9,811,000	:	\$ 14,911,000	\$ 3,911,000
New York	1,774,841,000	1,077,451,000	:	1,449,311,000	698,611,000
Philadelphia	33,158,000	11,058,000	:	21,206,000	10,866,000
Cleveland	51,461,000	49,161,000	:	66,142,000	51,042,000
Richmond	16,220,000	13,220,000	:	5,851,000	5,851,000
Atlanta	44,388,000	28,158,000	:	29,212,000	18,652,000
Chicago	226,158,000	110,245,000	:	179,148,000	75,806,000
St. Louis	45,943,000	29,514,000	:	28,812,000	21,612,000
Minneapolis	27,922,000	19,565,000	:	21,946,000	11,446,000
Kansas City	33,456,000	29,456,000	:	20,687,000	18,687,000
Dallas	25,667,000	17,237,000	:	19,980,000	12,360,000
San Francisco	189,750,000	105,840,000	:	116,640,000	71,340,000
TOTALS	\$2,488,984,000	\$1,500,716,000	c/	\$1,973,846,000	\$1,000,184,000

Includes \$237,667,000 noncompetitive tenders accepted at the average price of 98.751
 Includes \$160,325,000 noncompetitive tenders accepted at the average price of 97.223
 These rates are on a bank discount basis. The equivalent coupon issue yields are
 5.09% for the 91-day bills, and 5.74% for the 182-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 11, 1967

FOR IMMEDIATE RELEASE

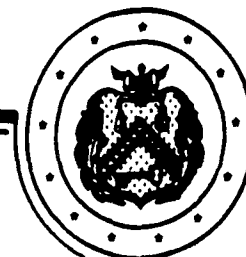
TREASURY ANNOUNCES SCHEDULE FOR REGULAR WEEKLY BILL AUCTIONS DURING THE HOLIDAY SEASON

The Treasury announced today that its next regular weekly bill auction will be held on Friday, December 15, rather than on Monday. The day for the auction is being advanced to assure ample time between it and the payment date during the pre-holiday season. Payment for and delivery of the bills will be on the normal day Thursday, December 21.

The Treasury added that for the subsequent two weekly bill auctions the announcements inviting tenders will be made on Monday, December 18, and Friday, December 22, and the auctions will be held on Friday, the 22nd and the 29th. The payment and delivery day for these issues will be Thursday as usual.

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TREASURY DEPARTMENT



WASHINGTON, D. C.

December 11, 1967

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing December 21, 1967, in the amount of \$2,400,015,000, as follows:

91-day bills (to maturity date) to be issued December 21, 1967 in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated September 21, 1967, and to mature March 21, 1968, originally issued in the amount of \$1,000,249,000, the additional and original bills to be freely interchangeable.

182 -day bills, for \$1,000,000,000, or thereabouts, to be dated December 21, 1967, and to mature June 20, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Friday, December 15, 1967. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on December 21, 1967, in cash or other immediately available funds or in a like face amount of Treasury bills maturing December 21, 1967. Cash and exchange tender will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT
Washington

FOR RELEASE P.M.'S
FRIDAY, DECEMBER 15, 1967

REMARKS OF THE HONORABLE TRUE DAVIS
ASSISTANT SECRETARY OF THE TREASURY
AND UNITED STATES EXECUTIVE DIRECTOR
OF THE
INTER-AMERICAN DEVELOPMENT BANK
BEFORE THE
LOS ANGELES ROTARY CLUB
THE STATLER HOTEL, LOS ANGELES, CALIFORNIA
FRIDAY, DECEMBER 15, 1967, 12:00 NOON, PST

THE TRUE MEASURE OF A NATION: RESPONSE TO THE CHALLENGES

A proverb familiar to Rotarians in the Twenties -- and surely familiar to Rotarians today -- states that it is easier to pull down than to build up. Rotarians are interested in building, in strengthening, not alone the character of individuals, but also the character of our cultural institutions. All of us are concerned with problems affecting individuals in their relations with each other and the problems of change and growth affecting the cities in which we live. Without attempting to flatter Rotarians, I think that it would be a reasonable proposition to state that you are interested, first and foremost, in constructive criticism; and through such criticism you help improve the environment in which you live.

This has been a year of criticism -- a year in which every critic with a message has been given ample opportunity in our communication media to express himself. If we were to believe all we have read and heard we could only conclude that we are, as a people and as a nation, morally and spiritually bankrupt. For most of the criticism that we have been subjected to has been destructive in nature. The desired effect of this type of criticism is to pull down our institutions rather than to strengthen them, to weaken the faith we have in each other, and to destroy the confidence we have in ourselves.

Much of this criticism has been leveled at our Government and at the people who direct its activities. It has even been said of the Treasury Department that we are so concerned, so preoccupied with law enforcement, including the collection of taxes, with fiscal and monetary affairs, with financing the public debt, and with other related matters of national and international finance, that we are oblivious to the social problems of our society, ignorant of the cultural changes affecting us, and adamant against social change in developing countries.

This criticism, like so much of the criticism surrounding us, is just not true. One could easily arrive at such an opinion through a cursory examination; but a thorough understanding of the Treasury as an advocate of proposals, recommendations, and courses of action reveals not only a deep concern for human welfare in our own country, but for the welfare of human beings in other countries.

The instruments with which we have to work -- the tools of our trade, so to speak -- are instruments called tax, fiscal, and economic policy. When we argue and propose -- as we have done in the past and will continue to do in the future -- for a fair, just, and equitable tax policy, it is precisely because we want the American people -- not just a privileged few, but all -- to be treated fairly, justly, and equitably. When we argue for a tax reduction, as we did in the early Sixties, we are concerned with stimulating our economy toward full employment and enabling more Americans to enjoy the fruits of their labor and the rewards of our technological achievements. When we argue for a tax surcharge -- as we are now doing and have done for the past 12 months -- we do so because we are first and foremost concerned with protecting the purchasing power of our money so that individuals will not suffer personal financial hardships, and social programs will not stop because of exorbitant financial costs.

In carrying our fiscal policy, we are vigilant about preventing disruptions in the money markets which are invariably overcrowded with demands; because any disruption, quick or prolonged, hurts people, harms vital programs in need of financing, and hinders necessary progress. Similarly, our efforts to strengthen the economic structures of other

countries, as well as the financial foundations upon which these structures rest, are designed to help other governments help their people achieve a higher standard of living. In doing this, we are advancing social progress and hindering, if not preventing, social decay and degradation.

I have dwelled momentarily on Treasury matters not primarily because I believe Treasury policy needs clarification or justification, but rather to illustrate the correlation between Treasury's action and our response to the challenges of our times. Such a correlation exists, in one degree or another, in every branch of government and in most of the numerous agencies and bureaus of government. It has to, for government is of the people, by the people, and -- above all else -- for the people.

No government and people have been confronted with as many challenges as we have faced in the last quarter of a century. The leadership of the Western World after World War II came to us not because we coveted it, but rather because we inherited it. It was a legacy we accepted quickly, knowing full well that in our acceptance we were obligating ourselves to fulfill the inherent responsibilities within such a legacy. Part of this legacy obliged us to help keep peace throughout the world, which necessitated heavy world-wide deployment of human resources and material strength. Another part compelled us to help developing countries whose leaders and people believed -- and quite justifiably -- that the richest, largest, and technologically most advanced nation in the world had a moral responsibility to assist those who for so long had been deprived of, or denied, the opportunity to grow.

I think it is a tribute to all Americans not only that we recognize these innumerable challenges from without, but more importantly, that our response as a people was immediate and effective and our contributions permanent to peace and meaningful to mankind.

Concurrent with the challenges that faced us from without, we suddenly were face to face with many challenges arising from within. Many of these challenges were new, resulting from structural changes that took place in our society during and immediately after World War II. Others, however, were the result of our not having fully faced up to problems that had existed in our society for decades, and

toward which we had moved pitifully slow or not at all in finding solutions. Nevertheless, once we recognized the challenges that faced us across the entire spectrum of our activity, we responded as a people and a nation toward their sane and sensible resolution. It's about time, I believe, to recognize how far we have progressed toward the realization of our domestic national goals, how hard we have worked to resolve our problems, and how much closer we have moved, as individual human beings and as a collective nation of some 200 million, toward ameliorating social and legal injustices toward Negroes and other disfranchised and impoverished minorities.

We have had this year far too much derogatory criticism reflected in all media of communication about the imperfections of our society, about our shortcomings as individual human beings, and about our failures as a nation to affect quick solutions to some of the challenges we face -- either because we don't care or because we are incapable of doing anything better. The plain truth of the matter is, however, that the vast majority of Americans are not only conscious of existing imperfections, but are working mightily to correct these imperfections and accelerate our rate of effective response to every challenge confronting us -- at home and overseas.

There are more people working in harmony today in our country toward mutual goals and common concerns than at any other time in our history. This is not an accomplishment of insignificance. It is an incredible achievement.

It would be ordinary if we were few in number, of one religion, of one color, of one nationality. But we're not. The ethnic, cultural and racial threads that form the tapestry we call the United States are complex, delicate, and diversified. We cannot determine precisely where one thread begins, how it weaves its way through this miracle of design, where it needs strengthening, or how it always should be treated.

Our primary interest -- the primary interest of all Americans -- should be to preserve the tapestry and thus to enrich the design. For from the very beginning of our country we have constantly changed the design. Threads have been rewoven and reshaped when necessary. New ones have continuously been added. We have always striven to preserve and enrich the tapestry, never to destroy or damage it. Similarly, we have always striven to fit into this design the separate, ever-changing parts -- those separate, diverse, and varied ethnic and cultural aspirations and desires of our people. We should

be more proud, I believe, of what we have done, are doing, and will do in the immediate future rather than being ashamed of what we have not yet done, or of having handled portions of our endeavors at too slow a speed.

Very few nations have been as conscious as we have been to challenges to our country from without and to our way of life from within. Our brief history has been a succession of responses to these challenges, from these responses we have developed into the most highly industrialized nation in the World, reflecting the highest per capita income and one of the highest standards of living. We have also developed into one of the most humane nations in relation to ourselves and to other peoples of the world.

The challenges from without, which every generation has faced, have been primarily a succession of wars against ideologies that have threatened our survival as a free democratic nation. The challenges from within have been more numerous and far more complex. In one way or another, they all have been related to our efforts as a heterogeneous people to resolve prejudices arising from religious, racial, and cultural differences; to affect a harmonious and profitable relationship between management and labor; to create a physical environment conducive to man's enjoyment of life; to create an educational system and an intellectual environment where the best in man is nurtured; and to safeguard and strengthen the inalienable rights that we are all guaranteed, regardless of race, creed, color, or wealth, under the laws of our land.

We have not always succeeded in our numerous endeavors. We have not always acted promptly, nor as effectively as we might have. We have not always come up with the best possible response. But over the course of some 14 generations, our achievements far outweigh our failures. More importantly, where we have not achieved success, where -- upon reflection -- we recognized past mistakes in judgment, we have always tried to render better judgments, to right previous wrongs, and to improve or eliminate in our thinking and behavior patterns any degrading thought or action that detracts from us as human beings and as a nation dedicated to justice and fair play.

Far too many of our critics today, at home and around the world, view our country and our people like a photographer in love with a 175 millimeter lens. For love of detail, perspective is lost. They see some three million people unemployed, many because they are unemployable; they do not see that

there are more than 75 million people regularly employed and that every year millions of young people are added to our work force -- more than six million, in fact, in the past seven years. They see a crisis when inventories rise or fall, when interest rates climb or drop, when the stock market dips or soars; they forget that for 82 months we have enjoyed a sustained healthy economic growth rate. The benefits of this unprecedented period of prosperity may be seen across the entire spectrum of human activity -- in the rise of personal and corporate income after taxes, in home ownership, in minimum wage protection, steady employment, and greater security through social security.

This type of critic focuses on the high school drop-out, the hippy and the beatnik, all of whom are getting harder to find. He's blind or indifferent to the startling facts that over three-fourths of our young people finish high school, that 40 percent go on to college, that in 1965 our colleges awarded almost one-half million four-year degrees, and that almost 360 thousand students were enrolled in graduate schools working for advanced degrees, and that in the last four years college enrollment has increased by almost two million to its present enrollment of almost six million students. He does not see that some 9 million educationally deprived boys and girls have benefited from the Elementary and Secondary Education Act -- a modern landmark in the history of our educational response to the challenges we faced. Nor does he see that over one-half million physically and mentally disabled citizens have been rehabilitated and given gainful employment.

With his high-powered lens, our critic zooms in on those families living in poverty or straddling the poverty income line. He does not see the progress made in combating and eliminating poverty, where today people are crossing the poverty line more than twice as fast than in the previous four-year period, where more than 5½ million Americans have been lifted above the poverty line, and where close to 3½ million children and young Americans have benefited through such programs as Headstart, Neighborhood Youth Corps and Job Corps Training, and that the diets of nearly two million needy Americans have been improved through the Food Stamp Program.

The critic of civil rights, his perspective limited by the range of his own mental vision, emphasizes existing imperfections while ignoring or deprecating the great accomplishments we have made in the past few years.

What have some of these been? The number of Negro families earning above \$7,000 a year has increased 28 percent -- more than double the number since 1960. In five Southern States, Negro voter registration has increased by over one-half million since the passage of the Voting Rights Act three years ago. The educational gap between Negro and white students is constantly narrowing. Nearly a hundred Negroes have been appointed to high executive and advisory posts in the Federal Government, including the first Negro Supreme Court Justice, the first Negro Cabinet Member, the first Negro member of the Federal Reserve Board, the first Negro woman Federal Judge, and the first Negro woman Ambassador. Perhaps even more important, we have seen within recent days the election of a Negro United States Senator, a Negro Mayor of Cleveland, Ohio, and Gary, Indiana, and a Representative to the Louisiana House of Representatives.

One could go on, but that's quite unnecessary.

The enlightened American knows all this and more.

He knows that we have made, are making, and will make continuing progress in response not only to social challenges, but to challenges facing us in our efforts to eliminate from our physical environment all undesirable features of our culture. So, too, does he know that we are making progress fulfilling in a humane way our world-wide commitments to preserve peace and stability wherever peace and stability are threatened by those who still believe that that which is won by subversion, sabotage, guerrilla warfare, or revolution is more beneficial than that which is honorably attained through peaceful, constructive efforts of mankind.

Nor for one moment, however, are we oblivious or indifferent to the problems we face that require greater attention, more money, and more effective approaches to their solutions. Unfortunately, we have become so used to instant tea and instant coffee that some Americans think

we can come up with instant solutions to complex problems. Let me assure you, there are no easy answers. Instant solutions to complex problems are either unavailable or undesirable.

Americans have always been confident that the answers to the challenges of the present are in the future, rather than in the past. This is why we have come so far, and this is why we will continue to improve and progress -- as individuals and as a collective nation of 200 million people. When we look back, let it be only to see how far we have progressed. When we look ahead, let it be to see how quickly and assuredly we can respond to the challenges we might face.

TREASURY DEPARTMENT
Washington

FOR RELEASE P.M.'S
THURSDAY, DECEMBER 14, 1967

REMARKS OF THE HONORABLE TRUE DAVIS
ASSISTANT SECRETARY OF THE TREASURY
AND UNITED STATES EXECUTIVE DIRECTOR
OF THE INTER-AMERICAN DEVELOPMENT BANK
BEFORE THE CALIFORNIA CLUB
LOS ANGELES, CALIFORNIA
THURSDAY, DECEMBER 14, 1967, 12:00 NOON, PST

I think it is reasonable to state that most Americans expect things to be done quickly and to be done well. Quality of performance and swiftness of execution were concepts we accepted early in our country's history. Regardless of how our national energies were used, or toward which goal they were directed, we endeavored -- and for the most part succeeded -- to keep in balance these two characteristics of thought and action. When necessary, we controlled our impatience to get the job done quickly in order that the job should be done well. We certainly never sacrificed quality of performance for swiftness of execution.

Yet it seems to me lately, especially during the past years, more and more Americans are less concerned with quality of performance. Whether things are done well is currently not as important to many Americans as it once was. What is important to so many today is to solve the problems we face now, to get the jobs

over and done with quickly, to get on with other business and fast. Clean out the urban ghettos -- now! End the war in Vietnam -- now! Gid rid of poverty -- now!

Most of the criticism we have been subjected to in gargantuan proportions during the past year has resulted from the growing inability of people to control such impatience, or to bridle the desire to substitute swiftness of execution for quality of performance. We've become so used to instant tea and instant coffee, to all types of services based on "in by nine, out by five" that we are coming to expect instant solutions to problems that we face. Surely we should realize by now that instant solutions to complex problems are neither available nor desirable. And instant services, particularly in the complex area of social problems, often intensify the problem rather than relieve the stress on those who are its victims.

However loud or numerous the critics, the truth is that we

have made excellent progress during the past seven years toward the resolution of every important problem we have faced. Our progress has not often been as swift as some people desire, nor as expeditious as some conditions might seem to warrant. Nonetheless, great progress has been made.

A great deal of intelligent deliberation during the Sixties in debates over methods of solving our problems was the direct result of a desire to make certain that recommended proposals were the best available in keeping with our concept of quality performance. Nowhere was this more apparent than in our national efforts in the early part of this decade to re-vitalize and strengthen our economy.

May I briefly restate some important facts we were then faced with. Unemployment was intolerably high. Our economy was sick. Business investment was abnormally low. Business had failed to maintain an adequate level of growth, and as a result could not compete in world markets against other industrialized

countries whose rate of growth surpassed ours.

To restore vitality to the private economy it was necessary to free American enterprise from policies that had stifled private investment. It was imperative to provide business incentives that would enable business and industry to expand and grow. One of the first things we did was to revise depreciation guidelines for tax purposes. Then Congress, at the President's request, enacted a tax credit of 7 percent on new investment in machinery and equipment.

Paralleling these important fiscal measures, we also adopted a dual approach to over-all economic policy. A massive, across-the-board income tax reduction increased the general level of demand in the private economy and enhanced the incentives for productive investment. Through wage-price guidelines, we encouraged wage-price restraint so that measures for expanding productivity and aggregate demand would result in rapid and real

growth.

The end result of these and other enlightened policies was the greatest upsurge of economic well-being in the history of the world. These constructive efforts did not come about quickly nor without serious discussions and debate among vitally concerned segments of our society.

Old myths had to die. Skepticism about the effectiveness of proposed uses of tax, fiscal, and economic tools at our disposal had to be overcome. One point we emphasized time and again, both to the Congress and the American people, was that these same tools could and would be used later, if necessary, to control inflationary elements in our economy, to dampen excessive demands for capital goods or investment credit, or slow down economic expansion if we felt that further acceleration would be detrimental to our national interests.

Last year, at the request of President Johnson, the Congress

suspended the special incentives to investment, including the 7 percent tax credit on investment and accelerated tax depreciation procedures. In August of this year, the President asked Congress to enact a temporary surcharge of ten percent on individual tax liabilities, and a similar levy on corporate taxes. He asked that Congress apply these surcharges on corporations effective July 1 of this year and on individuals effective October 1. These two specific requests, I would like to emphasize, recognize that positive use of the tax system is not a one-way street. It embraces the sterner aspect of restraint, as well as the pursuit of tax reduction.

Our Congress listens most attentively to testimony of individuals who are recognized authorities in their fields when they present opinions regarding proposed Congressional legislation. They certainly listened most attentively to the numerous distinguished experts in the fiscal, monetary, and economic areas who

testified in behalf of the President's tax surcharge proposal.

Never have so many recognized authorities -- in areas where unanimity of opinion is a rare phenomenon -- been in such complete agreement regarding the necessity for a surcharge on individual and corporate taxes.

Yet, it is rather ironic that something which should have been done NOW, when it was proposed, or as soon as possible thereafter, has not been done, will not be done this year, and may not be accomplished in sufficient time next year to help alleviate excessive pressures on our economy.

Paralleling Congress' refusal to take positive action in this area, we have witnessed an advance in prices, wage increases in excess of productivity gains, and a rise in interest rates. Inflation is no longer a possibility. Inflation is with us now. When we face it again in 1968 -- in the form of a New Year's present of an old year's problem -- it will remind us of how

negligent we have been, as individuals and as representatives of important segments in our society, about keeping our financial-economic house in order.

We have enjoyed an unprecedented period of prosperity -- 82 consecutive months. Surely none of us wants to see the good results of our individual and collective efforts blown away on the winds of inflation. Perhaps as a New Year's resolution we could declare our willingness to work together in a determined effort to control every inflationary element in our economy. If we agree on this, then let us use the same fiscal and tax instruments in 1968 to relieve tensions in our economy that we used in 1961 and the following years to accêlerate our economy to these unprecedented heights.

One of the first orders of business then would be the enactment of the surcharge on individual and corporation tax liabilities that President Johnson first mentioned to the Congress in

January of this year. To accomplish this, however, will require further positive action on the part of our business-banking-financial fraternity to convince the Congress -- especially in an election year -- of the imperative necessity for such action. Such fiscal action is imperative; otherwise the burden of restraint could fall on the Federal Reserve System with deleterious effects to the mortgage market. The quick passage of this proposed tax surcharge will be of inestimable value in relieving pressure demands on an economy that is now volatile.

Following this, business and labor should make every effort to establish and adhere to a wage-price guideline policy of restraint, comparable to that which served us so admirably from 1961 to this year. Labor and business must accept this as a joint responsibility; -- otherwise there can be no substantial or enduring policy, -- there can be no lasting benefit to our economy.

President Johnson emphasized this point earlier in the month when, speaking before the Business Council, he said:

"Nobody benefits from a wage-price spiral. Labor knows that it does not. You know that, business does not. And surely the American people do not. Yet business says it is labor's responsibility to break the spiral, and labor says it is yours. I say it is everyone's responsibility. It is the responsibility of Government, of labor, and of business."

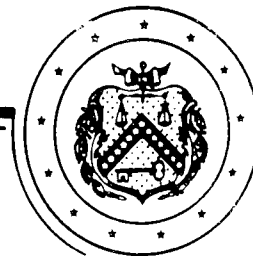
Paralleling our national efforts to create and abide by a meaningful wage-price guideline policy of restraint, every American should exercise individual fiscal restraint in order to help relieve existing pressures on our financial markets, to help restore sound economic growth, and to further protect the strength of our dollar -- which is the world's major currency. The enactment of the proposed tax surcharge, of course, will have considerable effect on private spending, and will materially

aid us in achieving these desirable and essential objectives.

The federal government, meanwhile, will continue, as it has effectively done in the immediate past, to practice fiscal restraint by reducing federal expenditures to an absolute minimum consistent with defense commitments and national domestic requirements.

The problem we face as a nation in controlling or eliminating inflationary elements in our economy is everybody's problem -- housewives as well as trust officers, employees as well as employers, labor as well as management. The strengthening of our dollar should be our nation's highest priority. For upon its continued strength rest all our national endeavors. In this endeavor, each of us should commit himself to the most practical, possible extent. If we do, then we need not worry about the eyes of the rest of the world, now focused upon us, questioning our ability to respond to this new challenge we now face.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 13, 1967

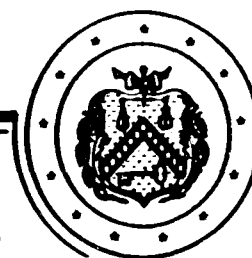
FOR IMMEDIATE RELEASE

TREASURY MARKET TRANSACTIONS IN NOVEMBER

During November 1967, market transactions in direct and guaranteed securities of the Government investment accounts resulted in net purchases by the Treasury Department of \$219,976,500.00

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TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR RELEASE 6:30 P.M.,
Friday, December 15, 1967.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated September 21, 1967, and the other series to be dated December 21, 1967, which were offered on December 11, 1967, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts of 182-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	91-day Treasury bills maturing March 21, 1968		:	182-day Treasury bills maturing June 20, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.723	5.052%	:	97.189 a/	5.560%
Low	98.696	5.159%	:	97.131	5.675%
Average	98.704	5.127% 1/	:	97.139	5.659% 1/

a/ Excepting 1 tender of \$300,000

48% of the amount of 91-day bills bid for at the low price was accepted

27% of the amount of 182-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 22,324,000	\$ 12,324,000	:	\$ 7,138,000	\$ 7,138,000
New York	1,851,604,000	923,644,000	:	1,737,001,000	729,941,000
Philadelphia	44,754,000	22,754,000	:	17,814,000	6,789,000
Cleveland	46,998,000	29,998,000	:	50,122,000	41,022,000
Richmond	10,711,000	10,711,000	:	9,047,000	6,377,000
Atlanta	41,198,000	32,158,000	:	35,846,000	25,846,000
Chicago	231,954,000	129,002,000	:	225,903,000	98,953,000
St. Louis	39,294,000	36,474,000	:	29,792,000	23,192,000
Minneapolis	25,183,000	19,623,000	:	23,502,000	12,102,000
Kansas City	25,471,000	23,471,000	:	18,588,000	17,588,000
Dallas	19,842,000	14,842,000	:	14,299,000	9,099,000
San Francisco	364,678,000	245,698,000	:	129,060,000	21,963,000
TOTALS	\$2,724,011,000	\$1,500,699,000 b/	:	\$2,298,112,000	\$1,000,010,000 c/

/ Includes \$208,665,000 noncompetitive tenders accepted at the average price of 98.704

/ Includes \$135,707,000 noncompetitive tenders accepted at the average price of 97.139

/ These rates are on a bank discount basis. The equivalent coupon issue yields are 5.28% for the 91-day bills, and 5.92% for the 182-day bills.

TREASURY DEPARTMENT
and
FEDERAL RESERVE BOARD

FOR IMMEDIATE RELEASE

Washington, D.C.
December 16, 1967

STATEMENT BY THE HONORABLE HENRY H. FOWLER,
SECRETARY OF THE TREASURY, AND
THE HONORABLE WILLIAM McCHESNEY MARTIN,
CHAIRMAN OF THE FEDERAL RESERVE BOARD

The Secretary of the Treasury and the Chairman of the Federal Reserve Board today issued the following statement:

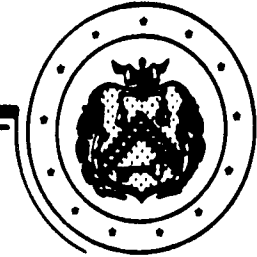
The United States stands firm in its determination to maintain the gold value of the dollar.

The central banks of Belgium, Germany, Italy, the Netherlands, Switzerland, and the United Kingdom support this position and continue to participate fully with the United States in policies and practices in support of the price of gold at \$35 an ounce.

The operation of the London gold market will continue unchanged.

The United States authorities and the European central banks concerned endorse this position unanimously and are cooperating in the interest of maintaining the stability of the international monetary system.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 18, 1967

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of 2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing December 28, 1967, in the amount of 2,401,593,000, as follows:

91-day bills (to maturity date) to be issued December 28, 1967, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated September 28, 1967, and to mature March 28, 1968, originally issued in the amount of 1,000,271,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated December 28, 1967, and to mature June 27, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard Time, Friday, December 22, 1967. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

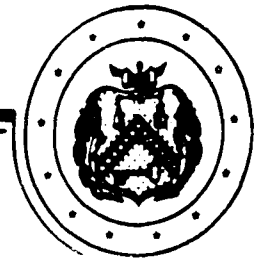
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on December 28, 1967, in cash or other immediately available funds or in a like face amount of Treasury bills maturing December 28, 1967. Cash and exchange tender will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 18, 1967

FOR IMMEDIATE RELEASE

TREASURY'S MONTHLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$1,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing December 31, 1967, in the amount of \$1,401,121,000, as follows:

272-day bills (to maturity date) to be issued January 2, 1968, in the amount of \$500,000,000, or thereabouts, representing an additional amount of bills dated September 30, 1967, and to mature September 30, 1968, originally issued in the amount of \$1,000,206,000, the additional and original bills to be freely interchangeable.

366-day bills, for \$1,000,000,000, or thereabouts, to be dated December 31, 1967, and to mature December 31, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Tuesday, December 26, 1967. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. (Notwithstanding the fact that the one-year bills will run for 366 days, the discount rate will be computed on a bank discount basis of 360 days, as is currently the practice on all issues of Treasury bills.) It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders

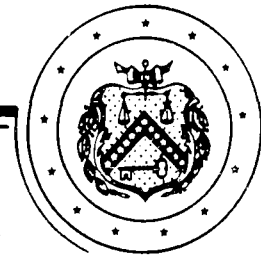
from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on January 2, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing December 31, 1967. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 21, 1967

FOR IMMEDIATE RELEASE

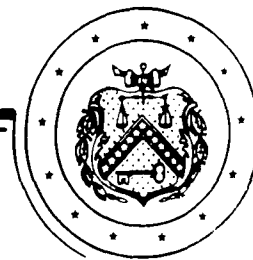
UNITED STATES AND MEXICO SIGN \$100 MILLION EXCHANGE AGREEMENT

Secretary of the Treasury Henry H. Fowler and the Ambassador of Mexico, Hugo B. Margain, today signed a \$100,000,000 Exchange Stabilization Agreement between the United States Treasury, the Bank of Mexico, and the Government of Mexico, replacing a similar agreement signed in December, 1965 which expires at the end of 1967. The 1965 agreement was in the amount of \$75,000,000 and was increased to \$100,000,000 in May, 1967.

The Agreement signed today represents a continuation of stabilization arrangements between the United States and Mexico which have been in effect since 1941, and have proved beneficial to the financial relationships between the two countries. The agreement provides reciprocal swap facilities available for use both by Mexico and by the United States. These swap facilities strengthen the ability of the financial authorities to cooperate effectively and to conduct such stabilization operations as may be desirable from time to time to promote stable and orderly conditions in the exchange markets.

The new agreement will be effective during the two-year period ending December 31, 1969.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 22, 1967

FOR IMMEDIATE RELEASE

UNITED STATES INCOME TAX CONVENTIONS WITH TRINIDAD AND TOBAGO AND WITH CANADA ENTER INTO FORCE

The Treasury Department has announced that instruments of ratification have been exchanged of an income tax convention between the United States and Trinidad and Tobago and of a supplementary convention amending the United States-Canada income tax convention.

The convention with Trinidad and Tobago was brought into force December 19, 1967, and the supplementary convention with Canada took effect on December 20, 1967.

The convention with Trinidad and Tobago is an interim agreement while discussions between that country and the United States continue on an income tax convention of general application. The convention deals only with the rate of withholding tax on distributed profits.

The convention provides that dividends paid by a corporation of one of the contracting states to residents in the other contracting state shall be subject to a withholding tax rate of 25 percent, rather than the statutory rate of 30 percent which applies in both countries. However, the withholding rate is reduced to 5 percent on dividends paid by a corporation of one state to a corporation of the other state which owns 10 percent or more of the outstanding voting stock of the paying corporation. In addition, the withholding tax imposed by Trinidad and Tobago on the profits paid to its home office by a permanent establishment of a U.S. corporation is also reduced to 5 percent.

The supplementary convention with Canada eliminates an unintended tax privilege which resulted from the interaction of Canadian tax law and the provisions of the tax treaty between the United States and Canada.

The treaty provides that a company organized in Canada and receiving investment income from the United States is subject to a 15 percent U.S. withholding tax on such income rather than the usual 30 percent. However, a company organized under

Canadian law but deriving its income from outside Canada is exempt from Canadian taxes under Canadian law if the company is managed or controlled outside Canada. Canadian legislation of a few years ago eliminates this tax-exempt status for Canadian corporations subsequently created, but does not apply retroactively. This combination of provisions permits such a company created prior to that legislation to be used by third country residents to avoid U. S. taxes.

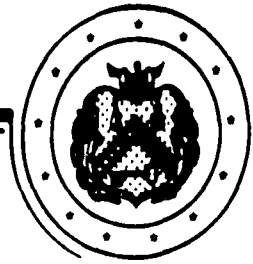
The supplementary convention eliminates this tax haven situation by denying the reduced rate of U.S. withholding tax on investment income under the treaty to a corporation which is exempt from tax in Canada because it is regarded as not being resident in Canada.

The 1945 income tax convention between the United States and the United Kingdom, as modified by various supplementary protocols, was extended in its application to Trinidad and Tobago as of January 1, 1959. Trinidad and Tobago became independent in 1962, and, in 1965, notified the U.S. Government of its intention to terminate the application of the 1945 convention, as modified.

Discussions on the pending convention were begun in October 1965. It was signed on December 22, 1966, and submitted to the Senate on February 23, 1967.

The supplementary convention with Canada was signed on October 25, 1966, and submitted to the Senate on January 25, 1967. It will supplement the existing 1942 convention between the United States and Canada, as modified by the supplementary conventions of 1950 and 1956.

TREASURY DEPARTMENT



WASHINGTON, D.C.

December 22, 1967

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing January 4, 1968, in the amount of \$2,400,723,000, as follows:

91-day bills (to maturity date) to be issued January 4, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated October 5, 1967, and to mature April 4, 1968, originally issued in the amount of \$1,000,305,000, the additional and original bills to be freely interchangeable.

183-day bills, for \$1,000,000,000, or thereabouts, to be dated January 4, 1968, and to mature July 5, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Friday, December 29, 1967. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

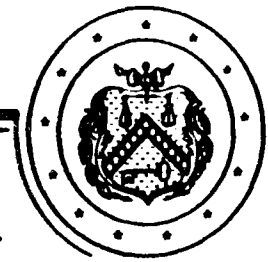
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on January 4, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing January 4, 1968. Cash and exchange tender will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR RELEASE 6:30 P.M.,
Friday, December 22, 1967.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated September 28, 1967, and the other series to be dated December 28, 1967, which were offered on December 18, 1967, were opened at the Federal Reserve Banks today. Tenders were invited for 1,500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	91-day Treasury bills maturing March 28, 1968		:	182-day Treasury bills maturing June 27, 1968	
	Price	Approx. Equiv. Annual Rate		Price	Approx. Equiv. Annual Rate
High	98.748	4.953%	:	97.224 a/	5.491%
Low	98.730	5.024%	:	97.201	5.536%
Average	98.739	4.989% 1/	:	97.212	5.515% 1/

a/ Excepting 1 tender of \$1,000,000

10% of the amount of 91-day bills bid for at the low price was accepted

38% of the amount of 182-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 19,468,000	\$ 9,468,000	:	\$ 14,786,000	\$ 3,536,000
New York	1,786,994,000	1,117,994,000	:	1,526,280,000	807,780,000
Philadelphia	31,933,000	14,933,000	:	13,828,000	5,470,000
Cleveland	57,239,000	39,439,000	:	38,362,000	20,688,000
Richmond	11,493,000	9,593,000	:	17,431,000	8,361,000
Atlanta	35,773,000	27,473,000	:	24,275,000	14,408,000
Chicago	265,417,000	131,717,000	:	225,534,000	61,431,000
St. Louis	38,431,000	34,431,000	:	29,827,000	19,587,000
Minneapolis	11,107,000	10,107,000	:	9,416,000	4,316,000
Kansas City	31,902,000	25,902,000	:	30,910,000	21,180,000
Dallas	23,578,000	13,678,000	:	27,160,000	12,860,000
San Francisco	135,152,000	65,282,000	:	101,945,000	20,495,000

TOTALS \$2,448,487,000 \$1,500,017,000 b/ \$2,059,754,000 \$1,000,112,000 c/

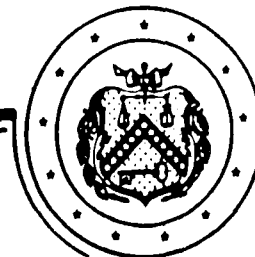
Includes \$212,756,000 noncompetitive tenders accepted at the average price of 98.739

Includes \$150,426,000 noncompetitive tenders accepted at the average price of 97.212

These rates are on a bank discount basis. The equivalent coupon issue yields are

5.14% for the 91-day bills, and 5.77% for the 182-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR RELEASE 6:30 P.M.,
 Tuesday, December 26, 1967.

RESULTS OF TREASURY'S MONTHLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated September 30, 1967, and the other series to be dated December 31, 1967, which were offered on December 18, 1967, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,000,000,000, or thereabouts, of 272-day bills and for \$1,000,000,000, or thereabouts, of 366-day bills. The details of the two series are as follows:

PERCENTAGE OF ACCEPTED NONCOMPETITIVE BIDS:	272-day Treasury bills maturing September 30, 1968		:	366-day Treasury bills maturing December 31, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	95.833	5.515%	:	94.408	5.500%
Low	95.777	5.589%	:	94.307	5.600%
Average	95.803	5.555% <u>1/</u>	:	94.364	5.544% <u>1/</u>

56% of the amount of 272-day bills bid for at the low price was accepted
 81% of the amount of 366-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 132,000	\$ 132,000	:	\$ 10,501,000	\$ 10,501,000
New York	877,256,000	361,376,000	:	1,148,138,000	728,658,000
Philadelphia	15,421,000	9,541,000	:	11,552,000	7,602,000
Cleveland	14,002,000	14,002,000	:	33,258,000	33,258,000
Richmond	575,000	575,000	:	2,912,000	2,912,000
Atlanta	8,404,000	3,404,000	:	19,466,000	19,466,000
Chicago	106,131,000	49,931,000	:	140,304,000	99,304,000
St. Louis	10,480,000	7,480,000	:	17,515,000	17,325,000
Minneapolis	14,825,000	14,825,000	:	15,069,000	15,069,000
Kansas City	1,728,000	1,728,000	:	4,399,000	4,399,000
Dallas	11,400,000	7,400,000	:	11,692,000	10,692,000
San Francisco	76,726,000	29,766,000	:	78,336,000	50,956,000
TOTALS	\$1,137,080,000	\$ 500,160,000 <u>a/</u>		\$1,493,142,000	\$1,000,142,000 <u>b/</u>

Includes \$16,945,000 noncompetitive tenders accepted at the average price of 95.803
 Includes \$46,543,000 noncompetitive tenders accepted at the average price of 94.364
 These rates are on a bank discount basis. The equivalent coupon issue yields are
 5.84% for the 272-day bills, and 5.89% for the 366-day bills.



WASHINGTON, D.C.

December 28, 1967

FOR IMMEDIATE RELEASE

PROTOCOL TO THE UNITED STATES - BELGIUM
INCOME TAX CONVENTION EXTENDED

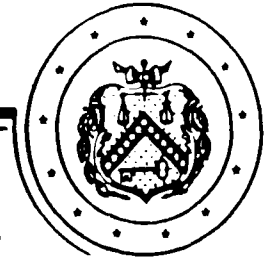
The Treasury Department today announced that the United States and Belgium have agreed, in an exchange of notes, to extend the protocol of May 21, 1965, amending the convention for the avoidance of double taxation of income.

The protocol will remain in effect for income of calendar years or taxable years beginning after December 31, 1967, but ending before January 1, 1971. It will apply to payment of taxes payable at source before January 1, 1971.

The present income tax convention between Belgium and the United States was signed October 28, 1948 and has been amended three times, by the supplementary conventions of September 9, 1952 and August 22, 1957, and by the protocol of May 21, 1965, which further amended the convention in light of modifications in the Belgian income tax law.

The exchange of notes keeps the protocol in force through 1970, by which time it is expected that a new income tax convention will have been negotiated.

TREASURY DEPARTMENT



WASHINGTON, D.C.

RELEASE 6:30 P.M.,
Friday, December 29, 1967.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated October 5, 1967, and the other series to be dated January 4, 1968, which were offered on December 22, 1967, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 183-day bills. The details of the two series are as follows:

PERCENTAGE OF ACCEPTED NONCOMPETITIVE BIDS:	91-day Treasury bills maturing April 4, 1968		:	183-day Treasury bills maturing July 5, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.722	5.056%	:	97.168	5.571%
Low	98.700	5.143%	:	97.146	5.614%
Average	98.710	5.103% <u>1/</u>	:	97.157	5.593% <u>1/</u>

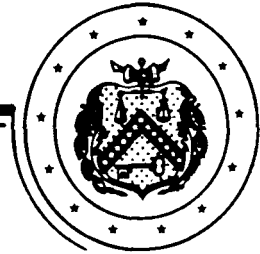
40% of the amount of 91-day bills bid for at the low price was accepted
1% of the amount of 183-day bills bid for at the low price was accepted

APPLIED TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Atlanta	\$ 19,126,000	\$ 9,126,000	:	\$ 14,321,000	\$ 4,321,000
New York	1,690,735,000	1,084,135,000	:	1,477,372,000	759,519,000
Philadelphia	32,682,000	20,682,000	:	18,992,000	7,789,000
Pittsburgh	33,461,000	22,461,000	:	56,346,000	25,156,000
Richmond	9,651,000	9,651,000	:	4,112,000	3,812,000
St. Louis	41,489,000	33,129,000	:	26,922,000	13,772,000
San Francisco	261,894,000	125,934,000	:	248,191,000	118,189,000
St. Louis	37,359,000	30,359,000	:	33,973,000	13,923,000
Minneapolis	23,119,000	17,319,000	:	15,704,000	4,704,000
Cincinnati	26,214,000	22,214,000	:	15,808,000	11,793,000
St. Louis	12,021,000	12,021,000	:	11,212,000	11,212,000
San Francisco	188,041,000	113,241,000	:	129,263,000	25,694,000
TOTALS	\$2,375,792,000	\$1,500,272,000 <u>a/</u>		\$2,052,216,000	\$1,000,084,000 <u>b/</u>

Includes \$215,043,000 noncompetitive tenders accepted at the average price of 98.710
Includes \$125,505,000 noncompetitive tenders accepted at the average price of 97.157
These rates are on a bank discount basis. The equivalent coupon issue yields are 5.26% for the 91-day bills, and 5.85% for the 183-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 3, 1968

FOR IMMEDIATE RELEASE
WEDNESDAY, JANUARY 3, 1968

INDUSTRY-GOVERNMENT SPECIAL TASK FORCE ON TRAVEL RESCHEDULES FIRST ORGANIZATION SESSION FOR JANUARY 11 IN WASHINGTON

The first meeting of the Industry-Government Special Task Force on Travel will be held at the Treasury in Washington on January 11, Task Force chairman Robert M. McKinney announced today.

The new January 11 date for the Task Force's first meeting--which was originally scheduled for January 16--was prompted by President Johnson's directive, at his New Year's Day press conference, that the Task Force submit an interim report in 45 days--by February 15--and its final report within 90 days--by April 1.

Pointing out that the 1968 travel deficit will exceed \$2 billion, the President called for a \$500 million deficit reduction through an intensified program to attract more visitors to the United States, and to encourage Americans to refrain from non-essential travel outside the Western Hemisphere for the next two years.

The President then directed the Task Force "to report within 45 days on the immediate measures that can be taken, and to make its long-term recommendations within 90 days."

The Task Force members are: Robert M. McKinney, Santa Fe, N.M., chairman; William Bernbach, New York, N.Y.; Professor Daniel J. Boorstin, Chicago, Ill.; Governor John A. Burns, Honolulu, Hawaii; Edward E. Carlson, Seattle, Wash.; Howard L. Clark, New York, N.Y.; Arthur Frommer, New York, N.Y.; Frank Hildebrand, Austin, Texas; Frank N. Ikard, New York, N.Y.; John H. Johnson, Chicago, Ill.; Willis G. Lipscomb, New York, N.Y.; Winston V. Morrow, Jr., Garden City, N.Y.; William D. Patterson, New York, N.Y.; Gerald Shapiro, New York, N.Y.; Lew R. Wasserman, Universal City, Calif.; Anthony M. Solomon, Department of State; Winthrop Knowlton, Department of the Treasury; Harry M. Shooshan, Department of the Interior; Donald G. Agger, Department of Transportation; Charles S. Murphy, Civil Aeronautics Board; Andrew F. Brimmer, Federal Reserve System; and John W. Black, Department of Commerce.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

January 3, 1968

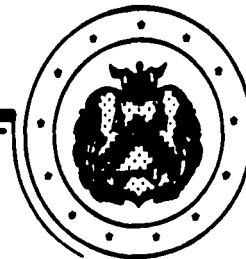
FOR IMMEDIATE RELEASE

The Treasury today announced that it has transferred \$450 million in gold from its Treasurer of the United States account to its Exchange Stabilization Fund. The transfer was made on December 28, 1967. The gold was used in part in December to make settlement for the United States' share in support operations in the London gold market in December and the balance, as is customary from time to time, to provide the Exchange Stabilization Fund with additional resources to meet future contingencies.

The total of such transfers in 1967 was \$1,175 million of which \$925 million was subsequent to the sterling devaluation. The transfers this year were approximately twice that of last year but one-half billion less than that in 1965.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

January 3, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing January 11, 1968, in the amount of \$2,501,746,000, as follows:

91-day bills (to maturity date) to be issued January 11, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated October 13, 1967, and to mature April 11, 1968, originally issued in the amount of \$1,000,840,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated January 11, 1968, and to mature July 11, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard Time, Monday, January 8, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

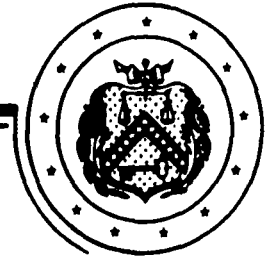
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on January 11, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing January 11, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained at any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 3, 1968

IMMEDIATE RELEASE

AUCTION OF TAX ANTICIPATION BILLS

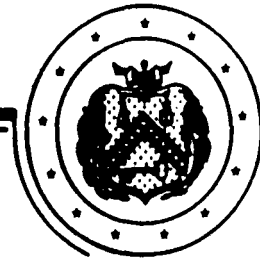
The Treasury Department announced today the forthcoming auction of \$2.5 billion of tax anticipation bills maturing in June 1968. The bills are in addition to the \$3 billion of June tax bills already outstanding.

The bills will be auctioned on Tuesday, January 9, for payment on Monday, January 15. Commercial banks may make payment for the bills by crediting Treasury and loan accounts.

The bills mature on June 24, 1968, but may be used at face value in payment of Federal taxes due on June 15, 1968.

F-1120

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 3, 1968

R IMMEDIATE RELEASE

TREASURY OFFERS ADDITIONAL \$2.5 BILLION IN JUNE TAX BILLS

The Treasury Department, by this public notice, invites tenders for \$500,000,000, or thereabouts, of 161-day Treasury bills (to maturity date), to be issued January 15, 1968, on a discount basis under competitive and non-competitive bidding as hereinafter provided. The bills of this series will be designated Tax Anticipation Series and represent an additional amount of bills authorized October 9, 1967, to mature June 24, 1968, originally issued in the amount of \$3,005,517,000. The additional and original bills will be freely interchangeable. They will be accepted at face value in payment of income taxes due on June 15, 1968, and to the extent they are not presented for this purpose the face amount of these bills will be payable without interest at maturity. Taxpayers desiring to apply these bills in payment of June 15, 1968, income taxes may submit the bills to a Federal Reserve Bank or Branch or to the Office of the Treasurer of the United States, Washington, not more than fifteen days before that date. In the case of bills submitted in payment of income taxes of a corporation they will all be accompanied by a duly completed Form 503 and the office receiving these bills will effect the deposit on June 15, 1968. In the case of bills submitted in payment of income taxes of all other taxpayers, the office receiving the bills will issue receipts therefor, the original of which the taxpayer shall submit on or before June 15, 1968, to the District Director of Internal Revenue for the district in which such taxes are payable. The bills will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Tuesday, January 9, 1968. Tenders will also be received at the Treasury Department, Washington. Each tender must be for an amount in multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractional parts of a cent may not be used. It is urged that tenders be made on the printed forms and returned in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

All bidders are required to agree not to purchase or to sell, or to make any agreements with respect to the purchase or sale or other disposition of any bills of this issue at a specific rate or price, until after one-thirty p.m., Eastern Standard time, Tuesday, January 9, 1968.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for \$400,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids. Payment of accepted tenders at the prices offered must be made or completed at the Federal Reserve Bank in cash or other immediately available funds on January 15, 1968, provided, however, any qualified depository will be permitted to make payment by credit in its Treasury tax and loan account for Treasury bills allotted to it for itself and its customers up to any amount for which it shall be qualified in excess of existing deposits when so notified by the Federal Reserve Bank of its District.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice, prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 4, 1968

FOR IMMEDIATE RELEASE

STUART E. SEIGEL NAMED TO TREASURY POST

Treasury Secretary Henry H. Fowler today announced the appointment of Stuart E. Seigel as Associate Tax Legislative Counsel.

Mr. Seigel, who has been with the Office of Tax Legislative Counsel since 1965, succeeds Thomas A. Troyer, who recently resigned to join the Washington law firm of Caplin and Drysdale.

Mr. Seigel, 34, was born in New York City. He received a B.S. degree from New York University in 1953, and an LL.B. from New York University Law School in 1957. While at the N.Y.U. Law School, he was Associate Editor of the Law Review.

After finishing his schooling in New York, Mr. Seigel came to Washington to work in the Chief Counsel's Office of the Internal Revenue Service. While there he attended the Evening Division of the Georgetown University School of Law, where he received a Master of Laws in Taxation in 1960.

For more than eight years the appointee worked in the Office of Chief Counsel, I.R.S., where he was Attorney-Advisor, and a Trial Attorney, representing the Government in tax cases before the Tax Court of the United States. Mr. Seigel joined the staff of the Tax Legislative Counsel, Main Treasury, in October, 1965.

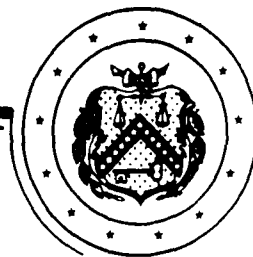
The Office of Tax Legislative Counsel furnishes the Assistant Secretary for Tax Policy and other policy-making officials of the Department with legal advice and analysis with respect to tax matters, and assists in the development of tax legislation.

The appointee is a member of the American Bar Association, the Federal Bar Association and the American Judicature Society.

Mr. Seigel is married to the former Joyce R. Meyers, of New York. They have three children, Charles, Lee and Suzanne, and make their home at 412 Sisson Court, Silver Spring, Maryland.

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REASURY DEPARTMENT



WASHINGTON, D.C.

January 4, 1968

FOR IMMEDIATE RELEASE

MINT MARKS RESTORED TO COINS

The 1968 United States coins, which carry mint marks for the first time since the 1964 dated coins, were shown today at the Denver Mint. Miss Eva Adams, Director of the Mint, and Mrs. Marian Rossmiller, Superintendent of the Denver Mint, presided at ceremonies which included the inspection of a specimen proof coin set bearing the San Francisco mint mark.

This marks the first time in history that mint marks will appear on proof coins. Mint marks have not been on United States coins since passage of the Coinage Act of 1965 which prohibited the use of mint marks because of the coin shortage. In 1967 the Congress repealed this prohibition thereby authorizing the restoration of mint marks. Mint marks are important to the operation of the Mint because they provide an effective control over the coinage by identifying the issuing institution.

To achieve uniformity, Miss Adams has directed that all mint marks be placed on the obverse (face) of the coins. The mint mark on the cent, nickel, dime and quarter will be to the right of the portraits, while on the half dollar it will appear in the center under the portrait of the late President Kennedy.

Coins produced at the Denver Mint will carry a small "D" mint mark, and the proof coins struck at the San Francisco Assay Office will bear a small "S" mint mark. In the past, proof coins were made at Philadelphia and bore no mint marks. Traditionally, coins made at the Philadelphia Mint are distinguished by the absence of mint marks.

Proof coin sets, which consist of a specially made half dollar, quarter, dime, nickel and cent, have not been produced since 1964. Their production was discontinued at the end of that year so that full production facilities would be given over to making regular issue coinage to alleviate the existing coin shortage.

Beginning late in 1965, however, conditions permitted the production of special mint sets at the San Francisco Assay Office. Although these sets are better in quality than any of the regular uncirculated coin sets previously packaged by the Mint, they are not of proof quality. The manufacture of these sets has been discontinued with the resumption of the production of proof coins.

Miss Adams said that "during 1967 the Mint facilities produced over seven billion coins, and in 1966 more than nine billion were produced, thereby completely eliminating the coin shortage except for the half dollar." She added that "the half dollar is now beginning to circulate more freely in various sections of the country and is on the way to resuming its normal commercial function as a medium of exchange."

The 1968 coins will enter circulation through normal channels -- the Mints make distribution of regular issue coin directly to the Federal Reserve banks and branches, and it is the requisitions of the commercial banks upon them for supplies that determine the amounts of the shipments into the various areas.

Requests for the 1968 proof coin sets should be directed to the Officer in Charge, United States Assay Office, Numismatic Service, 350 Duboce Avenue, San Francisco, California 94102. The price of \$5.00 per set includes first class registered mail fee. The maximum number of sets per order is 20 sets.

TREASURY DEPARTMENT



WASHINGTON, D.C

January 5, 1968

FOR IMMEDIATE RELEASE

INDUSTRIAL PAYROLL SAVINGS COMMITTEE MEETS JANUARY 9 WITH SECRETARY FOWLER

The U. S. Industrial Payroll Savings Committee, made up of top executives of American business and industry appointed by Secretary of the Treasury Henry H. Fowler, meets in Washington on Tuesday, January 9, to review program accomplishments in 1967 and to formulate plans for the 1968 campaign.

Secretary Fowler and other Administration leaders will meet with the Committee. William P. Gwinn, President and Chief Administrative Officer, United Aircraft Corp., East Hartford, Conn., is to be installed as 1968 Chairman, succeeding 1967 Chairman Daniel J. Haughton, Chairman of the Board, Lockheed Aircraft Corp., Burbank, Calif.

Haughton is to preside over the meeting, to be held in the Benjamin Franklin Room of the State Department's Diplomatic Functions Suite, with a reception at 6:00 and dinner at 7:00.

Other speakers on the day's program include Under Secretary of the Treasury for Monetary Affairs, Frederick L. Deming, and Glen R. Johnson, National Director of the Treasury's Savings Bond Division. There will also be a special message from President Lyndon B. Johnson.

During the past year, the Committee, members of which led Payroll Savings activities in the major industrial and geographic areas of the country, spearheaded a drive "For Freedom's Future" in which 2,606,640 new payroll savers or savers who increased their purchases were signed up for the regular purchase of Savings Bonds and Freedom Shares. Of these, 716,000 were from within companies of the Committee members. In terms of dollar volume, the Committee's accomplishment comes to \$3.5 billion.

A list of the 1967 Committee and of the new members who will serve on the 1968 Committee is attached.

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U. S. INDUSTRIAL PAYROLL SAVINGS COMMITTEE
1968 MEMBERS

Ex Officio General Chairman

Honorable Henry H. Fowler
Secretary of the Treasury

1968 Chairman

William P. Gwinn
President
United Aircraft Corporation
East Hartford, Connecticut

1963-1967 Chairmen

Daniel J. Haughton
Chairman of the Board
Lockheed Aircraft Corporation
Burbank, California
(1967 Chairman)

Lynn A. Townsend
Chairman of the Board
Chrysler Corporation
Detroit, Michigan
(1966 Chairman)

Dr. Elmer W. Engstrom
Chairman of the Executive
Committee
Radio Corporation of America
New York, New York
(1965 Chairman)

Frank R. Milliken
President
Kennecott Copper Corporation
New York, New York
(1964 Chairman)

Harold S. Geneen
Chairman and President
International Telephone and
Telegraph Corporation
New York, New York
(1963 Chairman)

Geographic Members

Charles F. Adams
Chairman of the Board
Raytheon Company
Lexington, Massachusetts

J. Paul Austin
President
The Coca-Cola Company
Atlanta, Georgia

Edd H. Bailey
President
Union Pacific Railroad Company
Omaha, Nebraska

Robinson F. Barker
Chairman of the Board
PPG Industries
Pittsburgh, Pennsylvania

Roy C. Echols
President
Indiana Bell Telephone Company
Indianapolis, Indiana

Francis E. Ferguson
President
The Northwestern Mutual Life
Insurance Company
Milwaukee, Wisconsin

Robert O. Fickes
President and Chairman
Philco-Ford Corporation
Philadelphia, Pennsylvania

Richard A. Goodson
President
Southwestern Bell Telephone
Company
St. Louis, Missouri

J. E. Gosline
President
Standard Oil Company
of California
San Francisco, California

Fred L. Hartley
President
Union Oil Company of California
Los Angeles, California

Sherman R. Knapp
President
Northeast Utilities Service
Company
Hartford, Connecticut

John F. Lynch
President
La Gloria Oil and Gas Company
Houston, Texas

Wilfred D. MacDonnell
President
Kelsey-Hayes Company
Romulus, Michigan

Donald A. McMahon
President
Monroe International, Inc.
Orange, New Jersey

Robert D. O'Brien
Chairman of the Board
Pacific Car and Foundry Company
Renton, Washington

Robert T. Person
President
Public Service Company of Colorado
Denver, Colorado

Vernon R. Rawlings
Vice President
Martin-Marietta Corporation
Baltimore, Maryland

Robert W. Reneker
President
Swift & Company
Chicago, Illinois

Frederick W. Roth
President in Charge of
Operations
Gould-National Batteries, Inc.
St. Paul, Minnesota

Marion Sadler
President
American Airlines, Inc.
New York, New York

William C. Safford
President
The Western and Southern Life
Insurance Company
Cincinnati, Ohio

Horace A. Shepard
President
TRW Inc.
Cleveland, Ohio

Clyde Skeen
President
Ling-Temco-Vought, Inc.
Dallas, Texas

Industry Members

William R. Adams
President
St. Regis Paper Company
New York, New York

J. L. Atwood
President
North American Rockwell Corp.
El Segundo, California

Orville E. Beal
President
The Prudential Insurance Company
of America
Newark, New Jersey

D. C. Burnham
President
Westinghouse Electric Corporation
Pittsburgh, Pennsylvania

L. du P. Copeland
Chairman of the Board
E. I. du Pont de Nemours
& Company, Inc.
Wilmington, Delaware

Edward S. Donnell
President
Montgomery Ward and Company
Chicago, Illinois

Ben S. Gilmer
President
American Telephone and Telegraph
Company
New York, New York

James M. Hait
Chairman
FMC Corporation
San Jose, California

Herbert E. Harper
President
Public Service Coordinated Transport
Maplewood, New Jersey

Mr. John D. Harper
President
Aluminum Company of America
Pittsburgh, Pennsylvania

Honorable Richard J. Hughes
Governor of New Jersey
Trenton, New Jersey

W. Maxey Jarman
Chairman
Genesco, Inc.
Nashville, Tennessee

Byron Jay
President
The Great Atlantic & Pacific
Tea Company, Inc.
New York, New York

David M. Kennedy
Chairman of the Board
Continental Illinois National
Bank and Trust Company of
Chicago
Chicago, Illinois

Joseph L. Lanier
Chairman
West Point-Pepperell, Inc.
West Point, Georgia

T. V. Learson
President
International Business
Machines Corporation
Armonk, New York

John P. Levis
Chairman
Owens-Illinois, Inc.
Toledo, Ohio

Michael R. McEvoy
President
Sea-Land Service, Inc.
Elizabeth, New Jersey

Louis W. Menk
President
Northern Pacific Railway Company
St. Paul, Minnesota

Robert L. Milligan
Chairman of the Board
Pure Oil Company
Palatine, Illinois

Thomas F. Patton
Chairman and President
Republic Steel Corporation
Cleveland, Ohio

William Wood Prince
President
Armour and Company
Chicago, Illinois

James M. Roche
Chairman of the Board
General Motors Corporation
New York, New York

Watson F. Tait, Jr.
Chairman of the Board
Public Service Electric
and Gas Company
Newark, New Jersey

Charles C. Tillinghast, Jr.
President
Trans World Airlines, Inc.
New York, New York

Jack Valenti
President
Motion Picture Association
of America, Inc.
Washington, D. C.

George R. Vila
Chairman and President
Uniroyal, Inc.
New York, New York

U. S. INDUSTRIAL PAYROLL SAVINGS COMMITTEE
1967 MEMBERS

Ex Officio General Chairman

Honorable Henry H. Fowler
Secretary of the Treasury

Geographic Members

Frank Armour, Jr.
Vice Chairman of the Board
H. J. Heinz Company
Pittsburgh, Pennsylvania

Allen G. Barry
President
New England Telephone
& Telegraph Company
Boston, Massachusetts

John B. Bunker
President
Holly Sugar Company
Colorado Springs, Colorado

Norton Clapp
Chairman of the Board
Weyerhaeuser Company
Tacoma, Washington

J. E. Countryman
President
Del Monte Corporation
San Francisco, California

Charles H. Dolson
President
Delta Air Lines, Inc.
Atlanta, Georgia

Chairman

Daniel J. Haughton
Chairman of the Board
Lockheed Aircraft Corporation
Burbank, California

Robert O. Fickes
President & Chairman
Philco-Ford Corporation
Philadelphia, Pennsylvania

Philip O. Geier, Jr.
President
The Cincinnati Milling
Machine Company
Cincinnati, Ohio

Richard A. Goodson
President
Southwestern Bell Telephone Co.
St. Louis, Missouri

Paul A. Gorman
President
Western Electric Company, Inc.
New York, New York

William P. Gwinn
President
United Aircraft Corporation
East Hartford, Connecticut

Gordon Hanes
President
Hanes Corporation
Winston-Salem, North Carolina

John F. Lynch
President
La Gloria Oil and Gas Company
Houston, Texas

G. Barron Mallory
President
P. R. Mallory & Company, Inc.
Indianapolis, Indiana

Arjay Miller
President
Ford Motor Company
Dearborn, Michigan

Thomas F. Patton
Chairman and President
Republic Steel Corporation
Cleveland, Ohio

William J. Quinn
President
Burlington Lines
Chicago, Illinois

Vernon R. Rawlings
Vice President
Martin-Marietta Corporation
Baltimore, Maryland

Frederick W. Roth
President
Gould-National Batteries, Inc.
St. Paul, Minnesota

Clyde Skeen
President
Ling-Temco-Vought, Inc.
Dallas, Texas

Robert S. Stevenson
Chairman
Allis-Chalmers Manufacturing Co.
Milwaukee, Wisconsin

W. A. Strauss
President
Northern Natural Gas Company
Omaha, Nebraska

Watson F. Tait, Jr.
Chairman of the Board
Public Service Electric
& Gas Company
Newark, New Jersey

Charles B. Thornton
Chairman of the Board
Litton Industries, Inc.
Beverly Hills, California

Industry Members

Harlee Branch, Jr.
President
Southern Company
Atlanta, Georgia

Donald C. Burnham
President
Westinghouse Electric Corp.
Pittsburgh, Pennsylvania

Gilbert W. Fitzhugh
Chairman of the Board
Metropolitan Life Insurance Co.
New York, New York

Ben S. Gilmer
President
American Telephone and Telegraph
Company
New York, New York

John D. Harper
President
Aluminum Company of America
Pittsburgh, Pennsylvania

Fred L. Hartley
President
Union Oil Company of California
Los Angeles, California

Amory Houghton, Jr.
Chairman of the Board
Corning Glass Works
Corning, New York

Honorable Richard J. Hughes
Governor of New Jersey
Trenton, New Jersey

W. M. Jarman
Chairman of the Board
Genesco Inc.
Nashville, Tennessee

Walter H. Johnson, Jr.
Senior Vice President
Interpublic, Inc.
New York, New York

James A. Linen
President
Time Inc.
New York, New York

Robert L. Milligan
Chairman of the Board
Pure Oil Company
Palatine, Illinois

William B. Murphy
President
Campbell Soup Company
Camden, New Jersey

Herman H. Pevler
President
Norfolk & Western Railway
Roanoke, Virginia

James M. Roche
Chairman of the Board
General Motors Corporation
New York, New York

Marion Sadler
President
American Airlines, Inc.
New York, New York

Jack Valenti
President
Motion Picture Association
of America, Inc.
Washington, D. C.

H. E. Whitaker
Chairman
Mead Corporation
Dayton, Ohio

TREASURY DEPARTMENT



WASHINGTON, D.C.

RELEASE 6:30 P.M.,
January 8, 1968.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated October 13, 1967, and another series to be dated January 11, 1968, which were offered on January 3, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. Details for the two series are as follows:

TYPE OF ACCEPTED NONCOMPETITIVE BIDS:	91-day Treasury Bills maturing April 11, 1968		:	182-day Treasury Bills maturing July 11, 1968	
	Price	Approx. Equiv. Annual Rate		Price	Approx. Equiv. Annual Rate
High	98.731	5.020%	:	97.301 <u>a/</u>	5.339%
Low	98.708	5.111%	:	97.272	5.396%
Average	98.716	5.080% <u>1/</u>	:	97.282	5.376% <u>1/</u>

a/ Excepting 1 tender of \$10,000

14% of the amount of 91-day bills bid for at the low price was accepted
of the amount of 182-day bills bid for at the low price was accepted

TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 24,087,000	\$ 14,087,000	:	\$ 23,323,000	\$ 13,323,000
New York	1,699,950,000	927,750,000	:	1,444,343,000	634,143,000
Philadelphia	35,602,000	22,602,000	:	18,478,000	10,478,000
Cleveland	41,259,000	41,259,000	:	36,323,000	28,495,000
Richmond	18,015,000	15,015,000	:	5,949,000	5,949,000
Santa	54,884,000	44,304,000	:	30,759,000	24,759,000
Chicago	276,167,000	217,367,000	:	212,503,000	122,822,000
St. Louis	54,929,000	47,629,000	:	53,338,000	44,000,000
Minneapolis	26,760,000	24,760,000	:	21,969,000	19,469,000
Kansas City	31,782,000	29,782,000	:	21,581,000	21,581,000
Dallas	28,679,000	23,679,000	:	24,685,000	17,685,000
San Francisco	119,221,000	92,021,000	:	107,507,000	57,858,000

TOTALS \$2,411,335,000 \$1,500,255,000 b/\$2,000,758,000 \$1,000,562,000 c/

includes \$280,945,000 noncompetitive tenders accepted at the average price of 98.716
includes \$187,664,000 noncompetitive tenders accepted at the average price of 97.282
these rates are on a bank discount basis. The equivalent coupon issue yields are
.23% for the 91-day bills, and 5.62% for the 182-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 9, 1968

FOR IMMEDIATE RELEASE

INDUSTRIAL PAYROLL SAVINGS COMMITTEE SETS TWO MILLION 1968 CAMPAIGN GOAL

Fifty-six of America's top executives, representing 23 geographic areas and 27 industries and state government, met with Secretary of the Treasury Henry H. Fowler today to initiate plans to sign up 2,000,000 Americans as new savers or increased allotments for the purchase of U. S. Savings Bonds and Freedom Shares during 1968. They are members of the U. S. Industrial Payroll Savings Committee, first established in 1963.

For 33 of the group, this was their first such meeting. They were installed officially as new members of the Committee for 1968, following their meeting with Secretary Fowler and other Treasury officials, in the State Department's Benjamin Franklin Dining Room. Each was presented with a Certificate of Appointment, signed by the Secretary.

In making the appointments, Secretary Fowler said, "Your Committee now represents the nation's largest markets, as well as its major industries. Some of you are responsible for organizing campaigns in your respective geographic areas. Others will concentrate on the larger employers in their related industries. Your abilities and your energies -- cast together with the cause of Savings Bonds and Freedom Shares -- can only add substantially to the growth and strength of the economy."

The Chairman of the Industrial Payroll Savings Committee for 1968 is William P. Gwinn, President and Chief Administrative Officer, United Aircraft Corp., East Hartford, Conn. In acknowledging Mr. Gwinn's acceptance as Chairman, Secretary Fowler said, "The vital volunteer activity which you will now head is additional evidence of responsible patriotism on the part of American business. The President joins with me in a firm conviction that such outstanding public service as that performed by your Committee adds strength to our financial structure, helps to offset the forces of inflation and substantially supports the valor of our servicemen in Vietnam."

Mr. Gwinn succeeds Daniel J. Haughton, Chairman of the Board, Lockheed Aircraft Corporation, Burbank, Calif. Mr. Haughton will remain active as a member-at-large of the 1968 Committee, joining with other former chairmen -- Lynn A. Townsend, Chairman of the Board, Chrysler Corp., Detroit, 1966; Dr. Elmer W. Engstrom, Chairman of the Executive Committee, Radio Corporation of America, New York, 1965; Frank R. Milliken, President, Kennecott Copper Corporation, New York, 1964, and Harold S. Geneen, Chairman and President, International Telephone and Telegraph Corp., New York, 1963.

In addition to providing over-all direction for the national Payroll Savings effort, the business executives who formed the 1967 Committee spearheaded Payroll Savings drives in their own companies -- for a total of 716,000 savers. And purchasers of the Freedom Shares/Savings Bonds combination accounted for 334,000 of that number. The Committee exceeded its national goal of 2,500,000 new savers or savers who increased their payroll allotments. In terms of dollar volume, the 1967 Committee's accomplishment comes to \$3.5 billion.

In a special message to the industrialists, President Lyndon B. Johnson complimented the 1967 Committee. His remarks stressed the urgent need to stabilize our economy, preserve the value of the dollar and offset the deficit in the balance of payments. He cited the values of the Savings Bonds Program in that all-out national effort.

Commenting on the Committee's accomplishments, Secretary Fowler said, "Your 1967 Payroll Savings campaign throughout industry was a shining example of distinguished and enlightened self-service by the business community in meeting the needs of the nation."

Incoming Chairman William P. Gwinn told the members, "Secretary Fowler has clearly spelled out the economic facts. As individuals deeply involved in the commerce and industry of our nation, I am sure we fully appreciate the need for maintaining the stability of the dollar. In Savings Bonds, and their sale through Payroll Savings, we have a powerful, positive instrument for helping to keep not only

our economy strong but the dollar stable. This is not a one-way street, for the individual who participates builds a nest egg for himself and his family at the same time."

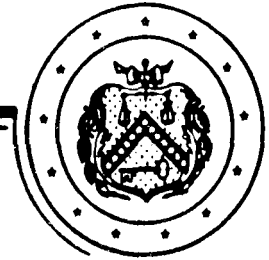
Another highlight of the meeting was the presentation of awards to outgoing Chairman Haughton and members of his Committee. Mr. Haughton received the Treasury's Medal of Merit, while Committee members were presented with Silver Medals of Merit.

The session -- which got underway in the afternoon -- was opened by Under Secretary of the Treasury for Monetary Affairs, Frederick L. Deming, who introduced the new members of the 1968 Committee.

Glen R. Johnson, National Director of the Treasury's Savings Bonds Division, spoke of the outstanding team spirit shown by the Committee and outlined the guidance and logistical support available from his Division.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

LEASE 6:30 P.M.,
y, January 9, 1968.

RESULTS OF TREASURY'S OFFER OF ADDITIONAL \$2.5 BILLION OF JUNE TAX BILLS

The Treasury Department announced that the tenders for an additional \$2,500,000,000, reboughts, of Tax Anticipation Series Treasury bills dated October 9, 1967, maturing 4, 1968, were opened at the Federal Reserve Banks today. The additional amount of which were offered on January 3, 1968, will be issued January 15, 1968, (161 days maturity date).

The details of this issue are as follows:

Total applied for - \$6,332,020,000
 Total accepted - \$2,500,362,000 (includes \$367,380,000 entered on a non-competitive basis and accepted in full at the average price shown below)

Range of accepted competitive bids:

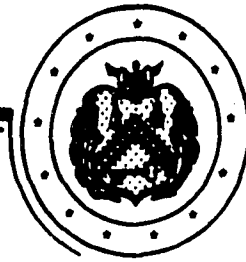
1/ Excepting one tender of \$40,000.
 High - 97.788 a/ Equivalent rate of discount approx. 4.946% per annum
 Low - 97.727 " " " " " " 5.082% " "
 Average - 97.738 " " " " " " 5.058% " " 1/

(2% of the amount bid for at the low price was accepted)

Federal Reserve District	Total Applied For	Total Accepted
Atlanta	\$ 239,520,000	\$ 167,020,000
Boston	2,905,082,000	754,502,000
Chicago	250,915,000	174,915,000
Cleveland	323,717,000	71,567,000
Dallas	85,655,000	44,255,000
Denver	176,675,000	119,175,000
Detroit	789,348,000	335,490,000
Houston	215,207,000	158,907,000
Indianapolis	220,670,000	131,660,000
Kansas City	116,409,000	96,109,000
Los Angeles	223,380,000	107,380,000
San Francisco	785,442,000	339,382,000
TOTAL	\$6,332,020,000	\$2,500,362,000

This is on a bank discount basis. The equivalent coupon issue yield is 5.26%.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 10, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing January 18, 1968, in the amount of \$2,501,068,000, as follows:

91-day bills (to maturity date) to be issued January 18, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated October 19, 1967, and to mature April 18, 1968 originally issued in the amount of \$1,000,119,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated January 18, 1968, and to mature July 18, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, 5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard Time, Monday, January 15, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on January 18, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing January 18, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT
Washington

REMARKS BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY, BEFORE
LUNCHEON-MEETING OF 1968 "SHARE IN FREEDOM"
SAVINGS BONDS VOLUNTEER CONFERENCE
COTILLION ROOM, SHERATON PARK HOTEL, WASHINGTON, D.C.
WEDNESDAY, JANUARY 10, 1968, 1:55 P. M., EST

Chairman Gwinn, Distinguished Guests, Ladies and Gentlemen -- I am delighted to be here with you and to witness the inspiring example that this superb audience is giving the American people.

As volunteers in the cause of good citizenship, you are putting patriotism into practice. You are demonstrating -- not your rights -- but your responsibilities.

Your numbers are impressive and the importance of your callings more so. You exemplify the simple truth on the cover of your colorful campaign brochure as stated by a great President -- "I go for all sharing the privileges of the Government who assist in bearing its burdens."

In an altogether fitting observance of New Year's day, President Johnson launched an Action Program to maintain the strength of the dollar and preserve the soundness of the Free World monetary system by restoring our international payments to balance.

This was an act of singular courage and decisiveness, but also an act of challenge -- to you and to me -- whatever our respective callings -- public or private.

The challenge was to all responsible citizens to join in the "very necessary and laudable effort to preserve our country's financial strength."

Today we launch a related and equally laudable effort for the same noble purpose -- for the sale of U.S. Savings Bonds, like the restoration of our balance of payments to equilibrium, will preserve a strong dollar -- at home or abroad.

And that strong dollar is the bulwark of both our domestic and international monetary system.

It has helped bring the greatest economic miracles of all times.

It has underwritten unprecedented prosperity for the people of the United States who are now in the 83rd month of sustained economic growth shared with our near neighbors.

It has helped bring back a war-torn Europe and Japan to share in that prosperity.

It is helping to bring new life and strength and hope to the developing world of Asia, Africa and Latin America.

It is turning back the naked aggression in Southeast Asia, which, if left unchecked, would light the fires and fears of war in other parts of the world.

The strength of the world economy and the functioning of the international monetary system depend to a large extent on the level of economic activity in the United States and the maintenance of a stable dollar -- stable in terms of prices and of exchange rates.

Yes, as the President said on New Year's day -- a strong dollar protects and preserves the prosperity of businessman and banker, worker and farmer -- here and overseas -- as it is restoring peace and security.

And it is our job to protect and preserve the strength of the dollar for these tasks in the years ahead.

The New Year is a time for action -- for decisive action pursuant to firm resolution.

Today -- this month -- we are concerned with three related areas for decisive action and firm resolution to strengthen the dollar by:

- taking action to deal directly with our balance of payments deficit through the selective temporary and longer term measures set forth by the President on January 1;

- making it "the first order of business" -- as termed by the President -- to restore the first line of defense of the dollar -- a strong American economy -- by moving decisively in the direction of balance in our budget and stability in prices and unit labor costs with the enactment of the anti-inflation tax increase, coupled with an austere budget, appropriate monetary policy, and a more effective voluntary program of wage-price restraint, and

- launching here today the most intensive, effective effort since World War II to meet to the maximum extent the government's borrowing needs outside the over-crowded money markets through the sale of U.S. Savings Bonds and Freedom Shares, thereby financing the debt in an anti-inflationary manner.

First, I would like to discuss briefly three questions that seem to arise frequently about the President's new balance of payments program.

Why were these measures -- some of them drastic and unprecedented -- taken at this particular time when we have had this problem around for a long time and it concerns a deficit that is only a fraction of one percent of our national output of goods and services?

It is apparent that even today, many of our people are not fully aware of the urgent necessity of restoring a balance in our international payments. The U. S. economy is strong and prosperous. The international transactions of the United States, while very large in terms of the world economy, are small relative to our total production, consumption and investment. Why should the United States or the world be disturbed about a balance of payments deficit that at worst has been only a fraction of one percent of our output of goods and services?

Despite the magnitude of our domestic economy, the foreign transactions of the United States are very important to our economic well-being and indispensable to the Free World. Imports of foodstuffs, raw materials and finished goods are

essential for our production and our high standard of living. The overseas expenditures of the U.S. Government for foreign aid and defense are vital to our objectives of world peace and security. U. S. private foreign investment or lending is profitable to our banking and business institutions, important for economic growth and development in many other countries, and an inherent part of the functions of the dollar as the preeminent international currency.

The cost of these imports, security expenditures abroad, foreign investment, and -- yes -- our travels to other lands for pleasure or profit, must be paid for by exports of goods and services, the earnings of our foreign investments, foreign investment and tourism in the United States, and other foreign exchange receipts. When our total foreign payments are more than our foreign receipts, some of the excess dollars received by foreigners are sold to their monetary authorities in return for local currency.

To some extent and for some time, foreign central banks are willing to add such dollars to their reserves. but when the accumulation of dollars is large in amount and continues for a long time, some foreign central banks no longer add these dollars to their reserves but convert them into gold.

Our total foreign payments have exceeded our total foreign receipts steadily since 1958. As our gold reserves were very large then -- they were larger at the end of 1957 than they had been at the end of 1950 -- there was no urgency about restoring our balance of payments. In fact, nearly all countries had very small reserves and many were eager to add to their dollar reserves.

Nevertheless, President Eisenhower instructed the Department of Defense and other Government agencies to economize on their foreign expenditures. President Kennedy strengthened the earlier program and introduced new measures, including those designed to increase U. S. exports, to hold down U. S. purchases of foreign securities and to increase foreign purchases of U.S. securities. A renewed capital outflow in 1964 made it necessary for President Johnson to introduce a voluntary program for holding down foreign direct investment and foreign bank loans.

It had been hoped that the normal adjustment of international payments would enable us to restore our payments without restrictive measures. In fact, from 1959 to 1964, we made good progress in reducing our payments deficit because of the growth of our exports of goods and services, and because of the rise in earnings from our foreign investments, and because of the savings on the government account. The sharp increase in our private capital outflow, however, prevented the achievement of balance in 1964.

In 1965 and 1966, the accelerated expansion in the U. S. economy and the war in Vietnam placed renewed pressure on the balance of payments. The great boom resulted in an extraordinary increase of imports, very much more than the increase of exports. The costs of our forces in Vietnam added substantially to our foreign payments. Thus, while the voluntary program reduced the capital outflow considerable from the peak of 1964, the payments deficit persisted. No progress was made in 1967 because our imports continued to rise nearly as much as our exports, the foreign exchange costs of Vietnam rose further to over \$1.5 billion, and private capital outflows and the tourism deficit again increased.

The devaluation of sterling brought the balance of payments problem to an acute stage. It resulted in a loss of confidence in currencies and was accompanied by a large outflow of foreign funds from the United States and a burst of speculative buying of gold. This was a threat not only to the dollar but to the international monetary system as a whole. While the speculation was repulsed with the cooperation of the members of the gold pool, it has underlined the urgency of placing the dollar once more in an impregnable position. With the implementation of the Rio resolution for creating Special Drawing Rights by the International Monetary Fund, the world will be assured of an adequate supply of reserves without the necessity of depending on continued U.S. deficits. The time has come, therefore, when it is necessary and desirable to take decisive measures to eliminate the payments deficit. That will be done through the Action Program.

The second question often raised in connection with the President's new balance of payments program is why were measures selected that were restrictive of spending abroad in the private sector -- business and direct investment, banking and tourism -- instead of reducing Government expenditures overseas?

The answer is twofold. For some years the Government has conducted a rigorous program to reduce and neutralize the balance of payments costs of its overseas expenditures resulting in the saving of billions of dollars of foreign exchange. Government spending abroad consists primarily of military expenditures resulting from the positioning of our military forces beyond our borders in the interest of maintaining our security and that of our allies in Europe and the Far East, and foreign aid provided to certain of the less developed countries directly or in association with other financially powerful nations in international organizations such as the World Bank, the Inter-American Development Bank and the Asian Development Bank.

In the field of military expenditures a very stringent program, developed and rigorously executed by the Defense Department under the leadership of Secretary McNamara, has saved billions of dollars in foreign exchange costs of our military expenditures abroad. I invite any who raise the question as to what the Government is doing to hold down the balance of payments consequences of its own expenditures abroad to secure a copy and read carefully a 26 page Report released last week by the Department of Defense. That Report reviewed the most intensive program being executed by that Department in a variety of measures to reduce the balance of payments impact of maintaining our security abroad.

For a few examples -- actual numbers of military personnel deployed abroad have been reduced to the degree consistent with our security commitments to our allies.

Military strength levels in Western Europe have been reduced by 67,000 since the peak of the Berlin build-up in March 1962 and there will be an additional reduction of 35,000 in 1968 resulting from arrangements made last year on a new force rotation principle.

There has been a continuing effort to encourage participation by military personnel stationed in foreign countries in voluntary programs designed to channel available disposable income back to the United States -- premiums on savings returned home, the use of military payments certificates in Vietnam and, more recently, the establishment of a rest and recuperation program in Hawaii for military personnel serving in South Vietnam are examples.

Actions taken to reduce the number of foreign nationals employed in connection with military operations abroad has resulted in substantial reduction of this category of foreign exchange cost in all areas except Southeast Asia.

Expenditure for material, supplies and services and major equipment from U. S. sources rather than off shore has received very great emphasis. The Defense Department is also attempting to achieve maximum feasible use of U.S. owned excess currencies and barter arrangements as a means of conserving defense dollar expenditures entering into the balance of payments.

A program to conduct sales of U.S. type military equipment to our allies to further the practice of cooperative logistics and standardization of equipment and reduce costs to our allies and to ourselves has had the result of offsetting, at least partially, the unfavorable payments impact of our deployments abroad in the interest of collective defense. Receipts from these sales have increased from an annual rate of \$300 million a year in fiscal 1961 to close to \$1.6 billion in fiscal 1967.

The reduction of the foreign exchange impact of foreign aid by tying it to the purchase of U.S. goods and services -- a program inaugurated in the latter part of the Eisenhower

Administration -- has been rigourously pursued. Whereas in 1959 only forty percent of our bilateral aid dollars were being spent on U.S. goods and services, tying procedures have been continually strengthened so that the percentage has been increased to nearly ninety percent. Recognizing that tying procurement to U.S. sources may not itself be enough to reduce to the extent necessary the impact of the aid program on the balance of payments if the purchases made with the funds merely substitute aid exports for commercial exports, special efforts are being made to insure that aid financed exports will be "additional."

But the President's new balance of payments program did not stop with pointing to past and current efforts to reduce the impact of Government expenditures abroad on our balance of payments. In speaking of these efforts he said: "I am convinced that much more can be done. I believe we should set as our target avoiding a drain of another \$500 million on our balance of payments."

To achieve this objective, he took three steps -- directing the Secretaries of State, Treasury and Defense to initiate prompt negotiations with our allies to minimize further the foreign exchange costs of stationing our troops within their borders, instructing the Director of the Budget to find ways of reducing the number of Government civilian employees working overseas, and instructing the Secretary of Defense to find ways to reduce further the foreign exchange impact of personal spending by U. S. forces and their dependents in Europe.

Of course, there are those who would argue that Government expenditures overseas should be further reduced by bringing our forces back to the United States into a kind of "fortress America." To this contention the answer is clear. In the words of the President: "We cannot forego our essential commitments abroad, on which America's security and survival depend."

When a family has a cash stringency because there is more outgo than there is income and it has to cut down on spending and/or try to increase its earnings, I believe the head of that family would make a very poor choice of means if he decided to cancel the insurance policies on which family security was based.

The third question asked about the President's new balance of payments program is -- won't the reduction of outflow of dollars from the United States or flow-back of dollars to the United States cause a sharp deflation in the remainder of the world?

Again, the answer is in two parts. First, the monetary and fiscal authorities in other countries can take domestic measures to provide additional money and credit in their own currencies for the dollars that no longer come or the dollars that go home by adopting more expansionary monetary and fiscal policies.

Second, the early availability of additional monetary reserves to the world's total in the form of Special Drawing Rights in the International Monetary Fund through a new facility now being provided by the collective action of the 106 member countries in that organization should remove the concern that the elimination of the U. S. deficit will endanger a healthy growth in the monetary reserves of the rest of the world. In past years there have been fears that more intensive action to eliminate the deficits in our balance of payments which have characterized past years and added to the reserves of other nations at a time when little, if any, newly mined gold was being added to world monetary reserves would cause a worldwide recession as a scramble by countries for reserves resulted in "beggar thy neighbor" policies, sharp deflation or escalating international interest rates. Now the risks of cutting our deficit too much are negligible.

Last September at the Annual Meeting of the International Monetary Fund in Brazil the Governors representing the 106 member countries unanimously approved a resolution directing the submission to Governments by March 31, 1968 of the first major amendment to the Articles of Agreement of the IMF since the original Agreement at Bretton Woods in 1944. This amendment, the product of two years of intensive negotiations inaugurated in July 1965 at the initiative of our President, would provide a facility for the deliberate creation of additional monetary reserves supplementary to gold and the reserve currencies such as dollars in the form of "Special Drawing Rights." These Rights would be distributed to the central banks of the 106 member countries in accordance with their percentage quotas in the Fund. They could be used for an unconditional call on the currencies of other countries in accordance with procedures set forth in an extensive "Outline of a Plan" which was approved as a basis for the amendment.

When operational -- this new facility will supply additional liquidity to the world in amounts needed to accommodate an increasing volume of trade and capital movements. The international monetary system would no longer depend for additional reserves on newly mined gold excess to increasing industrial and decorative use and sporadic speculative demand and additions to the holdings of dollars in official reserves of other countries resulting from variable deficits in U. S. balance of payments.

In the words of the President, as our movement toward balance curbs the flow of dollars into international reserves, "it will therefore be vital to speed up plans for the creation of new reserves -- the Special Drawing Rights -- in the International Monetary Fund. These new reserves will be a welcome companion to gold and dollars, and will strengthen the gold exchange standard."

I have discussed the three questions most often raised about the President's new balance of payments program. Sometimes those who have not studied the President's statement carefully ask a fourth question -- why does the program try to restrict certain outflows instead of tackling the more fundamental problem of handling our internal economy so as to avoid the inflation that is the root cause of the problem?

The answer is that the President's balance of payments program incorporates in very specific terms measures for tackling this fundamental problem. Indeed, he labels them in his Message as "the first order of business" and uses the word "urgent" in describing them saying: "No business before the returning Congress will be more urgent than this: to enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus."

In addition, the President directed his Cabinet officers to work with leaders of business and labor "to make more effective our voluntary program of wage-price restraint 'and' prevent our exports from being reduced or our imports increased by crippling work stoppages in the year ahead."

This brings us in a natural transition to a concern for the strength and stability of the U. S. economy which is the first line of defense of the dollar.

To sustain the kind of economy that has given us nearly seven years of continuous growth, we have urgent business before us.

We need a tax increase, and we need it now.

President Johnson last August requested a temporary, ten percent surcharge. He did this in the face of a dangerous deficit, rising interest rates and the threat of unacceptable inflationary pressures.

Since that time a consensus in favor of a tax increase has emerged among responsible leaders throughout the country, including many of you here today. It takes a sense of true responsibility for an industrialist, who is responsible to his stockholders, to recommend greater taxes.

The labor leader, elected by the members of his union to represent their best interest, must show a similar sense of wise fortitude.

The professional economist, who is paid to be right more often than he is wrong, evaluates the economic climate most carefully before he goes down the line for a tax increase.

And the responsible journalist and business writer, whose views often mold the public thinking on important questions affecting the economic course of our daily lives, must be doubly cautious about what he commits to paper.

In a way, all of these have as much to lose from making wrong judgment on this question as a member of Congress.

But -- to get the action that counts we need to add to the singular near unanimity among many of the nation's foremost businessmen and labor leaders, economists, industrialists, bankers and financial leaders who have recommended a tax increase -- the votes of the majority of the members of the House of Representatives and the Senate.

A failure to take this tax action promptly will risk a declining trade surplus. This trade surplus is the mainstay of our balance of payments position. It can rapidly decline -- as it did in late 1965 and 1966 -- when a floodtide of imports were induced by an economy running at a very high rate of speed. When our rate of economic growth in money terms expands at a rate of eight or nine percent, there is an increasing propensity to import. In that situation, imports occupy an increasing percentage of our gross national product and our trade surplus evaporates. We cannot afford to let that happen, cancelling our savings effected by the direct measures in the President's program.

A failure to take this tax action promptly and decisively will cause strain, tension and a scramble in our domestic credit markets, endangering the housing industry and the satisfaction of credit needs of states and local government and small business on reasonable terms.

A failure to take this tax action promptly will give rise to doubt at home and abroad on the health of the dollar -- and the will and capacity of the American Government and people to protect it from the internal danger of an inflation which is accompanied by a wage-price spiral.

Let me be clear: The Number One domestic and international legislative objective of this Administration remains passage of this badly needed tax surcharge.

I ask you to give your help in support of this measure.

This brings us to the last of the three programs being launched this January to strengthen the dollar -- your principal business of the day and, I hope, an important part of your business for the year -- promoting the sale of U. S. Savings Bonds.

Buying and holding U. S. Savings Bonds are actions more important to our nation's economic stability today than ever before. These bonds not only support our fighting men in Vietnam and our commitment to the defense of freedom throughout the world, but they strengthen the dollar by strengthening our economy at home and guarding against the forces of inflation.

In the days and months to come, all of us -- in government, in banking and finance, in industry and commerce -- must share an extra burden of responsibility in maintaining a steady economic footing while we continue to move ahead.

Now, more than ever before, it is essential that we finance our debt in the soundest possible way; that we do all we can to place more of the debt in the hands of savers. You well know that participation in the Savings Bonds Program is a measurable and effective means of accomplishing both these objectives, because you have done an outstanding and admirable sales job.

I am convinced our program can be expanded. We have good products." Savings Bonds are an attractive investment. To be sure, higher rates are available in today's markets than the 4.15 percent rate of interest on our Savings Bonds. But our bonds do have advantages, namely, safety, convenience, liquidity, and certain tax benefits in terms of deferred income as well as exemption from State and local income taxation. Similarly, our newer "Freedom Shares" with a 4.74 percent rate of interest are very attractive and worthwhile investments too.

In closing let me express a debt of gratitude from the Treasury to you who are doing so much in the promotion of the sale of Savings Bonds. The growing stockpile of Savings Bonds assists the Treasury materially in managing the nation's finances -- maintaining a stable economy at home, and a strong economic position internationally, to back our stand for freedom in Vietnam and elsewhere in the world.

The fact that so many Americans participate in the regular purchase of Savings Bonds is irrefutable and inspiring evidence of the effective energies and talents that you leaders of business, labor and finance have put into our programs to

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 10, 1968

FOR IMMEDIATE RELEASE

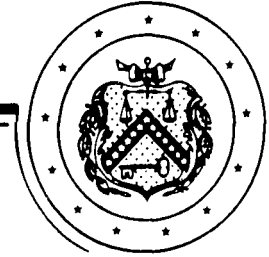
TREASURY MARKET TRANSACTIONS IN DECEMBER

During December 1967, market transactions in direct and guaranteed securities of the Government investment accounts resulted in net purchases by the Treasury Department of \$51,741,000.00.

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F-1128

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 11, 1968

FOR IMMEDIATE RELEASE
THURSDAY, JANUARY 11, 1968

McKINNEY OUTLINES TASK FORCE ON TRAVEL WORK PROGRAM AND ANNOUNCES APPOINTMENT OF COMMITTEE CHAIRMEN

Robert M. McKinney, chairman of the Industry-Government Special Task Force on Travel, today listed 12 areas of study the Task Force will pursue before submitting recommendations to the President on how to attract more visitors to the United States, and reduce our balance of payments deficit. He also announced the appointment of the chairmen who will head the 12 working parties.

Objectives of the Task Force, Mr. McKinney said, are:

- (1) to determine practical steps which can be taken quickly to produce early improvement in the travel sector of the balance of payments;
- (2) to determine medium and long term measures to bring U.S. travel expenditures and receipts into better balance, and to recommend the necessary steps that should be taken in both the private and government sectors to accomplish this objective; and
- (3) to determine how best to help foreign visitors improve their knowledge and understanding of the U.S. and the American people through first-hand experience, and to provide a new bridge of understanding through tourism between the U.S. and other countries, including Eastern European and developing nations.

The 12 committee chairmen and the areas of activity each committee will study are:

COMMITTEE ONE -- Chairman, William D. Patterson,
The Saturday Review

Provide statistical information, including projections of U.S. travel receipts and expenditures in 1970 and 1975, under various assumptions. Submit an analysis of factors which tend to limit or impede travel or which would be advantageous to build upon. Recommend the most promising major markets for rapid expansion of visitor travel, and analyze current travel trends within the United States.

COMMITTEE TWO -- Chairman, E. O. Cocke, Trans World Airlines

Evaluate the effectiveness of present American travel promotional programs by U. S. private industry, including sources of funding; target areas and objectives, and scale of efforts. Analyze potential new target areas; magnitude of efforts required; methods for financing new programs; new government-industry roles; ways to increase assistance from travel-related industries, and the possibility of cooperative participation by federal, state and local governments with private industry. Recommend how better to mobilize the travel industry, both in the U. S. and foreign countries, and new promotional programs most likely to produce significant response.

COMMITTEE THREE -- Chairman, Howard L. Clark,
American Express Company

Consider solutions to problems currently encountered in creating and selling tours within the United States. Recommend measures required to design and produce tours which can compete successfully with tours offered in competing travel areas outside the U.S.; ways to increase student and educational travel; travel for purposes of conventions, conferences, and incentive programs, and how to enlist the cooperation of U.S. international corporations and organizations.

COMMITTEE FOUR -- Chairman, Willis G. Lipscomb,
Pan American World Airways

Report what new efforts should be asked from the transportation industry -- including airline, bus, railroad, shipping, car rental, sightseeing, automobile, tire and petroleum companies.

COMMITTEE FIVE -- Chairman, Edward E. Carlson,
Western International Hotels, Inc.

Report on what new efforts should be asked from hotels and potential providers of other accommodations (e.g., youth hostels, college dormitories). Seek new government efforts for improving services and facilities in federal, state, and local parks, monument areas, etc.

COMMITTEE SIX -- Chairman, George Moore,
First National City Bank of New York

Report on what new efforts should be asked from banking, credit card, and insurance companies.

COMMITTEE SEVEN -- Chairman, Frank N. Ikard,
American Petroleum Institute

Suggest new efforts which would assist in increasing travel to the U.S. through better visitor information, services, and host programs. Consider travel attractions, museums, sightseeing services, guides, interpreters and host programs in major cities and resorts, as well as guide books, maps, travel brochures, and news media in formulating recommendations. Seek new ways to help foreign visitors improve their knowledge and understanding of the U.S. through first-hand experience with our way of life, attitudes, and aspirations.

COMMITTEE EIGHT -- Chairman, Winston V. Morrow, Jr.,
Avis Rent a Car Service

Advise on ways and means of reducing costs of travel to and within the U.S. and of acquainting potential travelers with such lowered costs. Consider the cumulative impact of costs of transportation to and within the U.S., accommodations, meals, shopping, sightseeing, travel attractions, accident, and medical insurance etc

COMMITTEE NINE -- Chairman, Donald G. Agger,
Department of Transportation

Examine domestic and international transportation policies of the federal government as they affect the balance of payments. Study federal policies on rates, including rate differentials and "directional fares" -- fares, making travel to the U. S. attractive -- for international travelers, carrier certifications, bilateral and multilateral transport agreements, U.S. and foreign regulations impeding competition by U.S. carriers, special arrangements for group travel and other methods of reducing cost of transportation to the U.S. Suggest ways of assisting U.S. flag carriers to obtain a larger share of international travel.

Consider ways of simplifying and facilitating frontier formalities (visas, customs, immigration, agriculture inspection, public health, etc.). Consider how better to mobilize federal programs and resources affecting tourism, including the role of a national tourist office. Consider possible relief from indirect and direct taxes for visitors and/or the travel industry. Consider anti-trust matters related to coordinated domestic programs of the tourist and travel industries (common special rates for foreign tourists in hotels and restaurants, pooling of language and other special service resources, etc.).

COMMITTEE TEN -- Chairman, Frank Hildenbrand, Texas
Tourist Development Agency

Explore new ways for state and local governments to assist through tax incentives, promotional programs, facilities development, host activities, and other measures. Seek ways of increasing cooperation with federal and/or travel industry promotion and other programs -- including possibilities of the government matching private promotional funds.

COMMITTEE ELEVEN -- Chairman, John Black,
United States Travel Service

Report on what can be learned from other governments and governmental entities about methods of improving visitor earnings. Explore means of reducing barriers imposed by foreign governments which impede travel to the U.S. (Such as currency restrictions, travel restrictions, free entry provisions, etc.). Consider ways of increasing travel from Eastern European and developing nations to the U.S.

COMMITTEE TWELVE -- Chairman, Stuart Guy Tipton,
Air Transport Association

Draft a new national travel policy in line with the objectives of the Task Force and leading to intensified travel within the U.S. by both U.S. citizens and foreign nationals through: new services and technologies in the travel industry; new facilities and attractions so designed and located as to have maximum impact in attracting and serving foreign visitors; new methods of cooperation between travel and travel-related industries and the federal government; new relationships between federal, state, and local government, and new legislation and/or regulatory and administrative practices designed to make the U. S. more competitive in the international tourist market.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

January 12, 1968

FOR A.M. RELEASE

SATURDAY, JANUARY 13, 1968

MELVIN I. WHITE RECEIVES TREASURY AWARD ON LEAVING POST

Melvin I. White, who is leaving the Treasury today to resume his teaching post at Brooklyn College, City University of New York, has been awarded the Department's Exceptional Service Award by Secretary of the Treasury Henry H. Fowler.

During the past two years Mr. White has been Deputy Assistant Secretary for Tax Policy to Stanley S. Surrey, Assistant Secretary of the Treasury for Tax Policy.

Mr. White, a professor of economics, took a leave of absence from Brooklyn College early in 1966. Prior to his appointment as Deputy Assistant Secretary, he was a Consultant to the Treasury on tax matters, a position he will continue to hold.

Secretary Fowler cited Mr. White's work in helping shape the thinking, within and without the Treasury, on the nature and structure of tax changes to meet swings in our economy, his work in the development of the major domestic legislative measures of 1966 and 1967 -- the investment credit legislation and the surcharge proposal -- and his efforts to develop major research studies in tax policy, with special emphasis on the use of econometric and other analytical techniques.

The award citation said:

"In all ... of his labors in his two years with the Department, he has displayed a rare ability to comprehend complex matters and translate them with remarkable clarity into more easily understood concepts."

A native of Cincinnati, Ohio, Mr. White, 49, holds a B.A. degree with High Honors from the University of Cincinnati and a Ph.D. in economics from Columbia University where he was a University Fellow. He is a member of Phi Beta Kappa and of the honorary forensic society, Tau Kappa Alpha.

He served as a staff economist with the Council of Economic Advisers in 1947-1948 and as an economist on the staff of the Federal Reserve Board, 1948-1950.

Mr. White, who was a Fulbright Professor in Norway and France in 1956-1957, also has been a consultant on various fiscal projects for the City of New York. He also has served as a research associate with the National Bureau of Economic Research, New York, and has performed research work for the Brookings Institution, Washington. He is the author of numerous articles in various economic journals, and is a member of several professional organizations in the field of economics.

Mr. White is married to the former Anne Schapiro of New York, a statistician. They have four children. They made their home at 5526 Westbard Avenue, Bethesda, Maryland.

A copy of the citation which accompanied the award is attached.

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Attachment

CITATION

Exceptional Service Award

Melvin I. White

As Deputy Assistant Secretary for Tax Policy, Melvin I. White has been a principal member of the Treasury Department's fiscal policy team.

He has had a leading part in shaping the thinking, within and without the Treasury, on the nature and structure of tax changes to meet swings in our economy. This led to an active participation in the major domestic tax legislative measures of 1966 and 1967--the investment credit suspension and restoration and the surcharge proposal. In addition, he also played a key role in the formulation of policy in the important area of tax reform. Alongside these current programs, he has materially advanced the Department's efforts to develop major research studies in tax policy, with special emphasis on the use of econometric and other analytical techniques.

In all of these activities, and the rest of his labors in his two years with the Department, he has displayed a rare ability to comprehend complex matters and translate them with remarkable clarity into more easily understood concepts. To his work he has brought a keen and scholarly mind, solidly grounded in the learning of public finance, and a full awareness of the concerns and uses of Government policies. His deep understanding of the responsibilities of the Treasury and its role in fiscal policy has served the Department well. That service fully merits this Exceptional Service Award.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 12, 1968

FOR IMMEDIATE RELEASE

FRANK W. SCHIFF TO BECOME NEW DEPUTY UNDER SECRETARY FOR MONETARY AFFAIRS

Frank W. Schiff, a senior staff economist of the President's Council of Economic Advisers, will be appointed Deputy Under Secretary for Monetary Affairs, Treasury Secretary Henry H. Fowler announced today.

Mr. Schiff will succeed Peter D. Sternlight, who resigned in November to return to the Federal Reserve Bank of New York after two years' service as Deputy Under Secretary. Mr. Sternlight continued to perform most of the duties of the Treasury office on a loan basis until December 22.

As Deputy Under Secretary, Mr. Schiff will assist Frederick L. Deming, Under Secretary for Monetary Affairs, with domestic and international financial matters, and will supervise Treasury's Office of Debt Analysis, Financial Analysis, and Domestic Gold and Silver Operations.

Mr. Schiff is expected to assume his duties at Treasury in early February. During the interim, the Treasury has arranged with the Board of Governors of the Federal Reserve System for Albert R. Koch, Deputy Director of the Federal Reserve's Division of Research and Statistics, to serve as a Treasury consultant on monetary affairs.

Mr. Schiff has played an important role since 1964 in the Council of Economic Advisers' work on domestic and international financial problems. He has been closely involved in international discussions on balance of payments adjustment and international liquidity. As a member of the United States delegation to Working Party 3, the balance of payments subcommittee of the Organization for Economic Cooperation and Development, he was a major contributor to the subcommittee's report on the balance of payments adjustment process.

From 1951 until the fall of 1964, Mr. Schiff was with the Research Department of the Federal Reserve Bank of New York, holding varied positions relating to domestic and international finance. He was editor for several years of the Bank's Monthly Review and Annual Report. He also served as a member of a System-wide committee that undertook a basic reevaluation of the Federal Reserve's financial research program. In 1955 and again in 1957, he went to Vietnam as adviser to the newly created National Bank. He was an Assistant Vice President of the New York Federal Reserve Bank when he was granted leave of absence to join the staff of the Council of Economic Advisers.

Mr. Schiff, 46, is a native of Greifswald, Germany. He attended high school in New Rochelle, New York, and received an A.B. degree from Columbia University in 1942. After serving as an executive in private industry and overseas with the U.S. Army during World War II, he pursued graduate studies in economics at Columbia. He also served as a member of the university's economics faculty from 1946 to 1951.

Mr. Schiff is a member of Phi Beta Kappa, the Council on Foreign Relations, the American Economic Association, and the American Finance Association. He lives at 1330 New Hampshire Avenue, N. W., Washington, D. C.

Mr. Koch, who is serving as a Treasury consultant until Mr. Schiff assumes his new duties, received a B.A. degree from Oberlin College in 1936 and M.A. and Ph.D. degrees from Columbia University in 1937 and 1943, respectively. After employment at the National Bureau of Economic Research, teaching experience at the Wharton School of Finance, University of Pennsylvania, and military service in World War II, he joined the research staff of the Board of Governors of the Federal Reserve System in 1946. He has been Deputy Director of the Division of Research and Statistics since 1966.

TREASURY DEPARTMENT

Washington

FOR RELEASE ON DELIVERY

REMARKS OF THE HONORABLE ROBERT A. WALLACE
ASSISTANT SECRETARY OF THE TREASURY
BEFORE A LUNCHEON OF THE SILVER USERS ASSOCIATION
WALDORF-ASTORIA HOTEL, NEW YORK, NEW YORK
FRIDAY, JANUARY 12, 1968, 1:00 P.M.

THE TREASURY SILVER AND COINAGE PICTURE, JANUARY 1968

THE OPPORTUNITY TO DISCUSS THE SILVER AND COINAGE SITUATION WITH THE SILVER USERS ASSOCIATION IS MOST WELCOME. THIS GROUP HAS A NATURAL STAKE IN SILVER, NOT SIMPLY BECAUSE YOU "USE" IT, AS YOUR NAME IMPLIES, BUT BECAUSE IT IS A VITAL INGREDIENT IN YOUR BUSINESSES. THE REAL SILVER USER IS THE CONSUMER. DIRECTLY OR INDIRECTLY, THIS IS JUST ABOUT EVERY ONE OF US.

MOREOVER, I THINK IT'S ABOUT TIME I ADDRESSED ONE OF YOUR MEETINGS. AFTER ALL, I HAVE BEEN CONCERNED WITH COINAGE AND SILVER SINCE 1961. NOT ONLY THAT, BUT, OBVIOUSLY, ONE OF MY KINSMEN STARTED A VERY IMPORTANT SILVER USING FIRM -- WALLACE SILVERSMITHS.

WELL NOW, JUST A MOMENT. I WILL HAVE TO CHECK THAT. I MAY HAVE THAT WALLACE CONFUSED WITH THE ONE IN THE SILVER PRODUCING AREA WHO STARTED THE TOWN OF WALLACE, IDAHO.

I MUST STRAIGHTEN THIS OUT. I HAVE THE SAME PROBLEM REMEMBERING WHETHER I AM RELATED TO GEORGE WALLACE -- OR HENRY WALLACE.

PERHAPS I AM RELATED TO THEM ALL.

I SHALL KEEP MY REMARKS BRIEF SINCE THIS WOULD BE THE LAST AUDIENCE TO REQUIRE AN EDUCATION ON THE HISTORY OF SILVER PROBLEMS AND POLICIES. CONSIDERING YOUR INTEREST IN SILVER, HOWEVER, YOU CERTAINLY HAVE A RIGHT TO KNOW AS MUCH OF THE FACTS AS POSSIBLE. MOREOVER, WHERE FACTS DRIFT INTO OPINIONS ON POLICIES, YOU NEED TO KNOW THE CONSIDERATIONS INVOLVED IN REACHING FINAL DECISIONS.

THE JOINT COMMISSION ON THE COINAGE IS, OF COURSE, THE BASIC GROUP FOR THE CONSIDERATION OF POLICY ALTERNATIVES. IT WAS THE INTENT OF THE CONGRESS IN CREATING IT WITH THE ENACTMENT OF THE COINAGE ACT OF 1965 THAT THE COMMISSION SHOULD PLAY A VITAL ROLE IN THE FORMULATION OF ALL IMPORTANT SILVER AND COINAGE POLICIES. OF COURSE, WE IN THE TREASURY DEPARTMENT CANNOT AVOID THE FINAL RESPONSIBILITY FOR ALL ACTIONS TAKEN.

THE COMMISSION HAS BEEN AN INVALUABLE ASSET TO THE COUNTRY. OF ITS 24 MEMBERS, 12 ARE LEADING MEMBERS OF CONGRESS WHO ARE CONCERNED WITH SILVER POLICIES, 8 PUBLIC MEMBERS ARE APPOINTED BY PRESIDENT JOHNSON, AND 4 ARE DRAWN FROM THE EXECUTIVE BRANCH OF THE GOVERNMENT. TREASURY SECRETARY FOWLER IS THE CHAIRMAN.

THE COMMISSION HAS MET THREE TIMES. SIGNIFICANT ACTIONS WERE TAKEN AFTER THE FIRST TWO MEETINGS ON MAY 18 AND JULY 14, 1967. AFTER THE MAY MEETING, THE TREASURY RESTRICTED SALES OF ITS SILVER AT THE \$1.29 AN OUNCE PRICE TO INDUSTRIAL USERS ONLY. AFTER THE JULY MEETING, THIS CEILING PRICE WAS DROPPED ALTOGETHER. SINCE THEN ALL SALES HAVE BEEN MADE ON THE BASIS OF COMPETITIVE BIDS AT THE MARKET. AT THE THIRD MEETING, WHICH TOOK PLACE ON SEPTEMBER 18, THE COMMISSION REVIEWED DEVELOPMENTS FOLLOWING THEIR PREVIOUS HISTORIC DECISIONS TO SEE IF ANY FURTHER CHANGES WERE WARRANTED. NONE WERE RECOMMENDED. THE NEXT MEETING WILL BE MARCH 1, 1968, AT WHICH TIME ANOTHER REVIEW OF CURRENT POLICIES WILL BE UNDERTAKEN.

COINAGE SITUATION

FOR SEVERAL YEARS, THE THREAT OF SEVERE COIN SHORTAGES HAS CONSISTENTLY LURKED IN THE BACKGROUND OF ALL OUR SILVER POLICIES -- SO MUCH SO THAT ALL OF THESE POLICIES HAVE BEEN GEARED TO THE PREVENTION OF WHAT COULD BE A GENUINE CATASTROPHE -- A NATION WITHOUT ENOUGH COINS TO CONDUCT ITS BUSINESS.

OUR MOST DANGEROUS PERIOD IN THIS RESPECT WAS IN EARLY NOVEMBER 1965. AT THIS TIME, JUST BEFORE THE CHRISTMAS SEASON OF PEAK COIN DEMAND, AND DESPITE OUR TREMENDOUS LEVEL OF COIN PRODUCTION, OUR FEDERAL RESERVE INVENTORIES OF QUARTERS HAD ALMOST COMPLETELY DISAPPEARED. WE HAD AVAILABLE ONLY 15 MILLION OF THESE COINS FOR THE ENTIRE COUNTRY. FORTUNATELY, UNDER THE AUTHORITY OF THE COINAGE ACT PASSED A FEW MONTHS BEFORE, WE HAD BEEN ABLE TO PRODUCE 200 MILLION OF THE NEW CLAD QUARTERS WHICH WE QUICKLY PLACED IN CIRCULATION, THEREBY AVOIDING WHAT MIGHT HAVE BEEN A REALLY MISERABLE SITUATION.

EARLY IN 1966, I TOLD A CONGRESSIONAL COMMITTEE THAT AT LEAST IN THE CASE OF THOSE COINS VITAL TO CIRCULATION -- THE PENNY, NICKEL, DIME, AND QUARTER -- THERE WOULD BE NO MORE SHORTAGES. NEVERTHELESS, WE STILL FACED THE TASK OF PRODUCING ENOUGH OF THE NEW CLAD DIMES AND QUARTERS TO OFFSET THE POSSIBILITY OF A COMPLETE DISAPPEARANCE OF SILVER DIMES AND QUARTERS BEFORE WE COULD SAFELY STOP TREASURY SALES OF SILVER AT \$1.29 AN OUNCE. SHORTLY BEFORE WE COULD ACCOMPLISH THIS GOAL -- IN MAY OF 1967 -- WE WERE CONFRONTED WITH A RUN ON OUR SILVER SUPPLIES WHICH MADE IT NECESSARY FOR US TO STOP SALES OF SILVER AT THIS PRICE EXCEPT TO THOSE WHO WERE IN THE SILVER BUSINESS.

BY MID-JULY OF 1967, WE HAD PRODUCED ENOUGH OF THE CLAD DIMES AND QUARTERS TO REPLACE ALL THE SILVER COINS OF THESE DENOMINATIONS ESTIMATED TO BE IN CIRCULATION. THUS, ON JULY 14 THE COMMISSION RECOMMENDED, AND THE TREASURY ADOPTED, A POLICY CEASING SALES OF SILVER AT \$1.29 AN OUNCE.

FUTURE SALES OF TREASURY SILVER WERE TO BE MADE BY THE GENERAL SERVICES ADMINISTRATION AT A RATE OF TWO MILLION OUNCES A WEEK.

AS A SAFETY FACTOR, THE FEDERAL RESERVE BANKS NO LONGER ISSUED SILVER COINS. MIXED SILVER AND CLAD DIMES AND QUARTERS WHICH FLOWED BACK FROM THE BANKING SYSTEM TO THE FEDERAL RESERVE BANKS WERE HELD IN MINT AND FEDERAL RESERVE INVENTORIES. THE COINS ISSUED TO REPLACE THEM WERE ALL MADE OF THE NON-SILVER, CLAD MATERIAL.

NOW, IN EARLY JANUARY 1968, WE HAVE GONE THROUGH ANOTHER CHRISTMAS SEASON WITHOUT ANY PROBLEMS. I CAN NOW SAY WITHOUT ANY EQUIVOCATION WHATSOEVER THAT THERE IS ABSOLUTELY NO DANGER OF A SHORTAGE OF QUARTERS, DIMES, NICKELS, AND PENNIES IN THE FORESEEABLE FUTURE.

THE 40 PERCENT SILVER HALF-DOLLAR REMAINS IN SHORT SUPPLY, BUT EVEN THIS COIN HAS ACHIEVED CIRCULATION IN MANY PARTS OF THE COUNTRY.

TREASURY SILVER SUPPLIES

AT THE LAST MEETING OF THE COINAGE COMMISSION ON SEPTEMBER 18, WE MADE A "BEST ESTIMATE" OF THE AMOUNT OF SILVER WHICH WOULD BE AVAILABLE ON JUNE 30, 1968. BY THAT TIME, WE WILL HAVE ALLOTTED TO THE OFFICE OF EMERGENCY PLANNING 165 MILLION OUNCES OF SILVER AS A DEFENSE STOCKPILE. MOREOVER, AFTER THAT DATE, SILVER CERTIFICATES WILL NO LONGER BE REDEEMABLE FOR SILVER. WITH THE OEP STOCKPILE REQUIREMENT MET AND SILVER CERTIFICATES NO LONGER REDEEMABLE FOR SILVER, WE CAN KNOW BY JUNE 30 HOW MUCH SILVER WE WILL HAVE AVAILABLE FOR SALES TO THE MARKET AND FOR FUTURE COINAGE. ALLOWING FOR THE CONTINUED SALE OF TREASURY SILVER AT A RATE OF TWO MILLION OUNCES A WEEK, PROVIDING FOR THE STOCKPILE REQUIREMENT, SILVER CERTIFICATE REDEMPTIONS AND COINAGE, OUR ESTIMATE THEN WAS THAT THE AMOUNT OF SILVER WE WOULD HAVE AVAILABLE ON JUNE 30, 1968, IN BULLION AND IN COINS, WOULD BE BETWEEN 350 AND 400 MILLION OUNCES. ADDITIONAL SILVER WOULD BECOME AVAILABLE AFTER THAT DATE AS A RESULT OF FUTURE INFLOWS OF SILVER COINAGE.

FOUR MONTHS HAVE ELAPSED SINCE THAT PROJECTION WAS MADE. OUR EXPERIENCE TO DATE, WHICH TAKES INTO ACCOUNT AN ADDITIONAL FOUR MONTH'S INFLOW OF SILVER COINS AND FOUR MONTH'S REDEMPTIONS OF SILVER CERTIFICATES, INDICATES THAT THIS ESTIMATE WAS ACCURATE. AS WE HAD ANTICIPATED, THE TREASURY'S TOTAL HOLDINGS OF SILVER IN BULLION AND COINS ARE NOW ACTUALLY LARGER THAN THEY WERE LAST SEPTEMBER, DESPITE THE COPPER STRIKE WHICH AFFECTS THOSE COMPANIES PRODUCING SILVER AS A BYPRODUCT OF COPPER.

AS OF SEPTEMBER 18, WE HAD IN MINT AND FEDERAL RESERVE INVENTORIES AN ESTIMATED 125 MILLION OUNCES OF SILVER IN THE FORM OF COINS. SINCE THAT TIME, AN ADDITIONAL 85 MILLION OUNCES HAS BEEN TAKEN IN, BRINGING THE TOTAL ESTIMATED HOLDINGS OF SILVER IN COINS UP TO 210 MILLION OUNCES. TO MEET THE SEPTEMBER ESTIMATE OF SILVER AVAILABLE FROM THIS SOURCE BY JUNE 30, WE NEED TO ADD ONLY 45 MILLION OUNCES. I AM CONFIDENT THAT WE WILL EASILY EXCEED THIS AMOUNT. WE HAVE NOT YET MELTED ANY OF THESE BECAUSE OF THEIR POSSIBLE USE AS A STANDBY SOURCE OF COINS IN CASE A NEED HAD DEVELOPED DURING THE 1967 CHRISTMAS SEASON. THIS CONTINGENCY IS NOW PAST. WHILE NOT NEEDED NOW, THE SILVER IN THESE COINS COULD BE MADE AVAILABLE FOR USEFUL PURPOSES BENEFICIAL TO BOTH SILVER USERS AND TAXPAYERS WHENEVER NECESSARY.

SALES OF TREASURY SILVER

WHILE THERE WILL ALWAYS BE DIFFERENCES OF OPINION OVER DETAILS, BOTH THE SILVER USERS AND TAXPAYERS HAVE ALREADY BENEFITED BY THE GSA SALES OF SILVER BULLION. SINCE AUGUST 4, GSA HAS SOLD 45 MILLION OUNCES OF SILVER FOR USE IN THE MANUFACTURE OF SILVER USING PRODUCTS, AND THESE SALES HAVE RESULTED IN A PROFIT OF \$22-1/2 MILLION TO TAXPAYERS.

FOR SOME TIME, IT HAS BEEN THE DESIRE OF THE TREASURY DEPARTMENT TO "GET OUT OF THE SILVER BUSINESS." BY THIS WE MEANT THAT WE WANTED TO STOP CONTROLLING THE PRICE OF SILVER, WHICH HAD BEEN NECESSARY IN RECENT YEARS IN ORDER TO PROTECT THE COINAGE. THIS FINALLY BECAME POSSIBLE LAST JULY.

NOW THERE STILL MAY BE SOME UNCERTAINTY AS TO WHY THE TREASURY'S WEEKLY SILVER OFFERING TO THE MARKET WAS SET AT TWO MILLION OUNCES. THE RATIONALE IS SIMPLY THIS: IF YOU EXCLUDE THE UNITED STATES FROM THE FREE WORLD, THERE IS VIRTUALLY NO SUPPLY-CONSUMPTION DEFICIT OF SILVER. WE ACCOUNT FOR THE ENTIRE FREE WORLD DEFICIT OF ABOUT 100 MILLION OUNCES A YEAR RIGHT HERE IN THE UNITED STATES. THIS IS NOT TO SAY THAT ALL THE SILVER SUPPLIES IN THE WORLD ARE MADE AVAILABLE FOR USE IN MANUFACTURING -- SOME OF IT MAY BE HELD FOR SPECULATIVE PURPOSES. BUT I THINK FEW WOULD EXPECT THE TREASURY DEPARTMENT TO MAKE UP FOR WHATEVER SPECULATIVE HOARDING TAKES PLACE. TO DO THAT WOULD BE TO CONTINUE CONTROLLING THE WORLD PRICE OF SILVER FROM WASHINGTON.

THE TWO MILLION OUNCES A WEEK RATE WOULD GENERALLY BE SUFFICIENT TO REPLACE BOTH THE U. S. AND THE WORLD DEFICIT, HAVING A GENERALLY NEUTRAL EFFECT ON THE PRICE OF SILVER. SELLING SILVER AT A GREATER RATE SHOULD THEORETICALLY HAVE A DEPRESSING EFFECT ON THE PRICE, WHILE SELLING IT AT A LOWER RATE SHOULD HAVE THE EFFECT OF PUSHING UP THE PRICE. SINCE IT WAS THE DESIRE OF THE COMMISSION THAT SILVER SALES SHOULD HAVE A NEUTRAL EFFECT ON THE PRICE, THE TWO MILLION OUNCES A WEEK RATE WAS SET. OF COURSE, THIS RATE CAN BE REVIEWED FROM TIME TO TIME. IT SHOULD BE REMEMBERED, HOWEVER, THAT THE SILVER SOLD AT THESE SALES IS SUPPLEMENTED BY THE ADDITIONAL SILVER BEING MADE AVAILABLE FOR USE THROUGH THE REDEMPTION OF SILVER CERTIFICATES.

REDEMPTION OF SILVER CERTIFICATES

DESPITE THE FACT THAT PREMIUMS ARE BEING PAID FOR SILVER CERTIFICATES BECAUSE THEY CAN BE USED TO OBTAIN SILVER FOR LESS THAN CURRENT MARKET PRICES, THE RATE OF THESE REDEMPTIONS IS NOT EXCEEDING EXPECTATIONS. THESE REDEMPTIONS HAVE AVERAGED ABOUT THREE MILLION OUNCES A MONTH SINCE THE BEGINNING OF JUNE.

AT THIS RATE, WE COULD EXPECT REDEMPTIONS TO BE IN THE NEIGHBORHOOD OF 20 MILLION OUNCES BETWEEN NOW AND JUNE 24, 1968, WHEN SILVER CERTIFICATES WILL NO LONGER BE EXCHANGEABLE FOR SILVER.

OTHER ISSUES

THERE ARE OTHER ISSUES OF INTEREST TO THIS GROUP WHICH WILL CONTINUE TO BE A SUBJECT OF DISCUSSION BY THE COINAGE COMMISSION. I WILL NOT GO INTO DETAIL ON THESE MATTERS.

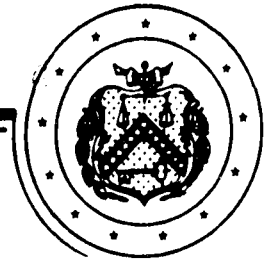
I THINK, HOWEVER, THAT ONE IMPORTANT CONSIDERATION SHOULD BE BORNE IN MIND, AND IT IS THIS: AMONG MANY MEMBERS OF CONGRESS, MEMBERS OF THE COINAGE COMMISSION, AND TREASURY OFFICIALS, THERE IS A DISTINCT LACK OF SYMPATHY FOR THOSE WHO ENGAGE IN HOARDING AND SPECULATION IN SILVER COINS. THEIR ACTIVITIES SEVERELY HANDICAPPED OUR ACTIONS TO DEAL WITH PAST COIN SHORTAGES. THE POSSIBILITY OF EVER PERMITTING THEM TO REAP WINDFALL PROFITS OF MILLIONS OF DOLLARS AT THE EXPENSE OF TAXPAYERS WILL, TO SAY THE LEAST, NOT BE VERY POPULAR.

CONCLUSION

I THINK THE RECORD OF CONGRESS, THE COMMISSION, AND THE TREASURY INDICATES A FULL AWARENESS OF THE PROBLEMS OF THE SILVER USERS. BUT I THINK WE WOULD ALL AGREE THAT THE GENERAL INTEREST OF THE NATION IS PARAMOUNT. UNTIL JULY OF LAST YEAR, YOU WERE THE BENEFICIARY OF THE POLICIES MADE NECESSARY BY COINAGE CONSIDERATIONS. YET, WHEN THE TIME CAME TO END THESE POLICIES, THIS GROUP WAS READY TO ACCEPT THE CHANGES, DESPITE THE RESULTING HIGHER COSTS OF YOUR RAW MATERIALS. FOR THIS OVERALL UNDERSTANDING OF THE TOTAL PROBLEM, WE IN THE GOVERNMENT ARE MOST GRATEFUL.

THANK YOU VERY MUCH.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 12, 1968

FOR IMMEDIATE RELEASE

ASSISTANT TREASURY SECRETARY TRUE DAVIS RECEIVES EXCEPTIONAL SERVICE AWARD

Secretary of the Treasury Henry H. Fowler has presented the Exceptional Service Award to Assistant Treasury Secretary True Davis.

Mr. Davis, former St. Joseph, Missouri, businessman, was cited for "extraordinary leadership and diplomacy in his supervision of the Bureau of Customs, the Bureau of Engraving and Printing, and until his transfer to the Department of Transportation, the United States Coast Guard."

"His outstanding qualifications and public-spirited service have contributed significantly to Treasury's enviable reputation for managerial and executive excellence. His warmth, thoughtfulness and manifest sincerity earned him the respect of all with whom he has associated," Mr. Fowler said.

Mr. Davis, who submitted his resignation for "compelling personal reasons," leaves the Department on January 15. He has served as Assistant Secretary since September, 1965. Appointed by President Kennedy, he had served as Ambassador to Switzerland from October 1963 until his nomination as Assistant Treasury Secretary by President Johnson.

In September, 1966, Mr. Davis assumed additional duties as United States Director of the Inter-American Development Bank.

Prior to his entry into Federal service, Mr. Davis was chairman of the board, president and/or director of 22 corporations. In 1967, he was presented the Americanism Award by the Veterans of Foreign Wars. Previous recipients of this award include Secretary of Defense Robert S. McNamara and J. Edgar Hoover, director of the Federal Bureau of Investigation.

The award was presented January 11 by Secretary Fowler at a formal dinner given in Mr. Davis' honor at the F Street Club. Secretary Fowler referred to Mr. Davis' career as an outstanding Government official, diplomat, and leading Midwestern business executive.

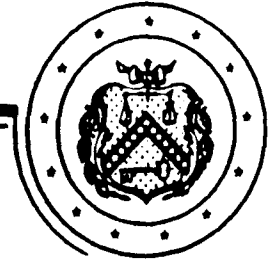
Among those attending were Under Secretary of the Treasury Joseph W. Barr, Under Secretary for Monetary Affairs, Frederick L. Deming; Mr. Olavi Munkki, Ambassador of Finland; Mr. Ricardo M. Arias E., Ambassador of Panama; Mr. Felix Schnyder, Ambassador of Switzerland.

Mr. T. Graydon Upton, deputy director of the Inter-American Development Bank; Mr. Harold F. Linder, president and chairman of the board of the Export-Import Bank of Washington, D. C.; Mr. Hobart Taylor, director of the Export Import Bank; Mr. Myer Feldman, former counsel to the President, and Admiral Willard J. Smith, Commandant of the U. S. Coast Guard.

Mr. Davis was born in St. Joseph, Missouri, December 23, 1919. Before starting his business career he attended Cornell University.

He is married to the former Virginia Brace Motter of St. Joseph, Missouri. They have three sons.

TREASURY DEPARTMENT



WASHINGTON, D.C.

PLEASE 6:30 P.M.,
January 15, 1968.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated October 19, 1967, and another series to be dated January 18, 1968, which were offered on January 10, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,000,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

TYPE OF ACCEPTED NONCOMPETITIVE BIDS:	91-day Treasury bills maturing April 18, 1968		:	182-day Treasury bills maturing July 18, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.723	5.052%	:	97.360	5.222%
Low	98.716	5.080%	:	97.348	5.246%
Average	98.718	5.072% <u>1/</u>	:	97.352	5.238% <u>1/</u>

1% of the amount of 91-day bills bid for at the low price was accepted
 31% of the amount of 182-day bills bid for at the low price was accepted

TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Albany	\$ 21,382,000	\$ 11,433,000	:	\$ 18,240,000	\$ 8,140,000
New York	2,610,151,000	1,133,881,000	:	1,476,106,000	719,695,000
Philadelphia	37,320,000	14,895,000	:	16,334,000	7,534,000
Richmond	53,623,000	30,098,000	:	59,291,000	36,091,000
San Francisco	23,372,000	9,866,000	:	5,289,000	4,989,000
St. Louis	50,501,000	19,988,000	:	40,180,000	14,730,000
Chicago	275,214,000	100,562,000	:	265,871,000	123,421,000
Louisville	63,439,000	46,095,000	:	52,440,000	35,690,000
Memphis	30,200,000	6,804,000	:	29,406,000	12,646,000
Cincinnati	30,665,000	24,115,000	:	17,089,000	12,437,000
San Antonio	30,452,000	20,452,000	:	22,319,000	11,119,000
San Francisco	326,159,000	83,859,000	:	101,084,000	13,755,000
TOTALS	\$3,552,478,000	\$1,502,048,000 <u>a/</u>		\$2,103,649,000	\$1,000,247,000 <u>b/</u>

Includes \$249,374,000 noncompetitive tenders accepted at the average price of 98.718
 Includes \$150,270,000 noncompetitive tenders accepted at the average price of 97.352
 These rates are on a bank discount basis. The equivalent coupon issue yields are 5.22% for the 91-day bills, and 5.47% for the 182-day bills.

TREASURY DEPARTMENT
Washington

FOR RELEASE: UPON DELIVERY

REMARKS OF THE HONORABLE JOSEPH W. BARR
THE UNDER SECRETARY OF THE TREASURY
BEFORE THE
ANNUAL CONVENTION OF THE
AGRICULTURAL NITROGEN INSTITUTE
MARRIOTT MOTOR HOTEL, ATLANTA, GEORGIA
WEDNESDAY, JANUARY 17, 1968, 1:00 P.M. , EST.

AGRICULTURAL DEVELOPMENT AND
THE BALANCE OF PAYMENTS

It gives me great pleasure to be here with you today, and particularly appreciate the opportunity to speak to the leaders of one of our most basic American industries.

I am keenly aware of the significance of this industry from several standpoints. I have been a farmer myself. Also, during the past year or two at the Treasury, I have worked very closely with the financial institutions of the Farm Credit Administration that have helped develop and expand American agriculture. Finally, I have had occasion to study at first hand the economic situation of the "third world" -- the developing nations of Latin America, Asia and Africa -- which so pointedly, and often poignantly, demonstrates the crucial role of agriculture in almost every economy.

It may surprise you to hear that a Treasury official does have occasion to concern himself with foreign agricultural development.

However, the Treasury serves a consultative function in connection with the international financial aspects of all of our country's foreign aid programs. Moreover, we are directly responsible for the United States' participation in the multilateral development lending institutions -- the World Bank and its International Development Association, the Inter-American Development Bank, the Asian Development Bank, and the new African Development Bank.

In my work on these matters and my travels in the developing nations, it has been confirmed many times over that the development of agriculture is one of the most essential -- if not the most essential -- ingredients in any viable national or regional economic program.

The contribution that the United States can make to this process is not limited to the amount of development assistance funds we provide. At least as important is the technical knowledge and production know-how we have developed so well in our own country, and which is so sorely needed in Asia, Africa and Latin America.

Moreover, I am not speaking solely of our moral and foreign policy commitment as a Nation to assist the economic development of these regions. For your industry, and for the United States, the call of economic self-interest supplements the prompting of

conscience, for we ourselves can benefit from participation in our neighbors' efforts to feed their growing populations.

In other words, American companies can and do participate in this process through sound business operations:

-- By exporting your products to Africa, Asia and Latin America;

-- By investing in production facilities in these areas.

The "third world", in fact, may be your most promising market in both respects. During the past decade your industry has grown at an annual rate of about 10% on a worldwide basis, and it should continue its rapid expansion. But the growth rate in the less-developed countries has been projected as high as 15%, to meet the surging demand in those regions.

I know that many of you are very much mindful of these facts. The United States exported over \$200 million of manufactured fertilizer in 1966; and large investments have been and are being made by many of your firms in the developing nations.

What I perhaps can add to the discussion is a few comments on the relationship between these developments and the Treasury's special responsibility for the United States balance of payments -- our national "commercial self-interest."

In principle, both your exports and your sound foreign investments are advantageous to our long-run international financial posture:

-- Your exports add immediately to our trade surplus, and also over the long run help develop potential markets for U.S. exports.

-- Your investments are negative factors in the short run, to the extent that they involve capital outflows; but usually they will be positive factors in the long run if they are profitable, as most American overseas investments have been.

That is a simple statement of the situation. But particularly today in the balance of payments area, a simple statement cannot be adequate. As you know, President Johnson found it necessary on New Year's Day to announce a series of special measures concerning the balance of payments.

I know that you recognize that it took extraordinary courage and determination for the President to take the action he took on New Year's Day. A President never lightly calls for sacrifice and restraint on the part of the American people -- in any year much less an election year. The President's action reflects his determination to put the welfare and security of the nation and free world above all smaller considerations, and it is only fitting that the rest of

respond in that same spirit.

Let me therefore review for you briefly the circumstances that impelled the President to act, and the way in which the program that has been announced affects all of us.

In seventeen of the past eighteen years, the United States has sustained deficits in its balance of payments. In the early post World War II years these deficits were desirable and necessary:

- to redistribute the world's monetary gold reserves and to supplement them with dollars, and

- to provide a favorable environment for economic recovery in Europe, while, at the same time, permitting many barriers to the international movement of goods and capital which dated back as far as the 1930s to be dismantled.

However, by 1961 the desirable consequences of our deficits were clearly being outweighed by undesirable consequences. There was no longer a shortage of dollars; on the contrary, foreign official monetary authorities became reluctant to hold increasingly large amounts of their international reserve assets in the form of dollars, and this began to pose a real and unacceptable threat to the strength of the dollar. As a result, beginning in 1961, the United States Government took action to improve the balance of payments.

The measures instituted during the early 1960s included both the public and the private sectors:

-- We began to "tie" all of our foreign aid programs to U.S. procurement.

-- We reduced the foreign exchange cost of our other major government expenditure item, our military deployments, by a variety of techniques.

-- We reduced private capital outflows through the voluntary restraint programs administered by the Commerce Department and the Federal Reserve Board, and we also enacted the Interest Equalization Tax.

-- We initiated programs to increase our receipts from foreign investment in the United States and foreign tourism in this country.

-- Last, but assuredly not least, we improved our basic trade position through a remarkable record of price stability coupled with economic growth.

Through 1965, this program made good progress. Our deficits cut by two-thirds -- from \$3.9 billion in 1960 to \$1.3 billion in 1965.

The direct and indirect consequences of the buildup in Southeast Asia toward the end of 1965 interrupted our progress toward payments

ilibrium. In 1967, the combined impact of:

- further increases in our foreign exchange expenditures for Vietnam,
- increased outflows of capital for private loans and investments abroad,
- a substantially increased "travel deficit", and
- an improved but still inadequate trade balance,

left the United States payments position in an unsatisfactory state.

In addition, the shock of British devaluation in November of 1967 had the effect of sharply increasing our balance-of-payments deficit during the fourth quarter. We now estimate that the 1967 deficit will be in excess of \$3.5 billion, more than half of it occurring in the fourth quarter.

Sterling devaluation raised an international swell of speculation. We have turned it back, with the cooperation of our allies, and at some expense. But the threat to the dollar and the international monetary system must be answered in a more fundamental way. The shock provided by the British crisis dictated that new and decisive measures be undertaken immediately to bring the United States balance of payments into equilibrium.

The President, in his New Year's message, outlined four critical conditions which the new United States program must meet

In solving our problem. It must:

-- "Sustain the growth, strength and prosperity of our own economy.

-- "Allow us to continue to meet our international responsibilities in defense of freedom, in promoting world trade, and in encouraging economic growth in the developing countries.

-- "Engage the cooperation of other free nations, whose stake in a sound international monetary system is no less compelling than our own.

-- "Recognize the special obligation of those nations with balance-of-payments surpluses, to bring their payments into equilibrium."

What is the program the President has laid out within these conditions?

First, to sustain the prosperity of our domestic economy, as well as protect our international financial and commercial position, President Johnson called for prompt final action on the program of fiscal restraint that he proposed last year. The Congress and the Administration already have put into effect agreed reductions in government expenditures. The President now has called for enactment of the other part of the program -- the tax proposals -- as the first order of business.

Second, the President has set forth a series of specific measures dealing with each of the major components of our international payments position, designed to move us promptly to equilibrium.

Our balance of payments receipts come principally in these categories:

- A favorable trade surplus
- Dividends and other returns on foreign investments
- Foreign investment in the United States

On the outflow side, the principal items are:

- government expenditures for
 - military deployments overseas, in Vietnam and elsewhere
 - bilateral and multilateral foreign aid
- Private investment and lending abroad
- A net deficit for tourism and travel

The President's program calls for action in each of these categories, and is designed to obtain both immediate and longer-run improvement in our payments position.

1. On the trade account, one of the most fundamental sources of long-run strength in our international payments, we have recently concluded a basic step forward. The Kennedy Round of tariff negotiations will lead to a substantial reduction in tariff barriers,

and this will provide the opportunity for a further expansion in United States exports. We now must seek to reduce the impact of non-tariff barriers. Of these, perhaps the most significant are the border taxes imposed by a number of countries. Tax harmonization within the Common Market, although unobjectionable in itself, can disadvantage our competitive position in those countries. We have initiated discussions with our major trading partners and have begun exploring legislative measures to solve this problem.

2. Our export position also is effected by the availability of export financing. The President therefore has proposed both the liberalization of the rediscount arrangements in the Export-Import Bank, and the creation of a special new facility in the Bank to finance export sales of a slightly riskier nature. The latter proposal would particularly encourage sales to some of the developing nations, and therefore it relates directly to the subject with which I opened my remarks today.

3. The Foreign Investors Tax Act of 1966 was a major step in the direction of encouraging foreigners to invest in the United States economy. Following up on this, the government has engaged in a cooperative effort with the private financial community to make foreign investors aware of the opportunities in this area. These efforts will be continued and intensified.

4. On the government account, we have over the past several years effected substantial balance of payments savings through virtually complete tying of our foreign aid, and measures including reductions in overseas military personnel and in the number of foreign nationals employed abroad, maximum United States procurement, military sales to our allies, and a long list of other steps. Nonetheless the President has set a target of \$500 million in further savings in this category. Just last week, in this connection, he issued instructions to reduce expenditures of our foreign aid program by \$100 million. We are vigorously pursuing other actions to achieve the President's goal on the government account.

5. To reduce our "tourist deficit", the President asked all Americans to defer nonessential travel outside the Western Hemisphere. He also has called for prompt consideration of possible legislative measures to insure the achievement of a \$500 million improvement in this category in the balance of payments.

A call for such a reduction in travel by Americans was issued reluctantly, and only as a temporary measure. Over the long run, our objective must be to meet the problem in this area by increasing foreign travel to the United States. The President already had appointed a special blue ribbon task force, headed by former Ambassador Robert McKinney, to recommend positive measures in this

direction. He now has requested a speedup in the work of the task force, so that additional programs to increase our tourism receipts can be implemented at the earliest possible date.

6. Finally, the President determined that it is necessary to further tighten the existing voluntary restraints on private investment and bank lending overseas, and to make the investment controls mandatory to insure evenhanded application of the tightened limitations. As I have mentioned, although our foreign investments are a source of balance of payments strength over the long run, they do involve heavy short-run balance of payments outflows. To bring our payments immediately into equilibrium, some further moderation in these outflows is essential.

In taking this last step, the President took special account of the effects upon the developing nations and upon other countries that rely heavily on the United States as a source of capital. For this reason, I believe that your industry, and American companies in general, can and should continue to give active consideration to further overseas investment in the less developed countries.

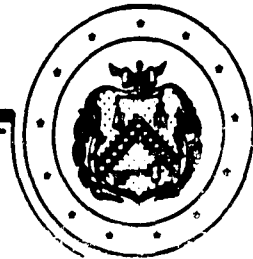
Not only are the overall limitations on such investments relatively liberal, but the program will be administered as flexibly as possible within the limitations to permit the continuation at about present levels of investment which are so important to the host nations

as well as to the United States.

I believe that the President's program is a sound one. It is designed to deal decisively with the urgent international financial problem that confronts the United States and all of the free world. It calls for understanding and restraint on the part of the American people, and for cooperation on the part of other nations. The response thus far -- both domestically and internationally -- has confirmed my belief that such understanding and cooperation will be forthcoming. With it, we shall succeed.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

January 17, 1968

OR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders or two series of Treasury bills to the aggregate amount of 2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing January 25, 1968, in the amount of 2,501,384,000, as follows:

91-day bills (to maturity date) to be issued January 25, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated October 26, 1967, and to mature April 25, 1968, originally issued in the amount of 1,000,763,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated January 25, 1968, and to mature July 25, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, 5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard Time, Monday, January 22, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

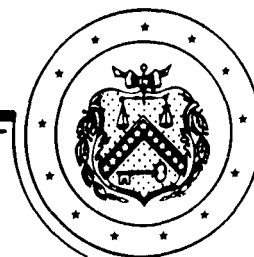
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on January 25, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing January 25, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 18, 1968

FOR A.M. RELEASE
FRIDAY, JANUARY 19, 1968

TREASURY ISSUES DOCUMENTARY REPORT ON U.S. BALANCE OF PAYMENTS DESCRIBING NEED FOR PRESIDENT'S ACTION PROGRAM

The U. S. Treasury Department today released a documentary report on "Maintaining the Strength of the United States Dollar in a Long Free World Economy."

The 229-page document describes in detail the background and reasons for the Action Program announced by President Johnson in his New Year's Day message to the nation on the balance of payments. The report also reviews what has been done and what is proposed -- both short and long-term -- to bring the nation's balance of payments to equilibrium and keep it there -- an equilibrium described by the President as "a national and international responsibility of the highest priority."

In a foreword to the report, Treasury Secretary Henry H. Fowler said that the U.S. program necessarily must involve cooperative actions and with other nations. "Without such cooperation," Mr. Fowler said, "it is not possible to achieve U.S. payments equilibrium in a manner conducive in the long term to an increased flow of trade and vital and to viable and sturdy arrangements for the security and development of the free world." Achievement of balance compatible with these objectives, he noted, will call for adjustments by America's trading partners and allies as well as by the United States.

The Secretary also said that the acceptance and execution of the program will require the understanding, support and participation of the entire Executive Branch of the Government, the Congress and the American people -- business, labor, financial and farm groups alike. He advocated speeding-up plans for the creation of new reserves -- Special Drawing Rights in the International Monetary Fund -- "as our government toward payments balance curbs the flow of dollars into

ernational reserves." A plan for such Special Drawing Rights approved at Rio de Janeiro last September by the IMF's member countries.

The Treasury document cited these "key resources" as ones which the U.S. has the strength to deal with its underlying long-range payments problems both constructively and sensibly:

- A strong economy with a Gross National Product in excess of \$800 billion -- representing 40 to 45 percent of world output;
- a large stock of foreign assets with powerful earnings potential. Gross assets abroad -- public and private -- total more than \$110 billion. The U.S. net long-term asset position -- approximately \$70 billion -- has increased every year for 20 years. Private overseas assets alone now generate annual earnings of about \$6 billion;
- a basic trade surplus which totaled approximately \$4 billion last year on which the U.S. must build;
- a strong reserve position -- nearly \$15 billion, or about 20 percent of world reserves -- even after losses of the past few years.

The report pointed out that "we can build on these elements of strength and move toward balance of payments equilibrium through short- and long-range measures vigorously implemented," and that passage of time "will ameliorate forces that presently exacerbate the balance payments deficit and hinder the fundamental progress achieved."

Ideally, the Treasury Department said, "the United States would solve its balance of payments problem through a gradual, long-range approach in which there was no interference with the free movement of goods and services, capital or people." However, the Treasury said, "the situation that confronts the United States today requires prompt and major corrective action. Long-term measures alone that hold gradually over time are not sufficient."

The Action Program announced by President Johnson on January 1 consists of general and specific measures, including short-range and long-range actions, designed to reduce sharply the U.S. payments deficit in 1968, and bring it into -- or close to -- equilibrium.

These measures include:

- Mandatory limits on direct investments abroad by U.S. companies to reduce the payments deficit in 1968 by \$1 billion;
- A voluntary program for reducing foreign credits from U.S. banks and other financial institutions, expected to bring a net inflow of at least \$500 million in such credits in 1968;
- Encouragement of more foreign travel to the U.S.; deferment of non-essential American travel outside the Western Hemisphere for the next two years, and exploring of appropriate legislation, all to reduce the U.S. travel deficit by \$500 million;
- A further reduction of \$500 million in the foreign exchange impact of government programs overseas through negotiations with our NATO allies to minimize foreign exchange costs of keeping our troops in Europe by purchases in the United States of more defense equipment and investment of exchange receipts in long-term U.S. securities; reduction of personal spending by U.S. forces and their dependents; reduction in the number of American civilians working overseas, and reduction of Agency for International Development foreign exchange costs by at least \$100 million in 1968;
- Activities to increase the U.S. trade surplus by encouraging exports, with a goal of a \$500 million increase in exports in 1968. Congress will be asked to support an intensified five-year program to promote the sale of U.S. industrial and agricultural products in foreign markets; \$500 million will be earmarked by the Export-Import Bank to provide better export insurance, to expand guarantees for export financing, and to broaden the scope of Government financing of exports; the Export-Import Bank will encourage banks to help firms increase their exports, and the Commerce Department will begin a Joint Export Association program to provide financial support to American companies joining together to sell abroad. Discussions have been initiated, particularly with nations having balance of payments surpluses, to minimize the handicaps to U.S. trade which arise from differences in national tax systems.

The Treasury said the Action Program "will entail sacrifices in this country and it may cause difficulties for some foreign countries." But in order to assure a fair sharing of these sacrifices, the Treasury said, the program has been widely spread over all sectors of the U.S. economy. To minimize adverse effects on the world economy, the program distinguishes among groups of countries on the basis of their ability to absorb reductions in their foreign exchange receipts.

"Restrictive measures are temporary," the Treasury said. "The policy of the United States is to support the unrestricted international flow of goods, services and capital under a stable international monetary system based on fixed values for currencies measured in terms of gold or the dollar, linked at \$35 an ounce."

An appropriate long-range balance of payments solution for the United States must, the Treasury said, be based on a substantial and growing surplus in trade and services, including earnings from foreign investments.

"Unfortunately, after a period of unprecedented stability, prices and costs rose in 1966 and 1967. The rapid expansion of the U.S. economy that is now under way threatens a further rise in prices and costs. This would endanger our economic prosperity and undermine our competitive position in world markets...The most important business before Congress is to complete this anti-inflation program by enacting a temporary surcharge on income and profits taxes," the Treasury said.

"Even a strong fiscal policy and a stringent credit policy cannot maintain price stability," it noted, "unless business and labor are willing to follow price-wage practices that conform to the needs of our economy...The country cannot afford the loss of output resulting from crippling work stoppages in critical industries. They reduce our exports and increase our imports."

The mandatory controls on direct investment outflows, the earlier voluntary guidelines for banks and the request to defer essential travel outside the Western Hemisphere "are all measures which the United States has adopted very reluctantly. The high cost of these measures is in itself a dramatic witness to the priority the United States attaches to doing its full share in reducing the balance in world payments -- and to the recognition that a break-down of the system would have involved far higher costs for the United States and even more for the world economy," the report said.

The reduction of the deficit in the U.S. balance of payments must be allowed, and even encouraged, by the rest of the world, the Treasury pointed out, adding that "major positive measures" by other countries are required to bring about payments equilibrium consistent with the achievement of sound world economic growth and freer as well as growing international transactions."

Treasury said it is a matter of the highest priority for European governments, particularly the governments of the EEC countries, to face fully the fact that their balance of payments positions must show a large change from excessive surplus to much more moderate surplus, perhaps even to moderate deficit, for a short period.

The document will be placed on sale in the near future by the Superintendent of Documents, Government Printing Office.

143A

MAINTAINING THE STRENGTH
of
THE UNITED STATES DOLLAR
in
A STRONG FREE WORLD ECONOMY

U. S. TREASURY DEPARTMENT
January 1968

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FOREWORD

As Secretary of the Treasury and Chairman of the Cabinet Committee on the Balance of Payments, I am releasing for public information a U. S. Treasury Department Report entitled "MAINTAINING THE STRENGTH OF THE UNITED STATES DOLLAR IN A STRONG FREE WORLD ECONOMY."

This document describes in detail the background and reasons for the Action Program announced by President Johnson in his "Message to the Nation" on the balance of payments of January 1, 1968. It describes what we have done to date and what we propose to do, both over the short and long term, to bring our balance of payments into equilibrium and keep it there--as, in the words of the President, "a national and international responsibility of the highest priority."

What we do must be compatible with the strength and stability of the U.S. economy because, in the final analysis, that is the strength of the dollar.

What we do in this American program is related to our international responsibilities because without a strong dollar, a healthy, stable international monetary system is not possible.

Moreover, this American program must, as a counterpart, involve cooperative actions by and with other nations. Without that cooperation, it is not possible to achieve U.S. payments equilibrium in a manner conducive in the long term to an increased flow of trade and capital and to viable and sturdy arrangements

for the security and development of the free world. Achievement of balance compatible with these objectives will call for adjustments by America's trading partners and allies as well as by the United States.

To secure the acceptance and execution of this program will require the understanding, support and participation of the entire Executive Branch, the Congress and the American people--business, labor, financial and farm groups alike--and also the governments and peoples of other nations with whom this country is cooperating in myriad trading, financial, security and developmental relationships.

As our movement toward payments balance curbs the flow of dollars into international reserves, the member countries of the International Monetary Fund, including the United States, should speed up plans for the creation of new reserves--Special Drawing Rights in the Fund--pursuant to the plan approved at Rio de Janeiro in September 1967.

It is the purpose of this Report to give some measure of vital understanding of the Action Program and its importance at this point of time to the people of the United States and peoples everywhere. Given understanding, support of and participation in its achievement are sure to follow.

Henry H. Fowler
Henry H. Fowler
Secretary of the Treasury

BALANCE OF PAYMENTS

Statement by the President Outlining a Program of Action.

January 1, 1968

WHERE WE STAND TODAY

I want to discuss with the American people a subject of vital concern to the economic health and well-being of this nation and the free world.

It is our international balance of payments position.

The strength of our dollar depends on the strength of that position.

The soundness of the free world monetary system, which rests largely on the dollar, also depends on the strength of that position.

To the average citizen, the balance of payments, and the strength of the dollar and of the international monetary system, are meaningless phrases. They seem to have little relevance to our daily lives. Yet their consequences touch us all -- consumer and captain of industry, worker, farmer, and financier.

More than ever before, the economy of each nation is today deeply intertwined with that of every other. A vast network of world trade and financial transactions ties us all together. The prosperity of every economy rests on that of every other.

More than ever before, this is one world -- in economic affairs as in every other way.

Your job, the prosperity of your farm or business, depends directly or indirectly on what happens in Europe, Asia, Latin America, or Africa.

The health of the international economic system rests on a sound international money in the same way as the health of our domestic economy rests on a sound domestic money. Today, our domestic money -- the U.S. dollar -- is also the money most used in international transactions. That money can be sound at home -- as it surely is -- yet can be in trouble abroad -- as it now threatens to become.

In the final analysis its strength abroad depends on our earning abroad about as many dollars as we send abroad.

U.S. dollars flow from these shores for many reasons -- to pay for imports and travel, to finance loans and investments, and to maintain our lines of defense around the world.

When that outflow is greater than our earnings and credits from foreign nations, a deficit results in our international accounts.

For 17 of the last 18 years we have had such deficits. For a time those deficits were needed to help the world recover from the ravages of World War II. They could be tolerated by the United States and welcomed by the rest of the world. They distributed more equitably the world's monetary gold reserves and supplemented them with dollars.

Once recovery was assured, however, large deficits were no longer needed and indeed began to threaten the strength of the dollar. Since 1961 your Government has worked to reduce that deficit.

By the middle of the decade, we could see signs of success. Our annual deficit had been reduced two-thirds -- from \$3.9 billion in 1960 to \$1.3 billion in 1965.

In 1966, because of our increased responsibility to arm and supply our men in Southeast Asia, progress was interrupted, with the deficit remaining at the same level as 1965 -- about \$1.3 billion.

In 1967, progress was reversed for a number of reasons:

- Our costs for Vietnam increased further.
- Private loans and investments abroad increased.
- Our trade surplus, although larger than 1966, did not rise as much as we had expected.
- Americans spent more on travel abroad.

Added to these factors was the uncertainty and unrest surrounding the devaluation of the British pound. This event strained the international monetary system. It sharply increased our balance of payments deficit and our gold sales in the last quarter of 1967.

THE PROBLEM

Preliminary reports indicated that these conditions may result in a 1967 balance of payments deficit in the area of \$3.5 to \$4 billion -- the highest since 1960. Although some factors affecting our deficit will be more favorable in 1968, my advisors and I are convinced that we must act to bring about a decisive improvement.

We cannot tolerate a deficit that could threaten the stability of the international monetary system -- of which the U.S. dollar is the bulwark.

We cannot tolerate a deficit that could endanger the strength of the entire free world economy, and thereby threaten our unprecedented prosperity at home.

A TIME FOR ACTION

The time has now come for decisive action designed to bring our balance of payments to -- or close to -- equilibrium in the year ahead.

The need for action is a national and international responsibility of the highest priority.

I am proposing a program which will meet this critical need, and at the same time satisfy four essential conditions:

- Sustain the growth, strength, and prosperity of our own economy.
- Allow us to continue to meet our international responsibilities in defense of freedom, in promoting world trade, and in encouraging economic growth in the developing countries.
- Engage the cooperation of other free nations, whose stake in a sound international monetary system is no less compelling than our own.
- Recognize the special obligation of those nations with balance of payments surpluses to bring their payments into equilibrium.

THE FIRST ORDER OF BUSINESS

The first line of defense of the dollar is the strength of the American economy.

No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus.

No challenge before business and labor is more urgent than this: To exercise the utmost responsibility in their wage-price decisions, which affect so directly our competitive position at home and in world markets.

I have directed the Secretaries of Commerce and Labor, and the Chairman of the Council of Economic Advisers to work with leaders of business and labor to make more effective our voluntary program of wage-price restraint.

I have also instructed the Secretaries of Commerce and Labor to work with unions and companies to prevent our exports from being reduced or our imports increased by crippling work stoppages in the year ahead.

A sure way to instill confidence in our dollar -- both here and abroad -- is through these actions.

THE NEW PROGRAM

But we must go beyond this, and take additional action to deal with the balance of payments deficit.

Some of the elements in the program I propose will have a temporary but immediate effect. Others will be of longer range.

All are necessary to assure confidence in the American dollar.

TEMPORARY MEASURES

1. Direct Investment

Over the past three years, American business has cooperated with the government in a voluntary program to moderate the flow of U.S. dollars into foreign investments. Business leaders who have participated so wholeheartedly deserve the appreciation of their country.

But the savings now required in foreign investment outlays are clearly beyond the reach of any voluntary program. This is the unanimous view of all my economic and financial advisers and the Chairman of the Federal Reserve Board.

To reduce our balance of payments deficit by at least \$1 billion in 1968 from the estimated 1967 level, I am invoking my authority under the Banking Laws to establish a mandatory program that will restrain direct investment abroad.

This program will be effective immediately. It will insure success and guarantee fairness among American business firms with overseas investments.

The program will be administered by the Department of Commerce, and will operate as follows:

- As in the voluntary program, overall and individual company targets will be set. Authorizations to exceed these targets will be issued only in exceptional circumstances.

-- New direct investment outflows to countries in continental Western Europe and other developed nations not heavily dependent on our capital will be stopped in 1968. Problems arising from work already in process or commitments under binding contracts will receive special consideration.

-- New net investments in other developed countries will be limited to 65% of the 1965-66 average.

-- New net investments in the developing countries will be limited to 110% of the 1965-66 average.

This program also requires businesses to continue to bring back foreign earnings to the United States in line with their own 1964-66 practices.

In addition, I have directed the Secretary of the Treasury to explore with the Chairmen of the House Ways and Means Committee and Senate Finance Committee legislative proposals to induce or encourage the repatriation of accumulated earnings by U.S.-owned foreign businesses.

2. Lending by Financial Institutions

To reduce the balance of payments deficit by at least another \$500 million, I have requested and authorized the Federal Reserve Board to tighten its program restraining foreign lending by banks and other financial institutions.

Chairman Martin has assured me that this reduction can be achieved:

- Without harming the financing of our exports;
- Primarily out of credits to developed countries without jeopardizing the availability of funds to the rest of the world.

Chairman Martin believes that this objective can be met through continued cooperation by the financial community. At the request of the Chairman, however, I have given the Federal Reserve Board standby authority to invoke mandatory controls, should such controls become desirable or necessary.

3. Travel Abroad

Our travel deficit this year will exceed \$2 billion. To reduce this deficit by \$500 million:

- I am asking the American people to defer for the next two years all nonessential travel outside the Western Hemisphere.
- I am asking the Secretary of the Treasury to explore with the appropriate congressional committees legislation to help achieve this objective.

4. Government Expenditures Overseas

We cannot forego our essential commitments abroad, on which America's security and survival depend.

Nevertheless, we must take every step to reduce their impact on our balance of payments without endangering our security.

Recently, we have reached important agreements with some of our NATO partners to lessen the balance of payments cost of deploying American forces on the Continent -- troops necessarily stationed there for the common defense of all.

Over the past three years, a stringent program has saved billions of dollars in foreign exchange.

I am convinced that much more can be done. I believe we should set as our target avoiding a drain of another \$500 million on our balance of payments.

To this end, I am taking three steps.

First, I have directed the Secretary of State to initiate prompt negotiations with our NATO allies to minimize the foreign exchange costs of keeping our troops in Europe. Our allies can help in a number of ways, including:

- The purchase in the U.S. of more of their defense needs.

-- Investments in long-term United States securities.

I have also directed the Secretaries of State, Treasury and Defense to find similar ways of dealing with this problem in other parts of the world.

Second, I have instructed the Director of the Budget to find ways of reducing the number of American civilians working overseas.

Third, I have instructed the Secretary of Defense to find ways to reduce further the foreign exchange impact of personal spending by U.S. forces and their dependents in Europe.

LONG-TERM MEASURES

5. Export Increases

American exports provide an important source of earnings for our businessmen and jobs for our workers.

They are the cornerstone of our balance of payments position.

Last year we sold abroad \$30 billion worth of American goods.

What we now need is a long-range systematic program to stimulate the flow of the products of our factories and farms into overseas markets.

We must begin now.

Some of the steps require legislation:

I shall ask the Congress to support an intensified five year, \$200 million Commerce Department program to promote the sale of American goods overseas.

I shall also ask the Congress to earmark \$500 million of the Export-Import Bank authorization to:

- Provide better export insurance.
- Expand guarantees for export financing.
- Broaden the scope of Government financing of our exports.

Other measures require no legislation.

I have today directed the Secretary of Commerce to begin a Joint Export Association program. Through these Associations, we will provide direct financial support to American corporations joining together to sell abroad.

And finally, the Export-Import Bank -- through a more liberal rediscount system -- will encourage banks across the Nation to help firms increase their exports.

6. Nontariff Barriers

In the Kennedy Round, we climaxed three decades of intensive effort to achieve the greatest reduction

in tariff barriers in all the history of trade negotiations. Trade liberalization remains the basic policy of the United States.

We must now look beyond the great success of the Kennedy Round to the problems of nontariff barriers that pose a continued threat to the growth of world trade and to our competitive position.

American commerce is at a disadvantage because of the tax systems of some of our trading partners. Some nations give across-the-board tax rebates on exports which leave their ports and impose special border tax charges on our goods entering their country.

International rules govern these special taxes under the General Agreement on Tariffs and Trade. These rules must be adjusted to expand international trade further.

In keeping with the principles of cooperation and consultation on common problems, I have initiated discussions at a high level with our friends abroad on these critical matters -- particularly those nations with balance of payments surpluses.

These discussions will examine proposals for prompt cooperative action among all parties to minimize

the disadvantages to our trade which arise from differences among national tax systems.

We are also preparing legislative measures in this area whose scope and nature will depend upon the outcome of these consultations.

Through these means we are determined to achieve a substantial improvement in our trade surplus over the coming years. In the year immediately ahead, we expect to realize an improvement of \$500 million.

7. Foreign Investment and Travel in the United States

We can encourage the flow of foreign funds to our shores in two other ways:

- First, by an intensified program to attract greater foreign investment in U. S. corporate securities, carrying out the principles of the Foreign Investors Tax Act of 1966.
- Second, by a program to attract more visitors to this land. A Special Task Force headed by Robert McKinney of Santa Fe, N. Mex., is already at work on measures to accomplish this. I have directed the task force to report within 45 days on the immediate measures that can be taken, and to make its long-term recommendations within 90 days.

MEETING THE WORLD'S RESERVE NEEDS

Our movement toward balance will curb the flow of dollars into international reserves. It will therefore be vital to speed up plans for the creation of new reserves -- the Special Drawing Rights -- in the International Monetary Fund. These new reserves will be a welcome companion to gold and dollars, and will strengthen the gold exchange standard. The dollar will remain convertible into gold at \$35 an ounce, and our full gold stock will back that commitment.

A TIME FOR RESPONSIBILITY

The program I have outlined is a program of action.

It is a program which will preserve confidence in the dollar, both at home and abroad.

The U. S. dollar has wrought the greatest economic miracles of modern times.

It stimulated the resurgence of a war-ruined Europe.

It has helped to bring new strength and life to the developing world.

It has underwritten unprecedented prosperity for the American people, who are now in the 83d month of sustained economic growth.

A strong dollar protects and preserves the prosperity of businessman and banker, worker and farmer -- here and overseas.

The action program I have outlined in this message will keep the dollar strong. It will fulfill our responsibilities to the American people and to the free world.

I appeal to all of our citizens to join me in this very necessary and laudable effort to preserve our country's financial strength.

#

SUMMARY AND CONCLUSIONS

The United States must, can and will correct its balance of payments problem. The action program announced by President Johnson on January 1st is a national and international responsibility of the highest priority. Our task now is to assure the success of that program.

This paper explains the importance of correcting our balance of payments problem and explains why a new program to achieve it has become necessary. Beyond that, it describes the kinds of adjustments that must now occur--in the United States and in other countries--if the new program is both to restore balance of payments equilibrium and to promote continued prosperity and economic growth in the United States and throughout the Free World.

The world faces the need to restore equilibrium in international transactions. The United States must cut its payments deficit now; it cannot allow its official reserve assets to run down without limit. Moreover, the smooth functioning of the present international monetary system, under which unparalleled prosperity and growth have been attained, requires that large and persistent surpluses and deficits be eliminated, and in particular that confidence in the main reserve currency--the U.S. dollar--be maintained.

The United States has acted decisively. It is in the interest of countries which have enjoyed balance of payments surpluses, as well as of the rest of the world, that they too act to facilitate the needed adjustments and hasten the day when undesirable restrictions can be removed. They must accept reductions in their surpluses. This involves policies leading to higher domestic levels of activity within the framework of stable prices. It requires receptivity to imports from developed and less-developed countries, acceptance of an appropriate share of the burdens of mutual defense and of economic development assistance, and greater encouragement of capital outflow.

A large part of the required adjustment can be achieved over the longer term without disturbance to the patterns of economic activity by which men earn their living. The United States must be able to finance its share of world trade and investment and defense without jeopardizing its international liquidity position and hence the very structure of the international monetary system. Europe must now arrange to play a larger role in the financing of all these activities and devote less of its financial resources to the accumulation of gold and foreign exchange reserves.

The Balance of Payments Problem

It is understandable that even today many of our citizens are not fully aware of the urgent necessity of restoring a balance in our international payments. The U. S. economy is strong and prosperous. Foreign transactions of the United States, while very large in terms of the international economy, are small relative to our total production, consumption and investment--relatively smaller than for almost any other country. Why should the United States or the world be disturbed about a balance of payments deficit that is only a fraction of one percent of our output of goods and services?

Despite the magnitude of our domestic economy, the foreign transactions of the United States are important to our economic well-being and indispensable to the free world. Imports of foodstuffs, raw materials and finished goods are essential for our production and our high standard of living. The overseas expenditures of the U. S. Government for foreign aid and defense are vital to our objectives of world peace and security. U.S. private foreign investment is profitable to our banking and business institutions and important for economic growth and development in many other countries. And travel enhances international understanding.

The cost of imports, travel abroad, security and aid expenditures overseas, and foreign investment must be paid for by exports of goods and services, the earnings of our foreign loans and investments, travel and investment by foreigners in the United States and other foreign exchange receipts.

In 1966 our total international payments, in so far as they can be measured, amounted to \$49 billion while our foreign receipts were nearly \$48 billion. The resulting deficit in our balance of payments amounted to \$1.36 billion. This increased to about \$3.5 to \$4 billion last year.

When our total foreign payments are more than our foreign receipts, some or all of the excess dollars received by foreigners are sold to their central banks, which can use them in a variety of ways--including holding them as reserves or buying gold from the United States. The result tends to be a deterioration in the liquidity position of the United States, as the ratio of its reserve assets (e.g., gold) declines relative to its liquid liabilities (e.g., dollars held by foreigners).

The United States is the major international banking center holding large deposits both for monetary authorities and for private banks, corporations and individuals. The dollar functions as the principal international currency. Its liquidity position must remain strong, like that of any bank, to retain the confidence of its depositors.

The U. S. deficit was welcome when it first developed in the early postwar years. Then, as now, the deficit consisted of capital outflows--both public and private--that exceeded the U. S. surplus on goods and services. It supplied reserves to foreign countries--principally European--which had drawn them down to finance the war and postwar reconstruction. More basically, the U. S. capital flow to Europe contributed to the European economic miracle and the smooth transition to European economic unity.

In the late 1950's, however, U. S. deficits began to become a source for concern. Not only did the size of the deficits rise, but they were financed more by sales of gold and less by foreign accumulation of dollars than in prior years. Although some foreign central banks had what they considered to be adequate supplies of dollars in their reserves, many countries had small reserves

and were still eager to add to their dollar reserves. There was still no high urgency about restoring balance to our international accounts. Nevertheless, President Eisenhower instructed the Department of Defense and other Government agencies to economize on their foreign exchange expenditures. With three years of large deficits culminating in a speculative outbreak in the London gold market in October 1960, new measures were called for. President Kennedy proposed measures to increase exports and other receipts, intensified efforts to cut government balance of payments costs, and later introduced the Interest Equalization Tax to hold down U. S. purchases of foreign securities. A sharp rise in U. S. capital outflows in 1964 made it necessary for President Johnson to introduce a voluntary program for holding down direct investment and bank loans abroad.

The rationale behind these measures was as follows:

- First, while the rising outflow of U. S. capital was moderated, U. S. international balance would be restored by the growth of the U. S. surplus on non-capital transactions.
- Second, modestly restraining the increase in U. S. foreign investments, particularly those in Western Europe, would have only a small effect on world economic growth in sharp contrast to other alternatives and would yield satisfactory balance of payments results over time.

From 1958-60 to 1965, we made good progress in reducing our payments deficit because of the growth of our exports of goods and services relative to our imports, because of the rise in earnings from our foreign investments, and because of the reduction in capital outflow in 1965.

In 1965 and 1966, we reduced our liquidity deficit by almost two-thirds from the average deficits of 1958-60 and one-half from the average of 1961-64. As this period progressed, however, the accelerated expansion of the U. S. economy and the war in Vietnam placed renewed pressure on the balance of payments. The boom resulted in an extraordinary increase in imports. The costs of our forces in Vietnam added substantially to our foreign payments.

Thus, while the voluntary program reduced the capital outflow considerably from the peak of 1964, the payments deficit persisted. There was retrogression in the first three quarters of 1967 because the foreign exchange costs of Vietnam rose further, private capital outflow increased, net tourist expenditures rose, and the European economic slowdown reduced European imports--and our exports.

The devaluation of sterling in November 1967 brought the balance of payments problem to an acute stage. Against the background of a persistent deficit in the U. S. balance of payments, the British move resulted in a weakening of confidence in currencies and was accompanied by a burst of speculative buying of gold and a resulting large loss of U. S. gold reserves in November and December. This was a threat not only to the dollar but also to the international monetary system as a whole.

While the speculation was repulsed with the cooperation of most of the members of the gold pool, it underlined the urgency of placing the dollar once more in an impregnable position. The time had come when it was necessary and desirable to take new and decisive measures to move the U. S. payments position strongly toward balance.

What was the best way to achieve this? Depressing the American economy is as unacceptable to most other nations of the world as it is to the United States. The United States occupies a unique role in the world economy. It is by far the largest exporting and importing country. It is the principal source of international capital. It is the largest donor of aid. Military forces stationed abroad are indispensable to the security of many countries--including the United States. For all these reasons the entire world is affected by the U. S. economy and the U. S. balance of payments. The volume of international trade, the prices of basic commodities, the cost of money and even the level of production and employment abroad respond to the U. S. economy. The United States must seek a solution to the payments imbalance through the expansion of the world economy rather than the contraction of its own, and consequently the world, economy.

The action program announced by President Johnson on January 1 avoids deflation, while underlining the urgent need for prompt enactment of an anti-inflationary tax increase, along with proper control of public expenditures, appropriate monetary policy, responsible wage and price decisions on the part of business and labor, and other measures to increase our export surplus.

Because the need to cut the U. S. payments deficit is urgent, the program also includes new and stringent temporary restraints on outflows of U. S. private capital and on foreign travel by Americans. Indeed, it is upon these uncongenial measures that we must rely for the largest immediate effects. These measures have been adopted reluctantly as an emergency matter. How soon they can be relaxed will depend greatly upon our own efforts to increase our trade surplus, reduce or neutralize government expenditures abroad, and encourage foreign travel and investment in the United States. It will depend upon the policy responses of other countries, especially of those countries in continental Western Europe that have experienced chronic payments surpluses in recent years.

International Monetary System

It is the relationship of the U.S. dollar and the U. S. payments position to the international monetary system that makes this program both a national and international responsibility. The present international monetary system has evolved substantially since the gold standard was in force for all of the large trading countries. During this long period of evolution, the very nature of the system has changed to conform to the needs of the world economy. The International Monetary Fund, established at Bretton Woods, embodies in its Articles of Agreement the main principles on which the international monetary system is now based. Essentially, it is a system in which the par value of each currency is expressed in terms of gold. The foreign exchange rates for currencies must be kept within 1 per cent of the parity. In most countries other than the United States, the central bank supports the currency, when the balance of payments is in deficit, by selling dollars in the

foreign exchange market; when in surplus, the central bank purchases dollars against its own currency in the exchange market. The United States is the only country that freely buys and sells gold as the method of meeting its obligation to maintain the international value of its currency.

Countries in deficit can receive medium-term credit from the International Monetary Fund while restoring their balance of payments without resort to measures destructive of national or international prosperity.

Such an international monetary system requires adequate monetary reserves to enable countries to meet payments deficits while they take measures to adjust their balance of payments. The monetary reserves of the world consist mainly of gold, U. S. dollars, and other currencies. As world trade and payments grow, the need for additional monetary reserves also grows. Since 1950, less than half of the increase in monetary reserves has been in the form of gold. More than half of the increase has been in the form of U. S. dollars acquired by the central banks of other countries. Without the growth of dollar reserves, the growth of world trade and payments would have been severely restricted and the world economy might have been subjected to serious deflationary pressures and instability.

In actual fact, the international monetary system has worked well. This is evident from the enormous expansion of world trade from \$55 billion in 1950 to about \$200 billion in 1967. The expansion of trade and payments and the stability of the international monetary system have been buttressed not only by growth of reserves but also by enlargement of international credit facilities. The resources of the International Monetary Fund were increased in two steps from over \$9 billion in 1958 to \$21 billion at present. The International Monetary Fund entered into an agreement with a number of industrial countries (the Group of Ten) under which they undertook to lend up to \$6 billion to

the Fund if this should prove to be necessary. A network of reciprocal currency agreements was established by the central banks of the large financial centers for swaps of each other's currency; the United States has such swap arrangements totaling \$7.1 billion with 14 central banks and the Bank for International Settlements. In order to help maintain confidence in the equivalence of gold and currencies at stable values, a number of countries formed a gold pool to maintain the orderly character of the London gold market.

These various measures helped the international monetary system to function effectively. Even so, it became evident that a more basic reform was necessary. The world can no longer depend entirely upon increases in gold and dollars to provide an assured and satisfactory growth of monetary reserves. The amount of newly-mined gold available will not provide for an adequate increase in world reserves. And it is not desirable from the point of view of the United States or the rest of the world that the growth of U. S. liabilities in the form of dollar reserves abroad should continue as in the past. A steady increase in U. S. liabilities, while its reserves decline, exposes the international monetary system to the threat of instability.

In 1965, at the initiative of the United States, the Group of Ten and the International Monetary Fund began to develop methods for creating a new reserve asset to supplement gold and dollars. These discussions have led to an agreement for the creation of Special Drawing Rights at regular intervals and in an amount necessary to assure an adequate growth of monetary reserves. This new supplement to existing reserve assets will be issued by the International Monetary Fund. All 107 members of that institution will be eligible to participate. At the annual meeting of the International Monetary Fund in Rio de Janeiro in September 1967, the Governors of the Fund unanimously approved a resolution providing for legal drafting of this proposal as an amendment to the Fund's Articles of Agreement. It is hoped and expected that the necessary legal steps will be completed late this year or early in 1969 and that the plan will then be put into operation promptly.

The Rio resolution for the creation of Special Drawing Rights (SDR) represents a landmark in the evolution of an international monetary system responsive to the needs of the modern world. When this system is in operation, the growth of monetary reserves can be adequate without depending either on the uncertainties of gold mining and gold hoarding or on persistent deficit in the U. S. balance of payments.

The early availability of SDR removes one of the concerns as to the impact of the U.S. balance of payments program--namely, a slowing of reserve growth and a consequent adverse effect on world trade and income. Early activation of the SDR plan can maintain an adequate growth of world reserves together with restoration of U.S. balance of payments equilibrium.

Strategy for Payments Improvement

The key resources which give the U.S. the strength to deal with its underlying long-range payments problem constructively and sensibly are:

- a strong economy with a Gross National Product in excess of \$800 billion, representing 40-45% of world output;
- a large stock of foreign assets with powerful earnings potential. Gross assets abroad -- public and private -- total more than \$110 billion. Our net long-term asset position -- approximately \$70 billion -- has increased every year for 20 years. Private overseas assets alone now generate annual earnings of about \$6 billion.
- a basic trade surplus, on which we must build;
- a strong reserve position (nearly \$15 billion, or about 20% of world reserves), even after losses of the past few years.

We can build on these elements of strength and move toward balance of payments equilibrium through short- and long-range measures vigorously implemented. Furthermore, the passage of time will ameliorate forces that presently exacerbate the balance of payments deficit and hide the fundamental progress achieved.

Ideally, the United States would solve its balance of payments problem through a gradual, long-range approach in which there was no interference with the free movement of goods and services, capital or people. Over the long run, the United States is, in fact, dedicated to just such an approach.

However, the situation that confronts the United States today requires prompt and major corrective action. Long-term measures alone that take hold gradually over time are not sufficient.

The President's Action Program

President Johnson's program is designed to bring about a sharp reduction in the United States payments deficit in the year ahead, bringing it into--or close to--equilibrium. The program consists of general and specific measures, short- and long-range actions.

As indicated in the President's message on January 1, 1968,

"The first line of defense of the dollar is the strength of the American economy.

"No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus.

"No challenge before business and labor is more urgent than this: To exercise the utmost responsibility in their wage-price decisions, which affect so directly our competitive position at home and in world markets.

"I have directed the Secretaries of Commerce and Labor, and the Chairman of the Council of Economic Advisers to work with leaders of business and labor to make more effective our voluntary program of wage-price restraint.

"I have also instructed the Secretaries of Commerce and Labor to work with unions and companies to prevent our exports from being reduced or our imports increased by crippling work stoppages in the year ahead.

"A sure way to instill confidence in our dollar -- both here and abroad -- is through these actions."

In addition, the Action Program contains these direct measures:

1. Direct investment. By Executive Order and regulations issued under the Banking Law, a mandatory limit has been placed on direct investment by U.S. companies in foreign affiliates. The program, together with its accompanying provisions on the repatriation of foreign earnings, is expected to reduce the payments deficit by \$1 billion in 1968.

In the highly-developed countries, principally in continental Western Europe, a moratorium is imposed on any new capital outflow from the United States, and a restraint is placed in the reinvestment of earnings from direct investment.

In a group of countries in which a high level of capital inflow is essential for economic growth and financial stability, and where adequate funds cannot be secured from other sources, U. S. companies may make new capital transfers for direct investment which together with reinvested earnings do not exceed 65 percent of the average of their capital outflow plus reinvested earnings in 1965 and 1966. The countries in the group subject to this limitation include, among others, Canada, Japan, Australia, New Zealand, the United Kingdom and the oil-producing countries.

In the less-developed countries, U.S. companies may make new capital transfers for direct investment which together with their reinvested earnings in these countries do not exceed 110 percent of the 1965-66 average.

The funds available for new investment through the retention of earnings or permitted transfers of new funds can be supplemented by borrowing abroad. Funds available from depreciation reserves abroad are also not counted as part of the new investment. Specific authorization will be required for any new transactions not falling within the targets set up for investors. The order does not apply to direct investment of less than \$100,000 in any year.

In accordance with the regulations, U.S. companies must repatriate from their share of the earnings of all their foreign business ventures in the three groups of countries amounts equal to the greater of (1) the same percentage of their share of total earnings from these three groups as they repatriated during 1964-66, or (2) so much of their share of earnings as may exceed the limit set for capital transfers to each group. In the case of the continental European countries where a moratorium on capital transfers applies, the applicable rule with respect to (2) above is that earnings in excess of 35 percent of investment in 1965-66 must be repatriated. In addition, short-term financial assets held abroad, other than in direct investments, are required to be reduced to the average level of 1965 and 1966 and held at this level.

2. Banks and other financial institutions. Revised guidelines have been issued by the Board of Governors of the Federal Reserve System for reducing foreign credits from U.S. banks and other financial institutions. The new guidelines are designed to bring a net inflow of at least \$500 million in 1968. The program is voluntary, although the President has given the Federal Reserve Board standby authority to invoke mandatory controls.

The Bank program also requests banks to reduce the amount of their term loans to developed countries of continental Western Europe by not renewing such loans at maturity and by not relending them to others. All banks are also asked to reduce the amount of outstanding short-term credits to developed countries of continental Western Europe by 40 percent of the amount outstanding at the end of 1967. As these loans are repaid, ceilings for outstanding foreign credits will be reduced correspondingly.

Revised guidelines for other financial institutions, such as insurance companies, mutual savings banks, pension funds, etc., request them to reduce their holdings of foreign assets covered by the program by 5 percent or more in 1968 compared with the amount of such assets held at the end of 1967. It is expected that these institutions will reduce to zero their holdings of liquid funds abroad, or to the minimum working balance required to conduct foreign business activities, even if this entails a decline in foreign assets by more than 5 percent.

In both programs, priority will continue to be given to credits for financing exports and to loans to the less-developed countries. The major effects of the revisions are focused on the developed countries of continental Western Europe.

3. Foreign travel. Our travel deficit increased substantially in 1967 to a figure estimated at approximately \$2 billion. The Administration believes that the best long-range manner to reduce this deficit is to encourage more foreign travelers to visit the United States. A special Task Force is at work on measures to accomplish this. The President has directed the Task Force to report within 45 days on the immediate measures that can be taken and to make its long-term recommendations within 90 days. Their recommendations will be acted on promptly. Meanwhile, however, more drastic measures are required on a temporary basis. A reduction of \$500 million in payments for foreign travel is essential for restoring our balance of payments. The President has therefore asked the American people to defer for the next two years all nonessential travel outside the Western Hemisphere. The Treasury is exploring with Congressional committees appropriate legislation to help achieve this objective.

4. Government expenditures overseas. The commitments for aid and defense, on which Free World security depends, necessitate very large expenditures abroad. These costs have risen sharply because of the Vietnam war. Over the past three years, a stringent program has substantially reduced these foreign exchange costs. The President has, nevertheless, set a target of a further reduction of \$500 million in the foreign exchange impact of such programs in 1968.

Negotiations will be initiated promptly with our allies in Europe and in the Pacific to minimize the foreign exchange costs of our military spending abroad. They can help, as they have, by purchasing in the United States more of the equipment for their defense needs. They can also offset the adverse effects of our military expenditures on the balance of payments by investing part of their foreign

exchange receipts in long-term U. S. securities. The Department of Defense has been instructed to find ways to reduce further the foreign exchange impact of personal spending by U. S. forces and their dependents. The President has instructed the Director of the Budget to find ways to reduce the number of American civilians working overseas. AID has been directed to reduce its foreign exchange costs by at least \$100 million in 1968.

5. Export increases. In the long run, the best way to restore our balance of payments is to increase our trade surplus by increasing the rate of our export growth. The surplus on goods and services must be the main source of the foreign exchange earnings needed to finance our private foreign investment and the overseas expenditures of the Government. While the expansion of U. S. exports is primarily a long-range program, special efforts in this direction can contribute as much as \$500 million to the improvement of the balance of payments in 1968.

The President will ask Congress to support an intensified five-year program to promote the sale of our industrial and agricultural products in foreign markets. The President will also ask Congress to earmark \$500 million of Export-Import Bank funds to provide better export insurance, to expand guarantees for export financing, and to broaden the scope of Government financing of exports. Through a more liberal discount system, the Export-Import Bank will encourage banks to help firms increase their exports. The Commerce Department will begin a Joint Export Association program to provide financial support to American companies joining together to sell abroad.

Since 1934, the United States has taken the lead in cooperative action to expand world trade through reciprocal reduction of tariffs. The policy inaugurated by President Roosevelt and Secretary of State Hull has been extended and broadened in every Administration since then. In the Kennedy Round, we climaxed three decades of intensive

effort to achieve the greatest reduction in tariffs in all the history of trade negotiations. Trade liberalization remains the basic policy of the United States.

Nontariff barriers, however, pose a threat to the continued growth of world trade and to the U.S. competitive position. We ask no unfair trade advantage. On the other hand, we cannot ignore the disadvantage to our trade resulting from the tax systems of our trading partners. Some countries, those that make extensive use of indirect taxes compared to personal and other income taxes, give across-the-board tax rebates on their exports and impose special border taxes on their imports. These tax practices are governed by the rules of the General Agreement on Tariffs and Trade, which we will seek through negotiation to adjust and expand international trade further.

The United States has initiated discussions, particularly with nations having balance of payments surpluses, to minimize the handicaps to our trade which arise from differences in national tax systems. We are also preparing legislative measures in this area whose scope and nature will depend on the outcome of these consultations.

Long-Range Aspects of the Balance of Payments Program

A drastic reduction in our balance of payments deficit is necessary to defend the dollar and to insure against a breakdown of the international monetary system. The action program will achieve this. The program will entail sacrifices in this country and it may cause difficulties for some foreign countries. In order to assure a fair sharing of these sacrifices, the program has been widely spread over all sectors of the U.S. economy. In order to minimize adverse effects on the world economy, the program distinguishes among groups of countries on the basis of their ability to absorb reductions in their foreign exchange receipts.

The action program is designed to deal with an emergency. We do not regard certain aspects of it as consistent with a long-range solution to our underlying balance of payments problem.

Restrictive measures are temporary. The policy of the United States is to support the unrestricted international flow of goods, services and capital under a stable international monetary system based on fixed values for currencies defined in terms of gold or the dollar, linked at \$35 an ounce. The world economy can operate most effectively only with a balanced pattern of international payments, achieved without restrictions. The international monetary system can function effectively only if monetary reserves can grow steadily at an appropriate rate without depending, as in the past, on a large infusion of dollar reserves derived from a payments deficit of this country.

When the fighting in Vietnam ends, the foreign exchange costs of our security efforts in Southeast Asia--now running at an annual rate of about \$1.5 billion--will drop and will help our balance of payments position. But it is important to remember that we had a balance of payments problem before Vietnam, and the cessation of the fighting will not in and of itself effect a cure. Much more is required if we are to terminate restrictive measures and at the same time maintain equilibrium. This we are determined to do. This is why the Action Program includes intensified longer-range balance of payments measures.

An appropriate long-range balance of payments solution for the United States must be based on a substantial and growing surplus in trade and services, including earnings from U.S. foreign investments. The present trade surplus is too small. It must be increased substantially through an expansion of U.S. exports. The Government is taking measures to encourage exports. U.S. producers will be able to benefit from these measures only if they strengthen their position in world markets by maintaining competitive prices and costs.

Unfortunately, after a period of unprecedented stability, U.S. prices and costs rose in 1966 and 1967. The rapid expansion in the U.S. economy that is now under way threatens a further rise in prices and costs. This would endanger our economic prosperity and undermine our competitive position in world

markets. The President has instituted rigorous controls on Government expenditures. The Federal Reserve is following a cautious monetary policy. The most urgent business before Congress is to complete this anti-inflation program by enacting a temporary surcharge on income and profits taxes.

Even a strong fiscal policy and a stringent credit policy cannot maintain price stability unless business and labor are willing to follow price-wage practices that conform to the needs of our economy. Furthermore, at a time like this, the country cannot afford the loss of output resulting from crippling work stoppages in critical industries. They reduce our exports and increase our imports. They may have an enduring effect on our trade position if the need for vital goods is met by imports not because of lower prices but solely because of greater assurance of a regular supply.

Not only our commodity exports, but our exports of services can be increased. We hope particularly that foreign tourists will come to the United States in growing numbers over the longer term.

The United States is eager--and working hard-- to encourage foreign direct investment in this country and investment in U.S. corporate securities. Foreign companies whose products are already familiar to U.S. buyers would find direct investment very profitable. We have an enormous market, efficient labor, and easy access to advanced technology. The attractiveness of U.S. corporate securities has been enhanced by the Foreign Investors Tax Act of 1966. The benefits granted by this legislation, as well as other factors, should result in a moderate but steady inflow of investment funds from abroad.

The United States recognizes its responsibility for adjusting its own balance of payments and it does not intend to shirk this responsibility. At the same time, it must be recognized that the U.S. balance of payments is part of a world pattern of payments. The counterpart of the deficits of some countries is the surpluses of other countries. Countries in surplus have a responsibility for adjusting their balances of payments and thereby facilitating the

progress toward international equilibrium that the U.S. action program makes possible. They can meet these responsibilities by reducing their barriers to trade, by increasing their aid to less-developed countries, by sharing adequately in the cost of common defense, by encouraging capital outflows, and, by maintaining a satisfactory pace of domestic economic expansion. As part of this vital adjustment effort, we should be able--indeed we must find ways--to work constructively with our allies on forms of bilateral and multilateral financial arrangements designed to neutralize the foreign exchange consequences of the locations of our troops and those of our allies. The arrangements should be long term and provide financial viability to our alliances.

The growth of reserves of the rest of the world will be sharply affected by the reduction in the U.S. deficit. Yet many countries will wish to see a gradual increase in their reserves as their international transactions expand. Therefore, it is important to implement as speedily as possible the plan agreed in outline last September to create new international reserves in the form of Special Drawings Rights in the International Monetary Fund.

I. The International Monetary System and Adjustment of Payments Imbalances

The problem of the U.S. balance of payments can be understood and analyzed only against the background of an understanding of the present international monetary system. This paper therefore begins with a description of the complex institutional framework within which world trade and payments are carried out. A second chapter discusses the current problems facing the present system. Subsequent chapters then proceed to analyze the key elements of the U.S. balance of payments problem in detail, the measures previously employed, and the President's new program.

A. The International Monetary System--Why and How it Works

An international monetary system provides means and methods of payments in order to facilitate international trade, capital and other transactions. In a world composed of various countries, each with its own currency, trade and capital movements across national borders have not only to be paid for as they are within any country, but have to be provided with a mechanism to convert one currency into another.

The American exporter to Italy usually wants to be paid in dollars--his currency. The Italian importer has lire. Some mechanism has to be provided to convert the lire into dollars to pay the American exporter. And if credit is involved, there needs to be a financing mechanism that crosses the frontier.

The requirements for handling international payments smoothly are:

- The various currencies should be convertible easily into each other.
- There needs to be confidence in the stability of the exchange rates of the major currencies against each other.
- The various countries need to have international reserves of unquestioned value so that if for a time their outpayments exceed their inpayments they can finance the difference by using these reserves.

- The system works more smoothly if owned reserves are supplemented by credit facilities to tide nations over periods of imbalance.

In a strict sense, the international monetary system is not a system at all. It is a series of arrangements, procedures, customs and institutions which have evolved over time and which are laced together by a network of formal and informal agreements. It has been partially codified as to objectives, principles and procedures by the Articles of Agreement of the International Monetary Fund (IMF). It has been aided by international cooperation on the part of the important central banks of the world--most notably through the so-called "swap network." It works partly through correspondent relationships of the major commercial banks of the world. Money and capital markets in the United States and Europe are important factors in making the system work. In recent years it has been strengthened by a series of consultative arrangements undertaken under the auspices of the Organization for Economic Cooperation and Development (OECD).

The system rests on five pillars:

- a dollar convertible into gold at \$35 per ounce;
- other major currencies convertible into dollars at stated rates of exchange--under IMF rules they may vary plus or minus 1 percent from parity;
- adequate international reserves and credit facilities designed to support these relationships;
- a general presumption that a country will over time be in equilibrium in its international position--that surpluses will be offset by deficits on the average;
- in seeking to adjust from deficit to surplus, or vice versa, a country will take into account the consequences of its actions on the world community.

B. The Role of the Dollar

In practice, all member countries of the IMF which have convertible currencies operate through their central banks or monetary authorities to keep their currencies in an established relationship to the dollar. For example,

the exchange parity of the D-mark is 4 to the dollar, or \$0.25. The IMF intervention limits are \$0.2475 and \$0.2525. In practice, the German Federal Bank intervenes within somewhat narrower limits. When the dollar is strong against the D-mark, the dollar price of the D-mark falls toward \$0.2475. The Bundesbank supplies dollars from its reserves to buy up the excess D-marks. When the D-mark is strong against the dollar, its dollar price rises toward \$0.2525. Then the Bundesbank supplies marks and buys dollars.

Each monetary authority acts essentially in the same way--intervening in its own markets to maintain the price of its currency vis-a-vis the dollar within the narrow band of plus or minus 1 percent from its parity.

The United States does not have to carry on operations like this. It fulfills its IMF parity obligations by freely buying and selling gold for dollars--only with monetary authorities and for legitimate monetary purposes, of course--at \$35 per ounce.

The point is that virtually every country does its market interventions by buying or selling dollars. It does so because the dollar is the major transactions or vehicle currency and is widely used in the payment and receipt transactions of international trade and capital flows. It does so because the dollar is a reserve currency and most countries hold dollars in their international reserves.

The dollar is both a reserve currency and a vehicle currency because:

- it is strong, being backed by a strong economy;
- it can be invested profitably because there exists a big money and capital market in the U.S.;
- it is known and is acceptable as a store of value--that is, it holds its purchasing power better than most other currencies;
- it is in sufficient supply so that there are dollars that can be used or borrowed for transactions; and
- it is convertible by monetary authorities into gold so that they are willing to hold it.

The U.S. did not deliberately make the dollar a reserve currency or a transactions currency. The dollar evolved as such out of its basic strength.

But this strength can be called into question in two ways:

- If the supply of dollars in foreign hands becomes greater than the amount foreign central banks and private holders want to hold, either because of their basic needs or for other reasons.
- If declines in the U.S. gold reserve and consequent unfavorable effects on the relationship between U.S. gold and U.S. dollar liabilities raise questions as to the ability of the U.S. freely to convert outstanding dollars into gold at \$35 per ounce.

It is to prevent such developments that the U.S. must achieve sustainable equilibrium in its payments position. Unless it does so, its liabilities to foreigners increase and its gold reserves decrease, and the monetary system becomes more vulnerable to a shrinkage in overall liquidity that can cause serious financial and business disruption through an international credit squeeze.

Foreign central banks and other official institutions hold some \$16 billion of liquid dollar assets. Private foreigners hold another \$16 billion.

The official holdings are reserves for the rest of the world and constitute nearly 30 percent of such reserves. But so long as they are not withdrawn in the form of gold, they have not reduced our reserves. Thus, our balance of payments deficit, unlike those of a nonreserve currency country, has been only partially reflected in a decline of gold reserves or in our reserve position in the IMF. A considerable part of our balance of payments deficit has been covered by an increase in our liabilities rather than by a reduction in our reserve assets.

While it is not necessary for a commercial bank to maintain liquid assets to cover all or even a major part of its liquid liabilities, the U.S. as a reserve center is a bank in a rather special sense, and needs to maintain a substantial reserve against its liabilities. It is important that our reserves be adequate to meet demands for conversion, and to maintain confidence in the bank on the part of the official and private dollar holders abroad.

Rising dollar liabilities which constitute reserves for other countries have permitted the world as a whole to build up its reserves more rapidly than would otherwise have been the case. A return of the United States to equilibrium would cut off this growth of reserves for these countries. It has become increasingly clear, therefore, that some other means of providing for the future growth in world reserves will be required. To this end, the members of the International Monetary Fund have now agreed on a plan for the deliberate creation of reserves through multilateral action. When this plan is in effect, the world would no longer be dependent upon gold and the deficits of the United States to provide for the expansion in world reserves which will be needed in the future.

Thus the role of the dollar as a reserve currency has been intertwined with the problem of our balance of payments and has also been related to the general problem of expanding world reserves. Through a multilateral system of reserve creation, we can relieve the dollar of its responsibility to provide for a growth in world reserves, and permit concentration on the balance of payments problem.

The following sections of this chapter set forth the elements of the international monetary system.

C. Exchange Rates

One of the distinguishing features of the present international monetary system is the relative stability of exchange rates. Under the Articles of Agreement of the International Monetary Fund--which since their adoption at Bretton Woods, New Hampshire, in 1944 have embodied the formal principles and procedures which underly the present system--countries undertake to maintain exchange rates for transactions in their currencies within a margin of one percent of a declared par value. This par value may be changed, with the approval of the IMF, in the event of a "fundamental disequilibrium" in a country's balance of payments. For the most part, however, all the members of the IMF have shown a strong preference for stable exchange rates that are changed only infrequently.

In order to maintain their currencies within a margin of one percent of the declared par value, the monetary authorities of almost all countries other than the United States intervene when necessary in their exchange markets, buying or selling dollars against their own currency. There are a few exceptions to this method of official exchange-market intervention (notably in the

sterling area), but for the most part the entire pattern of stable exchange rates is maintained by virtue of the fact that countries "peg" their exchange rates to the dollar.

Since most other countries peg their currencies to the dollar, the United States itself does not need to intervene in the exchange markets to maintain the value of the dollar in terms of other currencies. Although it may at times find it advantageous to do so in order to assure more orderly markets and more efficient and economical use of its reserves, the United States basically maintains its obligations regarding exchange stability in a very different manner: by freely buying and selling gold in transactions with monetary authorities (primarily central banks of other countries) at the price of \$35 an ounce. No country other than the United States freely buys and sells gold. The whole exchange-rate system is therefore pegged to gold only through the commitment of the U.S. monetary authorities to buy and sell gold freely at the \$35 price.

D. Reserves

In order to weather periods of deficit in a system of stable exchange rates, monetary authorities must hold reserves of internationally-acceptable liquid assets. If a central bank had no reserves with which to purchase its own currency at times when its currency was in excess market supply, it would have no choice but to ask the IMF to approve a change in its par value.

Reserves are held primarily in the form of gold and dollar claims on the United States. Because dollars are held so widely in countries' reserves, the dollar is the main "reserve currency" of the international monetary system. Countries in the sterling and franc areas hold part of their reserves in sterling or French francs, and thus--to a much lesser extent--the pound and the franc also function as reserve currencies. Gold and reserve currencies are supplemented by reserve credit available from the International Monetary Fund (see below).

After an initial accrual of dollars resulting from market intervention, the country can either retain its reserve gain in the form of dollars or choose to convert the dollars into another reserve asset, usually gold. Conversely, a country necessarily experiences a reserve loss by the act of selling dollars in its exchange market, thereby reducing its dollar holdings. In order to stand ready to intervene in the market, central banks have to

hold at least a working balance in dollars. This working balance can be replenished as necessary either by selling other reserve assets (such as dollar securities, time deposits, or gold) held by the monetary authorities or by drawing on the IMF or other credit facilities.

Many diverse factors enter into the decisions of central banks when they determine the proportions of their reserves to hold in gold, dollars, and other assets. Some central banks have traditionally held their reserves primarily in gold except for foreign-exchange working balances. Others have historically invested almost all their reserves in dollar or sterling assets. There are many different patterns of behavior in between these two extremes. Moreover, many countries have changed their reserve-composition policies over time.

One important motive for holding dollars is that they can be invested at interest. Gold does not earn any interest and actually costs something to store safely.

It has already been pointed out that the United States maintains its exchange stability obligations in a unique manner. It is equally true that the United States must of necessity have a unique policy with respect to its reserves. Whereas other countries use their reserves by buying or selling dollars in their exchange markets, the United States uses its reserves only to redeem excess dollars acquired by the monetary authorities of other countries.

This structural feature of the international monetary system has another important implication: when the United States does use its reserve assets to redeem outstanding dollar liabilities, this redemption--both in amount and timing--is determined by the reserve-asset preferences of foreign monetary authorities. The amount and timing of U.S. use of reserve assets is therefore not directly subject either to U.S. desires or to U.S. official policy actions. The United States can influence the rate at which it gains or loses reserves only by influencing the attitudes and asset preferences of foreign monetary authorities. One of the major factors influencing foreign official attitudes, of course, is the prevailing appraisal of the strength or weakness of the U.S. balance of payments and reserve positions.

Just as the United States uses reserves in a unique manner, it must hold its reserves subject to considerations that are unique. Whereas other countries have a range of assets from which to choose that includes gold, dollars,

other currencies, and reserve positions in the IMF, the United States has a much more restricted field of choice. It must hold assets which are acceptable to other countries when they call upon the United States to redeem our outstanding reserve-currency liabilities. While there is some scope for holding other countries' currencies in our reserves, it is clear that in the present system the United States must hold most of its reserves in gold.

Given the wide extent to which the dollar is used as the "intervention currency" and as a reserve currency, it is clear that the stability of the entire international monetary system is intimately bound up with the behavior of U.S. reserves. If a widespread feeling were to develop that U.S. reserve assets might be inadequate in comparison with the size of outstanding reserve-currency liabilities, or especially if U.S. reserve assets threatened to continue to decline simultaneously with a further large expansion of U.S. reserve-currency liabilities, dollar assets might be viewed with increasing distrust by individuals and governments all around the world. The U.S. Government fully appreciates the significance of the fact that the stability of the entire monetary system is interdependent with U.S. reserve and balance of payments policy. This fact and the desire to act responsibly in the face of it have been one of the primary considerations underlying U.S. balance of payments policy since the large payments deficits of 1958-60, accompanied by heavy gold losses, first underscored the existence of a problem.

E. Operations of the International Monetary Fund

In addition to the gold and reserve currencies which countries hold in their reserves outright (sometimes referred to as "unconditional" liquidity since they are usable without any outside institution or government placing conditions on their availability), countries have access to a pool of currencies in the International Monetary Fund. The amount of resources a country may draw from the Fund is governed by its quota, which reflects its economic size and importance relative to other countries. When initially paying in its quota subscription, each country subscribes 25 percent in gold and 75 percent in terms of its own currency. In return for agreeing that the 75 percent balance of its own currency may be drawn upon in case of need to finance other countries' drawings from the currency pool, countries obtain the right to draw the currencies of others from the Fund themselves under certain stipulated conditions.

The right of a country to draw on its gold subscription ("gold tranche") is essentially beyond challenge; so also is its right to draw on any credit balance it acquired as a result of other countries having drawn its currency. These two amounts together are described as the country's "reserve position in the Fund;" it is also a form of unconditional liquidity. Most countries, including the United States, regard their reserve positions in the Fund as an asset fully liquid and usable in case of balance of payments need, and accordingly include the Fund reserve position in their published reserves.

Under circumstances which involve increasingly stringent analysis and discussion of a country's economic policies, members of the Fund may draw successive further amounts from the Fund up to 100 percent of their quotas. These further borrowings in a country's "credit tranches" are not comparable to reserves. They are conditional credit facilities (hence sometimes referred to as "conditional" liquidity). They carry specific repayment obligations and interest charges.

The role of the International Monetary Fund in supplying conditional liquidity to governments for the purpose of maintaining stability in exchange rates and the adjustment of payments imbalances has expanded greatly since the inauguration of the Bretton Woods system. The aggregate quotas of all members of the IMF are now some \$21 billion. The appropriateness of quotas is reviewed every five years; the last round of general quota increases became effective in 1966. In addition to expanding the general level of quotas and selectively increasing the quotas of certain countries, the IMF was also strengthened in 1962 by an agreement among the ten main industrial countries (the "Group of Ten") known as the General Arrangements to Borrow (GAB). The GAB is an undertaking by these countries to lend the Fund specified amounts of their currencies (aggregating to the equivalent of about \$6 billion) if the Fund decides that supplementary resources are needed to forestall or cope with an impairment of the international monetary system. The GAB arrangements have been activated several times in connection with large U.K. drawings from the Fund.

The U.S. quota in the IMF is \$5.2 billion, out of total Fund quotas of about \$21 billion. As of the end of 1967, the United States had approximately \$400 million of its "gold tranche" and the full \$5.2 billion of credit tranches available.

F. Other Institutional Arrangements

In 1961, the new U.S. Administration began to foster the development of a new system of international short-term credits in the form of the "swap network" of the

Federal Reserve System, and also introduced the so-called "Roosa bonds." Both of these provide a type of exchange protection to the lending country. That is, the lending country is repaid in a constant value in its own currency, and is thereby protected against an exchange adjustment by the borrowing country. The United States, at the center of the swap network, can borrow foreign currencies and sell them in the market in lieu of making gold sales, in the expectation that a subsequent reversal of part of the outflow will reduce the eventual drain on its reserves. In the meantime the swap partner holds dollars with a form of exchange protection. Similarly, the United States has, itself, been able to extend credit and acquire foreign currency with exchange protection when, for example, Italy or Canada or the United Kingdom had an outflow of funds. This network of short-term reciprocal borrowing of reserves, frequently called "a first line of monetary defense," now totals about \$7.1 billion. It has helped to avoid gold losses resulting from short-term flows that were later reversed. When the United States has been drawn upon, other countries have been provided with dollars to hold their exchange rates stable.

Roosa bonds were designed to provide a longer-term instrument for the investment of dollars accumulated by foreign monetary authorities. Most of them have been denominated in the foreign country's currency as an added attraction to the purchasing country. A total of about \$1.5 billion of these bonds was outstanding as of November 30, 1967.

Since its reopening in 1954, the free market for gold in London has re-emerged as the largest and most important center in the world for free-market gold transactions. During most of the period since that time the flow of gold to the London market, from new production and Russian sales, has exceeded the various demands on it. Accordingly, the residual supply of gold was absorbed by central bank purchases and by the U.S. Treasury at prices varying fairly closely around the U.S. fixed price of \$35 per ounce. For short periods, sudden outbreaks of speculative demand for gold substantially exceeded the supply available to the market. Such a situation occurred in October 1960 when the market price rose to around \$40 and aroused widespread anxieties concerning the international monetary system. The U.S. monetary authorities supported the Bank of England in intervening in the London market to stabilize the price within an acceptable range.

In the following year, after a similar but milder strain on the London market, the U.S. authorities suggested that, in view of the mutuality of interest among the monetary authorities of the major industrial countries in maintaining orderly conditions in the gold and exchange markets, an informal gold selling arrangement be arranged among the group of central banks that are members of the BIS or are associated with it. Under the arrangement, each member of the group (Belgium, France, Germany, Italy, The Netherlands, Switzerland, the United Kingdom and the United States) undertook to supply an agreed proportion of such net gold sales to stabilize the market as the Bank of England, as agent for the group, determined to be appropriate. The U.S. share was 50 percent. This informal arrangement has essentially been continued (without French participation since mid-year 1967 and with the U.S. share at 59 percent since then), both as to purchasing net gold acquisitions as well as supplying net market demand. Representatives of the central banks participating in the "pool" meet periodically at Basle to discuss all aspects of the gold and foreign exchange markets, providing a means thereby to coordinate exchange operating policies as well as to keep fully informed of developments in the London and other gold markets.

G. The Dollar as a Transactions Currency

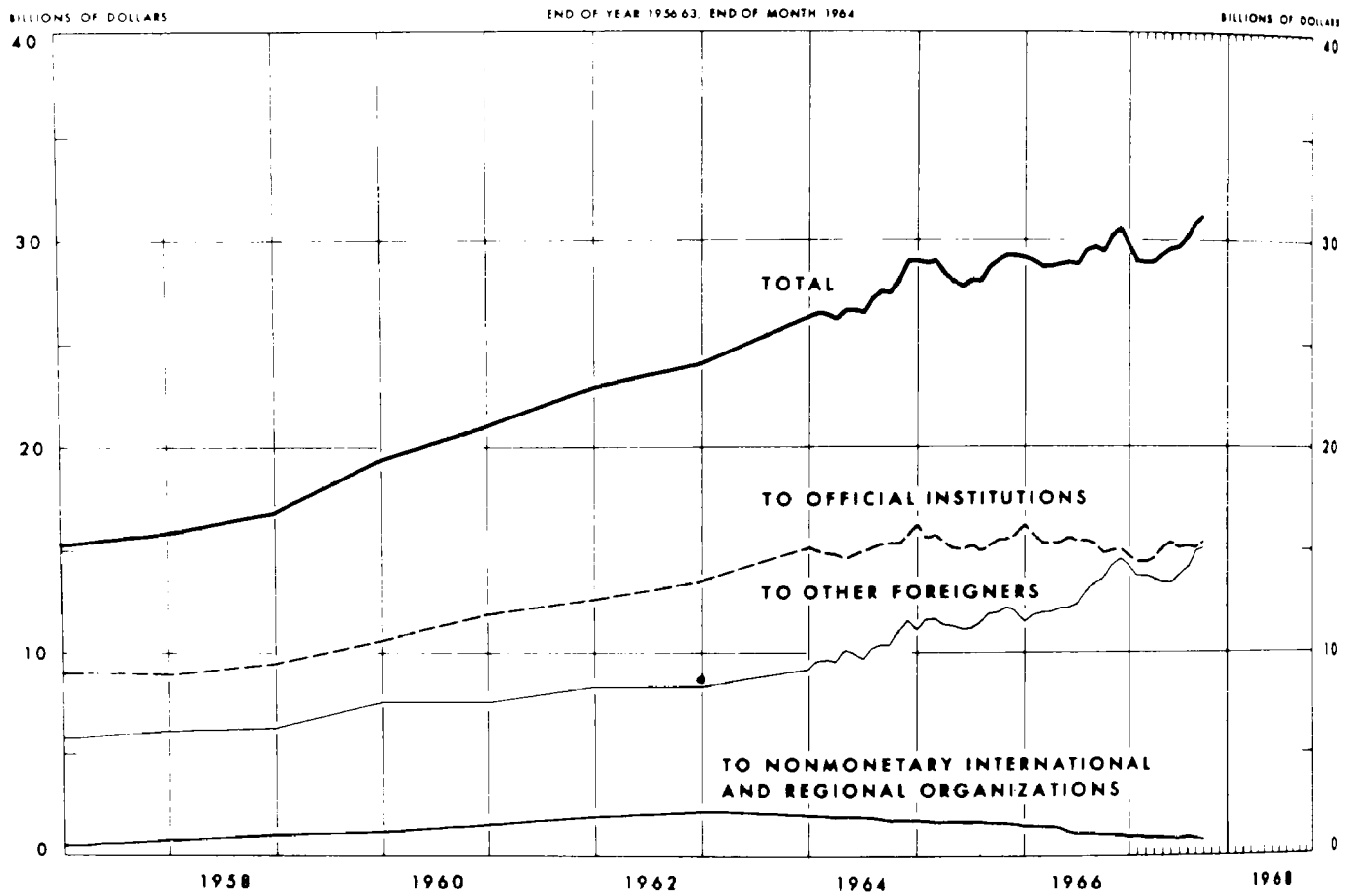
In addition to its role as the international monetary system's major reserve currency, the dollar is also the primary international means of payment and a major medium for the international investment of short-term funds. This "transactions demand" for dollars has grown greatly over the whole postwar period. In recent years the growing importance of the Euro-dollar market has provided further illustrations of the central versatile role played by the dollar in private international financial transactions.^{1/}

Chart I, entitled "Liquid Liabilities to Foreigners," gives some indication of how rapidly U.S. liquid liabilities to nonofficial foreigners have grown in the recent past. Liquid liabilities to "other foreigners"--foreign commercial banks (including the foreign branches of U.S. banks) and other private foreigners--increased over the period 1957 to 1967 from approximately \$6 billion to about \$16 billion. These

^{1/} Euro-dollars are deposits in banks outside the United States, principally in European financial centers, that are denominated in U.S. dollars.

LIQUID LIABILITIES TO FOREIGNERS

Chart 1



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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

liquid dollar assets of foreigners held in the United States are invested in demand and time deposits and money market paper. The secular growth in foreign private dollar holdings can be expected to continue in the future pari passu with continued expansion in world trade and other international transactions.

The existence of very large outstanding dollar liabilities, not only to foreign official institutions ("reserve-currency" balances), but also to private foreign individuals and organizations ("transactions-currency" balances) underlines the importance of maintaining confidence in the dollar and, more generally, in the international monetary system itself. The following chapter of this paper, which deals with current problems facing the international monetary system, returns to this important point.

H. Balance of Payments Surpluses and Deficits

When a country consistently loses reserves, it is in balance of payments "deficit." Conversely, if a country consistently gains reserves, it has a "surplus" in its balance of payments.

Strictly speaking, the matter is more complicated than that. "Surplus" and "deficit" are analytical concepts with a variety of possible definitions. For example, it may be appropriate in some circumstances to take into account changes in the foreign assets and/or liabilities of the country's commercial banking system--as well as changes in official reserves--in measuring a deficit.

The measurement of the U.S. balance of payments deficit is more complex than for other countries because of the unique position of the U.S. dollar, and was examined by a special review committee.^{1/} Following this report, the conclusion was reached that no single indicator of surplus or deficit was suitable for all purposes. The primary measure used in this paper is the balance on the "liquidity" basis, although for some purposes reference is made to the balance on the "official reserve transactions" basis.^{2/}

^{1/} See The Balance of Payments Statistics of the United States A Review and Appraisal, Report of the Review Committee for Balance of Payments Statistics to the Bureau of the Budget (E.M. Bernstein, Chairman), U.S. Government Printing Office, April 1965.

^{2/} For the differences between these two alternative **measures of the balance**, see Chart VII in Chapter III.

Balance of payments surpluses and deficits sometimes are desired. This was the case in the early 1950's, for example, when (on the definitions of surplus and deficit then in use) the European countries undergoing reconstruction had surpluses and the United States had deficits. These deficits and surpluses enabled the European countries to build up their reserves; the declines in the swollen U.S. gold reserves and the increases in our reserve-currency liabilities--representing as they did a redistribution and augmentation of the world's stock of reserve assets--were universally welcomed as such.

On the other hand, large and persistent payments imbalances, either surplus or deficit, are not sustainable and can give rise to instability in the international monetary system. There is an obvious limit to imbalances of the deficit type: countries can support their exchange rates with their reserves and credit facilities only so long as they have reserves or can arrange further credit. In the case of a reserve-currency country, there are limits to the willingness of private and official holders abroad to accumulate that currency. The limits on the ability of countries to run large and persistent surpluses are much less clear. What is clear, however, is that large and persistent surpluses impose strains on the international monetary system as great as those resulting from large and persistent deficits.

I. The Adjustment Process--Basic Objectives

Each individual country has its own multiple economic and social objectives. These include full employment and a satisfactory rate of growth, reasonable price stability, an equitable distribution of income, and balanced regional and sectoral development. While seeking to attain these objectives, as already noted, countries must also avoid large and persistent imbalances in their external accounts. It is also widely agreed (in the words of the Convention setting up the Organization for Economic Co-operation and Development) that countries should "promote policies designed to contribute to the expansion of world trade on a multilateral, nondiscriminatory basis in accordance with international obligations."

The international monetary system set up at Bretton Woods and based on a pattern of stable exchange rates was then and is now believed by its participants to be the most appropriate system designed to foster these objectives. The system has evolved over time to meet changing needs and problems. It is once again going through a key evolutionary stage, as the work on proposed amendments to

the IMF Articles of Agreement reaches completion, to establish a facility for deliberate reserve creation (see below) and to improve certain rules and practices of the Fund.

The simultaneous achievement of all the economic and social objectives described above, even for an individual country, is far from easy. Governments have only a limited number of policy tools at their disposal. They have not always been able or willing to use these tools in appropriate combinations. Governments in different countries attach different priorities to achievement of various internal and external aims. The nature of imbalances in payments, as well as the appropriate range and mix of instruments required to deal with them, can vary substantially from country to country in line with wide differences in economic and financial structure and in the nature of political institutions.

These difficulties have important implications for the speed and effectiveness with which the adjustment of payments imbalances can be attained. The adjustment process may work somewhat imperfectly, and in any case is apt to be gradual. In a few difficult cases, adjustment of payments imbalances may not take place at all, or will take place only with the costly sacrifice of some of the basic objectives that the system is intended to advance, unless a large measure of multilateral cooperation is brought to bear on the problem.

J. The Adjustment Process--Need for Multilateral Cooperation

The need for multilateral cooperation in achieving and maintaining balance of payments equilibrium has become increasingly widely recognized in the last few years. An understanding of this need has been particularly advanced by an international working group formed under the auspices of the Organization for Economic Co-operation and Development (OECD). The Economic Policy Committee of the OECD established a Working Party in 1961 for the specific purpose of promoting better international payments equilibrium. This group, consisting of senior officials from Ministries of Finance and other key government agencies and Central Banks concerned with balance of payments questions, has met together at approximately six-to-eight week intervals ever since. In 1964, the Ministers and Governors of the ten countries participating in the General Arrangements to Borrow suggested that this OECD working party, known as Working Party 3, make a study of the balance of payments adjustment process with a view toward improving the process of continuing international consultation and cooperation.

The Working Party's report on this subject was issued in August 1966. In addition to endorsing the commonly agreed view that prolonged imbalance in either direction is in general undesirable, the Working Party also noted that "the objectives of international consultation are broader and more general than the mere avoidance of imbalance. The purpose of consultation regarding adjustment policies is to ensure that the policies pursued by individual countries do not hinder others in the pursuit of the general aims of economic policy; more positively, the object is to ensure that as far as possible countries, while avoiding imbalance, collectively support each other in their policies."

The Working Party's report does not fail to point out that there are often inherent difficulties in managing an economy in a way which is consistent with domestic objectives, with the aims of its trading partners, with stable exchange rates, and with the general health of the world economy. But it also recognizes that there is clear room for improvement and that improvement is an urgent order of business. The report describes appropriate methods of dealing with these problems in different circumstances. It refers specifically to the need for clearer formulation of balance of payments aims; early identification and better diagnosis of payments problems; new and more selective instruments of economic policy; more timely action to correct inappropriate demand levels, competitive positions and capital flows; and a further strengthening of the processes of international consultation.

The U.S. Government has strongly supported the Working Party's report and its recommendations. At the recent meeting, November 30 to December 1, of the Ministers of the countries belonging to the OECD, for example, the United States representative, Under Secretary of State Eugene V. Rostow, said:

"We have no doubt that the Atlantic countries can resolve this problem, if they deal with it together, in ways which fortify the world monetary system and permit an early and assured return to growth patterns closer to our full employment objectives. All I am suggesting today is that we recognize that some aspects of the adjustment process require cooperative solutions and that we set about promptly to find them. Cooperation in handling the adjustment process, I suggest, is the next major step after Rio [see below for a discussion of the agreement reached in Rio de Janeiro in September 1967] for us to take in improving our machinery for managing the monetary system."

K. The Adjustment Process--Equilibrium for the System as a Whole

For any country to reduce its deficit or move into surplus, it is generally necessary for other countries to reduce surpluses or increase deficits. This is simply a statement of what must happen mechanically and statistically if payments imbalances are to be adjusted at all.

This inescapable interdependence of surpluses and deficits makes it very clear that countries must have compatible balance of payments aims if the whole system is not to be working at cross purposes. If all the countries in the system that are in surplus set their policies in such a way as to have continued surpluses, while deficit countries take active measures to eliminate their deficits, then either the deficit countries will still find themselves running deficits or else surplus countries will find that they have not been able to attain their targeted surpluses. All countries together cannot possibly achieve these inconsistent aims; someone is bound to be disappointed.

Virtually all countries take it as their balance of payments objective to be in surplus (and so to have growing reserves) over time. Few if any countries have indicated either a policy or a willingness to have their reserves fluctuate around a fixed level rather than around an upward trend.

It is understandable why countries tend to have this preference for surpluses. The volume of trade and other international transactions has a strong upward trend. It is a reasonable presumption that, because of this trend, the absolute size of imbalances will also increase over time. These facts alone suggest that reserves should likewise have an upward trend if they are to continue to be adequate to support the fixed exchange rate against balance of payments swings. Another factor leading countries not to attempt to reduce their surpluses may be a

propensity to discount an existing surplus as partly or wholly "temporary;" it is natural and prudent to conduct affairs so as to prepare for "rainy weather" in the future, and not to presume that current good fortune will continue. Even to the extent that countries aim at a long-run objective of a zero surplus over time, which they tend not to do, they still probably react more quickly to a deficit situation than when they are in surplus (if only because countries in surplus are under much less urgent and intense pressures to act to reduce the imbalance).

Given the set of prevailing attitudes which makes an upward trend in reserves (balance of payments surplus) the targeted long-run "norm" for each country taken individually, the obvious question suggests itself: when, if at all, can the international monetary system as a whole be in equilibrium? Given that it is difficult enough to bring about adjustment of payments imbalances even under ideal conditions where deficit countries take actions to reduce deficits and surplus countries willingly take cooperative actions to reduce their surpluses, how can the system possibly function smoothly when countries in surplus by and large do not want to see their surpluses reduced?

Happily, there is a solution to this dilemma. It is not the case that for every dollar of surplus in the system there must be an exactly offsetting dollar of deficit. When the gross deficits and gross surpluses (consistently defined) of all countries are offset against each other, the sum of the surpluses can exceed the sum of the deficits by the amount of new reserves being added to the system which are not at the same time the liability of a particular country. The key point of this relationship is that if new reserves of the appropriate kind are flowing into the system, it is possible for some countries to satisfy their preferences for reserve increases without necessitating that other countries be in corresponding deficit.

Up to the present time, the only "new reserves" which have allowed this margin to exist have been increases in countries' monetary gold stocks. When newly-mined gold is sold to a monetary authority, that government has a reserve gain without any other country having experienced a deficit. When the dollar component of world reserves increases, on the other hand, this increase in reserves does not allow the system as a whole to have a margin of

surpluses exceeding deficits. When the rest of the world adds to its dollar reserves, these new assets are also an increase in U.S. reserve-currency liabilities, and there is therefore a U.S. deficit corresponding to the surplus of the rest of the world. However, gold is not the only reserve asset that is capable of permitting the system to have a situation in which the sum of surpluses exceeds the sum of deficits. Deliberately created new reserve assets, such as the proposed Special Drawing Rights (SDR) described in the next chapter, will serve this function equally well.

Equilibrium for the system as a whole thus requires that new reserves--gold or new reserve assets such as SDR--be added to the system at such a rate that the sum of surpluses can exceed the sum of deficits by a reasonable margin. This condition for "equilibrium" of the system should be thought of as a necessary, but not sufficient, condition. Other considerations, such as the degree to which the system is promoting the achievement of its basic objectives, also need to be taken into account.

Only under these conditions is there a good chance of making countries' balance of payments aims mutually compatible; only then is there a plausible hope of attaining the objectives the system is intended to promote, including relative freedom from trade and payments restrictions while still getting the adjustment of payments imbalances to proceed smoothly.

What is a "reasonable" margin by which surpluses should exceed deficits? The answer to this question is not fully clear to the financial experts and economists who have studied this question. Broadly speaking, the rate at which new reserves should be added to the system should probably bear some relationship to the rate at which international transactions are expanding (though the two rates need not be the same and there is no necessity for a precise relationship). The margin should not be too small, and certainly should not be negative. Nor should the margin be an excessive one. At either of these two extremes, one would have to say that the system as a whole was in "disequilibrium."

It is important to be clear on the fact that the above condition for equilibrium of the system, if satisfied, in no way reduces the need for countries to avoid large and persistent imbalances in their external payments. It is still imperative for countries in large or prolonged deficit to reduce their imbalance. And it is just as important as ever for countries with large and persistent surpluses to reduce these surpluses to the point where they are moderate and broadly consonant with the rate at which reserves are growing in the system as a whole. The need for adjustment is not removed. The margin by which surpluses exceed deficits only means that, for each country individually and for the system as a whole, adjustment takes place around an upward trend in reserves rather than around a constant level.

II. Current Problems Facing the International Monetary System

A. The Need for a New Reserve Asset

The first chapter of this paper pointed out that virtually all countries want to see their reserves growing over time, and that the international monetary system as a whole can only be in equilibrium if new reserves of a particular sort are being added to the system at a rate sufficient to permit the sum of surpluses to exceed the sum of deficits by a reasonable margin. One of the current problems facing the monetary system is that this condition for equilibrium of the system is not any longer being satisfied.

New amounts of gold are no longer being added to monetary reserves. Monetary gold stocks have even declined in the last two years, as shown in Table 1 (although part of this reduction in the gold reserves of countries gave rise to reserve claims on the Fund as gold was paid in to the Fund in connection with the 1965-66 increase in IMF quotas). On the production side, newly-mined gold output--the bulk of which comes from South Africa--will be increasing slowly at best in the next few years. Experts predict that declines in output will eventually occur. On the consumption side, private demands for gold have been rising. The use of gold for artistic and industrial purposes has had an upward trend, as can be seen from the table, and this trend is expected to continue. ^{1/} The remainder of private gold absorption, referred to in the table as "residual" private demand, is composed of two elements: traditional demand for gold as an asset in which to invest savings, and demand of a more speculative nature based on expectations of an increase in the price of gold. The latter speculative demand can

^{1/} Data on the private absorption of gold are fragmentary. The distinction between "industrial and artistic" uses on the one hand and "hoarding" on the other is not a clear one, and the figures in the table are only estimates.

Period	1/ Exc	2/ Inc	3/ Exc	4/ Inc
1950				
1951				
1952				
1953				
1954				
1955				
1956				
1957				
1958				
1959				
1960				
1961				
1962				
1963				
1964				
1965				
1966				
1967--Jan				

Table 1

Estimated World Sources and Uses of Gold
(in millions of dollars)

Sources				Uses					
Production		Sales by the U. S. S. R.	Total	Change in Monetary Gold ^{1/}			Total	Other	
South Africa	Total ^{1/}			Total	Countries ^{2/}	IMF		Industrial Use ^{3/}	Residual
	408	--	850	335	292	43	515	180	335
	403	--	825	225	189	36	600	135	465
	414	--	850	230	68	162	620	160	460
	418	75	920	455	445	10	465	165	300
	462	75	970	670	632	38	300	130	170
	511	75	1,015	665	597	68	350	190	160
	556	150	1,125	490	606	-116	635	245	390
	596	260	1,275	690	1,202	-512	585	275	310
	618	220	1,270	680	528	152	590	280	310
	702	300	1,425	750	- 325	1,075	675	300	375
	748	200	1,375	345	312	33	1,030	345	685
	803	300	1,515	580	942	-362	935	380	555
	892	200	1,495	355	238	117	1,140	425	715
	960	550	1,905	830	712	118	1,075	435	640
	1,019	450	1,855	710	843	-133	1,145	555	590
	1,069	550	1,990	215	525	-310	1,775 ^{4/}	610	1,165 ^{4/}
	1,081	n.a.	1,445	- 45	- 828	783	1,490 ^{4/}	675	815 ^{4/}
.-Sept.	805	n.a.	1,075	-235	- 262	27	1,310	540	770

^{1/}Includes U.S.S.R., Other Eastern Europe, Communist China and North Korea.

^{2/}Includes Bank for International Settlements and European Fund.

^{3/}Includes, in addition to U.S.S.R., Other Eastern Europe, Communist China and North Korea, Other eastern countries where the purchase of gold is a customary mode of saving.

^{4/}Includes estimated purchases by Communist China as follows: 1965, \$150 million; 1966, \$75 million.

be expected to subside as doubts about the stability of the international monetary system and the gold price are resolved (see below). But the former so-called "savings" demand for gold, which is of significance primarily in less-developed countries and in some countries on the European continent, may well rise over time as incomes rise. From the development point of view, of course, it would be better to devise mechanisms to channel increased savings from increased incomes into productive investment instead of into a sterile asset--gold.

These considerations make it clear that the international monetary system cannot look to gold alone to satisfy the need for a secular growth in reserves.

It was previously pointed out that new gold taken into monetary reserves has historically been the only component of world reserve growth that makes possible an excess of total surpluses over total deficits. The fact that monetary gold reserves declined in 1967 takes on an added significance when viewed in this light. There has been no scope at all for some countries to be in surplus without other countries being in deficit.

What about sources of growth in world reserves other than gold? Is it possible to rely on them in the future?

Certainly it has been true that these other sources have supplied the greatest part of increases in reserves in the postwar period. Table 2 presents some data on the sources of growth in the 1950-67 period. From that table it can be seen that additions to foreign exchange reserves (overwhelmingly dollars)^{1/} accounted for more than half of the total increase in world reserves over the whole period from 1950 through 1964.

^{1/} Table 2 does not show the breakdown between the dollar component of foreign exchange reserves and the component held in other currencies. Since official reserves held in the form of sterling assets have actually declined since 1950, line B in Table 2 tends to understate the extent to which world reserve growth over the 1950-64 period depended on increases in official dollar holdings.

Table 2

Sources of Growth in Countries' Reserves, 1950-1967

	1960	1961	1962	1963	1964	1965	1966	1967 Jul.-June	Annual Averages		
									1950- 1959	1960- 1964	1965- 1966
	(in millions of dollars)										
<u>TOTAL CHANGES IN COUNTRIES' RESERVES</u> ^{1/}	<u>+3,082</u>	<u>+2,140</u>	<u>+ 425</u>	<u>+3,142</u>	<u>+2,453</u>	<u>+1,261</u>	<u>+1,486</u>	<u>- 455</u>	<u>+1,182</u>	<u>+2,248</u>	<u>+1,374</u>
A. Changes in Countries' Holdings of Gold ^{2/}	+ 312	+ 942	+ 238	+ 712	+ 843	+ 525	- 828	- 226	+ 423	+ 609	- 151
B. Changes in Foreign Exchange Reserves Excluding items D, E, and F below	+2,450	+ 494	+ 567	+2,122	+1,025	-1,109	- 140	+ 970	+ 600	+1,332	- 625
<u>TOTAL TRADITIONAL SOURCES</u> (Items A + B)	<u>+2,762</u>	<u>+1,436</u>	<u>+ 805</u>	<u>+2,834</u>	<u>+1,868</u>	<u>- 584</u>	<u>- 968</u>	<u>+ 744</u>	<u>+1,023</u>	<u>+1,941</u>	<u>- 776</u>
C. Changes in Reserve Positions in the IMF (Drawings on IMF Credit Tranches)	+ 320 (+ 21)	+ 588 (+1,008)	- 363 (- 433)	+ 145 (+ 84)	+ 215 (+ 349)	+1,221 (+1,589)	+ 954 (- 4)	- 434 (- 423)	+ 159	+ 181 (+ 206)	+1,088 (+ 793)
D. Changes in United States' Convertible Currency Reserves	--	+ 116	- 17	+ 113	+ 220	+ 349	+ 540	- 583	--	+ 86	+ 445
E. Dollars Generated by Drawings on U.S. Federal Reserve System Swaps by Other Countries	--	--	--	+ 50	+ 150	+ 275	+ 75	- 182	--	+ 40	+ 175
F. Securities Taken into U.K. Reserves	--	--	--	--	--	--	+ 885	--	--	--	+ 443
<u>TOTAL NON-TRADITIONAL SOURCES</u> (Items C + D + E + F)	<u>+ 320</u>	<u>+ 704</u>	<u>- 380</u>	<u>+ 308</u>	<u>+ 585</u>	<u>+1,845</u>	<u>+2,454</u>	<u>-1,199</u>	<u>+ 159</u>	<u>+ 307</u>	<u>+2,150</u>
	(per cent)										
<u>TOTAL CHANGES IN COUNTRIES RESERVES</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
A. Changes in Countries Holdings of Gold	10.1	44.0	56.0	22.7	34.4	41.6	- 55.7	49.7	35.8	27.1	- 11.0
B. Changes in Foreign Exchange Reserves, Except Non-Traditional	79.5	23.1	133.4	67.5	41.8	- 87.9	- 9.4	213.2	50.8	59.3	- 45.5
<u>Total Traditional Sources</u>	<u>89.6</u>	<u>67.1</u>	<u>189.4</u>	<u>90.2</u>	<u>76.2</u>	<u>- 46.3</u>	<u>- 65.1</u>	<u>163.5</u>	<u>86.6</u>	<u>86.4</u>	<u>- 56.5</u>
<u>Total Non-Traditional Sources</u>	<u>10.4</u>	<u>32.9</u>	<u>- 89.4</u>	<u>9.8</u>	<u>23.9</u>	<u>146.3</u>	<u>165.1</u>	<u>-263.4</u>	<u>13.5</u>	<u>13.7</u>	<u>156.5</u>

1/ Includes BIS, and EPU/EF holdings of gold.

2/ Excludes IMF holdings of gold, but includes holdings of the BIS and EPU/EF.

There is now widespread agreement, however, that it is no longer desirable for dollars (or other reserve currencies) to supply the major part of future additions to the world reserve pool. A continuous growth in dollar reserves, which was welcomed in the early 1950's, has gradually come to be regarded as a mixed blessing, and then as a growing strain on the international banking position of the United States. The reasons for this change in attitude are easy to understand. When foreign countries elect to retain part or all of their reserve increases in the form of dollars, these actions help to satisfy the need for expansion in world reserves. On the other hand, when the rest of the world taken together is experiencing reserve gains (which, as noted above, must be regarded as the norm which countries individually will seek to attain over time), and when the reserve gains are held in dollars, the United States necessarily has a deterioration in its liquidity position. The deterioration of the U. S. liquidity position which took place in the early postwar period of so-called "dollar shortage" was generally regarded as a good thing for the world economy. But of course the deterioration could not continue forever.

Given the fact that gold is not likely to supply major additions to world reserves in the future, it is often pointed out that the international monetary system seems to be in a dilemma. If the United States does not expand its reserve-currency liabilities (which, so long as the rest of the world is gaining reserves, means an "official settlements" deficit for the United States), the growth of reserves may be inadequate. If on the other hand the United States does expand its reserve-currency liabilities, the U. S. liquidity position and confidence in the dollar will deteriorate, ultimately undermining the stability of the system itself. On this reading of the problem, world reserves are bound to be either short in quantity or shaky in quality.

Charts II and III at the end of this chapter show the relationship of the growth trends of world trade and reserves over the period 1953-67. Chart IV traces the growth of reserves in various geographical areas, and Chart V shows the three main components of world reserves, in the period 1948-66.

Although growth in reserve-currency holdings of dollars has been the major factor in world reserve increases, there has been a moderate increase in "reserve positions in the IMF" (for a description, see Chapter I) and minor increases due to other factors. These other sources of reserve growth, which are referred to as "non-traditional" sources in Table 2, were particularly important in the last three years. While additions to monetary gold and increases in reserve currencies were either declining or failing to increase, in other words, these non-traditional sources were to some extent filling the breach. Not much comfort can be drawn from this fact, however, for the scope for further large increases in reserve growth from these sources is not extensive. For example, the role played by reserve positions in the Fund in adding to total world reserves, though very substantial in 1965-66, was actually negative in 1967 (as the United Kingdom and others repaid earlier drawings on the Fund).

When all the considerations enumerated above are set alongside one another, it is clear that a new reserve asset is needed in the international monetary system. A new asset is needed to ensure that the rate at which reserves are increasing in the system as a whole is adequate to prevent countries from having to sacrifice basic economic objectives as they compete to achieve their targets of balance of payments surpluses over time. A new reserve asset is also needed to ensure that the growth in reserves which does take place is the type of growth which reinforces, rather than undermines, the stability of the system. The type of new asset that is needed is one that can function as a genuine supplement to gold. It must be created and treated in such a way as to allow the system as a whole to have a margin by which surpluses can exceed deficits.

It is sometimes argued that the above analysis does not lead to the conclusion that a new reserve asset is desirable and necessary. There are two extreme points of view which maintain this position, at opposite poles from one another. The first view challenges the fundamental premise underlying the analysis--that a system of stable exchange rates and growing reserves constitutes the best environment for promoting and harmonizing countries' basic economic objectives. Proponents of this view favor an entirely

different kind of international monetary system based on freely fluctuating exchange rates, in which reserves of any type would play a relatively minor role. Advocates of the second extreme view favor a general increase in the price of gold, and argue that if this step were taken, gold reserves would then be adequate and creation of a new reserve asset would therefore be unnecessary.

Neither of these views has found any significant support within governments or business and financial communities. Meanwhile, the member countries of the International Monetary Fund have not shown any desire to abandon the institutional framework which has proved itself so well in the postwar period. Rather than embarking on an uncharted course that would be littered with pitfalls and uncertainties, it is clearly more sensible for all countries to cooperate together to bring about evolutionary changes in the present system that can build, and improve upon, the achievements of the past.

There is even less support for the extreme step of an increase in the price of gold than there is for a radical transition to a world of fluctuating exchange rates. Any such action would disturb the long-standing equality of gold and dollars as components of monetary reserves, and would mean that monetary authorities in the future would give a preference to gold over other monetary reserves. This would be inequitable and prejudicial to the interest of countries which have held a large portion of their reserves in the form of dollars. Moreover, a large-scale increase in the price of gold would abruptly supply the world with very large amounts of additional reserves, rather than providing for the moderate annual growth in reserves which is most suited to an efficient and sensible course of monetary evolution. The higher price of gold would provide windfall advantages to the gold-producing areas of the world, including the Soviet Union, and to those countries which have built up disproportionately large holdings of reserves in the form of gold. Moreover, reliance on this crude method of reserve expansion would only postpone for a time the development of another period of tension and strain in the monetary system, featured by gold speculation in anticipation of another round of increases in the price of gold. For these and other reasons the "Group of Ten" countries have conducted their work on the

improvement of the international monetary system on the general basis, adopted in 1964, that "a structure based, as the present is, on fixed exchange rates and the established price of gold, has proved its value as a foundation on which to build for the future."

The recent uneasiness in gold markets and discussion in some quarters of the revaluation of gold may be regarded as symptoms of the current problems facing the international monetary system. Gold is pre-eminently a monetary metal, and its price is determined by the action of the major monetary authorities in acquiring it at a fixed price. It is and should continue to be a stable and useful component of monetary reserves and not a means of speculating in anticipation of changes in the relative value of the components of international reserves. It is of fundamental importance to the international monetary system that there be no change in the monetary value of gold and the dollar relative to each other. The President has made clear that the United States will utilize its resources and adopt the policies necessary to maintain this essential monetary relationship.

B. The Rio Agreement: Special Drawing Rights

Fortunately, plans for the creation of a supplementary reserve asset, by conscious decisions of the world's monetary authorities, are well advanced.

Background and Negotiations Leading Up to the Rio Agreement. In his 1961 message to the Congress on the balance of payments and gold, President Kennedy pointed to the need for increased cooperation among the industrialized countries in order to maintain world growth and stability. It was recognized that the recent strengthening of a number of currencies, particularly in Europe, improved trade and reserve positions, widespread currency convertibility, and greater freedom for capital movements made likely greater swings in balance of payments positions. This meant that there would be greater susceptibility to disruptive short-term capital flows among the industrialized nations. While resources of the International Monetary Fund were probably sufficient to deal with the balance of payments problems of most of its membership, its resources in the currencies of the principal industrial

countries might not be sufficient to meet a major threat to the international monetary system. A borrowing arrangement to meet this special problem was negotiated in 1961, following discussions by a group of Governors of the Fund at their September Annual Meeting held in Vienna.

Under this agreement, the General Arrangements to Borrow, which became effective in 1962, ten countries undertook to lend to the Fund specified amounts of their currencies aggregating \$6 billion if supplementary resources were needed to forestall or cope with an impairment of the international monetary system. The United States commitment under this arrangement, which was renewed in 1966, is \$2 billion. Other participants are: Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden and the United Kingdom. Switzerland, though not a member of the Fund, undertook special bilateral arrangements with the Fund in order to associate itself with the arrangements.

This association, the "Group of Ten", thereby was formed through a mutual concern with the operations and strength of the international monetary system. In October, 1963, the Ministers and Central Bank Governors of the Ten asked their Deputies to "undertake a thorough examination of the outlook for the functioning of the international monetary system and of its future needs for liquidity."

On the basis of the very thorough study and report that resulted from this directive, the Ministers and Governors concluded, in a statement of August, 1964, that "the supply of gold and foreign exchange may prove to be inadequate for the over-all reserve needs of the world economy." They thereupon authorized a study of how to remedy this prospective shortage, through the creation of a new reserve asset.

From the summer of 1964 through the summer of 1965, a group of technical experts from Treasuries and Central Banks labored to bring into being a body of knowledge in this area. The result was the Report of the Study Group on the Creation of Reserve Assets-- better known as the Ossola Group, made public in August, 1965. This report provided an inventory of

the techniques by which reserves could be deliberately created and an analysis of the arguments for and against the use of each of these techniques.

It was at this point that the Secretary of the Treasury, acting on the authority of President Johnson, announced that the United States was ready to participate in high-level negotiations on reserve creation. At about the same time, there became available a report by the Subcommittee on International Exchange and Payments of the Joint Economic Committee of the Congress of the United States, under the Chairmanship of Congressman Henry Reuss of Wisconsin, called, "Guidelines for Improving the International Monetary System." Where the Ossola Report, by request of the Ministers and Governors, dealt with the technical aspects of the problem, the Guidelines Report performed the invaluable service of providing a legislative estimate of the urgency and dimensions of the problem under the highly-respected imprint of the Joint Economic Committee. Its basic conclusion was:

"World liquidity needs cannot adequately be met by existing sources of reserves (gold, dollars, and pounds sterling) or even by the addition of new reserve currencies. New ways of creating international reserves must be sought."

The Report stated, further, that:

"The need for action is pressing."

In order to ascertain the views of other countries, Secretary Fowler undertook personal and individual consultations with the other Ministers and Governors of the Ten. These individual consultations revealed a basis for joint progress.

As a result, at the time of the Annual Meeting of the Fund in September, 1965, it was agreed that the Deputies of the Ministers and Governors of the Group of Ten Countries should examine the various proposals for reserve creation to ascertain whether or not there was a basis for agreement on major points. In the meantime, the Executive Directors and staff of the International Monetary Fund were carrying on constructive studies of the problem.

At a Ministerial meeting of the Group of Ten, July 25-26, 1966, in The Hague, the Ministers and Governors of the Ten considered a report of their Deputies that represented a year of search for agreement on the essential elements of a plan for deliberate reserve creation. In addition to these elements of essential agreement, the Deputies' Report contained five workable schemes for the mechanism of reserve creation.

Basing their work on this report, the Ministers and Governors, in their Hague communique, agreed on basic principles for reserve creation. They reiterated their earlier conclusion that existing sources of reserves would not provide an adequate basis for world trade and payments in the longer run. They instructed their Deputies to begin a second stage of negotiations in which the views of the whole world would be represented, through a series of joint meetings between the Deputies of the Ten and the Executive Directors of the Fund, representing the 106 member nations of the International Monetary Fund.

Four such joint meetings of the Deputies and Executive Directors were held, from the fall of 1966 to the spring of 1967.

The Joint meetings succeeded in producing a draft outline plan, although a number of important open issues remained unresolved--primarily in the area of decision-making, mode of transfer between participating countries of the asset to be created, and requirements for reconstitution of balances of the asset following its use. These issues were considered by the Ministers and Governors of the Ten in two meetings in London, in July and August, and were resolved.

The outline plan, the "Outline of a Facility Based on Special Drawing Rights in the Fund," was submitted to the Governors of the Fund at their Annual Meeting in September in Rio de Janeiro by the Executive Directors of the Fund. By a resolution adopted unanimously, the Governors endorsed the outline plan, and requested the Executive Directors to submit amendments to the Fund Articles of Agreement to incorporate this plan. The proposed amendments were requested by no later than the end of March 1968.

Summary of the Plan for Special Drawing Rights (SDR)

The basic concept of the Plan is to provide for a new international asset which will be an effective supplement to existing reserve assets--gold, reserve currencies, and reserve claims on the Fund--one that will be a permanent addition to world reserves.

1. Quality as a reserve asset--SDR are to be denominated in units of account equivalent to the gold value of one dollar; they will have the strong backing provided by the solemn obligations of Fund members to accept them and pay convertible currency in return. They will bear a moderate rate of interest.

Each SDR is to be denominated in terms of 0.888671 grams of fine gold, the gold value equivalent of one U. S. dollar. That is, their value in terms of gold will be maintained. SDR will not, however, be redeemable in gold, and it would be against the rules for a country to use its SDR merely to change the composition of its reserves.

The backing of SDR will be unimpeachable. It will consist of a firm, unequivocal, and solemn obligation to accept the new asset when it is presented and to pay convertible currency in return. That obligation is the fundamental backing of the asset, and is the principal factor which will give it value as an asset.

Each participant will be obligated to accept SDR up to an amount equal to three times its cumulative allocations. This means that if a country had initially been allocated \$100 million in SDR's and still held all of these in its reserves, its obligation to accept additional SDR's would amount to \$200 million. If, on the other hand, it had spent all of its SDR's, its total acceptance obligation would be \$300 million. This acceptance obligation makes unnecessary and takes the place of the pool of currency used to back present IMF drawing rights.

2. Method of creation--SDR are to be created under an IMF procedure which will assure wide support for their creation, with final responsibility for decisions resting on the Fund Board of Governors. Each decision to create will authorize a specific amount of SDR.

The Managing Director of the Fund will be generally responsible for initiating proposals to start the machinery working, but it will be possible for the Fund Executive Directors or Governors to request a proposal for SDR creation from the Managing Director. The principal criterion for making a proposal is that there must be a widely-recognized global need for reserve creation.

SDR are not to be created for the purpose of making short-term and cyclical adjustments to the volume of international reserves. Rather, decisions will be taken from time to time to create a specific amount of SDR for a period as a whole, normally for five years ahead, but allocations will be made to participants at yearly intervals during the period. Such decisions will not be changed unless unexpected major developments require modification of the established trend.

Once a proposal is made, it must be considered and approved by the Fund. To assure that decisions for reserve creation will have the widest possible approval, the Managing Director will undertake full consultations to ascertain there is broad support for his proposal. The proposal, once put forward, and concurred in by the IMF Executive Directors, will be submitted for the approval of the Fund Governors voting by 85% weighted majority. If there were unexpected major developments, a simple majority could reduce the trend amount and an 85% majority could increase it. The technical possibility of cancellation of SDR by an 85% majority is also provided for.

3. Method of allocation--SDR are to be allocated to participants in proportion to their IMF quotas. All IMF members are eligible to participate. Allocations of SDR will take the form of book entries in a Special Drawing Account of the Fund.

The proposal to create an amount of new assets will be for a specific amount, the product of a wide consensus. SDR will be allocated to members of the Fund in proportion to their Fund quotas. For example, the United States has 24.6% of the total Fund quotas and thus would receive \$246 million of each \$1 billion of SDR created. Receiving an allocation of SDR means that the Fund would credit this amount to the United States on the books of the Special Drawing Account in the Fund.

4. Method of transfer--SDR will be transferred by debiting the SDR account of the user and crediting the SDR account of the receiver, with the receiver paying convertible currency to the user. There will be rules on eligibility to use, on countries to which transfer can appropriately be made, and on partial reconstitution of the amount used. The Fund will act as a kind of traffic director, guiding the flow of SDR as they are transferred from one country to another.

Countries will be expected to use SDR only for balance of payments needs or in light of their reserve position. A country's judgment as to its eligibility to use may not be challenged, but the Fund may make representations and direct SDR to a country which the Fund believes has failed to observe the expectation. This will help to assure an orderly flow of SDR and avoid instability resulting from shifts in the composition of reserves which might come about if, at a particular time, one of the three principal reserve assets--gold, dollars, and SDR--happened to look more attractive than the others.

SDR will normally be transferred to countries in strong balance of payments and reserve positions. Transfers of SDR may also go to countries in a strong reserve position even though they have moderate balance of payments deficits. In order to achieve a generally fair distribution of the SDR among the countries that meet the standards entitling them to receive SDR, the Fund will try to work toward equality, over time, in the ratios of their holdings of SDR to their total reserves or in the corresponding ratios to total reserves of their holdings in excess of their allocations.

A further principle of use concerns a country's obligation to reconstitute SDR balances, related to time and amount of use. For the first five-year period, a country's average net use of SDR, "shall not exceed 70% of its average net cumulative allocation during this period." If any country, for a time, exceeds this rate of use, the Fund would direct part of the natural flow of SDR to it, in order to promote observance of this standard. Thus, reconstitution will take place through a restoration of holdings of SDR in the account of the user with the Fund, with payment of convertible currency by the user to other users. In addition to the net average use rule, it is also provided that "Participants will pay due regard to the desirability of pursuing, over time, a balanced relationship between their holdings of Special Drawing Rights and other reserves." This provision is intended to draw attention to the idea of a balanced use of SDR along with other reserves over time and, thus, maintain a degree of stability, in a general way, in relative holdings of the new asset and existing reserve assets.

In implementing the basic principles of use, the Fund will act as a kind of traffic director, making known to eligible users which countries are the appropriate receivers of transfers and assuring that the flow to receivers is distributed in an equitable manner. It may provide that using and receiving countries may deal directly with each other in arranging transfers, but the Fund may act as an intermediary to bring eligible users and receivers together.

There is an area to which the Fund role as traffic director does not extend. An eligible user may select the country to which it wishes to transfer its SDR for the purpose of purchasing balances of its own currency held by the other country, provided the latter agrees to accept SDR. This provision is of particular interest to the United States, although it applies generally to any participant. Normally, the U. S. uses its reserve assets to buy dollar balances, and this provision permits the U. S. to use the new asset in much the same way as it uses gold provided both parties agree to the transaction. This does not modify, in any way, the U. S. firm commitment to buy and sell gold at \$35 an ounce.

C. Reduction of the Large and Persistent Payments Imbalances in the United States and Europe

With the agreement at Rio de Janeiro, now being followed up in the International Monetary Fund, important progress has been made in dealing with the long-term problem of an adequate rate of growth in international reserves. A second major problem that has been facing the international monetary system for a number of years is the protracted existence of large U. S. and European payments imbalances. With the passage of time, these imbalances--welcomed in the early years after the war--have proved difficult to adjust and have imposed increasingly severe strains on the international monetary system as they have accumulated. The United States deficit has meant a gradual but steady deterioration in the liquidity position of the United States. That is, our obligations to foreign countries of a liquid character have been growing. These obligations have risen to approximately \$32 billion, about \$16 billion representing the dollar holdings of official monetary authorities, and the remainder held by foreign commercial banks, corporations and individuals. At the same time the gold reserves of the United States have been reduced from nearly \$25 billion at the end of 1949 to \$12 billion at the end of 1967. Because of the central responsibility that the United States has for maintaining the convertibility of foreign dollar holdings into gold, the attenuation of the U. S. liquidity position, though it is still strong, calls with increasing urgency for effective action to halt this process by elimination of the persistent U. S. deficit.

At the same time there has been a persistent surplus in the Continental European countries, taken as a whole. This is closely related to the United States deficit (the two things are, broadly speaking, different sides of the same coin).

The hard core of these persistent surpluses in Continental European centers has been in the countries of the European Economic Community, taken together. Table 3 presents figures for several alternative measures of the aggregate surpluses of these EEC countries, as compared with measures of the U. S. imbalance for the period 1960-66. Although there are variations from year to year, and although the size and direction of change of the imbalances depend partly on which measure is used, the broad outline of the situation is clear. The United States and the European Economic Community as a whole were on opposite ends of a joint imbalance that, instead of being reduced, persisted quite tenaciously throughout the period.

There were, of course, substantial changes in the balance of payments positions of individual European countries during the past decade. Italy's balance of payments took a swing into deficit in 1963, for example, while Germany experienced a period of deficit in 1965 and early 1966. (The German balance of payments reverted to very large surplus later in 1966 and in 1967.) Nonetheless, these individual swings did not substantially alter the situation for the Continental and EEC countries taken as a whole.

Another element of imbalance in the network of world payments during the 1960's was the persistent weakness in the U. K. balance of payments and the resulting series of crises of confidence in the pound sterling. These crises of confidence, beginning in 1964, resulted in very heavy use of credit facilities to supplement British reserves, and provided the financial assets that further enlarged the surpluses of Continental European countries.

D. Maintaining Confidence in the Stability of the Present System

Throughout the period of the Sixties, there have been periods of strain on the international monetary system which have required international cooperation among monetary authorities. While these strains have been felt from time to time by other currencies, they tended since 1964 to center on the United Kingdom and

TABLE 3

Alternative Measures of Payments Imbalance, 1960-66,
European Economic Community and United States
(millions of dollars)

	<u>Balance on Non-Monetary Transactions (Surplus +)</u>	<u>Change in Official Position (Surplus +)</u>	<u>Change in Published Reserves (Increase +)</u>
<u>European Economic Community:</u>			
1960	3,225	3,454	3,594
1961	1,624	1,980	2,174
1962	178	519	674
1963	234	1,462	1,447
1964	2,147	1,926	1,752
1965	2,281	1,533	1,327
1966	1,252	1,159	1,148
1960-64 Annual Average	1,482	1,868	1,928
1965-66 Annual Average	1,767	1,346	1,238
1960-66 Annual Average	1,563	1,719	1,731
Cumulative Balance 1960-1966	10,941	12,033	12,116
<hr/>			
	<u>Balance on Liquidity Basis (deficit -)</u>	<u>Balance on Official Reserve Transactions (deficit -)</u>	<u>Decline in Gold Reserves and Reserve Position in the IMF ^{1/} (decline -)</u>
<u>United States:</u>			
1960	-3,901	-3,403	-2,145
1961	-2,370	-1,347	-722
1962	-2,203	-2,705	-1,516
1963	-2,671	-2,044	-491
1964	-2,800	-1,549	-391
1965	-1,335	-1,304	-1,571
1966	-1,357	+225	-1,108
1960-64 Annual Average	-2,789	-2,210	-1,053
1965-66 Annual Average	-1,346	-540	-1,340
1960-66 Annual Average	-2,377	-1,732	-1,135
Cumulative Balance 1960-66	-16,637	-12,127	-7,944

(cont. on next page)

1/ Does not include changes in U. S. holdings of convertible foreign currencies.

Sources and Notes: For details on consolidated EEC balance of payments, see Chapter IX. For details on U. S. balance of payments, see Chapter III below.

the position of the pound sterling. Despite a massive effort of international cooperation through the International Monetary Fund and through bilateral arrangements with other monetary authorities, a series of untoward events in 1967 led to the decision to reduce the par value of the pound sterling in November 1967.

Against the background of a persistent U. S. payments deficit, this development brought to the forefront the latent problems of maintaining confidence in the convertibility between gold and dollars, the two major elements in international reserves. It also led to substantial shifts of private funds out of several major currencies on the part of foreign gold speculators fed by expectations of a possible rise in the price of gold on the London gold market.

These disturbed conditions resulted in a substantial shrinkage in gold reserves during the 4th quarter of 1967, as gold was paid out of the reserves of the United States and other members of the gold pool consortium. While the effects of these transactions are somewhat complex, because of shifts between private and official holdings of dollars, the overall effect was also to reduce the supply of dollars in world money markets. This private movement to the sterile liquidity of gold has a tendency to tighten world interest rates, besides presenting the danger of a cumulative drain on the United States as an international banking center.

The necessity of taking a prompt and decisive action to nip in the bud any such tendency to cumulative pressure on the world's entire financial structure through an international move toward excessive conversions of dollars into gold provided the immediate urgency which called forth the new Action Program.

E. Mutual Responsibilities and the Need for Decisive Action

The three problems facing the international monetary system are obviously interdependent, so much so that it is impossible to deal with them separately. A full realization of this fact is the key to the multilateral efforts that are required to solve these problems.

First, it is necessary for the United States to take new and decisive steps to reduce its balance of payments deficit and arrest the long-standing deterioration in its liquidity position. Forceful action has now been taken, and this action, of necessity, unfortunately involves measures which have a substantial cost in terms of other economic objectives. The mandatory controls on direct investment outflows, the firmer voluntary guidelines for the banks and the request to defer nonessential travel outside the Western Hemisphere are all measures which the United States has adopted very reluctantly. The high cost of these measures is in itself a dramatic witness to the priority the United States attaches to doing its full share in reducing the imbalance in world payments-- and to the recognition that a breakdown of the system would have involved far higher costs for the U. S. and even more for the world economy.

Second, the reduction of the deficit in the U. S. balance of payments must be allowed, and even encouraged, by the rest of the world; indeed, major positive measures by other countries are required to bring about payments equilibrium consistent with the achievement of sound world economic growth and freer as well as growing international transactions. In other words, a substantial improvement in the United States external accounts must have a counterpart in adjustments of the balance of payments positions of countries that have excessive surpluses; it should not come at the expense of countries who are in weak payments and reserve positions.

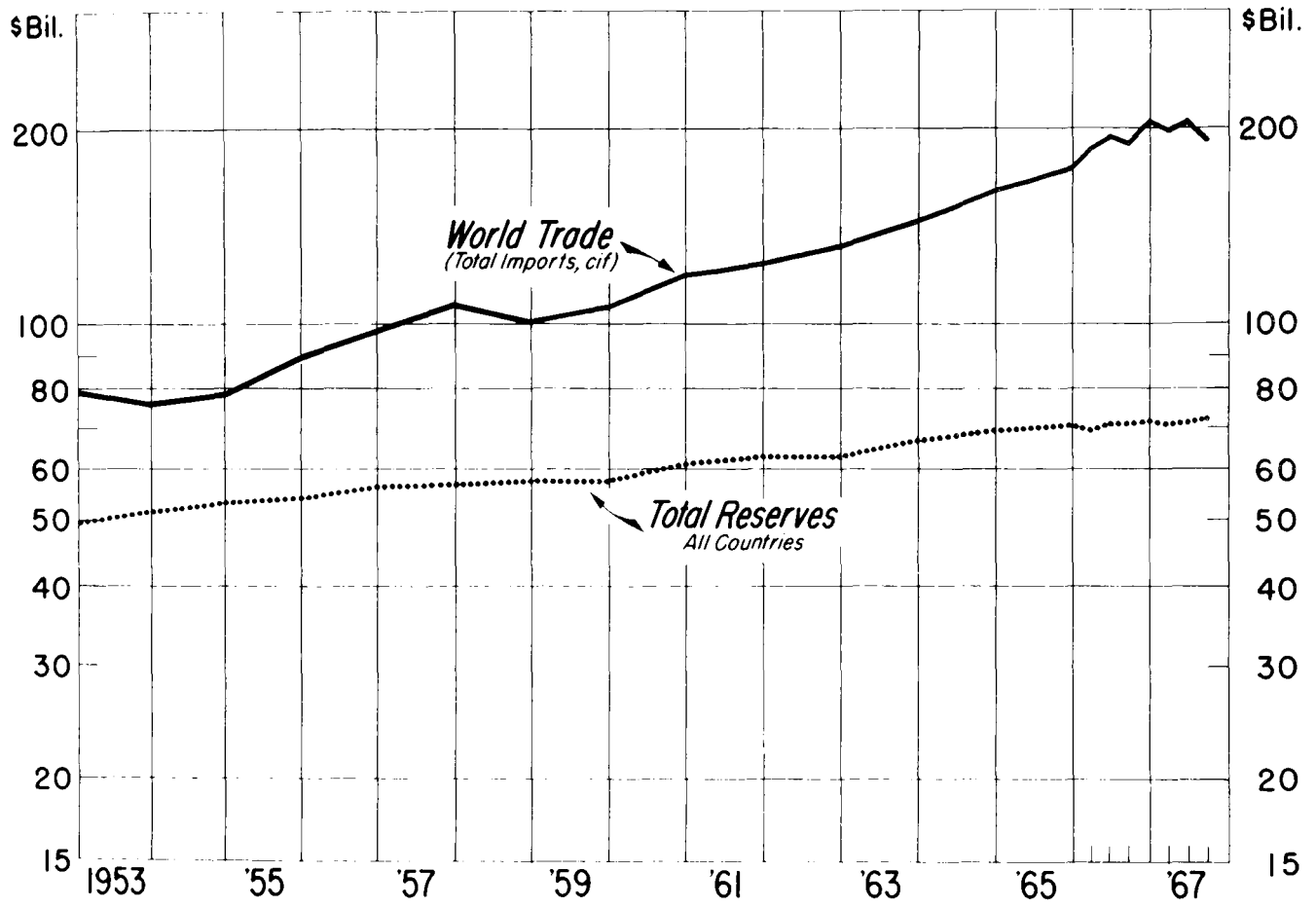
It is therefore a matter of the highest priority for European governments--again, particularly the governments of the EEC countries--to face the full implications of the fact that their balance of payments positions must show a large change from excessive surplus to much more moderate surplus, perhaps even to moderate deficit for a short period. These governments may even be called upon to take forceful actions themselves to make sure that this reduction in their imbalances does occur.

Third, all the member countries of the International Monetary Fund must make a sustained effort to complete the work on legal drafting of the SDR amendments, followed by a speedy adoption and activation of

the machinery itself. For reasons already given above, the introduction of SDR into the international monetary system is an absolutely essential part of an integrated effort to deal with the complex of problems facing the system.

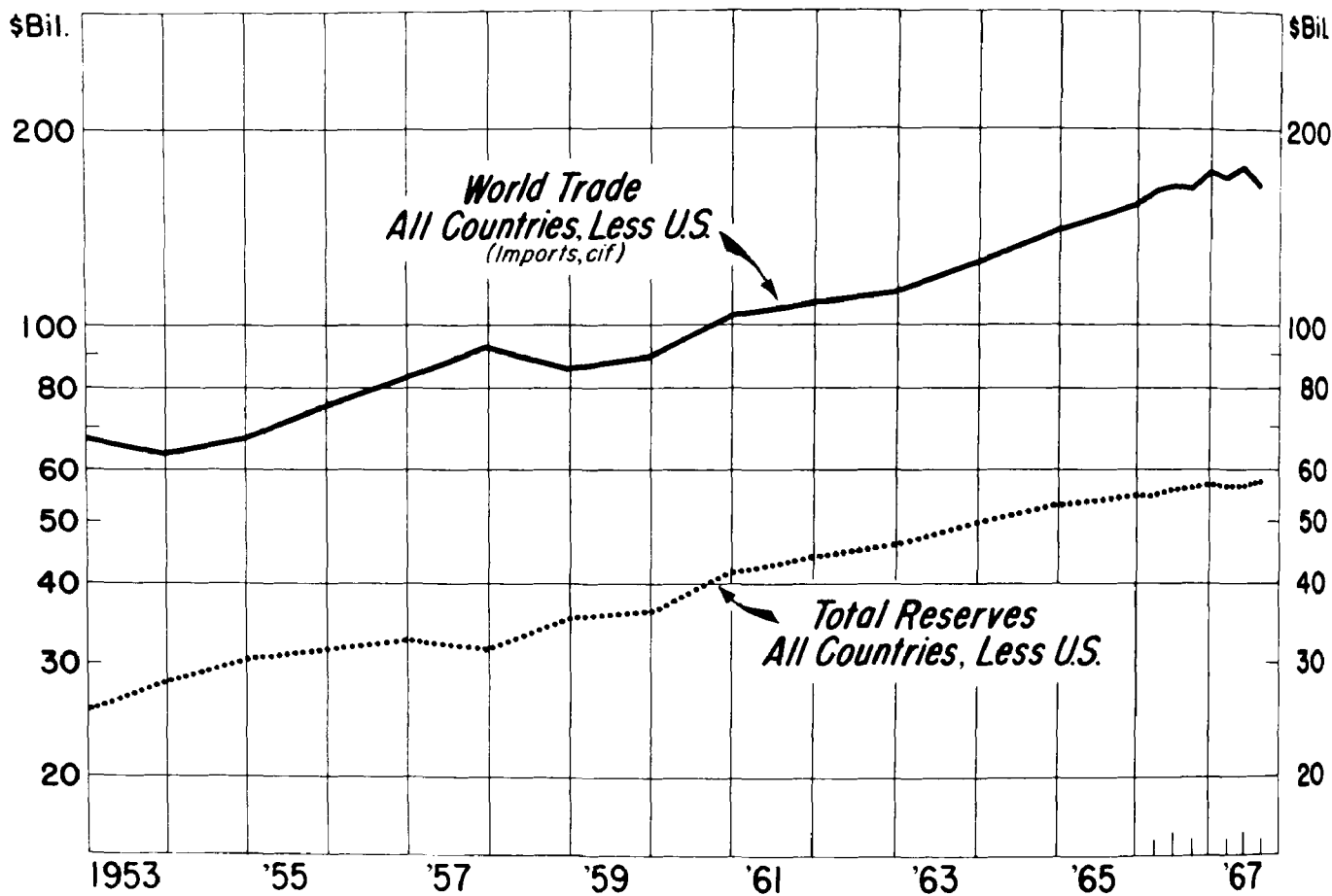
Chart II

WORLD TRADE AND MONETARY RESERVES



Source: *International Financial Statistics*.

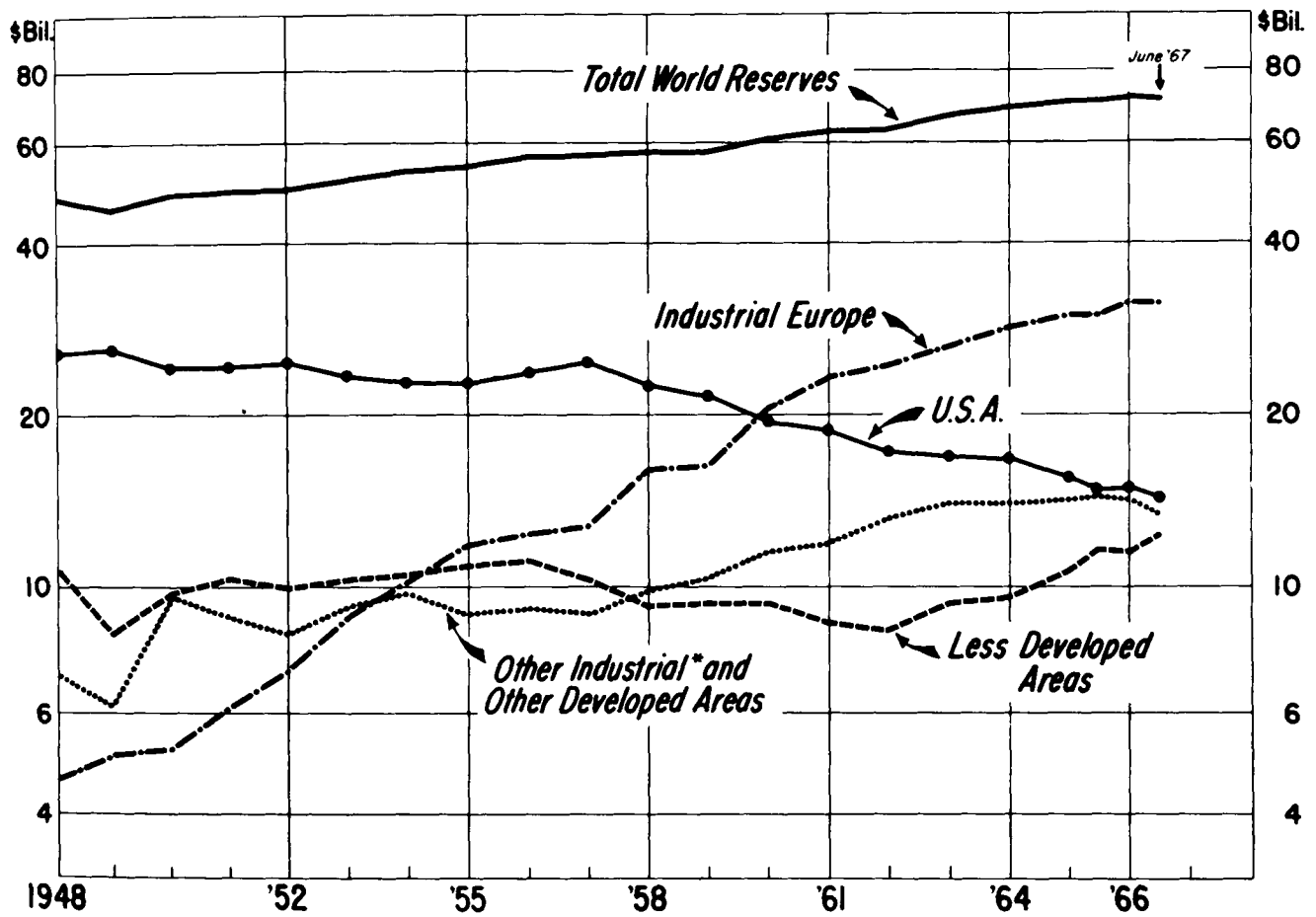
WORLD TRADE AND MONETARY RESERVES, LESS U.S.



Source: International Financial Statistics.

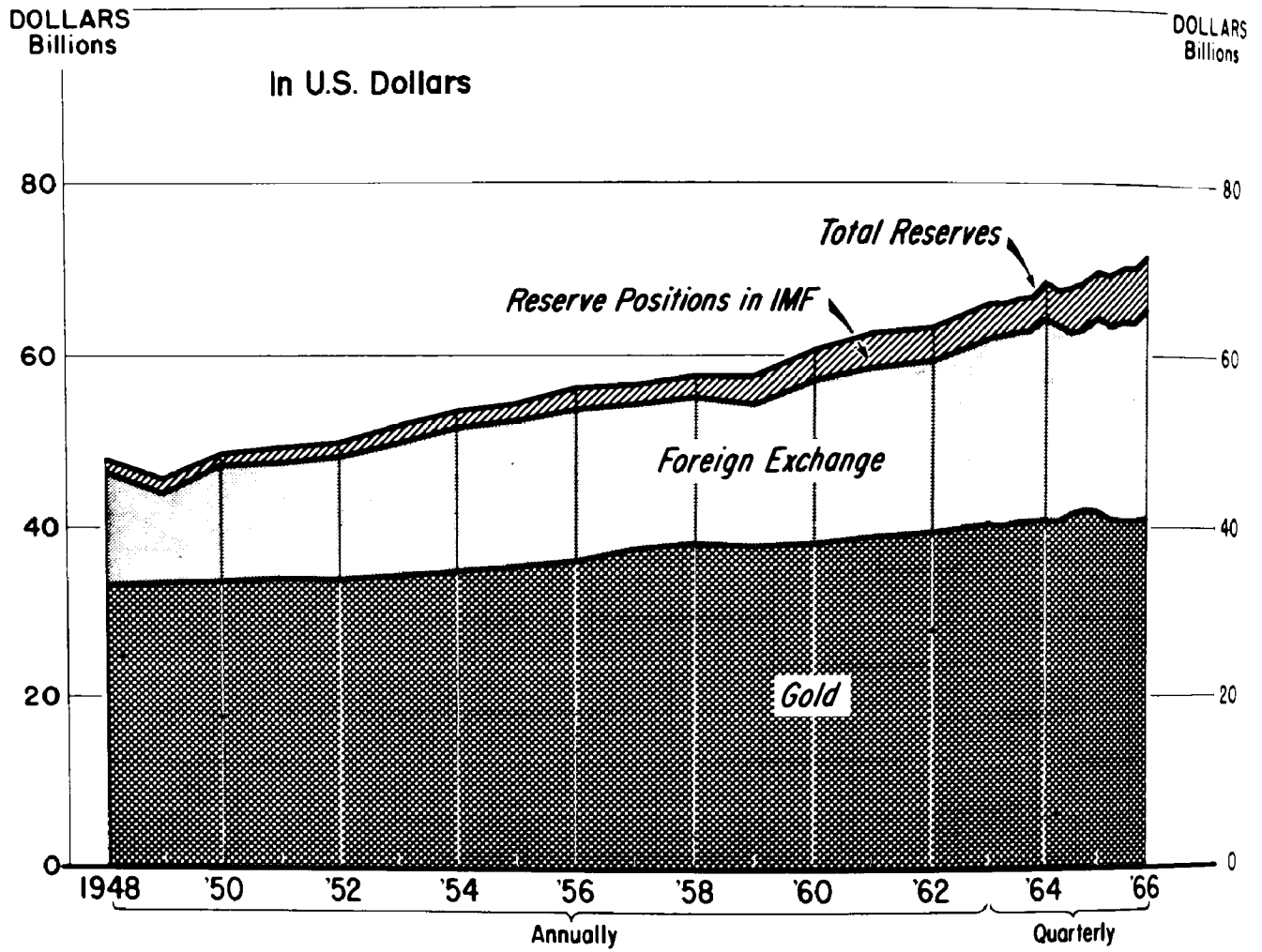
Chart IV

WORLD RESERVES BY MAJOR AREA, 1948-'67



*"Other Industrial" includes United Kingdom, Canada, and Japan.
Source: "International Financial Statistics."

COMPOSITION OF WORLD RESERVES, 1948-'66



Source: International Financial Statistics.

III. U.S. Balance of Payments--The Record to Date

This chapter traces the evolution of the U.S. balance of payments during the 1960's and the measures adopted to cope with the deficit.

In general, the United States has sought to improve its balance of payments in ways that are conducive to (1) vigorous economic growth at home and in the rest of the world, (2) reasonable price stability at home and abroad, (3) and the preservation of an international framework for trading and investing that encourages the best use of resources. The specific measures adopted have attempted to avoid interfering with the maintenance of international security and the flow of capital to developing nations while recognizing the special role of the U.S. dollar in the international monetary system.

A. Trends since World War II

For more than a decade after the end of World War II, the economic and financial policies of the United States and of other countries were influenced by an overriding need to get the world economy back on its feet. Tremendous progress was made--in physical reconstruction, in bringing the defeated countries, Germany, Italy, and Japan, back into the currents of world trade, in gradually dismantling much of the pre-war and wartime paraphernalia of exchange controls and trade controls, in rebuilding monetary reserves, in reactivating the machinery of private credit. Severe inflation was halted. To help Europe and Japan get into the position of financing themselves internationally by trade instead of American aid, many currencies were devalued in 1949. Later, the French franc was again devalued in 1957 and 1958.

In this earlier period the United States had a balance of payments deficit, but it was not one that this nation or other nations were concerned about. The deficit may be said to have been almost deliberately created, to help rebuild the economies of the rest of the world and to rebuild the monetary reserves of the rest of world. The great problem for the whole world was the "dollar gap," and we were doing our best to close it.

In the mid-1950's, Europe and Japan were rapidly regaining their economic strength. Between the recessions of 1954 and 1958, the United States had a consumption and investment boom during which our price level for metals and machinery rose 20 percent (from the end of 1954 to the end of 1957). By the end of 1959 those prices--particularly important in determining our international competitive position--were nearly one-fourth higher than in 1954. With Europe and Japan steadily increasing their ability to produce goods for export, conditions were being created that would make it more difficult than before for the United States to achieve an adequate surplus in the current account of the balance of payments--that is, a current surplus sufficiently large to cover the flows of U.S. private and Government capital to the rest of the world.

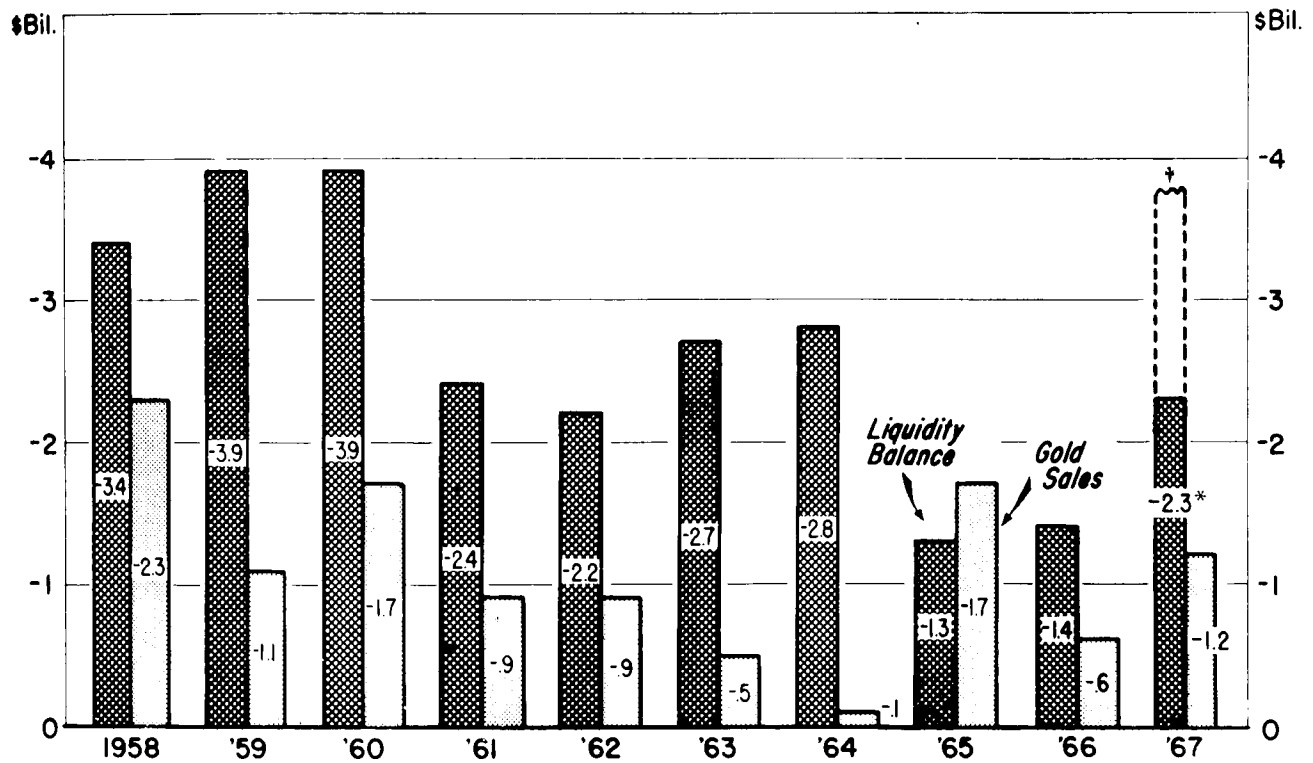
Beginning in 1958, the United States has had a long series of large international payments deficits. These deficits, and our reserve losses, averaged much larger in 1958-60 than in the preceding ten years, and though reduced after 1960 they remained excessive. (See Charts VI and VII.)

Throughout the last ten years, except in 1958 and 1959, the United States has had large annual surpluses in net exports of goods and services (nonmilitary plus private remittances and pension payments). But these surpluses have been inadequate to cover the net outflow of capital and the government overseas costs of our security. Furthermore, in the last two years, this surplus has dropped somewhat at the same time that private capital outflows and the costs of maintaining security have risen.

The overall deficits have eaten into our net reserve position. During the past ten years our gold reserves fell from \$23 billion to \$12 billion, while our liquid liabilities to foreign central banks and governments increased from \$9 billion to \$16 billion. Nearly half of these gold losses occurred in the period 1958-60.

In addition, our other liquid liabilities increased by about \$10 billion during the ten-year period in question. This growth of liquid liabilities to others than foreign central banks and governments served to hold down the amounts of the deficits that had to be financed by official reserve transactions, including gold sales.

U.S. BALANCE OF PAYMENTS ON "LIQUIDITY" BASIS AND GOLD SALES

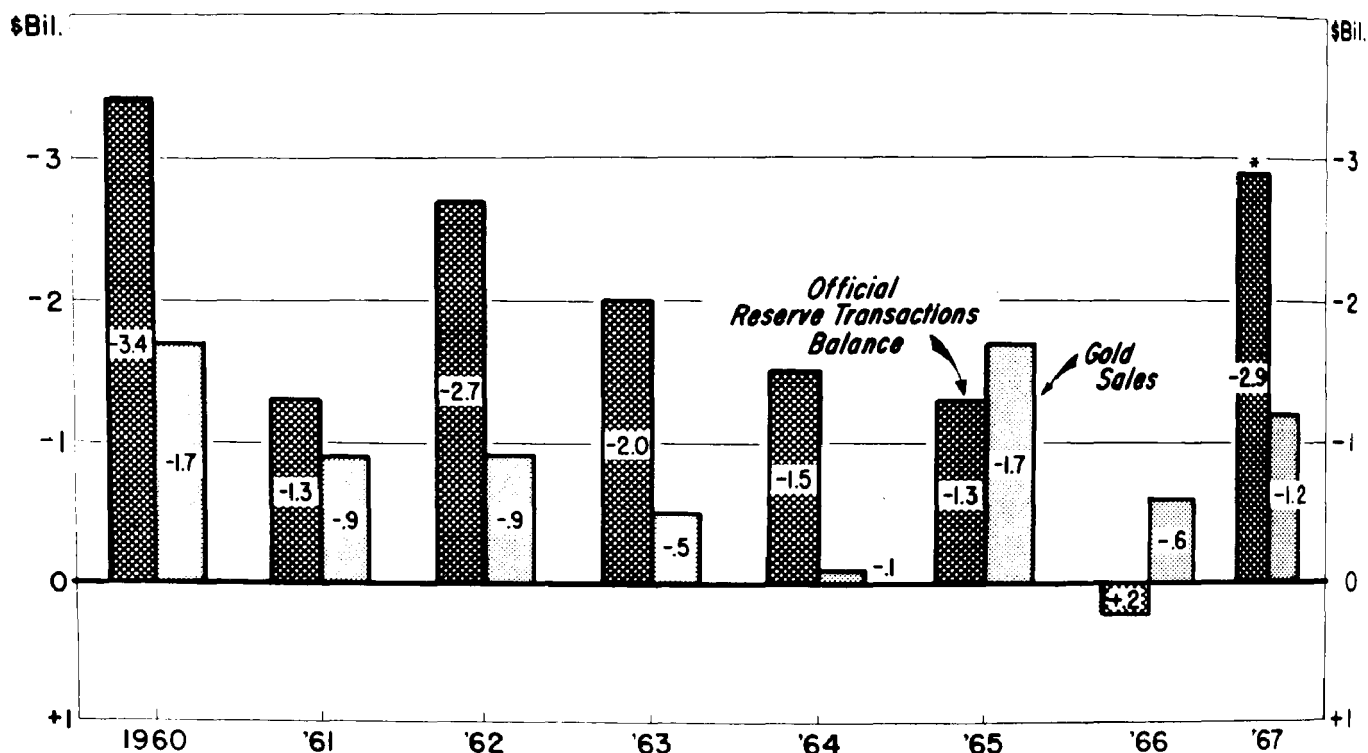


*First three quarters 1967 seasonally adjusted annual rate. *Preliminary full year estimate. -\$3.5 to -\$4.0.

Note. Includes sales for domestic industrial and artistic purposes. Also includes acquisitions from IMF of \$300 million of gold in 1960 and \$150 million in 1961 and a payment of \$259 million of gold for quota increases in 1965.

Chart VII

U.S. BALANCE OF PAYMENTS ON "OFFICIAL SETTLEMENTS" BASIS AND GOLD SALES



* First three quarters 1967 seasonally adjusted annual rate.

Note: The official settlements balance counts changes in dollar claims of foreign official monetary authorities — but not private holdings — in addition to reserve losses of the U.S. The liquidity balance counts changes in the liquid dollar holdings of all foreigners — private and public — as well as losses in reserves.

After the end of the long steel strike in 1959 we had for five years an unprecedented degree of stability in U.S. industrial prices, while creeping inflation was going on in the rest of the world. (See Tables 4 and 5.) Along with that price stability we had an unprecedentedly long period of uninterrupted economic growth, and a great expansion of both our international receipts and our international expenditures.

In the period from 1960 to 1964, the U.S. balance of payments was characterized by a growing surplus on current transactions as the U.S. competitive position improved. In this period the trade surplus increased markedly, and receipts of income from foreign investments rose sharply. Also, the balance of payments cost of foreign aid was reduced through tying aid to U.S. goods and services, and net military outlays decreased as a result of economies and offset sales.

The favorable trend in the balance on goods and services from 1960 to 1964 was offset, however, by a strong tendency for private capital outflow to increase-- a tendency that was dampened first by the Interest Equalization Tax (mid-1963) and later, in 1965, by the voluntary programs to restrain direct investment in subsidiary companies abroad and loans abroad by U.S. financial institutions.

Though the overall balance of payments position was sharply improved in 1965 as the result of the voluntary restraint programs, the current account surplus began to worsen again. Especially from mid-1965 to the end of 1966, the underlying position worsened as a result of both the foreign exchange costs of the Vietnam War and the impact on the U.S. trade balance of the sudden upsurge in demand and rising prices. In 1967 there was a pause in the previously very rapid rise in imports, but as a result of the recessions in economic activity in some important foreign countries the rise in our exports also slowed.

B. U.S. Balance of Payments Programs

In the period 1961-65, the Kennedy and Johnson Administrations launched a series of attacks on the balance of payments problem (see Tab A). These programs, described in Messages by President Kennedy in February 1961 and July 1963, and by President Johnson in February 1965, included in a broad spectrum of administrative and legislative measures designed:

TABLE 4

Wholesale Prices for Manufactures - U.S. and Major Foreign Competitors

(1960 = 100, national currency basis)

	<u>1958-1960 annual average</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>
European Economic Community						
France <u>a/</u>	95.6	103.0	104.1	107.2	109.8	110.4
Germany <u>b/</u>	99.2	102.3	104.6	105.8	106.6	109.2
Italy <u>b/</u>	100.7	99.8	104.2	110.1	113.8	116.8
United Kingdom <u>c/</u>	98.8	102.7	104.0	104.7	107.5	111.6
Canada <u>c/</u>	99.4	101.0	102.8	105.0	105.9	107.9
Japan <u>b/</u>	98.2	100.9	101.2	105.2	105.2	109.1
<hr/>						
United States <u>c/</u> <u>d/</u>	99.5	100.0	100.3	100.0	100.4	102.2
<hr/>						

a/ Intermediate goodsb/ Consumer goodsc/ Manufactured goodsd/ For purposes of international comparison, U.S. data represent an OECD reweighting of official U.S. indices, and exclude manufactured foods.Source: Derived from data in Main Economic Indicators, published by the Organization for Economic Cooperation and Development.

TABLE 5

Unit Labor Costs for Manufactures - U.S. and Major Foreign Competitors(1957 = 100, U.S. dollar basis) a/

	<u>1958-1960 annual average</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>
European Economic Community						
France	88	94	101	105	110	112
Germany	104	116	125	129	129	137
Italy	100	95	99	110	113	109
United Kingdom	104	111	114	113	114	120
Canada	100	94	88	87	36	87
Japan	101	100	109	113	111	118
<hr/>						
United States	104	106	105	104	104	103
<hr/>						

a/ Adjusted for changes in dollar parities of foreign currencies.

Source: Derived from data published by the Bureau of Labor Statistics, and the National Institute of Economic and Social Research.

- to increase American exports of goods and services;
- to increase inflows of portfolio capital and tourist receipts;
- to moderate private capital outflows;
- to reduce Federal Government foreign exchange outlays; and
- to strengthen international financial cooperation through such multilateral institutions as the International Monetary Fund and the Organization for Economic Cooperation and Development.

These Presidential recommendations for action shared a common philosophical underpinning, enunciated by President Kennedy in his February 1961 balance of payments message:

- The official price of gold will be maintained at \$35 per ounce;
- National security and economic development programs will be carried forward;
- Maximum emphasis must be placed on expanding exports. This requires that costs and prices be kept low and that the Government help to enlarge foreign markets for American goods and services;
- A return to protectionism is not a solution; and
- The United States must take the lead in harmonizing economic policies among those industrialized nations whose behavior has a major influence on the course of world income and trade.

This statement of policy was in accord with the general objectives of the Eisenhower Administration, as set forth, for example, in the January 1961 Economic Report of the President.

During 1961-64, fiscal and monetary policy aimed at encouraging noninflationary economic expansion, and as already noted there was improvement in the current account of the balance of payments in this period. Selective fiscal and monetary measures also affected the capital account of the balance of payments. These actions included:

- reductions in corporate income taxes;
- liberalized depreciation allowances, to bring our rates more closely into line with those of our major foreign competitors;
- passage of the 7 percent investment credit;
- carefully designed monetary policies to keep domestic long-term interest rates low while moving shorter-term interest rates higher to minimize short-term capital outflows ("Operation Twist").

Over the four-year period 1961-64, an improvement of more than \$3.7 billion took place in the following accounts:

- a higher commercial trade surplus (\$1 billion);
- reduced overseas dollar spending for foreign aid (\$400 million);
- economies in military spending abroad (\$200 million);
- increased deliveries on military offset sales to foreign countries by the Department of Defense (\$400 million);
- and an increase in profits and interest on past foreign investments (\$1.7 billion).

The net overall improvement for 1964, however, fell far short because of a sharp rise in overall private capital outflows, including both short- and long-term bank credits and direct investment. The \$3.9 billion deficit in 1960 was reduced to \$2.8 billion in 1964.

The new balance of payments measures introduced by President Johnson in February 1965 served to check the rapid growth that had been developing in private capital outflows. His message called upon the business and banking community to do everything in their power to help to reduce overall private capital outflows. In addition, the President asked for legislation to remove tax barriers to foreign investment in the United States, an extension and broadening of the Interest Equalization Tax, further efforts to promote U.S. exports and foreign tourism in this country, and reductions in duty-free allowances for returning American tourists.

In response to the voluntary credit restraint programs, U.S. private capital outflows dropped substantially and the balance of payments deficit on the liquidity basis was cut from \$2.8 billion in 1964 to \$1.3 billion in 1965.

C. Developments in 1966 and 1967

The year 1966 brought a halt to further progress toward equilibrium, owing primarily to:

- mounting direct costs of Vietnam, military expenditures related to Southeast Asia showing a further increase of \$700 million over those of the preceding year;
- a \$1.1 billion deterioration in our trade surplus which resulted from a flood of imports induced by unusually rapid and unbalanced increases in aggregate domestic demand and renewed inflationary pressures (associated in part with acceleration of defense outlays). U.S. export performance also was adversely affected by these factors, as well as by lagging economic growth in some major foreign markets.

On the other hand, U.S. capital outflow increased only a little in 1966, reflecting the continued effects of the Interest Equalization Tax, the Federal Reserve and Commerce Department voluntary restraint programs, as well as the tight credit conditions prevailing during much of the year. Meanwhile, there was a substantial increase in foreign capital inflow, as U.S. corporations sold securities abroad to finance direct

investment abroad and as the Treasury Department launched a campaign to acquaint foreign central banks and others with certain long-term investments in the United States -- notably certificates of deposit issued by commercial banks and certain federal agency bonds and participation certificates. Foreign purchases of these instruments were motivated by attractive interest returns as well as by the desire to reduce the large burden imposed upon the U.S. balance of payments by its growing overseas security and economic assistance efforts.

All in all, therefore, the liquidity deficit remained unchanged from 1965 to 1966. And the balance on the official settlements basis showed its first annual surplus, as the dollar holdings of foreign central banks fell substantially, reflecting the attraction of high interest rates for increased private dollar holdings in the Euro-dollar market and in the United States.

During the first three quarters of 1967 the balance of payments deficit was higher (at a seasonally adjusted annual rate) than in 1965-66.

The trade surplus increased only slightly from its depressed level of 1966. Imports leveled off with the slackening in aggregate demand in the U.S. economy in the first half of the year, but began to rise again toward the end of the year. Exports also leveled off, partly because economic activity in Western Europe was not expanding much during the spring and summer. Though activity was picking up in Germany in the autumn, conditions were still slack in a number of other countries.

There was a further increase in U.S. military expenditures in Vietnam in 1967 and a sizable increase in the outflow of U.S. private capital, particularly through purchases of foreign and international securities exempt from the IET, and through bank lending abroad. The larger capital outflow was in part a normal reflection of easier monetary conditions in the United States as compared with 1966. The improved liquidity of commercial banks helps to explain not only the increase in bank loans to foreign borrowers but also the repayment in the first half of the year of debt of head offices of banks to their branches

abroad. The result of this reflow shows up in the very large deficit on the official settlements basis in the first half of the year.

In the final quarter of 1967 there was a large deficit--substantially larger than the quarterly average through September. This further deterioration was accounted for, mainly, by the following factors: liquidation by the U.K. Government of the \$600 million balance in its portfolio of U.S. securities; speculative pressures in connection with the sterling devaluation; absence of substantial net foreign official acquisitions of long-term time deposits (as in 1966 and the first half of 1967); a deterioration in the trade surplus. (Complete data for the quarter are not yet available.)

Table 6 summarizes the U.S. balance of payments performance from 1958-60 through the first three quarters of 1967.

D. New Action Program

The British devaluation of sterling has reinforced the urgency of the need to improve the U.S. balance of payments. The British move created uncertainty and unrest in the international monetary system and doubts about the future stability of the dollar. These doubts arose in large part because of the persistence of large U.S. deficits and uncertainty as to whether the U.S. payments position would improve.

In these circumstances, it was urgent that the United States adopt strong measures to deal with the balance of payments problem. This it has done. Some of the new measures are clearly temporary. Others are of a long-run nature.

The U.S. program will inevitably create the need for adjustments elsewhere in the world. If the program is to lead to better and sustainable payments equilibrium, reduction of the U.S. deficit must be accompanied by reduction of surpluses in Western Europe.

The result will be a distinct slowdown in the rate of growth of world reserves, and as the United Kingdom repays its debts to the International Monetary Fund, possibly a decline in world reserves. This development will bring much closer the appropriate time for activation of the plan for creation of Special Drawing Rights.

TABLE 6

U.S. Balance of Payments: 1958-60, 1965, 1966, and Jan.-Sept. 1967
(billions of dollars)

	Average 1958-60	1965	1966	Jan.-Sept. 1967 (annual rate)
Trade Surplus	<u>3.02</u>	<u>4.77</u>	<u>3.66</u>	<u>4.35</u>
<u>Surplus on total private and Govt. non-military current account</u> <u>a/</u>	4.26	8.00	6.94	7.11
<u>Military and Govt. grant & capital transactions, net</u>	<u>-5.32</u>	<u>-5.26</u>	<u>-6.23</u>	<u>-6.60</u>
Net military <u>b/</u>	-2.89	-1.82	-2.75	-3.08
Of which: Increased expenditures related to Southeast Asia <u>c/</u>		(-0.25)	(-0.95)	(n.a.)
Gross grant & capital outlays <u>d/</u>	-3.19	-4.28	-4.68	-5.24
Repayments on Govt. credits and other Govt. capital receipts	0.76	0.85	1.20	1.72
(Net balance-of-payments cost of total Government- sector transactions) <u>e/</u>	(-3.71) <u>f/</u>	(-2.59)	(-3.24)	-3.49
<u>U.S. private capital, net</u>	-3.06	-3.74	-4.21	-5.05
<u>Other transactions, net</u>	0.42	-0.33	2.14	2.25
Of which: Foreign capital	(0.41)	(0.08)	(2.45)	(3.17)
(of which U.K. Govt. portfolio)	(--)	(-0.50)	(--)	(--)
 BALANCE ON LIQUIDITY BASIS	 <u>-3.71</u>	 <u>-1.34</u>	 <u>-1.36</u>	 <u>-2.28</u>
Balance on official settlements basis	n.a.	-1.30	0.23	-2.90

a/ Non-military goods and services plus remittances and pensions.

b/ Military expenditures less military cash receipts, as published by Commerce Department in balance-of-payments accounts. In 1958-60, less transfers under military sales contracts.

c/ Increases over calendar year 1964 level.

d/ Total foreign aid and credits, including outlays used on a "tied" basis to finance exports and other receipts of both private and Government sectors.

e/ Excludes from net Government transactions that part of foreign aid and credits used on a "tied" basis to finance exports and other private-sector receipts.

f/ 1960 only.

Note: Detail may not add to totals due to rounding.

Source: Derived from Department of Commerce data.

IV. An Intensified Effort to Achieve and Maintain A Healthy United States Trade Surplus

A. Introductory Comments

The keystone of a sound international financial position for the United States and the dollar is a substantial trade surplus.

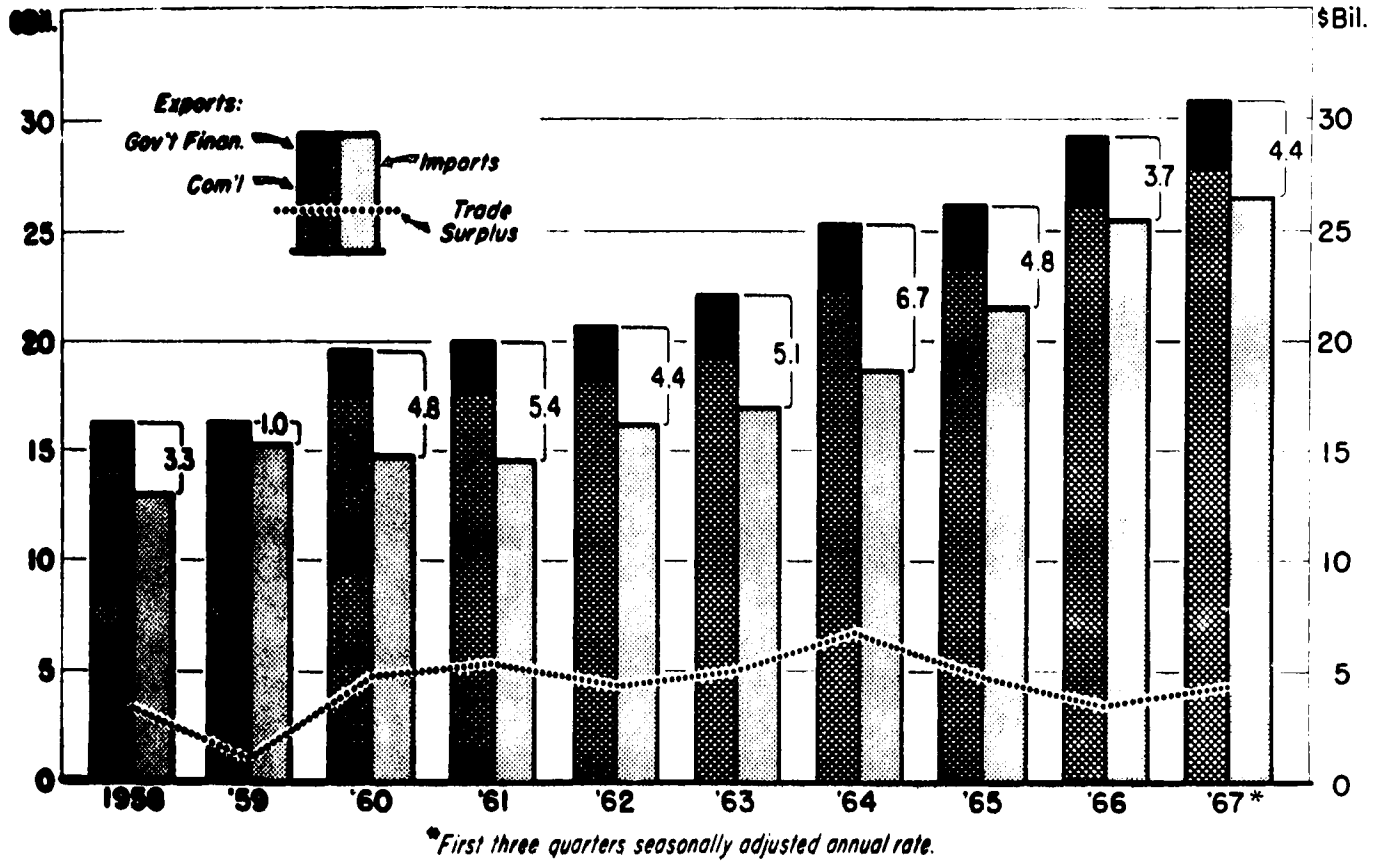
It is natural and desirable for a rich country like the United States to export capital, to give foreign aid, to provide its share of the common defense, and to have large numbers of its citizens traveling abroad. But all this is possible only if, in addition to income from foreign investments, the U.S. trade surplus is large enough to finance such expenses.

The U.S. has consistently had a trade surplus--an excess of exports over imports. In 1950-55, the surplus averaged \$2.2 billion; in 1955-60 it averaged \$3.8 billion; and in 1960-65 it averaged \$5.2 billion. It reached an all-time high of \$6.7 billion in 1964, but it narrowed in 1965 and dropped much further in 1966 when it reached \$3.7 billion. There was some strengthening of our trade surplus in 1967 to approximately \$4 billion.

Continued U.S. balance of payments deficits strongly suggest that the trade surplus has been inadequate. To determine what should be done about increasing it, we must first examine the basic forces affecting U.S. trade.

U.S. exports and imports are strongly influenced by the pressure of U.S. domestic demand, by changes in the U.S. competitive position, and by the economic growth and policies in our major overseas markets. What impact do these interrelated factors have on our trade?

UNITED STATES FOREIGN TRADE



U.S. Competitive Position in World Markets

As can be seen in Table 7, in the 1960's, U.S. unit labor costs in manufacturing declined slightly while those of our major European competitors rose significantly. If changes in relative costs were the only determinant of export performance, then we should have noticeably increased our relative share of world markets.

TABLE 7

Unit Labor Costs In Manufacturing For Selected
Industrialized Countries Since 1961 a/

	(1961=100)				
Country	1962	1963	1964	1965	1966 <u>b/</u>
United States	99	98	98	97	99
Canada.	99	100	100	95	99
France	107	112	118	119	116
Germany	107	111	111	117	123
Italy	108	118	124	122	118
Japan	108	113	111	118	125
United Kingdom	104	102	103	109	114

a/ Ratio of wages, salaries, and supplements to production; national currency basis.

b/ Preliminary.

Note.--Data relate to wage earners in Italy and to all employees in other countries.

Sources: Department of Labor and Council of Economic Advisers.

In point of fact, the U.S. held its share of world trade between 1961 and 1964, as Table 8, shows.

TABLE 8

<u>Year</u>	<u>U.S. Share of Total World Export of Manufactures</u>
1961	25.6
1962	26.5
1963	25.6
1964	25.8
1965	23.6
1966	23.5

Notes:

1. An adjustment for declassified U.S. special category exports was made by subtracting \$1.0 billion from U.S. and world totals in 1965 and 1966.
2. Excludes intra-EEC and intra-EFTA trade.

Source: United Nations Monthly Bulletin of Statistics
November and December 1967.

In 1966 and probably in 1967, the U.S. competitive position was eroded by increases in U.S. labor costs.

Another important reason for the decline in the U.S. share of world exports in the past two years has been the sharp difference in rates of economic expansion in Europe and the U.S.

Impact of Differences in Economic Expansion in the United States and Europe

The experience of the first half of the decade indicates the vital importance of sound domestic economic policies to growing U.S. trade surpluses. This is most clearly seen in an examination of the relationship of U.S. imports to the pace of U.S. economic expansion, as illustrated below:

TABLE 9

	<u>GNP (Current Prices)</u>		<u>Imports</u>		<u>As % of GNP</u>
	<u>\$</u> <u>billion</u>	<u>%</u> <u>Change</u> <u>(from</u> <u>previous</u> <u>year)</u>	<u>\$</u> <u>billion</u>	<u>%</u> <u>Change</u> <u>(from</u> <u>previous</u> <u>year)</u>	
1963	590.5	5.4	16.99	5.0	2.9
1964	632.4	7.1	18.62	9.6	2.9
1965	683.9	8.1	21.47	15.3	3.1
1966	743.3	8.7	25.51	18.8	3.4
1967 (first 3 qtrs.)	777.5	5.5	26.35	5.0	3.4

As the annual growth rate in GNP (current prices) moves up, imports climb more than proportionately. In 1965 and 1966, a period in which GNP growth exceeded 8 percent per annum, our average growth in imports exceeded 16 percent per annum.

Clearly, it was not only the rate of increase of GNP that was the causal factor, but also the fact that the economic slack which had existed in the early 1960's was being taken up in 1965 and was completely eliminated in 1966. In short, if the United States can maintain a noninflationary pace of economic expansion, the growth in imports is likely to be much more moderate than in 1965 and 1966.

What happens in our major markets is obviously of great importance in determining the level of U.S. exports. When foreign economies--principally Western Europe and Canada--are expanding, total world markets are likely to be strong and U.S. exports are likely to rise with a general increase in world trade. Where expansion is weak--as it was when it slowed markedly in Western Europe in 1966 and 1967--world trade and U.S. exports suffered. From 1960-63 to mid-1967, European industrial production increased only 26 percent while U.S. industrial production rose 36 percent--U.S. growth being more than a third faster. This was a major factor in the \$1.7 billion decline in the U.S. merchandise trade surplus from 1961 to 1966.

Foreign Trade Policies

Trade policy of foreign governments has an important impact on the U.S. trade accounts. The Kennedy Round, just completed, which will result in substantial reduction of barriers to trade, will strengthen national economies through expansion of both exports and imports. But, as far as we can now determine, this expansion will not basically alter the trade balance of any major country.

Other changes in trade policy, however, are not neutral in their impact on trade balances. In particular, recent changes in border tax adjustments--taxing imports and remitting taxes on exports--of some European countries, while consistent with the existing international rules of the General Agreement on Tariffs and Trade, will have an adverse effect on the U.S. trade balance.

B. Soundly Managing the U.S. Economy to Keep It Competitive and Stable

The above discussion shows the crucial importance to the U.S. trade balance of maintaining a noninflationary expansion in the United States. As in 1966, excessive increases in income--especially when we have full employment--will be quickly translated into higher prices and capacity bottlenecks with a resulting surge in imports and a slowdown in exports. We need the fiscal action proposed by the President on August 3, 1967--expenditures restraint and tax measures including surcharges on

corporate and personal income taxes. The performance of our trade account in the last few years underscores the need for responsible financial management by the Executive Branch, the Congress, management and labor.

With the economy picking up momentum in 1968, and with cost and price pressures increasing, we are faced not with the assurance of a continued improvement in our trade surplus but the threat of another downward movement.

The recent devaluation of sterling and subsequent speculative pressures in the gold market--reflecting the view held by many that the U.K. move will put further pressure on the U.S. balance of payments position--reinforce still further the need for responsible action on the fiscal front.

All other efforts to improve our balance of payments position will be undermined unless we avoid the kind of excessive growth that floods us with imports and unless we return to relative price stability and cost competitiveness in the United States economy.

The prompt enactment of the President's tax increase program is the single most important and indispensable step this Nation can take now to improve our balance of trade and payments and protect the dollar and the international monetary system.

The role of the Federal Government in the maintenance of an economic environment in which price and cost stability can be sustained is widely recognized by international financial authorities. The Balance of Payments Adjustment Process Report by Working Party No. 3 of the Organization for Economic Cooperation and Development stated:

"It is agreed that there are certain general principles (or 'rules of prudence') which should be followed by all countries in order to prevent as far as possible the emergence of balance of payments disequilibrium. In the field of demand management, it is agreed that it should

be a general object of fiscal and monetary policy to maintain demand at a level which is neither excessive nor deficient, and to promote a continuing expansion of total national expenditure in line with the trend growth rate of productive potential. There is also agreement that, in general, fiscal policy should play a major role in the management of demand."

Business and labor also have an important responsibility to protect our trade surplus by

- keeping wage demands and price decisions consistent with national productivity performance; and
- avoiding work stoppages or the threat of work stoppages in industries vulnerable to import or export competition at a time when our balance of payments position is under pressure.

Efforts to return to the price and cost stability that characterized the first five years of the decade require business and labor to exercise the utmost responsibility in their wage-price decisions. These decisions directly affect our competitive position at home and in world markets. Accordingly, the President has directed the Secretaries of Commerce and Labor and the Chairman of the Council of Economic Advisers to work with the leaders of business and labor to make more effective the voluntary program of wage-price restraint.

Work stoppages in major manufacturing, mining, or transportation industries, or the mere threat of such stoppages can also cause considerable difficulties for the balance of payments:

- Most directly, imports are encouraged and exports deterred because of work stoppages or threats of them when the collective bargaining contracts affecting a basic industry are due to expire. Take, for example, the relationship of trade in steel to the three-year collective bargaining contract in that industry; The steel strike of 1959, for example, cost us \$300 million in larger imports and \$200 million in lost exports. Imports jumped from 2.9 percent of U.S. consumption in 1958 to 6.1 percent in 1959. Many U.S. customers never returned to American mills.

In 1962, imports jumped from 4.7 percent to 5.6 percent of steel consumption, as a result of the threat of a strike, and in 1965, imports jumped from 7.3 percent to 10.3 percent of consumption, and the steel trade balance deteriorated by \$430 million--again without a strike. The threat of a steel strike in 1968 can bring in at least \$300 million of additional steel imports, and an actual strike would push this figure even higher.

-- But steel is not the only area of concern. The dock strike in 1965 appears to have cost an immediate \$700 million in our trade surplus, of which it is estimated that no more than half was subsequently regained. The current copper strike has already cost our balance of payments at least \$150 million.

While the United States is rich enough to afford the real cost which strikes impose, leaders of labor and management should be prepared seriously to consider whether there is any feasible way to give advance public assurance that there will be no work stoppage for the next year or two in industries capable of causing significant balance of payments trouble.

C. Keeping World Markets Open

We have witnessed two decades of progressive liberalization in international trade. From 1946 to 1966, Free World exports rose from less than \$50 billion to more than \$180 billion. This extraordinary growth in trade has been accompanied by the highest domestic growth rates the industrial world ever experienced.

The U.S. has played a leading role in this process of trade liberalization, a process climaxed by the recent conclusion of the Kennedy Round, in which all major trading countries of the Free World participated. Indeed, the Kennedy Round represents the most far-reaching liberalization of trade ever achieved in international negotiations.

Tariff cuts exchanged among all the participants affect about \$40 billion of world trade and about \$15 billion of U.S. trade. Reduction of tariffs on industrial products to the extent of 50 percent cover a very broad range of goods. Substantial, but somewhat smaller, reductions cover many more. This provides a challenge and an opportunity--a challenge to U.S. industry to use its competitive vigor to meet international competition in our markets at home, and an even greater opportunity to compete for a greater share of expanding

exports internationally. Reduced tariff barriers mean increased chances to trade.

At the same time however we have responsibility to avoid resorting to unilaterally imposed statutory quotas at home. Our trade surplus is uniquely vulnerable to the adverse impacts of a quota war--and that would be the certain aftermath of such protectionist action by the United States Congress.

D. Making U.S. Industry More Export Minded Through Selective Export Expansion Programs

In addition to intensified efforts to keep American exporters competitive and to keep foreign markets open, the United States will embark on a major new program of selective export expansion measures.

These new measures, described below, will provide additional help to businesses already active in the export field and those yet to enter it. The measures cover the general areas of export finance and export promotion. Some of them build on export expansion programs already launched in previous balance of payments programs and described in Tab A. Others are new and **experimental** and will start on a small scale. While immediate budgetary prospects do not permit a massive increase in outlays for export expansion purposes in fiscal year 1968 and fiscal year 1969, we envisage a gradual build-up in these programs to very sizable dimensions in coming years.

There is ample precedent for these new recommendations in actions taken by other governments to stimulate their exports.

We embark on this intensified program of selective export expansion measures because the superior price and cost performance by American industry may not be enough to improve our trade balance. Until quite recently, many U.S. corporations have been fully occupied with the immense task of serving the largest domestic market in the world. (In the past seven years the growth in the U.S. domestic market has been equivalent in size to the combined market of France, Italy, and the United Kingdom.)

Improved export performance by U.S. corporations depends not only on competitive strength in terms of price but on competitive strength in terms of delivery periods, credit terms, and marketing efforts as well. It also depends on zeal and a desire to venture for a position in foreign markets.

On May 23, 1967, the President said:

"One of the most ambitious goals we have for the months ahead is ... to try to fire up the producers of this Nation to attempt to make a substantial increase in our exports and to find new ways and means of bringing about that result."

The program described below is intended to do just this.

In devising this package of export expansion proposals, the Administration has been guided by

- the recommendations of the National Export Expansion Council;
- recommendations of American corporations already actively engaged in the export business and those not yet so engaged;
- recommendations of the American financial community;
- the budgetary realities of the day; and
- United States contractual obligations under the General Agreement on Tariffs and Trade (GATT).

1. Improved Export Financing

The Export-Import Bank is our key Government agency to help provide appropriate financial accommodation for our exports. As part of the new program to stimulate the flow of our goods into overseas markets:

- a. The Congress will be asked to earmark \$500 million of the already-requested \$4.5 billion authorization for Export-Import Bank to be used for greatly liberalized export insurance and export guarantee facilities in that bank. In addition, a portion of this sum should be earmarked to enable the Export-Import Bank to make loans carrying a higher degree of risk than carried by its traditional credits in those cases where the development of lasting and growing markets for U.S. products appears particularly promising.

- b. The Export-Import Bank will greatly strengthen and liberalize its rediscount facility for export paper, carrying such paper for longer periods of time and charging more attractive rates than is presently the case.
- c. To reinforce a. and b. above, the Export-Import Bank's Exporter Credit program will be greatly liberalized, providing the private community throughout the country with increased discretion and authority covering a new range of nations.

2. Intensified Export Promotion Activity

- a. As a result of initiatives arising from previous balance of payments programs, the Commerce Department has greatly intensified its export promotion activities in recent years. The number of commercial exhibitions at trade fairs and trade centers-- to cite just one result of these intensified efforts-- has climbed from 24 in fiscal 1963 to a planned total of 65 in fiscal 1968. The number of U.S. firms participating in these fairs and centers has jumped from 886 in 1963 to an estimated 2,390 this year. While overseas promotion activities involve foreign exchange costs, the balance of payments returns from these programs are believed to be exceptionally high. These returns are measured by annual questionnaires sent by Commerce to corporations participating in the activities in question.

In view of the success of these programs to date and the high returns derived therefrom, the Administration will ask the Congress for an additional appropriation of \$10-1/2 million in fiscal year 1969 to increase the sum spent on existing export promotion programs from the \$11-1/2 million presently authorized to \$22 million. During the five years, fiscal year 1970 to fiscal year 1974, we should plan in terms of increasing annual appropriations for these programs up to an annual level of \$50 million. The Secretary of Commerce feels that he can productively spend approximately \$200 million over the five-year period in question on these programs and the Congress will be asked to support such an intensified program.

- b. There are numerous small- and medium-sized companies in the United States which engage in no--or only in very limited--export activities. (Two thousand U.S. companies presently export from \$100,000 to \$10 million of goods and services annually.) These and many other companies could achieve more with additional assistance. Secretary of Commerce Trowbridge has developed a "Joint Export Association Plan" under which the Commerce Department would provide funds to firms associated for the purpose of cooperatively improving their export performance. The Secretary of Commerce has been directed to begin this program.

Funds would be provided to such Joint Export Associations for systematic development of export markets over a sustained period, ranging from two to five years, both in industrialized and developing countries. Government financial assistance provided for such market developments would be determined on a contract-by-contract basis, would generally not exceed 50 percent of the cost, and would phase out over time.

Expenditures for trade development activities eligible to be shared under this program would include those for the following activities:

- Advertising, Publicity
- Participation in trade fairs and other exhibitions
- Market research
- Supplying samples and technical data
- Overseas trade promotional visits
- Preparing and submitting bids (intended to cover specialized equipment and unusual projects, including blueprints, drawings, etc.)
- Operation abroad of sales offices, showrooms, warehouses, and service centers
- Training of sales and service personnel
- Product use familiarization programs
- Operation abroad of assembly and packaging facilities for U.S. products

Joint Export Associations could involve large, medium, and small firms, handling unrelated, complementary, or competitive products, although emphasis is expected to be placed primarily on the smaller firms.

In its initial stages, the Joint Export Associations program would be experimental. If the program were successful, requests for rather substantial additional appropriations could be made in subsequent years.

E. Keeping World Markets Fair

The success of our own export expansion program depends significantly not only on a competitively strong U. S. economy and on a liberal trade policy at home and abroad to keep world markets open. It also depends on the treatment our goods receive in world markets. A number of other countries--some of them in balance of payments surplus--have utilized financial measures, promotion, export rebates, and border tax adjustments to strengthen their trade positions. Some of these measures have put us at a relative disadvantage. To reduce the inequities and harmonize trade practices requires:

- a fresh look at some provisions of the GATT
- minimizing the disadvantages to our trade that result from the border tax systems of some of our trading partners and
- reducing nontariff barriers to our trade.

1. A Fresh Look at the GATT

The time has come to reexamine certain features of the General Agreement on Tariffs and Trade. That the United States has been a staunch supporter of the GATT, and the principles of liberalized trade for which it stands, should be clear to all. An enormous advance toward the expansion of world trade has been made under the GATT. Yet the application of some of its rules could limit the possibilities of expanding trade and with it the increase in U.S. exports, both so essential to all--here and abroad.

- Are the provisions of the GATT for countries in balance of payments difficulties more oriented toward restrictive rather than expansionary trade measures?

- Does the GATT incorporate principles--in the field of taxation and other government activities--that do not apply in today's world, and give advantages to some countries not available to others?
- Do the nontariff barriers which remain in existence throughout the world today limit the benefits achievable from past trade negotiations and limit the effectiveness of many GATT provisions?
- Should we not consider the possibility that changes in tax systems--either as a result of proposed harmonization arrangements in the European Economic Community or other modifications--will make some provisions of the 1947 agreement obsolete?

Article XII of the GATT permits countries in balance of payments difficulty to impose import quotas to help correct the disequilibrium in question. This right has been utilized by a number of countries in the postwar period. But the present rule may result in much harsher and more persistent impediments to world trade than required.

Careful consideration should be given to a revision of the GATT rules so that balance of payments difficulties could be eased by trade devices other than quantitative restrictions.

Ambassador Roth, the President's Special Representative for Trade, raised another urgent set of issues at the GATT Ministerial Meeting this fall as follows:

"Another serious problem area is the relationship of countervailing duties and subsidies. The United States has already raised this question in the Plenary under Agenda Item 16. At that time we emphasized that it was essential to undertake a broad-ranging examination of all aids to exports along with the countervailing duties, since one could not be considered in isolation from the other. We are very much concerned about the consequences of conflicting policies and practices in this area, both in agriculture and industry. This broad and complex area of fiscal adjustment is filled with danger for all of us where practices conflict. If order is to be brought into this field, we must have a clear idea of the nature and effects of these rapidly expanding practices, their relation to one another and to the rules by which we carry on our trade."

The GATT permits countries relying heavily on indirect systems of taxation to provide exporters with rebates and to impose border taxes on imports, while countries relying more heavily on direct taxation, such as the United States, are severely limited in taking comparable action.

Many economists and businessmen question the basic premise underlying these provisions. At one time, it was generally thought that the effects of indirect taxes were entirely passed on to consumers, while direct taxes were wholly absorbed by producers. The GATT rules, reflecting this supposition, allow indirect taxes to be rebated on exports and imposed on imports. But it is increasingly recognized today that border adjustment of indirect taxes creates an unwarranted advantage for some countries.

2. The Immediate Problem of Changes in Border Tax Rates

There is an immediate situation which creates an urgent trade problem. The member countries of the European Economic Community are embarked upon harmonization of their internal tax systems. This harmonization will result in increases in the border taxes and export rebates of some of those countries. Other European countries are also raising their border tax adjustments.

For over two years there have been multilateral and bilateral discussions under the aegis of the Organization for Economic Cooperation and Development of the trade effects of these planned changes in the European countries.

The United States representatives have repeatedly voiced their concern. They have pointed out that such increases will compound the trade advantages gained by the countries which rely on export tax rebates and border tax adjustments on imports of various indirect taxes. They have noted that both the present system and its impending intensification are contrary to the better workings of the international adjustment process and the role that could be fulfilled by surplus countries.

The United States cannot question a country's choice of an indirect tax system or the desire to change from one indirect system to another. But it is concerned with the effect on international trade of the changes in these adjustments which will take place as the EEC countries harmonize their indirect tax systems.

To bring about greater equity between these practices and the United States is an essential element in the balance of payments adjustment process.

Accordingly, the President has initiated discussions at a high level with foreign countries--particularly those nations with balance of payments surpluses--with a view to obtaining their prompt cooperation in minimizing the disadvantages to our trade which arise from differences in national tax systems. Legislative measures are also being prepared in this area whose scope and nature will depend on the outcome of these consultations.

3. Nontariff Barriers

Nontariff barriers abroad still act as impediments to our exports. We must seek not only to reduce and remove these nontariff barriers, but to remain alert against the establishment of new ones.

The U.S. Government has actively reviewed this area of concern:

In its September 1967 report on The Future of U.S. Foreign Trade Policy, the Subcommittee on Foreign Economic Policy of the Joint Economic Committee of the Congress of the United States stated:

"The United States should be prepared to become a leader in the review and mitigation of nontariff obstructions to international trade. The accomplishments of the Kennedy Round negotiations in reducing tariffs as such permits, indeed, calls upon all of the trading nations of the world to take a new and fresh look at the mass of nontariff barriers which have grown up over the years in most countries.

"Not infrequently, these nontariff barriers deny to the individual countries and the world the gains and efficiencies of free trade more effectively and more insidiously than the visible tariff obstructions themselves. Nontariff barriers are numerous and varied, sometimes having come into existence for good and understandable reasons or unfortunately, in some cases,

in response to special pleading or transient conditions in conflict with the long-run interest of the nations involved."

Ambassador Roth, the United States Special Trade Representative, said at the GATT Ministerial meeting on November 23, 1967:

"... As tariffs are reduced, these [nontariff] barriers take on an increasing significance. Indeed, they are already a matter of sharp concern to most of us.

"We think the first need is for an inventory of these restrictions. We do not yet have sufficient understanding of their scope, their significance and their intricate workings. But a useful examination will require positive effort by all nations, because many of these restrictions relate to basic national policies and practices. When this inventory is completed, the Contracting Parties should analyze their trade effects and examine various possible negotiating techniques which might be applied to them."

The reduction of these barriers is an important element in U.S. Government efforts to provide an international environment conducive to the expansion of world trade and a higher level of U.S. exports.

V. An Intensified Program to Moderate the Foreign Exchange Costs of Government Expenditures Abroad for Security, Development, and Other Activities

A. Introductory Comments

We are faced now, and will be in the future, with Government expenditures overseas to meet the costs:

- of our commitments abroad, on which America's security and survival depend,
- of our regular overseas establishments, and
- of contractual obligations overseas that arise in the operation of our Government.

We have pressed in all areas of the Government to achieve balance of payments savings, in our military expenditures, in economic assistance, and in our regular Government operations.

We must move ahead in all these areas even more intensively to achieve further balance of payments savings.

The President's program sets as our new target a \$500 million improvement over the present balance of payments costs of our defense, AID, and other Government expenditures abroad. The President has announced three steps to this end:

"First, I have directed the Secretary of State to initiate prompt negotiations with our NATO allies to minimize the foreign exchange costs of keeping our troops in Europe. Our allies can help in a number of ways, including:

- The purchase in the U.S. of more of their defense needs.
- Investments in long-term United States securities.

"I have also directed the Secretaries of State, Treasury and Defense to find similar ways of dealing with this problem in other parts of the world.

"Second, I have instructed the Director of the Budget to find ways of reducing the numbers of American civilians working overseas.

"Third, I have instructed the Secretary of Defense to find ways to reduce further the foreign exchange impact of personal spending by U.S. forces and their dependents in Europe."

Table 10 shows the net costs of the Government transactions to our over-all balance of payments. (More detail is shown in Tables 11 and 12.) The table shows that between 1960 and 1965 there was a \$1.1 billion drop in the net balance of payments cost of Government activities. Nevertheless, in 1965, the Government sector still showed a substantial deficit (\$2.6 billion). In 1966 (and again in 1967), the Government deficit increased significantly as a result of Vietnam expenditures. (Investments in long-term U.S. bank certificates of deposit made largely by foreign central banks as a result of the effort by the United States Treasury described earlier are not included in these figures.)

TABLE 10

Net Balance of Payments Cost
of Government Transactions

(billions of dollars)

<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	(Jan.- Sept. only)
-3.7	-3.0	-2.0	-2.5	-2.5	-2.6	-3.2	-2.6	

The foreign exchange costs of Government will not disappear when hostilities end in Southeast Asia. They will drop, but much of the opportunity to reduce the net cost to the U.S. balance of payments could be lost unless we exercise self-discipline and insist that other nations do their fair share in meeting joint responsibilities in the military and economic assistance fields.

Ways must be found to neutralize the foreign exchange costs of military expenditures in the common defense.

We must find ways to work constructively with our allies on bilateral and possibly multilateral arrangements designed to neutralize the foreign exchange consequences of the locations of our military forces and those of our allies.

The determination of the share a nation should bear in helping to meet the economic assistance requirements of the less-developed world and the security requirements of our community of nations requires difficult and continuous decisions on a host of issues. These issues cannot be resolved solely on the basis of domestic resources or budgetary considerations.

In the process of providing bilateral aid and contributions to multilateral financial institutions, we must constantly ask ourselves:

- What are other donor countries contributing?
- How aggressively have the institutions in question attempted to borrow in the capital markets of other donor countries?
- What are the recipients doing, through self-help efforts, to utilize the money efficiently and effectively?
- What safeguards are the institutions providing for donor countries that may from time to time be in balance of payments difficulty themselves?

B. Military

1. General Measures to Reduce External Military Expenditures

A detailed report by the Department of Defense on its efforts to reduce expenditures and increase receipts abroad is contained in Tab B.

Our efforts to hold down the foreign exchange costs of military programs have been substantial. Between calendar 1960 and calendar 1965 net military foreign exchange expenditures ^{1/} were reduced from \$2.8 billion to \$1.6 billion despite rising overseas costs and despite such events as the Berlin crisis build-up. The gap widened again in 1966 and in 1967 because of essential outlays for maintaining the shield of freedom in Vietnam. The net balance of payments costs of our defense expenditures for other purposes, although substantial, have been held strictly in check as the Secretary of Defense carried out the President's prior directives to intensify his program:

- to shift defense buying from sources abroad to sources in the United States;
- to reduce the staffs in overseas headquarters;
- to streamline overseas support operations;
- to work with our defense partners to increase their offset purchases of military equipment in the United States.

These and other measures described in Tab B have been taken while fully protecting our security interests and discharging our responsibilities. Military personnel levels outside Southeast Asia have been reduced. Employment of foreign nationals for support or service activities, setting Southeast Asia aside, has dropped. Military Post Exchanges emphasize U.S. goods in their display, pricing, and purchasing practices. Non-Vietnam overseas construction costs entering the balance of payments have been curtailed. On the individual level, a massive education effort has been undertaken to restrain foreign expenditures and increase savings in the United States.

These are general measures that have been taken and which should continue to be vigorously pursued. But they are not enough. Over the past six calendar years (1961-66), our military expenditures outside the United States have averaged \$3.1 billion. Even after taking

^{1/} The figures in this section (B) and those in Tab B are Defense Department data which have some technical differences in classification from the data published in the balance of payments accounts which are used in Table 12 in this Chapter and Table 6 in Chapter III.

account of receipts under the military offset arrangements with Germany and other sales of military equipment, the net foreign exchange costs of military outlays averaged \$2.0 billion.

These military outlays are rising. They were less than \$3.4 billion in fiscal year 1966 and \$4.1 billion in fiscal year 1967. The rising trend in our net military deficit is outlined by region in Table 11.

Vietnam may be viewed as temporary, and the extraordinary foreign exchange drains from it should decline in time. But other significant declines in balance of payments consequences of military deployments outside the United States will depend upon the neutralization of their balance of payments effect.

Two possible ways to neutralize these military expenditures, both involving action by the recipient countries, are:

- purchase of additional U.S. goods and services.
- long-term investments in the United States by central banks or governments.

We must successfully negotiate--bilaterally or multilaterally--long-term arrangements of this sort which offset our large remaining balance of payments costs on military account. No other course is consistent with the adjustment process, or fair and equitable.

2. European Area

Our commitments for the common defense are vital to U.S. security and cannot be put in question. The balance of payments cost to the U.S. of these commitments is substantial. Gross expenditures for the stationing of U.S. forces in Europe currently amount to about \$1.5 billion annually (a part of which has been offset by European purchases in the U.S.). We are now engaged in a renewed effort to find financially viable ways and means of meeting the security needs of the alliance while engaging with our allies in a continuing reexamination of the needs.

TABLE 11

U. S. DEFENSE EXPENDITURES AND RECEIPTS
ENTERING THE INTERNATIONAL BALANCE OF PAYMENTS
(In Millions of U. S. Dollars)

	Fiscal years								
	<u>Expenditures</u>			<u>Receipts</u> b/			<u>Net</u>		
	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>
Southeast Asia a/	350	711	1,206	10	13	68	-340	-698	-1,138
Japan	328	392	535	32	28	35	-296	-364	-500
Korea	80	123	171	5	3	3	-75	-120	-168
Western Europe	1,442	1,531	1,545	1,033	761	1,226	-409	-770	-319
Canada	208	181	220	62	73	41	-146	-108	-179
Other/Undistributed	<u>392</u>	<u>414</u>	<u>432</u>	<u>180</u>	<u>321</u>	<u>397</u>	<u>-212</u>	<u>-93</u>	<u>-35</u>
Total	2,800	3,352	4,109	1,322	1,199	1,770	-1,478	-2,153	-2,339

a/ Republic of China, Philippine Islands, Ryukyu Islands, Thailand and South Vietnam.

b/ Receipts include primarily (1) cash receipts from sales of goods and services through the Department of Defense and (2) barter. Data exclude receipts for military equipment procured through commercial U.S. sources except where covered by government-to-government agreements and data are currently available.

Source: Department of Defense

After consultation in NATO, the U.S. has made arrangements for redeploying about 35,000 U.S. military personnel from Germany in 1968. These forces will be based in the U.S. but will remain earmarked for use in Germany and will return there at regular intervals for training. This plan will also permit a reduction in the number of the Defense Department's foreign employees in Germany.

The Defense Department report contained in Tab B describes the U.S. military sales program, which was primarily responsible for increasing our receipts worldwide from \$300 million in FY 1961 to \$1.6 billion in FY 1967. Most of those sales were to our NATO allies. For six years, until last June, we had a series of "military offset agreements" with Germany under which the German Government undertook to buy from the U.S. military equipment and services costing an amount which offset the bulk of our defense expenditures in Germany. The German Government did not renew the agreements for the period after June 1967 but expects to continue major purchases in the U.S., although advance payments under the offset agreements (of which substantial amounts remain on deposit as of year-end 1967) will reduce our new receipts over the near term. During FY 1968 the German Bundesbank agreed to invest \$500 million in nonmarketable U.S. Treasury securities. This investment counts as a long-term capital inflow, reducing our payments deficit. It does not fully offset our expenditures in Germany.

Despite our offset agreement with Germany, the EEC countries gained an average of over \$300 million annually over the 1961-65 period from military transactions with the United States. In the absence of any neutralization arrangements, this figure will jump to nearly \$1 billion annually, beginning in July 1968.

The importance of neutralizing these costs was stressed by Secretary of State Rusk and Deputy Secretary of Defense Nitze at the NATO Ministerial Meeting on December 12, 1967. In a formal statement in behalf of Secretary of Defense McNamara, the latter said:

"We will, therefore, continue to maintain forces in Europe for as long as they are desired. In saying this, however, I must also point out an anomaly in European attitudes which cannot persist. This is that on the one hand there should be no diminution of U.S. forces, but that on the other hand the responsibility for meeting the balance of payments deficit caused by such large-scale continuing U.S. deployments in Europe is none of Europe's affair. It is essential that deficits suffered by countries as a result of their stationing troops abroad in the common effort should be treated and solved by their allies on a cooperative basis. We would welcome suggestions from our allies on how to meet this pressing problem, since its solution cannot be further postponed."

The United States intends to renew negotiations promptly with Germany and with other European countries where the U.S. has large military expenditures. We propose to explore ways and means of broadening our bilateral neutralization agreements into multilateral arrangements of a long-lasting character.

The economies we have made as a result of the move from France and those which will follow the redeployment of about 35,000 additional military personnel from Europe in 1968 are together expected to reduce our balance of payments costs on military account in Europe by over \$125 million a year. Nevertheless, the remaining balance of payments costs incurred as a result of large-scale deployments of U.S. forces in Europe are still substantial. We have made it clear to our allies that we consider it essential that deficits suffered by countries as a result of stationing troops abroad in the common effort should be treated and solved by the allies on a cooperative basis.

In addition to the other steps being taken to reduce the balance of payments costs of our military effort, the Secretary of Defense has been instructed to find ways to reduce further the foreign exchange impact of personal spending in Europe by Defense personnel and dependents.

3. East Asia

The mounting foreign exchange costs of our vital military actions in Vietnam have brought to the front the question of dynamic and viable financial relationships in that area of the world--both currently and when the fighting stops. The direct balance of payments costs attributable to our security efforts in Southeast Asia began to increase in 1965. By calendar year 1967 the increase totaled \$1.5 billion per annum (excluding indirect effects). But even before Vietnam, U.S. military costs in Asia were not insignificant.

We must intensify our efforts to reduce the impact of the foreign exchange costs of security operations in Asia--both now and after the fighting ends. We have already begun, in a number of countries, to encourage investment of official reserves--climbing dramatically in many instances because of U.S. military spending--in longer-term investments in the United States. This is mutually beneficial--helpful to the developing countries in putting aside a reserve for the future and helpful to the United States, which is now bearing heavy foreign exchange costs in the area. As experience in Europe has taught us, this is but one of a number of possible neutralization techniques. Very clearly, more needs to be done in Asia to neutralize U.S. balance of payments costs incurred in the common defense. More is being done, and can be done without detriment to economic development of the countries of East Asia.

The joint communique by President Johnson and His Excellency Prime Minister Sato of Japan on November 15, 1967, included an agreement

"...to enhance the usefulness of the joint United States-Japan Committee on Trade and Economic Affairs by establishing at an early date a subcommittee. This subcommittee will be a forum for consultation on economic and financial matters of importance to both countries, including the short and longer-range balance of payments problems of the two countries."

The first meeting of the subcommittee is scheduled for late January 1968.

C. Aid

1. Bilateral

We cannot expect to strengthen our balance of payments at the expense of the less-developed world. It is in our economic interest and in the world's economic interest to assist this vast group of nations with its vast potential for expanded world trade, output and employment, or world insecurity, hopeless poverty and frustration.

We seek to assist the less-developed nations toward a better life, but we seek to do it in a way that transfers primarily real resources when we are in balance of payments difficulties and emphasize both real and financial resources when we are in balance of payments surplus.

Our efforts in the past have been directed to two main areas:

- increasingly to tie bilateral foreign assistance to the financing of United States goods and services; and
- to have the other financially powerful countries of the Free World increase their assistance to the less-developed countries.

The fact that our agricultural sales program and the operations of the Export-Import Bank involve U.S. exports is well recognized. The AID story is less well recognized-- its role of assisting others while on an increasing scale supplying U.S. goods in ways that minimize any adverse balance of payments impact.

In most of the 1950's, U.S. bilateral assistance was open to international competitive bidding. Increasingly, this resulted in U.S. financing of procurement in other industrial countries which have recovered from the war and become increasingly competitive. While we were seeking to help the economically "have-not" nations, our help was hurting the dollar and adding to potential calls on our gold. This was inconsistent with our own and the world's balance of payments situation. By 1959 only 40 percent of our bilateral aid dollars were being spent on U.S. goods and services. At that time moves were started to place tighter limitations on the U.S. policy of worldwide procurement. Tying procedures have been strengthened over time.

Today, AID funds are spent primarily in the United States for goods and services procured in this country. Ninety-two percent of total AID expenditures will be spent in the United States. Of AID's total expenditures for commodity assistance, 96 percent will be for procurement of U.S. goods. Successive tightening of AID activities as part of our balance of payments program leaves only a few elements not specifically tied to U.S. goods and services--salaries and payments to AID overseas personnel and contractors, only a part of which is spent abroad, strictly limited offshore procurement, and AID's contribution to the multilateral Foreign Exchange Operations Fund in Laos and parts of some grants to overseas educational institutions.

On a balance of payments accounting basis AID's offshore expenditures were over \$900 million in FY 1961 and \$800 million in 1963. The balance of payments directive was to reduce its offshore expenditures to not more than \$500 million by FY 1965. The target was more than met. Despite a greatly expanded economic aid program for Vietnam, offshore expenditures were held to the target in FY 1966. As a result of AID's further tightening of tied procurement regulations, offshore expenditures are estimated at \$290 million in FY 1967 and at \$200 million in FY 1968. These figures do not take into account the repayments on loans made by AID and its predecessors.

The President, on January 11, 1968, directed that the foreign exchange costs of AID's activities be reduced by at least \$100 million in calendar year 1968 below the calendar 1967 level. The Agency will attempt to reduce its overseas expenditures to less than \$170 million by further restricting dollar payments for staff and services abroad and confining virtually all financial and commodity assistance to tied or barter-type procurement.

Now that our bilateral assistance program is almost completely tied, we are working to make sure that this assistance results in truly additional transfers of U.S. goods and services to the developing countries. This new effort to assure "additionality"--to assure that these exports are additional and that this assistance does not substitute for sales that the U.S. would have made on a commercial basis--has important long-range potential for our balance of payments. When an aid-receiving country buys U.S. goods financed by AID under a tying arrangement, it may be buying goods that it would otherwise have bought with dollars it already owns. Such dollars--free foreign exchange--can be used for purchases and payments either in the U.S. or elsewhere. Tying procurement to U.S. sources may not itself be enough to reduce to the extent necessary the impact of the AID program on the balance of payments.

To meet this potential balance of payments problem, a special task force of the Cabinet Committee on Balance of Payments has been formed to work with AID in a program to assure "additionality" of exports in our aid program. "Additionality Teams" have now visited a number of major aid-receiving countries. AID has begun to explore measures to ensure that AID-financed exports will be additional. This is an on-going effort that must be pursued diligently. As part of this effort, AID has included U.S. export promotion as a factor--although necessarily not the dominant one--in selecting capital projects. Attention is being paid to the selection of projects and goods that have a greater potential for "follow on" orders. U.S. Embassy commercial staffs in the more important aid-receiving countries are being strengthened with this purpose in mind.

This new program cannot succeed by Government efforts alone. U.S. industry and trade must play their role. In too many cases in too many developing countries our businessmen have not actively sought to establish the trade ties so essential in the international competition for new markets. The export expansion program of the Department of Commerce outlined earlier has an important role to play here and must be coordinated with the effort for "additionality".

2. Multilateral

In the field of the multilateral development finance institutions, new efforts have been made to assure the compatibility of our participation with our balance of payments policies. While these efforts have balance of payments improvement as an objective, they also seek to strengthen these institutions and fully preserve their multilateral character. The principles involve:

- improved burden-sharing, by capital exporting countries in their contributions and by developing countries in their self-help efforts.
- improved access of the development finance institutions to wider and more diversified world capital markets.
- mitigating the impact on our balance of payments when access to our own capital market is necessary.

- providing safeguards not only for receiving countries, but for contributing countries that may, from time to time, be in balance of payments difficulty themselves when long-term advance pledges are turned into requirements for payments.
- emphasizing contributions that take the form of goods and services when contributing countries find themselves in balance of payments difficulties and in the form of finance when countries are in surplus.
- more generally, seeking to insure that development finance more actively contributes to the international payments adjustment process while the aggregate level of development assistance, which for too long has been on an international plateau, is significantly increased.

As stated earlier, the determination of a nation's "fair share" of economic--or military--assistance is no simple matter. Years ago, as the other industrial countries regained economic strength, it became clear that the time had come to decrease reliance on a single country. This issue can no longer be resolved solely by relating the size of a given country's contribution to the size of its gross national product. The form in which a donor provides aid, the terms of its aid and its international liquidity position must be taken into account.

The overall effect of the World Bank operations has been a substantial positive factor to the U.S. balance of payments. In its own interest as a multilateral institution and with some urging by the U.S., it has energetically sought to raise capital on other markets. More than half of its funded debt is now held outside the United States. Nevertheless, in the face of its increased requirements for capital and still relatively underdeveloped capital markets abroad, access to the U.S. bond market has from time to time been approved. In each of these instances in recent years the proceeds of these bond issues were reinvested in the United States in a manner that neutralized, at least for a time, any impact on our balance of payments.

The Inter-American Development Bank has acted in the same fashion. It has raised substantial money abroad even under the handicap of going to nonmember country markets, and it has invested the proceeds of its U.S. borrowings in ways compatible with our balance of payments policies. It has recently taken further measures to attract nonmember capital by limiting procurement under its loans in accord with the financing that nonmembers make available on appropriate terms.

The International Development Association, affiliated with the World Bank, is in urgent need of replenishment. Other nations have shared with us to the extent of about \$1.50 for every \$1 we have contributed in meeting this need. Pursuant to President Johnson's directive, the Secretary of the Treasury has indicated our readiness to participate in a substantial replenishment which must include adequate balance of payments safeguards.

The newly-established Asian Development Bank has been characterized by burden-sharing in the fullest sense. Here 20 percent of the capital was provided by the United States and the rest by Japan, other regional donors, Canada, and Western Europe. The President has responded to a further Asian initiative with a request to the Congress to join with others in supplying special funds for concessionary lending by the Bank. In this case the balance of payments will be protected and the U.S. funds will be used only for procurement in the United States. It is in these ways--ways compatible with the realities of international finance--that the U.S. hopes to join with others in meeting the urgent needs of development of those economically less fortunate.

D. Other Departments and Agencies

In order to assure that all activities--not only the key military and aid activities--are brought into balance of payments focus, the overseas disbursements of all departments of Government have been brought under special review and control by the Director of the Bureau of the Budget. The review and control mechanism is called the Gold Budget. Increasingly vigorous screening of expenditures abroad by these other Federal departments and agencies must be continued if the Government is to play its full role in moderating the exchange costs of its own expenditures abroad.

The financial scope of the Gold Budget is large, roughly \$10 billion, taking receipts and expenditures together. The range of activities covered is very wide, from defense outlays to Post Office receipts and expenditures on international mail activities, from overseas payments on the public debt to the cost of operating overseas tracking stations by NASA for space flight missions.

The figures for any agency do not necessarily reveal the scope of the effort to achieve foreign exchange savings. Real foreign exchange savings in some cases have been offset by rising prices abroad which have raised the cost of ongoing programs.

The State Department, whose Gold Budget expenditures in FY 1967 totaled \$265 million compared with \$280 million in FY 1963, has undertaken a variety of actions to cut foreign exchange outlays, including:

- purchase of goods in the U.S. for use overseas, at costs up to 50 percent greater than those abroad;
- use of U.S. flag carriers to the largest extent possible for travel by Department personnel;
- consolidation of overseas posts, elimination of overseas positions, maximal use of U.S. postage for diplomatic pouch mail, and relocation of some courier operations in the U.S.

Despite the narrow margin for reductions, and the continually increasing costs of operation, overseas costs are now below the 1963 levels. The search for additional savings continues.

The United States Information Agency has striven for savings by centralizing operations and procurement where possible in countries where the U.S. Government holds local currencies in excess or near-excess of its needs and by increasing procurement of other goods in the U.S. Consolidation of some overseas operations and their removal to the U.S. are now under consideration.

The Atomic Energy Commission's expenditures abroad reflect purchases of uranium. Such purchases are being phased out entirely.

The Department of Agriculture spends money abroad for development of foreign markets for American foodstuffs, research activities, and payments to foreign-flag vessels to ship agricultural exports. Expenditures for foreign vessels reflected the shortage of U.S. shipping because of Vietnam supply needs. To the maximum extent possible, Agriculture uses excess U.S. holdings of foreign currencies to minimize the balance of payments costs of its activities.

As is well-known, the United States owns amounts of local currency in excess of its needs in a handful of less-developed countries. These holdings have resulted from sales, for local currency, of surplus agricultural products. While the use of these local currencies has helped us save dollars in a number of instances--where we could use the currencies in question in lieu of dollars--we have not been able to utilize all of the currencies acquired. The accumulation of large holdings of other countries' currencies clearly presents a variety of problems. Under the Food for Freedom Act of 1967, we are moving away from agricultural sales for local currency. The Act calls for a transition to dollar sales over a five-year period, except to the extent that the United States needs local currencies for its own uses, for mutual defense, or for "Cooley" loans.

Table 12 summarizes on the basis of our published overall balance of payments accounts, the identifiable impact of all of the foregoing Government transactions. Comparing the results for calendar year 1966 with 1960 levels:

- Net military expenditures had by 1964 been reduced by \$850 million; and, despite the subsequent increase of nearly \$1 billion in Southeast Asia related expenditures, net expenditures worldwide for 1966 did not exceed the 1960 level. In other words, apart from the Southeast Asia increase, net military expenditures in 1966 were down nearly \$1 billion, or more than one-third, from the 1960 rate.
- Net dollar outflows from all types of U.S. Government grants and credits (excluding, that is, the "tied" outlays serving to finance U.S. exports and other receipts from foreigners) had also been reduced by more than one-third, from \$1.1 billion to about \$700 million per year.

-- The balance of all other Government transactions appearing in the overall balance of payments accounts, while fluctuating widely from one year to another due largely to variations in special capital receipts, has generally shown some surplus. In 1966 this surplus was a little over \$200 million, up slightly from that in 1960.

The performance in holding down the foreign exchange costs of all our Government programs during the decade of the 1960's has been good, particularly when the burden of Vietnam is taken into account.

Nevertheless, we should make sure that further savings are obtained. We cannot let up on our efforts in this important area, for unless we can demonstrate conclusively that we are doing everything in our power to limit Government balance of payments costs, we cannot expect continuation of the fine cooperation received to date from the private sector in its efforts to help us solve our balance of payments problem. The Gold Budget will be a key instrument to insure that no stone is left unturned in finding areas where further savings can be made on Government account-- both now and after the end of hostilities in Vietnam.

TABLE 12

U. S. Government Transactions which Appear in Balance of Payments Accounts
(billions of dollars; by calendar years)

	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>
Military expenditures a/	-3.1	-3.0	-3.1	-2.9	-2.9	-2.9	-3.7
Military cash receipts a/	0.3	0.4	1.1	1.0	1.0	1.1	0.9
<u>Net military</u>	<u>-2.7</u>	<u>-2.6</u>	<u>-1.9</u>	<u>-2.0</u>	<u>-1.9</u>	<u>-1.8</u>	<u>-2.7</u>
Excluding increased expenditures related to Southeast Asia b/						(-1.6)	(-1.8)
<u>Gross grant & capital outlays not retained within Govt. sector c/</u>	<u>-3.2</u>	<u>-3.8</u>	<u>-3.9</u>	<u>-4.1</u>	<u>-3.9</u>	<u>-4.0</u>	<u>-4.3</u>
Excluding "tied" outlays to finance U.S. exports & other private-sector receipts	(-1.1)	(-1.1)	(-1.0)	(-0.8)	(-0.7)	(-0.7)	(-0.7)
<u>Net operational costs & receipts of other Govt. programs & activities d/</u>	<u>-0.2</u>	<u>-0.3</u>	<u>-0.3</u>	<u>-0.3</u>	<u>-0.4</u>	<u>-0.4</u>	<u>-0.5</u>
NET "OPERATIONAL" COSTS	-6.2	-6.7	-6.2	-6.4	-6.2	-6.2	-7.6
Excluding "tied" grants & capital & Southeast Asia military increases	(-4.1)	(-4.0)	(-3.3)	(-3.1)	(-3.0)	(-2.7)	(-3.0)
Govt. payments of interest & pensions	-0.5	-0.5	-0.6	-0.7	-0.7	-0.9	-0.9
Receipts of interest & cash amortization on Govt. credits e/	0.9	0.9	1.0	1.0	0.9	1.0	1.2
Special Govt. capital receipts, net f/	0.1	0.7	0.9	0.3	0.3	0.2	0.
NET GOVERNMENT SECTOR	-5.6	-5.6	-4.9	-5.9	-5.8	-5.9	-6.9
Excluding "tied" grants & capital	(-3.7)	(-3.0)	(-2.0)	(-2.5)	(-2.5)	(-2.6)	(-3.2)
Excluding also Southeast Asia military-expenditure increases						(-2.3)	(-2.3)

(TABLE 12 cont.)

- a/ Expenditure and cash receipts data are as published by Commerce Department in balance-of-payments accounts. They differ from Defense Department data by excluding (i.e., shifting from military to other entries): (1) on payments side, small amounts of retired pay, claims, grants, and net changes in foreign-currency balances purchased with dollars; and (2) on receipts side, certain military sales through commercial channels and barter sales.
- b/ Measured from calendar year 1964 level.
- c/ Differs from gross outlays shown in Table 6 by excluding that part of "tied" outlays used to finance military-sales contracts and other Government-sector receipts.
- d/ Represents total Government payments for miscellaneous services, less estimated one-half of government sales of such services not financed by "tied" grant and capital outlays.
- e/ Excludes non-scheduled repayments and those financed by new Government credits.
- f/ Includes non-scheduled repayments on Government credits plus Government nonliquid liabilities not associated with military-sales contracts or grant and capital outlays.

Note: Detail may not add to totals due to rounding.

Source: Derived from Department of Commerce data.

VI. An Intensified Effort for Temporarily Reducing Outflows of U. S. Capital

A. Financial Policy on U. S. Foreign Investment

In its Annual Report of 1967, the Council of Economic Advisers clearly enunciated U. S. financial policy on U. S. investment abroad:

"Over the years, the outflow of U.S. capital has made a major contribution to world economic growth. By providing capital to areas where it is relatively scarce, U.S. foreign investment raises foreign incomes and often leads to a more efficient use of world capital resources. U.S. direct investment has provided a vehicle for the spread of advanced technology and management skills. U.S. foreign investment also has yielded handsome returns to American investors and substantial investment income receipts for the balance of payments.

"Despite the advantages of U.S. foreign investment both to the recipient countries and to the United States, it can--like every good thing--be overdone. And it was being overdone in the early 1960's. Just as a person must weigh and balance opportunities for investment that will be highly profitable in the future against his current wants, so must a nation weigh the benefits of future foreign exchange income against current requirements. The costs of adjusting other elements in the balance of payments may be greater than the costs of sacrificing future investment income.

"It is often true that U.S. investment abroad generates not only a flow of investment income but also additional U.S. exports. From a balance of payments standpoint, this is an additional dividend. Yet it is also true, in some cases, that U.S. plants abroad supply markets that would otherwise have been supplied from the United States, with a consequent adverse direct effect on U.S. exports.

"It is sometimes held that the international flow of capital occurs always and automatically in just the economically 'correct' amount, and that any effort to affect this flow through government measures constitutes a subtraction from the economic welfare of the country of origin, the country of receipt, and the entire world community. Such a position cannot be sustained.

"While much of the large flow of U.S. capital to the developed countries is no doubt a response to a shortage of real capital there relative to the United States, the flow is also influenced by many other factors. These may include cyclical differences in capacity utilization, differences in monetary conditions and financial structure, speculation on exchange rates, tax advantages, and opportunities for tax evasion--none of which necessarily leads to a more rational pattern of international investment.

"High prospective returns on investment in a particular country may reflect a particular choice of policies in the recipient country that is quite unrelated to any underlying shortage of capital. If a country chooses to channel the bulk of its private saving into low productivity uses, if it employs a tight monetary policy, if it limits access of its own nationals to its capital market, it will attract foreign capital. Restraint on such capital flows may therefore merely mean that more of the adverse effect of such domestic policies on economic growth will rest--as perhaps it should--on the country that made the policy choice.

"Trade restrictions may also lead to a flow of capital that would not otherwise take place. U.S. investment in the EEC has, at least in part, been induced by the desire to get within the tariff walls erected around a large and growing market. If, however, a continued movement toward trade liberalization may be expected, the economic justification for some part of these capital flows is lessened.

"One major stimulant for direct investment abroad is undoubtedly the substantial advantage in technology and managerial skills which U.S. firms often possess. The international transfer of these factors may be embodied in a capital outflow independent of the relative scarcity of capital. Action would thus be appropriate, not necessarily to curtail the investment itself, which would interfere with the beneficial transfer of the scarce technology and skills, but to transfer the source of financing to the area receiving the direct investment. This, indeed, is the primary intention and the result of the present voluntary program on direct investment.

"Finally, differential monetary conditions among countries can induce capital flows. But monetary policy is an important and useful instrument of domestic stabilization and growth as well as of balance of payments adjustment Appropriate use of restraints on capital outflows in such forms as the voluntary programs and the IET can usefully supplement monetary policy in promoting domestic and international goals.

"In summary, . . . it is . . . clear that the United States should be a major capital exporter. The U.S. programs have been designed to maintain a reasonable flow of capital, especially to the less developed countries. But given the alternatives and the need to improve its payments position, the United States has restrained the outflow of capital as preferable to cutting essential international commitments, limiting international trade or restricting domestic--and world--economic growth."

Our stake in our corporations operating abroad, of course, goes far beyond our balance of payments returns from their operations. Indeed, since World War II, our corporations operating overseas have made a substantial contribution to the economic growth of the Free World, and it is difficult to overstate their importance to a continuation of that growth.

They are playing a growing role in the expansion of world trade and in providing capital and technology--as well as employment--in the countries in which they operate. Their contribution to growth in the developing countries is often a unique one. The rising incomes and economic progress to which they have contributed means their influence surpasses the economic sphere.

The benefits which have accrued, and should continue to accrue, from the growth of multinational corporations are today threatened by the rising tide of nationalism abroad. In many of the less-developed countries, a growing nationalism, mixed with state intervention or discrimination in varying degrees, has begun to create an uncongenial atmosphere for multinational private business. Indeed the same trend is evident in some of the developed countries where multinational companies have become well established.

There are no easy solutions to the problems of reconciling the interests of the various parties involved--host country, base country, and the overseas corporation itself. A first requirement is clearly a growing understanding of others' needs and problems on the part of all involved.

For its part, the U.S. Government seeks in countless ways to enlarge the freedom of opportunity for multinational corporations operating overseas--by diplomatic efforts to allay fears of foreign domination and exploitation, as well as to remove local barriers to foreign private investment, by programs aimed at deepening and widening understanding in less-developed countries of the workings of a privately-oriented economy, by programs to encourage and directly assist prospective investors in foreign countries, by tax treaty negotiations and by other efforts far too numerous to mention here.

B. Trends in U.S. Foreign Investment and Investment Income

The basic information on U.S. foreign investment and its impact on the U.S. balance of payments is contained in Tables 13-16. The major lessons are:

TABLE 13

Private International Investment Position of the United States a/

(billions of dollars)

	<u>Net Position</u>	<u>U. S. Investments Abroad</u>				<u>Foreign Investments in the U.S.</u>		
		<u>Total</u>	<u>Direct</u>	<u>Other Long Term</u>	<u>Short Term</u>	<u>Total</u>	<u>Long Term</u>	<u>Short Term</u>
1960	8.5	49.4	31.8	12.6	5.0	40.9	18.4	22.5
1961	9.9	55.5	34.7	14.3	6.5	45.6	21.4	24.2
1962	15.0	60.0	37.2	15.5	7.3	45.0	20.2	24.8
1963	16.6	66.5	40.7	17.6	8.2	49.9	22.8	27.1
1964	21.0	75.8	44.4	20.5	10.9	54.8	25.0	29.8
1965	24.6	81.1	49.3	21.6	10.2	56.5	26.4	30.1
1966	28.2	86.2	54.6	21.0	10.7	58.0	27.0	31.0

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a/ Includes short-term and marketable long-term U. S. Government obligations.
Excludes U. S. Government claims and nonliquid U. S. Government liabilities to foreigners.

Note: Detail may not add to totals due to rounding.

Source: Department of Commerce

TABLE 14

U. S. Direct Investment Abroad:
Value, Earnings and Yield

(billions of dollars)

	<u>Book Value</u>	<u>Earnings a/</u>	<u>Yield b/</u>
1950	11.8	1.9	17.7
1951	13.0	2.4	20.1
1952	14.7	2.5	18.9
1953	16.3	2.4	16.2
1954	17.6	2.5	15.6
1955	19.4	3.0	17.2
1956	22.5	3.5	18.2
1957	25.4	3.8	16.9
1958	27.4	3.3	12.8
1959	29.8	3.6	13.1
1960	31.8	4.0	13.3
1961	34.7	4.3	13.4
1962	37.2	4.8	13.9
1963	40.7	5.2	14.1
1964	44.4	5.8	14.3
1965	49.3	6.4	14.4
1966	54.6	6.7	13.6
1967 (est.)	n.a.	6.8	12.5

a/ Includes reinvested earnings plus fees and royalties.

b/ Total earnings as a percent of end-year book values of the previous year.

Source: Derived from U. S. Department of Commerce data.

TABLE 15

U. S. Direct Investment Abroad: Balance
of Payments Outflows and Income

(billions of dollars)

	<u>Outflows a/</u>	<u>Income b/</u>	<u>Net Balance of Payments Impact</u>
1950	-0.6	1.4	0.8
1951	-0.5	1.6	1.1
1952	-0.9	1.5	0.6
1953	-0.7	1.6	0.8
1954	-0.7	1.9	1.2
1955	-0.8	2.1	1.3
1956	-2.0	2.4	0.4
1957	-2.4	2.5	---
1958	-1.2	2.4	1.2
1959	-1.4	2.6	1.2
1960	-1.7	2.8	1.1
1961	-1.6	3.2	1.6
1962	-1.7	3.6	2.0
1963	-2.0	3.8	1.8
1964	-2.4	4.4	2.0
1965	-3.4 a/	4.9	1.5
1966	-3.1 a/	5.1	2.0

a/ Excludes direct-investment outflows financed by borrowing abroad through U. S. financing corporations.

b/ Includes direct investment fees and royalties.

Note: Detail may not add to total due to rounding.

Source: U. S. Department of Commerce data.

TABLE 16

Plant and Equipment Expenditures of Foreign Affiliates
of U. S. Companies, by Area

(billions of dollars)

	<u>1960</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>
<u>All areas, total</u>	<u>3.8</u>	<u>6.2</u>	<u>7.5</u>	<u>8.8</u>
Canada, total	1.3	1.6	1.9	2.4
Latin America, total	0.7	1.0	1.1	1.1
Europe				
Common Market, total) 1.1	1.2	1.4	1.9
Other Europe, total)	1.0	1.3	1.4
Other areas, total	0.7	1.4	1.9	2.0

Note: Detail may not add to totals due to rounding.

Source: U. S. Department of Commerce.

1. The large flows of U.S. investment abroad in the 1960's were an important factor in the U.S. deficit of these years. In each year since 1960 the net private international investment position of the United States has risen substantially.

2. These past investments are, nevertheless, a source of strength now. In 1960, U.S. direct investments abroad contributed to \$2.8 billion of earnings to the United States; this rose to \$5.1 billion in 1966.

3. The yield on U.S. direct investment abroad in the 1960's has been considerably below that of the 1950's.

4. Despite moderation of outflows from the United States for direct investment, the gross investment in plant and equipment expenditures by U.S. affiliates has increased from \$3.8 billion in 1960 to \$7.5 billion in 1965 to \$8.8 billion in 1966 and over \$9 billion in 1967.

5. Even if there were no new foreign investment by the U.S., earnings flows back to this country would continue because they are based on the stock of U.S. investment made to date. Moreover, with continued, even though reduced, U.S. investment abroad and with some improvement in the yields on these investments as economic recovery proceeds in Europe and as start-up costs are reduced, the earnings should rise.

In short, with the new capital restraint programs, we expect a major strengthening of the U.S. balance of payments through the reduction in capital outflows and increases in U.S. earnings on its foreign assets.

C. Limitations on Private Capital Outflows in 1968:
The New Program and the New Interest Equalization Tax

The history of the Interest Equalization Tax and the voluntary capital restraint programs administered by the Federal Reserve System and the Commerce Department are summarized in Tab D. These latter programs were strengthened on November 16, 1967, two days before the devaluation of sterling. In view of the present balance of payments situation and the need to bring about a decisive improvement, both programs were substantially tightened on January 1, 1968.

1. The New Federal Reserve Program for 1968

The Federal Reserve voluntary program announced on November 16, 1967, asked that participating banks keep their holdings of foreign assets within 109 percent of the amount outstanding at the end of 1964. This target ceiling was unchanged from that for 1967. Since banks were below target levels for 1967, however, there was leeway for outflows of bank capital. Moreover, to provide flexibility for banks with relatively small bases, banks were given the option of using the 109 percent ceiling or a 2 percent of total assets test. Banks were requested, therefore, to limit the use of their leeway. In addition, participating banks were requested to hold the level of nonexport credits to the developed countries of Western Europe to or below the amount outstanding on October 31, 1967.

This program is now further tightened in order to achieve a net inflow of at least \$500 million during 1968, primarily by reducing outstanding credits to the developed countries of continental Western Europe, while assuring that sufficient leeway is available to meet the essential credit requirements of export financing, and continuing the existing priorities for developing countries and certain other countries that are heavily dependent on the U.S. to provide the capital needed for economic growth and stability.

The outline of the program to accomplish the new 1968 objective is:

For banks, a reduction in credits by at least \$400 million

- General ceiling for 1968 on foreign credit extensions by banks to be fixed at 103 percent of each bank's 1964 base.
- Alternative provision for smaller banks to allow them a ceiling equal to each bank's 1967 ceiling plus one-third of the difference between that amount and 2 percent of its total assets at the end of 1966.
- Maturing term loans to developed countries of continental Western Europe not to be renewed; the repayments thereon not to be reloaned to residents of those countries; and each bank's overall ceiling on foreign credits also to be reduced by the amount of such repayments.

- Outstanding short-term loans to developed countries of continental Western Europe to be reduced by 40 percent during 1968 (at rate of at least 10 percentage points per quarter) with a corresponding reduction also being made in each bank's overall ceiling.

For nonbank financial institutions: a reduction of credits by at least \$100 million

- Holdings of foreign assets covered by the program to be reduced by at least 5 percent during 1968.
- Holdings of liquid funds abroad to be reduced to zero or minimum working balance requirements.
- New loans or investments in developed countries of continental Western Europe to be limited to credits essential for financing of U.S. exports.

2. The New Commerce Program for 1968

The Commerce voluntary program for U.S. corporations was also continued and strengthened for 1968 by an announcement on November 16, 1967. The 1968 target under the November program provided for an average rate of direct investment in developed countries during 1967 and 1968 equal to the annual average for the three base years. This compares as follows with targets under previous programs:

Total target for 1965-1966 = 90% of 1962-64 total
Total target for 1966-1967 = 80% of 1962-64 total
Total target for 1967-1968 = 66-2/3% of 1962-64 total.

The target cutback under the November program would have produced a savings, combining the outflow of direct investment and earnings retained abroad, in 1968 compared to that estimated for 1967 of some \$200 million.

The Commerce program on direct investment is now substantially tightened to produce a balance of payments savings of \$1 billion in 1968 as compared to the estimated 1967 level. The voluntary mechanism was judged not adequate to attain this goal and the new program is mandatory. It sets targets for geographic areas and will set targets for companies as has been the case under the voluntary programs. Similarly, it is directed to outflows of capital and reinvestment of earnings and not to the bricks, mortar and machinery that may be financed abroad. The major features of the new program are as follows:

- New capital transfers to countries in continental Western Europe and other developed nations not heavily dependent on our capital are to be stopped in 1968. Problems arising from work already in process or commitments under binding contracts should receive special consideration.
- New capital transfers to other developed countries, e.g. Canada, Japan, Australia, New Zealand, the U.K., and the oil-producing countries, are to be limited to 65 percent of the 1965-66 average of direct investment.
- New capital transfers to the developing countries are to be limited to 110 percent of the 1965-66 average of direct investment.
- U.S. businesses must repatriate from their share of the earnings of all their foreign business ventures in the three groups of countries amounts equal to the greater of (1) the same percentage of their share of total earnings from these three groups as they repatriated during 1964-66, or (2) so much of their share of earnings as may exceed the limit set for capital transfers to each group. In the case of the continental European countries where a moratorium on capital transfers applies, the applicable rule with respect to (2) above is that earnings in excess of 35 percent of investment in 1965-66 must be repatriated. U.S. business is also required to reduce short-term financial assets held abroad to the 1965-66 average level.

This new mandatory program still permits American corporations to invest abroad but they must rely to a far greater degree than before on foreign sources of funds, such as depreciation, foreign borrowings (either in local markets or the Euro-dollar market), the sale of equity to foreigners, and, within the limits permitted, retained earnings. They must utilize bank borrowings (from foreign banks, including branches of U.S. banks), foreign private placements and public offerings of securities in foreign capital markets.

3. The Interest Equalization Tax

The Interest Equalization Tax, adopted in 1963, imposes a tax on bonds and stocks purchased by Americans from foreigners in the developed countries. Canada and, to an extent, Japan, were excepted on sale of new issues. The IET was later extended to apply to loans with a maturity of one year or more. Direct investments are not covered by the IET.

The two-year extension of the IET through July 1969, recently enacted by Congress, changed the law to make it a more flexible policy instrument by granting the President discretionary authority to vary the rate of tax within a range equivalent to an added cost of zero to 1-1/2% per annum to foreign borrowers. After being raised temporarily to the 1-1/2% level during the period of Congressional consideration, the tax was reduced on August 30, 1967, to 1-1/4%.

This lowering of the tax rate by Presidential Executive Order emphasized again the fact that the purpose of the Interest Equalization Tax is to equalize the interest cost of borrowing between U.S. and foreign capital markets.

The IET is not designed to halt completely the outflow of portfolio capital from the U.S. but rather, by equalizing borrowing cost, to moderate the rate of outflow to a level which is dependent upon factors other than substantial basic interest rate differentials.

In addition to changing the rate of the tax, the Congress also strengthened the procedure for establishing American ownership of a foreign security in order to permit tax-free transactions among American owners. It is now necessary for an American seller of a foreign security to show by means of a validation certificate either that he paid the tax when the shares were originally acquired or that these shares were exempt from the tax.

D. A Capital Flows Policy for the Long-Range Future

At present, the United States clearly must moderate the outflows of private capital, weighing carefully the eventual yield such outflows will bring against their immediate foreign exchange costs.

In this connection, it is important that these restraints be clearly temporary and administered with flexibility. And finally, it is important that they help generate structural improvements in overseas capital markets. We believe the present program meets these long-term aims:

- It emphasizes an approach as close to previous voluntary programs as possible. Much of it requires no specific legislation. Its success in reducing balance of payments losses will continue to be largely attributable to the cooperation of U.S. companies. It is in the context of an overall program aimed at achieving balance in as short a time as possible and lends itself to phasing out as soon as conditions permit.
- Within the limits established, decisions under the program will continue to be made in the market place. Companies will, subject to these limits, be able to move ahead with what they judge the more vital investments, deferring or canceling other investments providing less promising returns. The temporary program restricts capital outflows from the U.S. and sets certain limits on the reinvestment of foreign earnings, but companies can proceed with their foreign projects beyond these amounts if foreign financing is obtained. Similarly, the Interest Equalization Tax is not a prohibitive tax. It permits American companies and individuals to make portfolio investments and bank loans abroad where there is an unusually high rate of return. Investments in marginally less profitable foreign credit instruments are discouraged.
- The recently obtained flexibility to vary the rate of the Interest Equalization Tax will assure that as the U.S. balance of payments position improves, it will be possible to reduce restraining policies gradually without fear that excessive outflows of capital will suddenly arise.

- The program as a whole is designed to moderate capital outflows only as much as deemed vital to obtain the needed improvement in the balance of payments.
- Both the direct investment and bank credit programs and the IET have been shaped by taking objectives other than the balance of payments into account--notably, the need to have a liberal flow of capital to the less-developed countries and to countries such as Canada which have a traditional reliance on the U.S. capital market. The programs also give high priority to the extension of credits--or the movement of capital--that help expand U.S. exports.

The direct investment and bank credit programs and Interest Equalization Tax, while short-term programs, are designed to have long-term consequences. Most importantly, the growth of the European capital market has been a priority goal of U.S. and European policy for many years. This market could not be developed to handle all of Europe's needs over night. But, by restraining foreign access to capital and money markets in the United States, the IET in conjunction with the Commerce and Federal Reserve programs has operated as one of the primary causes of a significant change in the size and structure of European financial markets.

The growth of the international bond market in Europe (shown in Table 17) has been striking. In 1962, the volume of new foreign bond issues sold in European markets was \$360 million. The flotation of such issues (including foreign issues in national markets in Europe and in the so-called Euro-bond market) accelerated during the second half of 1963 and in 1964 reached a level of \$991 million. In 1966 the amount of new flotation was \$1,286 million, an increase of more than 200 percent from the most recent pre-IET year. And, during the first three quarters of this year, new international issues floated in Europe were running at an annual rate of \$2.1 billion.

U.S. companies have made extensive use of this expanding European capital market to finance their overseas investment needs. Although there were no sales of new long-term issues abroad for the financing affiliates of U.S. companies during 1963 or 1964, the amount of such issues had reached the level of \$490 million in 1966 and promises to be still larger in 1967.

TABLE 17

New International Bond Issues Floated in Europe a/
(millions of dollars)

<u>Borrower</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>		
						<u>I</u>	<u>II</u>	<u>III</u>
Western Europe	190	362	662	660	686	233	330	293
Japan	25	64	209	25	--	--	--	--
Other Developed	54	90	42	83	40	25	120	20
Total Developed Countries	<u>269</u>	<u>516</u>	<u>913</u>	<u>768</u>	<u>726</u>	<u>258</u>	<u>450</u>	<u>313</u>
All Other Countries	14	14	41	24	33	20	45	40
International Institutions	63	4	37	83	36	--	34	--
Total	<u>346</u>	<u>534</u>	<u>991</u>	<u>875</u>	<u>795</u>	<u>278</u>	<u>529</u>	<u>353</u>
U. S. Subsidiaries <u>b/</u>	14	--	--	306	490 <u>c/</u>	117	132	202
Grand Total	<u>360</u>	<u>534</u>	<u>991</u>	<u>1,181</u>	<u>1,285</u>	<u>395</u>	<u>661</u>	<u>555</u>

a/ Includes issues denominated in foreign currencies as well as in dollars; also includes portion of foreign issues made in New York and sold to foreigners.

b/ Domestic based as well as foreign based.

c/ Excludes \$127 million exchange of convertible debentures for stock by a U.S. corporation to obtain major interest in a foreign enterprise.

Note: Detail may not add to totals due to rounding.

Source: U. S. Treasury

The European countries have been giving a great deal of consideration to capital market problems and to reforms that can and should be instituted. Both the Common Market and the Organization for Economic Cooperation and Development are actively working to stimulate improvement. The OECD has published a study on capital markets containing a number of recommendations for strengthening markets and increasing their efficiency. Member governments of the OECD are currently studying the applicability of these recommendations to their own markets. A number of reforms have been undertaken and some of the remaining governmental restraints in Europe on international capital movements have already been removed.

Unfortunately, progress in this area is not quickly achieved. The disparity between the capital export capacity of the U.S. market and that of capital markets abroad remains so wide as to require for the time being continuing restraint on capital outflows from the U.S.

The extent of this disparity is illustrated in Table 18 which indicates that between 1958 and 1965 the volume of securities floated abroad by the EEC countries exceeded the volume of foreign securities floated in the EEC markets. During the same period foreign securities totaling \$8.3 billion were floated in the United States and only \$400 million in U.S. securities were floated abroad. There are compelling reasons to believe, however, that the continued effective operation of the new Commerce and Federal Reserve programs and the IET will not only improve the U.S. balance of payments position in the short run but will help to induce some of the structural changes in capital markets abroad that will contribute to a sustained equilibrium in U.S. payments without control.

A successful capital flows policy also requires a substantial reduction in the differential between long-term interest rates in the United States and those in Europe. The gap between long-term government bond rates in the United States and those prevailing in the EEC countries in recent years has for the most part exceeded

TABLE 18

Gross International Security Issues
U.S. and EEC, Total 1958-1965

(millions of dollars)

<u>Country</u>	<u>Foreign Issues on Domestic Market</u> a/	<u>Domestic Issues Abroad</u> b/	<u>Balance (+ sign indicates net export of capital)</u>
Germany	418	250	+ 168
Belgium	132	393	- 261
France	68	253	- 185
Italy	120	264	- 144
Netherlands	<u>282</u>	<u>88</u>	<u>+ 194</u>
EEC Total c/	<u>1,020</u>	<u>1,248</u>	<u>- 228</u>
United States	<u>8,286</u>	<u>413</u>	<u>+7,873</u>

a/ Including international organizations.

b/ Including Euro-issues.

c/ Totals in first two columns include intra-EEC issues;
last column excludes these issues.

Source: Organization for Economic Cooperation and
Development, Report on Improvement of Capital
Markets.

1 percent and has at times exceeded 3 percent in the case of Germany. Differentials in industrial bond yields have often been even larger. The increase in U.S. long-term rates has within recent months narrowed the rate differentials somewhat. It is, however, inconceivable that the maintenance of such very high rates would be compatible with balanced economic growth at capacity rates in the United States itself. Moreover, it is undesirable for the U.S. to maintain for a long time high interest rates which would limit total investment in the developing countries and Europe. It has, therefore, been the U.S. desire to see the interest rate differentials narrowed through reductions in the long-term rates prevailing in European countries.

As the new United States program takes hold, it becomes even more critical that European countries pursue domestic monetary and fiscal policies that help to dampen upward pressure on interest rates.

As we move into the difficult but necessary area of mandatory controls on direct foreign investment by U.S. firms, it is clear, in short, that a maximum degree of understanding, cooperation and adjustment by private and public institutions, both foreign and domestic, will be required. We believe that circumstances will bring about that degree of understanding which was so evident under the voluntary program. By so reacting, all parties will hasten the return of free movement in the worldwide market place.

VII A Long-Range Program for Promoting Foreign
Private Investment in U. S. Securities

In his Special Message on the Balance of Payments in July 1963, President Kennedy urged that a positive action program be established to promote the overseas sale of U. S. corporate securities. The following October, he appointed an Industry-Government Task Force to develop a long-range program for promoting foreign portfolio investment in the United States.

The Task Force, chaired by the Secretary of the Treasury in his then capacity of Under Secretary of the Treasury, examined a large number of factors influencing the sale of U. S. securities to foreign investors. It sought to identify and appraise the legal, administrative, and institutional restrictions remaining in the capital markets of other industrial nations of the Free World which prevent the purchase of American securities by foreigners. This Task Force also reviewed governmental and private activities in the U. S. adversely affecting foreign purchases of our corporate securities. On the basis of these studies, it outlined a broad and intensive program designed to

- Improve the U. S. balance of payments by increasing foreign investment in U. S. private securities;
- Guide U. S. based international corporations toward making greater use of foreign-held funds where they do business; and
- Help establish conditions under which restraints upon the flow of capital between industrially advanced nations could be removed, diminished or allowed to expire.

The Foreign Investors Tax Act of 1966 emerged from the recommendations of the Task Force. It provided a firm base in the tax statutes to attract growing foreign savings for investment in the United States to help our long-range balance of payments position. The tax rates of foreigners deriving income from portfolio investment in U. S. corporate securities were reduced. The source rules for dividend payments were modified so that foreign investment corporations would find the purchase of U. S. securities more

attractive. In one of its key provisions, the Act brought U. S. estate tax laws on foreign investment more into line both with the tax situation of U. S. residents and with estate taxes applied in a large number of foreign countries. It thereby removed a major disincentive to the flow of long-term portfolio capital to the United States.

In addition to seeking ways to promote the sale of our securities abroad, the Task Force examined the possibilities of increasing foreign financing for U. S. corporations operating abroad. The recommendations it formulated to our international corporations on steps to maximize use of such financing were grounded in experience and tailored to our balance of payments objectives. Its recommendations were given substance in the voluntary balance of payments program announced in early 1965, which encouraged U. S. companies to increase their recourse to foreign funds for their operations abroad. In the form of new security issues alone, U. S. corporate borrowing abroad rose from virtually nothing in prior years to over \$300 million in 1965 and about \$500 million in 1966, with some further increase likely in 1967.

The task of encouraging foreign investment in the U. S. is perhaps less difficult than it would seem because of a number of factors which operate to attract this investment. The breadth of trading in our securities, the quantity and quality of information available on our corporations, the speed with which information is transmitted to stockholders, and the variety of investment instruments offered constitute one set of factors making the U. S. a place where every foreign investor should consider putting a portion of his long-term savings. The unique position of the dollar as an investment medium in the world today is another fundamental factor which should tend to pull portfolio capital from the rest of the world. Yet another is U. S. technological superiority in many areas, which has become increasingly important to the sophisticated investor.

There has been a balance of payments inflow resulting from net foreign purchases of U. S. corporate securities in 14 out of the last 18 years. The total derived from our balance of payments figures is shown in Table 19.

TABLE 19

Net Foreign Purchases of U. S. Corporate Securities^{a/}
1950 - Sept. 1967

(millions of dollars)

<u>Year</u>	<u>Net Purchases</u>	<u>Year</u>	<u>Net Purchases</u>
1950	- 7	1959	430
1951	126	1960	270
1952	37	1961	314
1953	70	1962	122
1954	135	1963	266
1955	172	1964	- 96
1956	313	1965	- 372
1957	228	1966	665
1958	- 6	1967 (Jan.-Sept.)	854

^{a/} Net purchases by foreigners of U. S. securities other than Treasury issues. Excludes purchases by international and regional organizations of U. S. agency bonds. Includes \$190 million in 1965, \$594 million in 1966, and \$329 million during Jan.-Sept. 1967 of new security issues sold abroad by U. S. corporations to finance direct investment abroad, and net sales of securities from official portfolio of U. K. Government. (See text discussion.)

Source: Derived from Department of Commerce and Treasury data.

Net outflows are shown in 1964 and in 1965. While the data show a substantial increase in this outflow in 1965, they reflect the sale of approximately \$500 million of securities held in the official portfolios of the U. K. as a result of wartime acquisitions. This was part of a British move to build up their foreign exchange reserves. In that same year net purchases of U. S. corporate securities by other foreigners were of much larger magnitude, offsetting to some degree the British Government sales. The net sell-off of U. S. securities was reversed during 1966 as foreigners acquired net over \$660 million of U. S. corporate securities. A substantial part of this flow were sales of bonds by Delaware-based subsidiaries of American corporations, for reinvestment of the proceeds abroad as a direct investment. Clearly, building on the experience of the past, an important contribution to the balance of payments can result.

Vigorous promotion efforts by the U. S. private community are required as a follow-up to the work of the Task Force. This will be bulwarked by the Foreign Investors Tax Act and other forms of Government cooperation. The New York Stock Exchange, as part of its educational program, has just produced a brochure summarizing the changes in U. S. tax laws as they effect non-resident investors, and outlining to investors everywhere the advantages of participating in the U. S. capital market.

Looking over the longer term, the securities of U. S. private firms should be one of our best selling exports. Increased foreign investment in these securities will create a more balanced two-way capital flow between the U. S. and other capital markets. This, in turn, will minimize the balance of payments impact of other long-term outflows from the United States. For these reasons we must undertake to utilize the provisions of the Foreign Investors Tax Act, and other features advantageous to foreign investment in the U. S. to increase the net inflow of this type of long-term investment capital. It is also clear that encouragement of foreign investment cannot stop at portfolio investment alone. We must encourage a hospitable climate to foreign direct investment--investment in brick and mortar and plants.

The Administration is continuing to work with individuals and corporations which participated in the Task Force and with other similar organizations, to encourage private activity aimed at drawing more

foreign investment to the United States. Of particular interest is the work of the recently formed Council of the U. S. Investment Community, which has as its goal the development of closer working relationships among portfolio managers and brokers here and in the major capital markets abroad. This group, which in October of this year sponsored a visit here by a group of European financiers for an on-the-spot view of U. S. investment possibilities, should continue to play a leading role in developing foreign interest in U. S. securities. Finally, we must continue our efforts in the OECD and directly with other governments to remove remaining impediments to an increased flow of investment to the United States.

In these and other ways we can respond to President Johnson's call, as part of the long-term measures in his new program, for "an intensified program to attract foreign investment in U. S. corporate securities, carrying out the principles of the Foreign Investors Tax Act of 1966".

VIII. A Long Range Program for Narrowing the Travel Gap Through Promotion of Foreign Travel in the United States and Temporary Measures to Restrain U. S. Travel Abroad

A. Introductory Comments

Americans spend more in travel to foreign countries than foreigners spend in travel to the United States. The outflow of dollars that results contributes substantially to our balance of payments deficits. We have sought to overcome this outflow by encouraging foreign travel here. This has been the primary focus of our balance of payments actions in the travel area throughout the 1960's. The stimulation and encouragement of foreign travel here rather than limiting American travel abroad has been--and is--an essential ingredient of our long-term balance of payments program.

Temporary action to reduce our overseas spending has now become imperative until the longer-term measures to increase our balance of payments receipts produce much better results. Because of the urgent necessity of correcting our balance of payments now, we must call on those Americans who would travel abroad to make some temporary sacrifices. We call on them and on the travel industry--just as we call on all others--to join in the program to eliminate the deficit in our international payments and keep the dollar strong.

Between 1960 and 1966, travel receipts from foreigners increased a total of 72 percent. Travel payments to foreigners by U.S. residents increased 51 percent. Nevertheless, the travel deficit increased from approximately \$1.2 billion to \$1.6 billion.

In 1967, the travel deficit is believed to have widened to approximately \$2 billion--in considerable part because of the impact of Expo 1967.

To reduce this deficit by \$500 million, the President as part of his 1968 balance of payments program called on "the American people to defer for the next two years all nonessential travel outside the Western Hemisphere". He also called on the Secretary

of the Treasury to explore with the appropriate Congressional committees legislation to help achieve this objective.

As part of the "Long-Term Measures" in his new balance of payments program, President Johnson called on the Industry-Government Special Travel Task Force set up on November 16, 1967 to speed up its work on a program to attract more visitors to this country. He directed this Task Force to report within 45 days on the immediate measures that can be taken, and to make its long-term recommendations within 90 days.

B. Position of the United States Travel Account

In recent years the trend in the U.S. travel account has become more unfavorable. (See Table 20.) With the continually rising level of income of the average American and the growing ease of foreign travel, Americans have tended to seek more travel opportunities abroad. The consequence has been a rapid growth in tourist outlays outside the United States, a growth which has outpaced increased receipts from foreign visitors in this country.

- In 1955 payments to foreign countries were \$1.4 billion.
- In 1960, shortly after the United States began to run an overall balance of payments deficit of serious proportions, travel payments in foreign countries reached the \$2.3 billion level.
- In 1966 the figure rose to \$3.4 billion, and for 1967 expenditures are estimated at about \$4.0 billion.

If U.S. travel receipts over past years had grown correspondingly to travel payments, these figures for total tourist expenditures in foreign countries would not pose a major problem. But while U.S. receipts from foreign visitors have made encouraging advances, the differential between receipts and expenditures has nevertheless risen sharply.

A major part of our travel deficit is normally with Europe (See Table 21). About one-third of what Americans spent for travel in 1966 went to Europe and the Mediterranean (Canada and Mexico constituting the bulk of the remainder). Americans spent \$.9 billion while traveling in Europe and the Mediterranean compared

TABLE 20

U. S. Travel Account a/
(billions of dollars)

<u>Year</u>	<u>Payments</u>	<u>Receipts</u>	<u>Net Deficit (-)</u>
1950	-0.90	0.47	-0.43
1951	-0.89	0.52	-0.37
1952	-1.01	0.61	-0.40
1953	-1.11	0.63	-0.48
1954	-1.19	0.66	-0.54
1955	-1.35	0.72	-0.64
1956	-1.51	0.77	-0.75
1957	-1.63	0.87	-0.76
1958	-1.78	0.91	-0.87
1959	-1.99	0.99	-1.00
1960 <u>b/</u>	-2.26	1.03	-1.24
1961	-2.29	1.06	-1.24
1962	-2.51	1.07	-1.44
1963	-2.73	1.13	-1.60
1964	-2.86	1.36	-1.50
1965	-3.16	1.55	-1.61
1966	-3.41	1.77	-1.64

a/ Including transocean fares.

b/ Begins new series; data for previous years are substantially comparable.

Note: Detail may not add due to rounding.

Source: U.S. Department of Commerce.

TABLE 21

Travel Deficits by Major Areas

(billions of dollars)

	<u>1960</u>	<u>1966</u>	<u>Percent Increase (+)</u>
<u>Canada and Mexico</u>			
Payments to	-0.77	-1.25	63
Receipts from	0.70	1.02	47
Deficit (-)	<u>-0.08</u>	<u>-0.23</u>	<u>204</u>
<u>European and Mediterranean</u>			
Payments to	-0.69	-0.92	33
Receipts from	.09	0.22	139
Deficit (-)	<u>-0.60</u>	<u>-0.71</u>	<u>17</u>
<u>All other Areas</u>			
Payments to	-0.30	-0.48	64
Receipts from	0.13	0.34	151
Deficit (-)	<u>-0.16</u>	<u>-0.15</u>	<u>-8</u>
<u>Transportation</u>			
Payments to foreign carriers by Americans	-0.51	-0.76	50
Receipts by U.S. carriers from foreigners	0.11	0.20	84
Deficit (-)	<u>-0.40</u>	<u>-0.56</u>	<u>40</u>
<u>Total</u>			
Payments	-2.26	-3.41	51
Receipts	1.03	1.77	72
Deficit (-)	<u>-1.24</u>	<u>-1.64</u>	<u>33</u>

Note: Detail may not add to totals due to rounding.

Source: Derived from data of U.S. Department of Commerce.

to only \$.2 billion spent by people from that area while traveling in the U.S. This \$.7 billion deficit plus a substantial part of \$.6 billion deficit on the costs of travel transportation points to a major area for correction in our balance of payments program--both short- and long-term range.

The travel deficit is significantly different with our neighbors in the Western Hemisphere. While there have been very substantial increases in U.S. travel to Canada and Mexico in recent years, our receipts from visitors from these two countries also increased substantially. U.S. travelers spent \$1.3 billion in Canada and Mexico in 1966, but because of their spending here our tourist deficit with them was \$.2 billion. Canadians traveling to the United States account for a larger part of these receipts, although when all the results are in for 1967, it is likely that Expo '67 will have changed the balance.

C. Measures Taken to Improve the Travel Balance

1. International Travel Act of 1961

The first step taken to enhance the U.S. tourist market was the passage of the International Travel Act of 1961, which had as its purpose "to strengthen the domestic and foreign commerce of the United States by providing for the establishment of the United States Travel Service within the Department of Commerce."

The U.S. Travel Service was designed to coordinate the programs of Government toward the purposes of the International Travel Act and to establish communication with individuals, businesses, and organizations related to international travel including state and local units. A major contribution of the United States Travel Service has been its overseas promotional activities carried on through foreign branch offices. The Travel Service has acted as a catalyst in advertising and sales promotion cooperation between Government and industry, to this end, it has employed various media at home and abroad for the promotion of foreign travel to the U. S. and to facilitate foreign travel throughout this country.

2. Cabinet Committee on Travel Planning and Promotion

Pursuant to his balance of payments message of February 1965, President Johnson asked Vice President Humphrey to form a Cabinet Committee for the purpose of bringing to bear continuing efforts of high-level Government officials toward increasing intra-Government and Government-industry coordination of activities affecting travel receipts. Achievements of the Cabinet Committee have included:

- simplification of customs entry,
- upgraded and expanded National Park facilities,
- pilot projects for improving tourist services in the Nation's Capital,
- creation of foreign language facilities at ports of entry, and
- creation of a favorable climate within Government for successful implementation of national travel programs.

3. Discover America, Inc.

Concurrent with the establishment of the Cabinet Committee, Discover America, Inc., was formed as a private nonprofit organization to bring the various elements of the U.S. travel industry together in an all-out effort to increase the size of the tourist market. The membership of Discover America comprises a broad cross-section of the private U.S. tourist industry and is wholly financed and directed by private enterprise. The organization has concentrated essentially on public information and promotion, liaison with various industry groups, and government relations.

4. Other Related Efforts to Reduce the Travel Deficit

In an effort to reduce U.S. tourist expenditures without affecting travel abroad, the Administration in its 1961 balance of payments program requested legislative action to reduce the comparatively very generous duty free exemption for purchases of foreign goods by returning tourists. The exemption was lowered from \$500 to \$100. There has been a balance of payments savings, but it has been more than offset by the increase in

the numbers of tourists going overseas. In October 1965, the exemption was reduced from \$100 of goods calculated at wholesale value to \$100 retail, the price actually paid rather than the lower wholesale value of the goods. The new law also reduced the exemption for liquor from a gallon to a quart for each returning tourist.

The Government also embarked on a stepped-up program to sell certain foreign currencies that it owns to American tourists and businessmen. This program has been intensified as a result of the Food for Freedom Act of 1966. While important, the program has only very limited applicability in coping with the travel deficit. The sale of those currencies which the Government owns in excess of its operating needs are helpful to our balance of payments. However, there are less than a dozen countries in which we have such "excess currency" holdings and while the amounts in these countries are very substantial, they are poorer countries and ones that account for a very small portion of our tourist spending. If the Government were to sell Western European currencies, for example, it would have to, in turn, buy these currencies for dollars and add to our balance of payments deficit. Nevertheless where "excess currencies" exist the sales program will be pursued vigorously.

Individual private industry, recognizing its stake in an expanded tourist market in the U.S., has also undertaken effective programs. For example, in November 1966 the American Express Company sponsored a tour of the U.S. for 500 European tourist agents in an effort to make them more familiar with American travel opportunities. United Airlines, in cooperation with Discover America, Inc., launched a large-scale program to encourage Americans to discover new vacations in their own country.

D. Need for a New Long-Term Action Program and the Establishment of the Special Task Force to Formulate it

The growing drain on our balance of payments resulting from growing foreign travel cannot be ignored. The Administration regards a long-term program in travel as a balance of payments imperative. In response to this need, President Johnson on November 16, 1967, appointed an Industry-Government Special Travel Task Force to:

- make specific recommendations as to how the Federal Government can best increase foreign travel to the United States and thereby improve our balance of payments; and
- build into its program ways and means that will insure that more foreign visitors truly learn to know our country and people.

In announcing his intentions, the President called attention to his previous statement that "the most satisfactory way to arrest the increasing gap between American travel abroad and foreign travel here is not to limit the former but to stimulate and encourage the latter."

The Task Force is headed by Robert M. McKinney, former U.S. Ambassador to Switzerland, and includes the following distinguished leaders in the field of travel, transportation, public relations, entertainment, publishing, hotelkeeping, education, and public service.

William Bernbach	President, Doyle, Dane, Bernbach
Daniel J. Boorstin	Professor of History University of Chicago
John A. Burns	Governor of Hawaii
Edward E. Carlson	President, Western International Hotels, Inc.
Howard L. Clark	President and Chief Executive Officer, American Express Company
Arthur Frommer	President, Arthur Frommer, Inc.
Frank Hildebrand	Director Texas Tourist Development Agency
Frank N. Ikard	President American Petroleum Institute
John H. Johnson	Editor and Publisher Johnson Publishing Co.
Willis G. Lipscomb (retired)	Vice President, Traffic and Sales Pan-American World Airways

Winston V. Morrow, Jr.	President, Director and Chief Executive Officer Avis Rent-A-Car System, Inc.
William D. Patterson	Vice President and Secretary Saturday Review, Inc.
Gerald Shapiro	Vice President and General Manager Hertz Rent-A-Car Division
Lew R. Wasserman	President, Music Corporation of America
Anthony M. Solomon	Assistant Secretary for Economic Affairs Department of State
Winthrop Knowlton	Assistant Secretary for International Affairs Department of Treasury
Harry M. Shooshan	Deputy Under Secretary for Programs Department of the Interior
Donald G. Agger	Assistant Secretary for International Affairs Department of Transportation
Charles S. Murphy	Chairman, Civil Aeronautics Board
Andrew F. Brimmer	Member of Board of Governors Federal Reserve System
John W. Black	Director, United States Travel Service Department of Commerce

In arriving at its recommendations, the Task Force will examine a variety of areas which have an impact on foreign travel. Its emphasis will be to make tourism in the United States more readily available and attractive for foreigners. It will look into actions which should be undertaken by the Government, by the private sector, and under joint effort by both. It will recommend areas where new legislation should be sought and where increased U.S. Government expenditure would be justified.

Areas of examination will include: the shortage of good medium-priced hotels in key cities; the use of vacant university facilities during vacation periods; the possibility of select tours for special interest groups; the possibility of directional aircraft fares; the difficulties foreigners face in renting, buying, and insuring automobiles in the U.S.; the adoption of international road signs on our highways; the use of qualified students as Federally certified guides and interpreters; the publication of an attractive, comprehensive guidebook for the U.S. translated into a variety of foreign languages; improvement of market research to maximize the tourist advertising dollar; possible new incentives for tour operators; legislation to assist foreigners' purchasing and driving a car during U.S. vacations; a new International Travel Act with a strong balance of payments orientation; study of measures adopted by those countries and cities which have been successful in attracting foreign tourists; a coordinated state and local government campaign to improve and promote tourist facilities; the encouragement of foreign government amendment of regulations inhibiting tourism by their residents; a summer job program for foreign college-age youths to work in U.S. hotels, restaurants, and airlines; space-available airplane travel for all foreign tourists in the U.S. and for foreign students on transoceanic flights; use of U.S. Government land to stimulate tourism; a dynamic visit-an-American-family program; cost reduction of transoceanic travel; competitive programs within the U.S. tour industry leading to Presidential citations and awards; possibility of prior purchase of meal tickets for use in the U.S.; availability of single price unlimited bus, rail, and air tickets usable during a specified time period; visa waiver regulation; and an intensified business visit program.

Based on the Task Force's recommendations, the Government will be better equipped to: coordinate private and public measures; initiate educational programs both abroad and in the U.S.; suggest new legislation to the Congress; and judge priorities for new expenditures.

U.S. Government assistance to our tourist industry has been minuscule by international comparisons. Last year, the U.S. Travel Service operated with a \$3 million budget--a budget that compares with \$10 million for Canada, \$10 million for Spain, \$7 million

for Mexico, \$5 million for France, and \$5 million for Greece. Much could be accomplished with a properly guided major budgetary effort on the part of the U.S. Government--more funds not only for the U.S. Travel Service, but also for improved customs and reception centers, translation services, and better park facilities.

The causes of our "travel gap" are many, the main ones being: higher per capita income in the United States; foreign government restriction on travel; the language barrier in the United States--oral and written; the cost of transoceanic transportation; the cost of tourism in the United States; and a U.S. travel industry not organized to receive and service middle-income, non-English-speaking visitors.

On the other hand, we do have many assets and these must be exploited: rising disposable income in many countries; unique attractions in the United States; and great worldwide curiosity about the United States. New ideas have been put forward--they should be tested. Other ideas should be developed. The successes of others should be investigated. The work has started--but it has not had a balance of payments orientation. More must be done and a new emphasis adopted. The Task Force will furnish guidance. Under the new balance of payments program its work has been accelerated.

E. Temporary Measures to Reduce the Travel Deficit

We are confident that the Special Travel Task Force will help produce an effective, constructive long-range program for increasing foreign travel to the United States with Federal, State, and private action. We recognize that even with its mission accelerated, it will take time to implement and translate into concrete results its recommendations for new actions that can be undertaken by the Government, by the private sector and under joint effort by both.

Meanwhile, for the reasons that have been outlined throughout this report, it is essential to reduce spending for travel abroad by Americans. The President's request that the American people defer for two years all nonessential travel outside the Western Hemisphere is clearly a call for temporary restraint. It is a request that is made only in the urgent national interest. It is a call on our citizens to participate in protecting the international financial strength of this country

rather than contribute to an erosion of that strength which would have unfortunate consequences for all. It is not a sacrifice of travel but only of nonessential travel abroad. It is our hope, expectation, our firm policy to eliminate this restraint on travel as quickly as possible--as soon as our long-term measures to increase our receipts from travel and from our trade surplus permit.

This temporary restraint on travel abroad will give added incentive to promote more energetically and more quickly and effectively foreign travel to these shores. The speed and effectiveness of carrying out this longer-term effort would make even more certain the early abandonment of the temporary measures of restraint. This process of adjustment of our travel account should have the support, cooperation and certainly the understanding of European countries whose surpluses have been in the counterpart of our balance of payments deficits.

The Secretary of the Treasury is in the meantime exploring with the appropriate Congressional Committee legislation to help achieve the objective of reducing the travel deficit by \$500 million in 1968. The exact character of any legislative measures will emerge from their consultations. The most effective actions, nevertheless, are those that will be taken by American citizens themselves.

IX. Adjustment Responses Expected of Trading Partners

A. Distribution of the Adjustment Among Countries

The importance of multilateral cooperation in making the adjustment process work smoothly was stressed in the first two chapters of this paper. There it was pointed out that as a matter of arithmetic a reduction of the U. S. deficit necessarily means that other countries will have to reduce their surpluses, move into deficit, or (for countries that are in deficit already) move deeper into deficit. The adjustment process should ideally proceed with minimal adverse effects on individual countries and on the world economic community in general. Adjustment will not occur in this relatively smooth manner, however, if the reduction in the U.S. deficit hits countries whose balance of payments positions are already weak. The improvement in the U.S. balance of payments therefore must, as stressed in Chapter II, have as its main counterpart a reduction in the surpluses in the balance of payments of the continental European countries. Within continental Europe, much the greatest part of the adjustment must come in the external position of the European Economic Community.

The adjustment of the present imbalance in world payments is not the sole responsibility of the United States and the EEC countries. But it is true that, with a few exceptions (which also are mainly in continental Europe), countries other than those in the European Economic Community do not have sufficient reserves or the balance of payments surpluses to bear the brunt of a reduction of the U.S. deficit.

The United States is not the only developed country whose balance of payments needs strengthening. The United Kingdom is also determined to achieve a substantial improvement in its external position. This improvement in the U.K. balance of payments should come about readily and smoothly following the recent devaluation of sterling, provided again that the major surplus countries are willing to tolerate--indeed, to encourage--offsetting changes in their balance of payments. The United States wants the new U.S. Action Program to create the fewest possible difficulties for the United Kingdom as that country restores balance in its own payments. And the United States is determined to avoid having the developing countries of the world bear the burden of the necessary U.S. retrenchment of its payments. It is doubly important, therefore, to have the greatest part of the adjustment take place in the continental European countries.

B. The Persistent EEC Surplus

There are interesting patterns that emerge when one compares the broad structures of the U.S. and the EEC payments positions (see Table 22). The EEC and the United States both have sizable outflows of official grants and capital, and both have large surpluses on private current account transactions. Whereas in the U.S. case military expenditures abroad far exceed the receipts from military transactions, however, the reverse is true for the Common Market. Primarily because of the large number of U.S. troops stationed in Europe and the foreign-exchange costs associated with keeping them there, the EEC has large receipts on military account. (EEC net military transactions with the United States are separated from the rest of the current account items in the balance of payments and shown separately on line 3 of Table 22.)

TABLE 22

STRUCTURE OF PAYMENTS POSITIONS OF THE U.S. AND THE EEC
1958-61 and 1962-66
(millions of dollars)

	<u>1958-1961 Annual Average</u>		<u>1962-1966 Annual Average</u>	
	<u>U.S.</u>	<u>EEC</u>	<u>U.S.</u>	<u>EEC</u>
1. Net military transactions	-2,775	895	-1,840	340
2. Official unilateral transfers	-1,690	-760	-1,890	-1,020
3. Non-military goods and services and other unilateral transfers	5,030	2,510	7,480	1,560
4. Official capital	-1,100	-690	-1,745	-420
5. Prepayment of official debt	295	-350	355	-315
6. Direct investment	-1,320	50	-2,535 ^{2/}	500
7. Other private long-term capital	-785	780 ^{1/}	-735 ^{2/}	815 ^{1/}
8. Non-bank short-term capital and errors and omissions	<u>-395</u>	<u>-145</u>	<u>-690 ^{2/}</u>	<u>-290</u>
9. Balance on non-monetary transactions	-2,740	2,290	-1,595	1,170
10. U.S. short-term banking claims	630	--	480	--
11. Short-term banking flows	--	-40	--	-100
12. Change in official position	--	2,330	--	1,270
13. U.S. balance on liquidity basis	-3,370	--	-2,075	--
14. (U.S. balance on official settlements basis)	(n.a.)	--	(-685)	--

^{1/} Includes direct investment for Belgium, also for France for years 1958, 1959.

^{2/} The figure for "Other Private Long-Term Capital" includes an inflow of \$885 million borrowed in Europe by American corporations for investment abroad. Of this sum, \$569 million is included as an outflow under direct investment and \$310 million under short-term non-banking capital (and errors and omissions). If an adjustment were made for these offsetting transactions, the average outflow of direct investment would be \$2,421 million, the outflow of other long-term capital would be \$912 million, and the outflow of non-banking short-term funds and errors and omissions \$628 million.

Source: IMF, Balance of Payments Yearbook; U.S. Department of Commerce, Survey of Current Business.

The other major difference in the structure of the U.S. and EEC balance of payments is in the private capital accounts. The EEC has tended to have large net inflows of private nonmonetary capital, while the United States has experienced large outflows on private capital account. The strength, flexibility, and competitiveness of the U.S. capital market, the large volume of U.S. saving, and the importance of the United States as the dominant international financial and banking center all help to explain why U. S. private capital outflows were so large and growing so rapidly in the 1960's. Conversely, the underdevelopment of--and restrictions imposed in--European capital markets help to explain why the EEC countries taken together have been net importers, rather than net exporters, of private capital funds. As Table 22 brings out, direct investment inflows into the EEC countries have been large, but not so large as the net inflows of other private long-term capital.

The absolute size of the imbalance in EEC external payments and receipts is alone an indication of its importance as the main counterpart in the world to the large U.S. deficit. The high per capita incomes in the EEC and the very high level of reserves (see Table 23) are further indications that the major burden of accepting the adjustment resulting from the U.S. program should fall on these countries.

Further evidence to suggest that the EEC surpluses have been excessive and that the EEC balance of payments must show the weakening which will be the counterpart to the reduction in the U.S. and U.K. imbalances is provided by a comparison of data on countries' reserve increases and growth in trade. Table 24 presents figures which show the reserve gains of some of the more important countries that have been gaining reserves over the entire 1960-66 period and, for the same period, the growth in their imports (changes in the value of imports between 1959 and 1966). Since reserve

TABLE 23

Geographical Composition of World Reserves

End-September 1967

	<u>Millions of dollars</u>	<u>Per cent</u>
<u>European Economic Community</u>	<u>25,110</u>	<u>34.9</u>
Belgium-Luxembourg	2,551	3.5
France	6,750	9.4
Germany	7,889	11.0
Italy	5,445	7.6
Netherlands	2,475	3.4
<u>Other Major Countries in Continental Europe</u>	<u>6,891</u>	<u>9.6</u>
Austria	1,439	2.0
Portugal	1,188	1.6
Spain	1,108	1.5
Switzerland	3,156	4.4
<u>Scandinavian Countries 1/</u>	<u>2,391</u>	<u>3.3</u>
<u>Canada</u>	<u>2,682</u>	<u>3.7</u>
<u>Japan</u>	<u>2,047</u>	<u>2.8</u>
<u>United Kingdom</u>	<u>2,733</u>	<u>3.8</u>
<u>United States</u>	<u>14,649</u>	<u>20.3</u>
<u>Other Developed Areas - Not included above</u>	<u>3,412</u>	<u>4.7</u>
<u>Less Developed Areas</u>	<u>12,115</u>	<u>16.8</u>
<u>World Total</u>	<u>72,030</u>	<u>100.0</u>

Source: International Financial Statistics, January 1968. Reserves consist of gold, foreign exchange and reserve positions in the Fund.

1/ Denmark, Finland, Norway, and Sweden.

2/ The major countries in this grouping are Greece, Iceland, Ireland, Turkey, Yugoslavia, Australia, New Zealand, and South Africa.

3/ Figures for less developed areas (and therefore for world total) are partly estimated by International Monetary Fund.

TABLE 24

Reserve Gains and Growth in Trade, 1960-1966

	(1) Growth in Reserves <u>1/</u> (\$ million)	(2) Growth in Trade <u>2/</u> (\$ million)	Ratio of Reserve Gain to Trade Growth (<u>1+2</u>)
France	4,997	6,755	.740
Switzerland	1,261	2,021	.624
Portugal	314	547	.574
Austria	636	1,183	.538
(EEC countries as a group)	(12,110)	(29,338)	(.413)
Spain	996	2,779	.358
Italy	1,855	5,220	.355
Germany	3,238	9,554	.339
South Africa	320	1,026	.312
Belgium	1,014	3,732	.272
Sweden	549	2,168	.253
Netherlands	1,006	4,077	.247
Norway	246	1,081	.228
Australia	319	1,511	.211
Denmark	269	1,401	.192
Mexico	106	598	.177
Canada	664	3,906	.170
Japan	672	5,925	.113
United Kingdom	299	5,227	.057
United States	-6,623	10,739	-
46 Countries Experiencing Net Reserve Gains <u>3/</u>	22,666	66,618	.340
Total, All Countries in World <u>4/</u>	14,265	85,800	.166

Source: International Financial Statistics, January 1968.

- 1/ Change in Reserves (Gold, Foreign Exchange, and Reserve Position in the Fund) between December 31, 1959 and December 31, 1966.
- 2/ Change in Value of Imports (cif) between calendar years 1959 and 1966, as reported in International Financial Statistics, pp.35-37.
- 3/ Includes all countries (a) whose reserves are reported separately by IFS (p.16), (b) for which comparable trade data were available, and (c) whose reserves increased over the 1960-66 period. Of the 62 countries listed separately in the IFS reserve tables, 46 had reserve gains while 16 had reserve losses (total reserve losses for these 16 countries were \$8,320 million).
- 4/ Change in Reserves is the net change for the total of all countries' reserves. Growth in Trade is the change in total world imports (IFS tables).

gains over time are one important measure of a country's balance of payments surplus, the figures on reserve changes in Table 24 can be used as a rough yardstick for comparing the relative size of countries' cumulative net surpluses in the current decade. The data on growth of imports in column two of the table can serve as a crude proxy for the growth of a country's international transactions. The final column of Table 24 calculates the ratio of a country's cumulative net surplus to the growth in its "transactions" (imports). Countries are ranked in the table by these ratios; the further one moves down the list of countries, the lower the ratio of reserve gains to trade growth.

For example, France at the top of the list had an increase in its published reserves between December 31, 1959 and December 31, 1966 of \$5.0 billion. French imports increased in value between 1959 and 1966 by some \$6.8 billion. The ratio of French reserve gains to trade growth was very high, the former being nearly three-fourths the size of the latter. Even discounting for the fact that French reserves were abnormally low in 1958 and 1959, which is the starting point for the comparison, it is clear that compared with other countries France had quite disproportionate reserve gains. Moving towards the other end of the spectrum one finds countries such as Canada or Japan, whose reserve gains were only some 10-20 per cent of the growth in their trade. At the bottom of the list of individual countries, two other ratios are shown, the first is the ratio for all the major countries taken together who were in "surplus" (had a reserve gain) for the entire period. The second is the ratio for all countries in the world, regardless of whether or not they were in surplus.

An upward trend in reserves (balance of payments surplus) is the targeted long-run "norm" for virtually all countries (see Chapter I). So long as the total amount of reserves in the system is growing at a reasonable pace, moreover, the existence of a moderate net reserve gain over an extended period must be judged as one piece of evidence of a successful balance of payments policy. Excessive reserve gains, on the other hand, are clear indicators of an imbalance in payments that needs to be rectified. The definitions of "moderate" and "excessive" reserve gains, to be sure, are not clear. But the analysis in Chapters I and II does suggest one possible criterion which might be used, namely, that a country has had an excessive reserve gain if its cumula-

tive net surplus over some reasonably long and appropriately chosen period has been markedly greater relative to the growth in its international transactions than could possibly prevail in the system as a whole (the ratio that would prevail, in other words, if every country were moderately in surplus and sharing in the total reserve growth proportionately to the growth in its own transactions).

On the basis of this criterion, an examination of Table 24 brings out very clearly that all of the EEC countries and several of the other major European countries have had excessive surpluses in the 1960-66 period. Countries such as Canada and Japan, on the other hand, have experienced moderate reserve gains much more consonant with the rate at which reserves were growing in the system as a whole. The "norm" for proportionate reserve growth in the 1960-66 period might roughly be taken as the ratio shown on the last line of the table for all countries taken together; if no country had lost reserves over the period and if each country had shared proportionately in the growth of total reserves that actually took place, each country individually would have had a ratio of reserve gains to trade growth roughly equal to one-sixth (.166). The data in the table therefore strongly reinforce the conclusion that it is the surpluses of the Continental European countries that need to be reduced pari passu with the reduction of the U.S. and U.K. deficits.

C. Need for Compatible Adjustments

The EEC countries have up until now generally considered it inappropriate to reduce their current account surpluses materially and have suggested that adjustment should occur primarily, if not fully, through changes in their capital accounts. Increased capital flows from the EEC countries to the rest of the world will benefit all parties and help the adjustment process. An increase in the flow of capital to the less-developed countries is one of the basic objectives of the OECD. Structural adjustments of this nature would appear to be highly desirable, if they could be achieved by measures consistent with economic growth and the expansion of world trade. Nevertheless, it is uncertain that the EEC countries will in the near future be prepared to undertake structural adjustments that will result in really substantial net capital outflows, even if they permit a reduction in the present net capital inflow. In this event, they must be prepared to face up realistically to the need for allowing changes in the other components of their international accounts.

D. Shifts in European Capital Flows and Development of European Capital Markets

Reductions of Flows of U.S. Capital to Europe.
The flow of U.S. private capital (excluding short-term banking funds) from the United States to Europe averaged roughly \$1.1 billion annually from 1962 through 1966. The flow to the EEC countries alone averaged less than \$700 million. From 1962 through 1964, there was a flow of portfolio capital to Europe, but, in 1965 and 1966, under the influence of the interest equalization tax, the voluntary restraint program, and tight monetary conditions in the United States, the net flow was toward the United States. Direct investment flows to the EEC countries roughly averaged \$700 million annually from 1964 through 1966, 1/ excluding reinvested earnings of about \$100 million annually

Elimination of the movement of U.S. capital to continental Western Europe will make a contribution to needed balance of payments improvement but will not solve the whole adjustment problem by itself.

Over the longer pull, these capital flow restraints must be liberalized in the interest of continued growth in world investment, improvement in technology, efficient means of mobilizing financial capital, and efficient financing of world trade. In a world short of capital, and with pressing capital needs, it is not an appropriate long-run payments adjustment to place restrictions on capital flows.

1/ This figure includes proceeds of borrowing by special Delaware corporations to finance direct investment abroad.

Inducing European Capital Outflows. In recent years, yields on long-term Government bonds in the EEC countries have exceeded those in the United States by well over 1 percent. German rates have generally ranged from 2 percent to nearly 4 percent higher. Differentials in industrial bond yields have often been larger. Only within recent months, when U.S. long-term rates have moved to the highest level in more than 40 years and most of the EEC countries were experiencing a period of relatively low economic growth, has this differential narrowed. Even now, however, long-term rates in Europe remain significantly higher than those prevailing in the United States. How high U.S. rates would have to go in order to draw funds out of Europe in the required volume is impossible to determine.

It is quite clear, however, that such action could not be taken without damaging impact on other areas of the world. The Adjustment Process Report of Working Party 3 (see Chapter I) takes specific note of this problem. It recognizes that the policies of advanced countries powerfully affect other countries and urges that in formulating adjustment policies, consideration be given to the interests of the international community as a whole. How could the United States establish monetary conditions which would induce large-scale flows of funds from Europe to the United States without also affecting the availability of capital to developing countries and other nations such as the United Kingdom, Canada and Japan for whom international flows have been important?

Long-term interest rates in the United States could not be driven to the extraordinarily high levels which would be required and maintained there without causing short-term rates to rise as well. Short-term banking funds could easily move

in such volume as to imperil the reserves of vulnerable countries and perhaps even endanger the liquidity of foreign financial institutions and lead to an escalation of interest rates everywhere. Moreover, the maintenance of such rates would not be compatible with balanced economic growth in the United States itself or in Europe. A slowdown in economic growth in the United States and Europe has an impact, in turn, on growth rates elsewhere. For these reasons, it is desirable that the needed narrowing in interest rate differentials be brought about more through reductions in prevailing rates within Europe than by increased rates in the United States.

The extent to which the structural readjustment in payments positions can be brought about by the development of a large-scale net outflow of long-term capital from the EEC countries will, therefore, depend largely on what the EEC countries themselves can and will be prepared to do. Some of them are making vigorous efforts to strengthen and improve their capital markets. Others are seeking to strengthen the role of fiscal policy in managing the level of internal demand. Hopefully more progress will be made along these lines.

Nevertheless, the prospects for rapid reduction in interest rates or the early elimination of remaining barriers to foreign borrowing in the EEC countries do not seem particularly bright. Budgetary problems appear to be blocking substantial increases in the volume of governmental assistance to developing nations. Consequently, it seems unlikely that the EEC countries will soon achieve the level of net long-term capital outflow which would be necessary to offset a current account surplus of the magnitude now in prospect.

E. Offsetting the Balance of Payments Impacts of Military Expenditures

A major contribution to short-term payments equilibrium would be achieved if strong countries in both Europe and Asia with which the United States is allied in a common defense undertaking were prepared to enter into special arrangements to compensate for the balance of payments impact of U. S. military expenditures in these countries. If military strategy requires that the forces of one country be stationed on the territory of another to provide for the common defense, the country furnishing the military forces ought not to be expected, in addition to assuming the budgetary burden, to meet the foreign exchange costs. Nor are countries in which forces are stationed entitled to economic advantage from this fact alone.

There are various methods by which the balance of payments impact of such military expenditures can be counterbalanced. The most important and desirable long-run method is for other items in recipient countries' balance of payments accounts, such as trade or private capital flows, to adjust. And to some extent, the country receiving the balance of payments advantage can make military purchases in the country suffering the disadvantage. Another possibility is for the beneficiary nation to make long-term official investment in the other country. Approaches such as these can be either bilateral or multilateral. Conceptually, there are substantial advantages in the multilateral approach in a multilateral world. Since these various techniques are within the power of governments, offsetting the balance of payments impacts of military expenditures would appear to be a question of political willingness.

F. Adjustment through Changes in the Private Current Account

There remains the question of adjustment through other private current account transactions. One obvious means by which adjustment in the current account could be fostered would be for the United States to continue to improve its competitive position by maintaining a better cost and price stability than surplus countries. The surplus countries cannot and should not be expected deliberately to overexpand the level of demand in their economies to the point where unacceptable inflation occurs. It is a sine qua non for the United States to preserve a growing economy with stability in costs and prices so as to preserve and strengthen its competitive position in international trade. The scope for adjustment to occur by changes in relative competitive positions is therefore rather narrow, although it is certainly not absent altogether. At a minimum, surplus countries have a very clear responsibility to achieve their growth and stabilization objective without depending upon further increases in their current account surpluses.

The current account--and particularly the trade account--is subject to other influences. For example FEC and other countries have actively used export rebates and import taxes (border tax adjustments) and this has tended to increase trade surpluses even of countries in overall balance of payments surplus. Such adjustments are permitted by the GATT, but the time has come to reexamine the GATT rules and their relationship to balance of payments adjustment, as well as the practices under these rules.

In current circumstances, there is also room for adjustment through the reduction or elimination by other countries of tariffs and nontariff barriers and liberalization of government procurement policies. Such actions could contribute not only

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There are various methods by which the balance of payments impact of such military expenditures can be counterbalanced. The most important and desirable long-run method is for other items in recipient countries' balance of payments accounts, such as trade or private capital flows, to adjust. And to some extent, the country receiving the balance of payments advantage can make military purchases in the country suffering the disadvantage. Another possibility is for the beneficiary nation to make long-term official investment in the other country. Approaches such as these can be either bilateral or multilateral. Conceptually, there are substantial advantages in the multilateral approach in a multilateral world. Since these various techniques are within the power of governments, offsetting the balance of payments impacts of military expenditures would appear to be a question of political willingness.

F. Adjustment through Changes in the Private Current Account

There remains the question of adjustment through other private current account transactions. One obvious means by which adjustment in the current account could be fostered would be for the United States to continue to improve its competitive position by maintaining a better cost and price stability than surplus countries. The surplus countries cannot and should not be expected deliberately to overexpand the level of demand in their economies to the point where unacceptable inflation occurs. It is a sine qua non for the United States to preserve a growing economy with stability in costs and prices so as to preserve and strengthen its competitive position in international trade. The scope for adjustment to occur by changes in relative competitive positions is therefore rather narrow, although it is certainly not absent altogether. At a minimum, surplus countries have a very clear responsibility to achieve their growth and stabilization objective without depending upon further increases in their current account surpluses.

The current account--and particularly the trade account--is subject to other influences. For example EEC and other countries have actively used export rebates and import taxes (border tax adjustments) and this has tended to increase trade surpluses even of countries in overall balance of payments surplus. Such adjustments are permitted by the GATT, but the time has come to reexamine the GATT rules and their relationship to balance of payments adjustment, as well as the practices under these rules.

In current circumstances, there is also room for adjustment through the reduction or elimination by other countries of tariffs and nontariff barriers and liberalization of government procurement policies. Such actions could contribute not only

to better international payments balance but also to the preservation of price stability in the EEC countries themselves. Indeed, the Adjustment Process Report recommends that, "Wherever possible, it is desirable that adjustment should take place through the relaxation of controls and restraints, over international trade and capital movements by surplus countries, rather than by the imposition of new restraints by deficit countries".

Improving the U.S. Trade Balance

President Kennedy's 1961 Message

Legislative

Congress requested to add 41 foreign service commercial attaches and to increase its trade mission program from 11 to 18 per year.

Administrative

Commerce Department to step up its support of U.S. exporters.

President of the Export-Import Bank directed to submit a new program for export financing to make the competitive advantage of U.S. traders equal to that of foreign exporters.

Secretary of the Treasury directed to undertake a study of how private financial institutions could participate more broadly in providing export credit facilities.

President Kennedy's 1963 Message

Legislative

Request that the Export-Import Bank's charter be renewed, including its new program of guaranteeing short- and medium-term export credits through the Foreign Credit Insurance Association.

Request that the \$6 million additional appropriation of funds for the Commerce Department's export expansion program be approved by the House of Representatives.

Administrative

Secretary of Commerce directed to take corrective measures through the Maritime Administration to realign ocean freight rates unfavorable to U.S. exports.

Announcement that a White House Conference on Export Expansion would be convened to provide a boost to the export program.

President Johnson's 1965 Message

Legislative

Request that Congress approve a \$13 million budget request for export expansion.

Administrative

Announcement that efforts to assure American industry sound and fully competitive export financing would be stepped up.

Increased efforts "to eliminate such artificial barriers to U. S. exports as discriminatory freight rates on ocean traffic."

President Kennedy's 1961 Message

Administrative (Continued)

Secretary of Agriculture directed to survey means for expanding exports of farm products.

Increased effort in GATT tariff negotiations to reduce tariff and other barriers to U.S. exports.

Underlining the importance to U.S. exports of maintaining competitive costs, improving productivity, and stabilizing, or where possible, lowering prices.

President Kennedy's 1963 Message

Administrative (Continued)

Announcement that the Department of Agriculture's new auction program for direct sales of cotton abroad would increase exports by as much as \$100 million over the previous year's level.

President Johnson's 1965 Message

Administrative (Continued)

Request to business and labor to adhere to the Government's wageprice guideposts in order to maintain the U.S. competitive position.

Improving the U.S. Balance on Tourist Expenditures

Legislative

Request for the U.S. to begin a major program to bring more foreign tourists to this country. (Legislation creating the U.S. Travel Service was enacted June 29, 1961.)

Recommendation that the duty-free allowance for American travelers returning from abroad be reduced from \$500 to \$100. (Enacted August 10, 1961.)

Legislative

Requested the Congress to approve the full amount of the appropriation requested for the U.S. Travel Service.

Legislative

Request that the duty-free exemption for American tourists returning to the U.S. be further reduced to \$50, based on the price actually paid for goods and limited to goods actually accompanying the traveler.

President Kennedy's 1961 Message

President Kennedy's 1963 Message

President Johnson's 1965 Message

Administrative

Administrative

Announcement of a "See America Now" program to encourage Americans to see and learn more about their own country.

Request that the tourist industry "strengthen and broaden the appeal of American vacations to foreign and domestic travelers."

Improving the Net Impact of U.S. Investments Abroad

Legislative

Legislative

Legislative

Congress requested to "enact legislation to prevent the abuse of foreign 'tax havens' by American capital abroad as a means of tax avoidance." (Revenue Act of 1962 enacted October 16, 1962.)

Request that the Congress approve the Interest Equalization Tax (IET) to raise the cost to foreigners of borrowing in the U.S. by the equivalent of approximately 1% per annum. (Enacted September 2, 1964 retroactive to the date of the Presidential message.)

Request that the Congress extend the Interest Equalization Tax for two years and amended it to include nonbank credit of one-year or more maturity.

Request that the Congress "grant statutory exemption from the anti-trust laws to make possible the cooperation of American banks in support of our balance-of-payments objectives." (See below.)

President Kennedy's 1961 Message

Administrative

The Secretary of the Treasury requested to evaluate whether U.S. "tax laws may be stimulating in undue amounts the flow of American capital to the industrial countries abroad through special preferential treatment."

President Kennedy's 1963 Message

Administrative

Recognized Federal Reserve efforts to stem the outflow of short-term capital by raising interest rates while maintaining adequate domestic credit.

President Johnson's 1965 Message

Administrative

Announcement that the IET would be extended to bank loans with maturities of 1-3 years.

Establishment of a Voluntary Cooperation Program for "American businessmen and bankers to enter a constructive partnership with their Government to protect and strengthen the position of the dollar in the world." Under this program the Secretary of Commerce later requested 600 U.S. companies to review their foreign transactions, particularly with their affiliates, and to improve their foreign exchange positions by 15 to 20%. Under the voluntary program for financial institutions, administered by the Board of Governors of the Federal Reserve System, banks were later asked to keep their foreign asset positions at the end of 1965 at a level not exceeding 105% of their end-1964 positions.

Increasing Foreign Investment Activity in the United States

President Kennedy's 1961 Message

Administrative

Announcement that Western European countries with strong reserve positions would be requested to eliminate restrictions on investment by their citizens in the U.S. Initiation through the Department of Commerce of "a new program to bring investment opportunities in the U.S. to the attention of foreign investors."

President Kennedy's 1963 Message

Administrative

Request that the Treasury Department in consultation with the State Department:

- (1) identify and make a critical appraisal of foreign restraints to foreign investment in the United States;
- (2) review Government and private activities which adversely affect foreign purchases of U. S. private securities; and
- (3) coordinate and encourage a broad and intensive effort by the U. S. financial community to sell U. S. private securities abroad.

President Johnson's 1965 Message

Administrative

Request to Congress that various administrative and tax barriers to foreign investment in the U. S. be eliminated. (The Foreign Investors Tax Act was enacted November 13, 1966.)

Government Operations

Administrative

The Director of the Bureau of the Budget, in consultation with the Secretary of the Treasury, was requested to institute special procedures for analyzing foreign expenditures by the various government agencies (the "Gold Budget" procedure).

Administrative

Announced substantial savings achieved under the Gold Budget program and prospective future substantial achievements, including benefits which would stem from Congressional legislation permitting freer use of holdings of the currencies of a number of aid-receiving countries.

Administrative

Announced that 85% of new AID commitments were now spent within the U. S.

Requested the Secretary of Defense:

- (1) "to shift defense buying from sources abroad to sources in the U.S.;

President Kennedy's 1961 Message

Administrative (Continued)

A closer review of foreign exchange expenditures for economic assistance programs was announced.

New measures were taken to reduce the foreign exchange outflows associated with U.S. military expenditures abroad. The Secretary of Defense was asked to "review the possibilities for savings and logistic support of our forces, including the combined use of facilities with our allies." And instructed to "urge the purchase of the newer weapons and weapons systems of those of our allies capable of doing so."

President Kennedy's 1963 Message

Administrative (Continued)

Announced that during FY 1964 AID commitments tied to U.S. exports would rise beyond 80% of the total. Also, that AID expenditures abroad would be further reduced to about \$500 million less than during FY 1961.

Announced that foreign defense outlays had declined substantially and that efforts to sell more defense items to major allied countries had met with considerable success.

President Johnson's 1965 Message

Administrative (Continued)

(2) to reduce the staffs in overseas headquarters;
(3) to streamline overseas support operations; and
(4) to work with our defense partners to increase their offset purchases of military equipment in the U. S."

Management of Gold and International Reserves

Legislative

Requested that the Federal Reserve Act be amended to permit payment to foreign governments and monetary authorities of higher than usual rates of interest. Instructed the Secretary of the Treasury to use the authority already extended to him by the second Liberty Bond Act to make available special security issues at preferential interest rates.

Administrative

Announced that special government transactions had covered \$1.4 billion of the 1962 deficit. These included prepayment of debt by foreign countries, advance payments on military purchases here, and the issuance by the Treasury of medium-term securities to foreign official holders of dollars. Efforts to secure such special receipts were expected to have a continued favorable effect on the balance of payments. Announced that the International Monetary Fund had approved the United States' request for a \$500 million standby arrangement.

Administrative

Reiterated that "the dollar is, and will remain, as good as gold, freely convertible at \$35 an ounce."

SUMMARY OF ACTIONS BY THE DEPARTMENT OF DEFENSE
TO REDUCE NET FOREIGN EXCHANGE COSTS,
1961 - 1967

Introduction

The Department of Defense has long recognized that, due to the size of U. S. defense expenditures entering the international balance of payments (IBP), it has a major responsibility to reduce the foreign exchange costs associated with defense activities to the minimum consistent with the requirements of national security. In recent years, this continuing concern has been expressed in a wide range of Department of Defense programs serving to hold down and, where feasible, to reduce defense IBP costs and to increase receipts. These programs have been re-emphasized and expanded during the past two years as the intensification of hostilities in Southeast Asia (SEA) sharply raised foreign exchange costs. As part of this renewed effort, the Secretary of Defense in April 1967 re-emphasized the need to continue concentrated attention on the Department of Defense balance of payments program, and outlined more than 20 separate actions or studies relating to various facets of the program.

The primary function of the Department of Defense is to provide for the security of the United States. Therefore, balance-of-payments considerations cannot be overriding, or indeed, examined independent of requirements stemming from our national security objectives, including fulfillment of our commitments to help provide for the security of other nations. The Department of Defense balance-of-payments program has been developed and is being carried out under two general guidelines: first, essential combat capability must be maintained and second, expenditure reductions must be achieved without creating undue hardship for U. S. military and civilian personnel and their families.

The following table summarizes balance-of-payments data relating to U. S. defense activities:

U. S. DEFENSE EXPENDITURES AND RECEIPTS
ENTERING THE INTERNATIONAL BALANCE OF PAYMENTS
FY 1961 - 1967 1/ 2/

(\$ billions)

	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>
<u>EXPENDITURES</u>							
U. S. Forces and Their Support	\$2.5	\$2.5	\$2.5	\$2.6	\$2.5	\$3.1	\$3.9
Military Assistance	.3	.2	.3	.2	.2	.2	.1
Other (AEC, etc.)	<u>.3</u>	<u>.3</u>	<u>.3</u>	<u>.1</u>	<u>.1</u>	<u>.1</u>	<u>*</u>
TOTAL	\$3.1	\$3.0	\$3.1	\$2.9	\$2.8	\$3.4	\$4.1
<u>RECEIPTS</u>	<u>-.3</u>	<u>-.9</u>	<u>-1.4</u>	<u>-1.2</u>	<u>-1.3</u>	<u>-1.2</u>	<u>-1.8</u>
NET ADVERSE BALANCE	\$2.8	\$2.1	\$1.7	\$1.7	\$1.5	\$2.2	\$2.3
Increase in SEA- related Exp. over FY 1961	\$ -	\$ *	\$.1	\$.1	\$.2	\$.7	\$1.5

1/ The data reflected in this table are on a gross basis. They do not reflect so-called feedback effects, e.g., as U. S. military expenditures increase in a foreign country, that country will in turn be in a position through these increased earnings to increase its imports from the U. S. directly or through third countries. Expenditure data also include expenditures in foreign currencies purchased from U. S. Treasury. In FY 1967, these expenditures were approximately \$200 million, of which \$26 million were in excess or near-excess currencies.

2/ Details may not add due to rounding.

* Less than \$50 million.

Between FY 1961 and FY 1965, the net adverse balance on the defense account was reduced from about \$2.8 billion to less than \$1.5 billion. This reduction was achieved through (1) a substantial rise in receipts from sales of U. S. military goods and services to foreign countries, (2) a reduction in overseas uranium purchases of more than \$200 million, and (3) a successful effort to hold down Department of Defense expenditures in the face of (a) rapidly increasing foreign wages and prices, (b) increases in pay and allowances for U. S. military personnel (16% between FY 1961 and FY 1965), and (c) considering SEA related increases, a net increase in U. S. military personnel deployed in foreign countries.

Between 1961 and 1966 over-all wages in France rose by 41%, in Germany by 52% and in Japan by 61%; during the same period wages increased in the U. S. by only 20%. Similarly, the cost of living rose in France by 19%, in Germany by 16%, and in Japan by 34% from 1961 to 1966 -- but in the U. S. by only 9%. Average annual wages -- including social security benefits under local law and other related costs -- paid for foreign nationals on Department of Defense rolls also have increased markedly during the last six years. For example, from FY 1961 through FY 1966 average foreign national wage costs to the Department of Defense increased in France, Germany, and Japan by approximately 50%. While relative increases in prices and wages can have an eventual favorable impact on the U. S. competitive position in foreign markets and hence on the U. S. balance-of-payments position, for the Department of Defense they simply increase the cost of maintaining our defense posture overseas. (In Western Europe alone, it is conservatively estimated that such price and wage increases serve to increase Department of Defense foreign exchange expenditures by over \$40 million annually.)

In FY 1966 and FY 1967, as a result almost entirely of the U. S. effort in SEA, Department of Defense expenditures rose markedly. Between end FY 1965 and end FY 1967, about 452,000 additional U. S. military personnel were deployed in SEA countries. During the same period total military strength in all foreign countries, including SEA, increased by about 434,000. Hence, in areas outside of SEA, there was a net reduction of approximately 18,000 military personnel.

Concurrent with the substantial increase in U. S. military strength in SEA, there was a substantial increase in logistical support requirements for military operations in South Vietnam. The extensive construction program included deep water ports, logistic depots and airfields. The supplies and equipment needed in Vietnam include more than one million different items. This reorientation and tremendous expansion of effort in SEA is shown in the following table which highlights shifts in military IBP expenditures by major geographic area:

U. S. DEFENSE IBP EXPENDITURES BY MAJOR AREA
FY 1961 - 1967

(billions of dollars)

<u>Fiscal Year</u>	<u>Western Europe</u>	<u>Asian Countries^{1/}</u>	<u>Canada</u>	<u>Other</u>	<u>World-wide^{2/}</u>
1961	\$1.6	\$.6	\$.4	\$.5	\$3.1
1962	1.6	.6	.3	.5	3.0
1963	1.6	.6	.3	.5	3.1
1964	1.5	.6	.3	.5	2.9
1965	1.4	.7	.2	.5	2.8
1966	1.5	1.1	.2	.6	3.4
1967	1.5	1.7	.2	.6	4.1

^{1/} Japan, Philippine Islands, Republic of China, Ryukyu Islands, South Vietnam and Thailand. These data should not be equated with increases in SEA-related expenditures over 1961, shown in the table on page 2, or with "costs of the war" since there have been increased expenditures in other geographic areas resulting either directly or indirectly from the Vietnam conflict. Other adjustments also are required to derive estimated SEA-related "war costs."

^{2/} Details may not add due to rounding.

Although there was a marked net increase in Department of Defense IBP expenditures in FY 1966 and FY 1967, this net increase would have been significantly higher had it not been for the Department of Defense balance-of-payments policies already in effect at the time hostilities were intensified and the new measures which have been undertaken since that time.

Reductions in Expenditures by U. S. Military, Civilian and Dependent Personnel Overseas

The Department of Defense balance-of-payments program relating to reductions in foreign exchange expenditures by U. S. personnel has three main focal points: first, a strenuous effort to review requirements for U. S. military and civilian personnel in foreign countries, with a view to reducing these requirements where feasible; second, continuing stress on voluntary actions by individuals to reduce personal spending on the local economy; and third, efforts to hold down IBP expenditures related to nonappropriated fund activities.

a. Military Strength Levels in Foreign Countries

Special procedures governing U. S. military strength in foreign countries have been developed during the past several years. These procedures, which supplement normal manpower requirements reviews, reflect the continuing Department of Defense effort to assure the assignment and continued deployment of military personnel in foreign countries at the minimum levels necessary to meet military requirements. Under these procedures, an over-all end fiscal year ceiling on military strength in foreign countries is established for each military department. In certain cases there are additional subsidiary country and/or area ceilings.

Since 1963, although there has been an over-all net increase in U. S. military strength in foreign countries, there also have been a substantial number of actions which served to reduce such requirements for military personnel without detriment to U. S. national security objectives and with beneficial balance-of-payments effects. Some of these actions are as follows: In FY 1964, three U. S. air defense units in Spain were phased out; SAC Reflex B-47 operations were consolidated in Europe (and later the B-47's were redeployed from Europe) and U. S.

personnel requirements in U.S. military headquarters in foreign countries were reduced by 15% below end FY 1963 levels. (These actions served to reduce military strength requirements in foreign countries by about 6,500.) In FY 1965, the Army's Line of Communication (LOC) in France was reorganized and three U.S. interceptor squadrons and a C-124 transport squadron were withdrawn from Japan to the U.S. (On completion of these actions, military strength requirements in foreign countries had been reduced by more than 7,000 spaces.) In FY 1966 and FY 1967, over 20 overseas activities were consolidated, reduced or discontinued with a savings of about 8,000 military spaces. In FY 1967, also, there was a gross reduction in U.S. military manpower requirements in Europe of about 18,000 U.S. military and civilian personnel resulting from the U.S. relocation from France. These reductions stemmed in part from special Department of Defense manpower revalidation procedures associated with the relocation.

Certain of the earlier actions outlined above, and others, served to reduce U.S. military strength in Western Europe by approximately 51,000 between March 1962 (the peak of the Berlin Buildup) and March 1965. Between March 1965 and March 1967, there was a further net reduction of approximately 16,000 U.S. military personnel in Western Europe.

b. Expenditures by Individuals

A continuing effort is made by the Department of Defense to encourage participation by its personnel stationed in foreign countries in voluntary programs designed to channel available disposable income back to the U.S. These programs were initiated by the Department of Defense early in 1961. As applied to individuals, these programs emphasize and encourage voluntary actions to reduce spending on the local economy, to increase use of payroll allotments and other voluntary savings programs and to increase spending in U.S. controlled facilities, including use of U.S. operated recreation areas.

In 1966 and 1967, existing programs relating to voluntary reductions in personal spending by Department of Defense personnel stationed in foreign countries were intensified and new programs were initiated. Disbursement procedures were modified to make it easier for servicemen to leave their pay "on the

books." Regulations were amended to permit servicemen to increase the size of their allotments sent home. In addition, the Uniformed Services Savings Deposit Program was enacted. The law and accompanying Executive Order revitalized the old Soldiers, Sailors and Airmen's Deposit Program. Participation in the program is limited to military personnel on active duty in a foreign area. Amounts deposited under the program earn interest at the rate of 10% per annum, compounded quarterly and interest is paid on deposits up to a maximum of \$10,000 while the depositor is on a duty assignment for more than 90 days outside the U. S. or its possessions or Puerto Rico. Any part of unallotted current pay and allowances (in multiples of \$5), including a re-enlistment bonus paid in a foreign country, may be deposited.

Against the background of the actions outlined above, the Department of Defense undertook in August 1966 a concerted effort to encourage greater participation by all its members in foreign countries in the voluntary balance-of-payments program. The Directorate for Armed Forces Information and Education is producing and distributing materials supporting these personal savings programs, including Bulletins for Commanders, a special Fact Sheet for Servicemen, a special film and radio and television and press material. In November 1966, 277,000 copies of a special Fact Sheet entitled "Your Personal Savings Program" were issued. Later in the year about 300 copies of a 10-minute film entitled "Gold and You" were distributed for showing to Department of Defense personnel. This film explains the U. S. balance-of-payments program, outlines ways and means of achieving reductions in IBP spending by U. S. personnel, and emphasizes the revitalized Uniformed Services Savings Deposit Program as an attractive avenue of saving. In this respect, as of September 30, 1967, there was \$183.5 million in gross deposits in the program. (It is recognized that these deposits -- as in the case of savings associated with similar programs -- cannot be equated directly with equivalent net IBP savings since some portion of the new deposits are made in place of other forms of savings or expenditures which would not enter the international balance of payments.)

Currently, the Office of the Secretary of Defense and the military departments are taking additional steps to provide more comprehensive orientation on the U. S. IBP problem to Department of Defense personnel prior to their assignment overseas.

In South Vietnam, the efforts to encourage voluntary reductions in personal spending serve also as a significant part of the over-all effort to reduce inflationary pressures in the local economy. Additional measures in South Vietnam include a special piaster budget for spending by U.S. agencies in that country, the use of military payment certificates and a prohibition on the use of regular American currency in the country as part of the effort to eliminate unauthorized currency transactions. In this respect, the rest and recuperation (R&R) program recently established in Hawaii for military personnel serving in South Vietnam also serves to hold down the foreign exchange cost resulting from R&R leaves outside U.S. dollar areas. On the basis of an average expenditure of about \$265 per man on R&R in foreign countries, use of Hawaii as an R&R site is estimated to result in foreign exchange savings of about \$20-\$25 million in FY 1968.

c. Nonappropriated Fund Activities

It is the policy of the Department of Defense to promote the sale of U.S. items in overseas nonappropriated fund activities. Military exchanges and other nonappropriated fund activities in foreign countries have been directed to take whatever steps are possible, within the limits of sound business practice, to stock merchandise of U.S. origin to the greatest practicable extent. At the same time, it is recognized that there is a demand for foreign merchandise by U.S. personnel stationed in foreign countries and that a more favorable effect on the U.S. balance of payments will result if such goods are purchased through U.S.-operated nonappropriated fund resale activities than procured directly on the local economy or from other foreign outlets. Accordingly, nonappropriated fund resale activities in foreign countries are authorized to procure for resale foreign-made goods available in the local market, subject to certain restrictions. Among these restrictions is the requirement that the price of foreign items sold in overseas exchanges

and other retail outlets must be at least as high as the selling price prevailing on the local economy. This pricing policy in effect permits a lower markup and more attractive prices on U. S. goods because of the additional profit from sales of foreign items, thus stimulating demand for U. S. products.

The Department of Defense also has expanded the use of catalogues to emphasize the availability of U. S. merchandise. In the fall of 1966, the Navy Ship Store Office distributed 25,000 U. S. commercial catalogues specially printed for the Navy to all overseas exchanges and to some 50 ships located outside the U. S. The Army and Air Force Exchange System also has established a "mail a gift" service for U. S.-made items which can be delivered in the U. S. In July 1967, the Military Departments were requested to review the sale of foreign merchandise directly or through concessionaires, by the various clubs, messes and sundry funds and curtail such sales by eliminating items, restoring to the military exchanges the responsibility for the sale of those items normally sold through that channel and by minimizing the presence of display type concessionaires.

In July 1967, new procedures were approved governing overseas exchange procurements based on a percentage of foreign merchandise procurement expenditures to total exchange sales, including Vietnam -- 27-1/2% for July-December 1967 and 25% for January-June 1968 -- and a concurrent re-emphasis on U. S. merchandise sales. This action was designed to halt and reverse the increase in the proportion of foreign procurement expenditures to total sales experienced in the July-December 1966 period in SEA and concurrently, to increase emphasis on better stockage of U. S. merchandise and to assure the highest priority for purchase, promotion and sale of U. S. manufactured items. This program is being monitored closely in order to assure that there is no shift by Department of Defense personnel from purchasing in the exchanges to purchasing foreign items on the local economy. Early in August 1967, the Military Departments also were requested to conduct a thorough review of items stocked for resale in exchanges to ensure in-stock positions of U. S. manufactured goods in demand and to substitute comparable U. S. manufactured items for foreign goods wherever feasible.

This continuing stress on foreign exchange economies in the nonappropriated fund area rests on a base of actions taken during the FY 1961 - FY 1966 period. In FY 1960, the overseas military exchanges spent about \$150 million for the purchase of foreign merchandise and total exchange sales were slightly less than \$500 million. In FY 1966, expenditures for foreign merchandise were slightly less than the FY 1960 level, but total exchange sales had risen to slightly more than \$700 million, or a \$200 million increase over FY 1960. The nonappropriated fund activities have provided, and provide today, perhaps the single most significant avenue through which U. S. military and civilian personnel and their dependents in foreign countries "return" dollars to the United States.

Actions Relating to Foreign Nationals

The Department of Defense has made strenuous efforts to hold employment of foreign nationals to minimum essential levels. Major emphasis on reducing employment of foreign nationals was initiated in July 1963 with some actions to be effective by end FY 1964 and additional actions scheduled by end FY 1965. The results of the FY 1964-1965 program are reflected in the following table, which also reflects FY 1966-1967 SEA related increases:

FOREIGN NATIONAL STRENGTH AND DOD IBP EXPENDITURES
FY 1961 - 1967

<u>Fiscal Year</u>	<u>Foreign National Strength (March 31 Data)</u>	<u>DOD IBP Expenditures (\$ Millions)</u>
1961	243,100	\$370
1962	242,800	400
1963	240,000	440
1964	223,300	425
1965	198,200	410
1966	203,800	440
1967	261,100	530

Between FY 1963 and FY 1965, there was an over-all net reduction of close to 42,000 foreign nationals employed on Department of Defense rolls and a concurrent decrease in IBP expenditures for foreign nationals of about \$30 million, in spite of some upward pressure in this area already being experienced as a result of the conflict in SEA. (During this period Department of Defense U. S. civilian strength in foreign countries remained relatively stable.) But the savings shown do not fully reflect the actions taken, in as much as foreign national wage costs were steadily rising during the period. If the FY 1963-1965 reductions had not been made, and if SEA foreign national employment increases had been added to the FY 1963 employment level, total foreign national expenditures in FY 1966 could have been well above \$500 million, and in FY 1967 well above \$600 million, instead of at the levels reported.

The increase in foreign national employment during the last two fiscal years is attributable almost entirely to SEA requirements. From March 1965 to March 1967, foreign national employment in Vietnam alone increased by about 47,000, while for the same period the number of foreign nationals in Western Europe declined by an additional 4,000. (Between March 1961 and March 1967, there was a net reduction of approximately 28,000 foreign nationals in Western Europe.)

Expenditures for Materials, Supplies and Services and Major Equipment

Department of Defense policies place primary emphasis on use of U. S. materials and supplies in support of U. S. defense activities. Efforts to restrain IBP expenditures for materials, supplies and equipment can be related initially to a Presidential directive in November 1960 calling for reductions in Department of Defense procurement abroad during CY 1961.

Beginning in January 1961, Department of Defense purchases (excluding Military Assistance Program (MAP), nonappropriated fund procurements and POL) normally were "returned" to the U. S. when costs of U. S. supplies and services (including transportation and handling) for use outside the U. S. did not exceed the

cost of foreign supplies and services by more than 25%. In mid-1962 the standard 25% differential was increased to 50%, and on a case-by-case basis could exceed 50%. These policies, which are continually re-emphasized, remain in effect today. Hence, in cases where the U.S. versus foreign procurement source is to be determined on price differential grounds, a 50% premium in favor of U.S. end products or services is acceptable automatically and cases over \$10,000 where the price differential is over 50% continue to be forwarded to the Deputy Secretary or the Secretary of Defense for procurement source determination. From CY 1961 through FY 1967, about \$340 million in procurements had been diverted from foreign products to U.S. products or services under this program, at an additional budgetary cost of about \$75 million, or about 22%.

Similarly, for Department of Defense procurements of goods and services for use in the U.S., case-by-case review procedures using the 50% differential as a "bench mark" were initiated in July 1962. The 50% differential was subsequently formalized as a part of Department of Defense procurement regulations with a clear statement that this policy would be kept in force only as long as is required by the U.S. balance-of-payments situation. From FY 1963 through FY 1967, based only on cases where foreign source bids were received, approximately \$13 million in procurements which normally would have been foreign were returned to U.S. sources at an additional budgetary cost of approximately \$4 million, or about 31%.

With respect to purchases of POL, in FY 1967 the Department of Defense returned to the U.S. somewhat over \$100 million of the approximately \$570 million which normally would have been earmarked for overseas procurement; thus, about 20% of Department of Defense overseas procurement requirements in FY 1967 were purchased in the U.S. Additional returns have been determined to be infeasible, principally on economic grounds, e.g., the additional budgetary cost involved would greatly exceed any benefits in foreign exchange savings.

Emphasis on reducing Department of Defense expenditures overseas for material, supplies and services is continuing. The Secretary of Defense in July 1967 approved a recommendation

to establish as a FY 1968 objective a reduction in IBP expenditures for subsistence in foreign countries below FY 1967 expenditures, which were about \$100 million, under specific guidelines. Similarly, in mid-July 1967, the Deputy Secretary of Defense confirmed the use of more stringent criteria governing the selection of foreign research and development projects. The Director, Defense Research and Engineering also has directed that a semiannual review of all foreign projects be made to ensure full compliance with these criteria.

Reductions in Expenditures for Construction and Operation of Overseas Facilities

Department of Defense efforts to reduce expenditures relating to the construction and operation of facilities in foreign countries have two principal focal points. First, the Department of Defense has attempted to operate required facilities at minimum costs under groundrules which in part require that maintenance and repair of real property be conducted at levels sufficient only to ensure continuity of operations and to preclude uneconomical costs due to excessive deterioration. As part of this effort, there are continuous reviews to seek out areas where base closures or consolidation of activities can be achieved without detriment to national security objectives and with savings in budgetary and IBP costs. Second, the Department of Defense has eliminated or deferred all construction not essential to military needs and attempted to reduce the foreign exchange costs of essential construction even where additional budgetary costs are required.

Proposed construction programs in foreign countries are subject to special reviews as to essentiality, and those which are approved are designed, where permitted by the applicable country-to-country agreements, so as to reduce foreign exchange costs to a minimum. Under specially developed construction procedures, the Department of Defense is emphasizing the use of: (1) U. S. procured materials, (2) U. S. Government furnished materials and equipment, (3) U. S. flag carriers, (4) prefabricated buildings manufactured in the U. S., and (5) competent troop labor. It is recognized that these construction procedures may result in increased budgetary costs;

however, extra budgetary costs generally are considered acceptable provided the added cost over normal construction methods does not exceed 50% of the amount of reduction achieved in IBP costs. These special procedures also may be acceptable as approved on a case-by-case basis even though premium costs may exceed 50%.

In view of the magnitude of the construction program in SEA, particularly in Vietnam, an extraordinary effort has been made to reduce the IBP impact of the program. The results of this effort can be stated very simply. Of the over \$1.4 billion in approved and funded construction for South Vietnam, almost \$1 billion had been expended through June 30, 1967. But, only about \$250 million, or approximately 25%, of these expenditures were foreign exchange costs. This achievement also must be considered in the light of the extreme urgency under which much of the construction work has been accomplished.

The emphasis to restrict overseas construction projects to those necessary to meet national security objectives continues also in other geographic areas. As a result of a study called for in April 1967, the Secretary of Defense subsequently approved an action to hold IBP expenditures for military construction, including NATO Infrastructure, but excluding expenditures for construction in Vietnam, to \$270 million in FY 1968.

Military Assistance Program

Military assistance IBP expenditures generally are reflected in three separate areas: offshore procurement, NATO Infrastructure and all other MAP costs. An intensive effort is being made to hold down IBP costs in all these areas.

In December 1960, the Department of Defense issued instructions to the Unified Commands to review the MAP in their respective area and to recommend adjustments that would lead to reductions in dollar expenditures abroad either through deletion or deferral of requirements or through transfer to the U. S. of sources of supply. Initially, recommendations for changes were limited to adjustments which would not increase budgetary costs to the Department of Defense by more than 10%. This differential subsequently was raised to 25%, and beginning in December

1963, the 50% differential relating to military functions appropriations procurements was applied also to MAP offshore procurement. In addition, policy guidance was revised in mid-1963 to require that offshore procurements under MAP cost sharing agreements be limited essentially to the fulfillment of prior commitments. Under the policies outlined above, IBP expenditures for MAP offshore procurement were reduced from about \$160 million in FY 1963 to less than \$50 million in FY 1967, and all other MAP expenditures entering the IBP were reduced by about one-third during this period.

Military Assistance Program funds also were used during the FY 1961-1967 period to provide the U. S. contribution to NATO multilateral efforts, the most significant of which is NATO Infrastructure, i.e., the joint U. S.-Allied funding of airfields, communication facilities, firing ranges and other facilities. During 1966, the U. S. negotiated a reduction in its percentage share contributed to NATO Infrastructure from 30.85% to 25.77%.

Stringent control procedures to restrain MAP IBP costs, stemming in part from the provisions in the Foreign Assistance Act of 1961, as amended, remain in effect today. For example, in addition to the percentage guidelines outlined above with respect to offshore procurement, the Assistant Secretary of Defense (International Security Affairs) must certify before foreign procurement can be undertaken that failure to procure outside the U. S. would seriously impede the attainment of MAP objectives.

Military Sales Program

During the FY 1961 - FY 1967 period, the U. S. military sales program has resulted in important balance-of-payments benefits to the U. S. In FY 1961, Department of Defense cash receipts, which stem in large part from military sales, were slightly over \$300 million. By FY 1963, Department of Defense cash receipts had risen to well above \$1 billion and during the FY 1963-1967 period have averaged close to \$1.3 billion, with unusually large receipts of close to \$1.6 billion in FY 1967.

The principal objective of the foreign military sales program, however, is basically the same as that of the U. S. grant aid program, i.e., to promote the defensive strength of our allies in a way consistent with over-all U. S. foreign policy objectives. Encompassed within this over-all objective are several specific goals:

1. To further the practice of cooperative logistics and standardization with our allies by integrating our supply system to the maximum extent feasible and by helping to limit proliferation of different types of equipment.

2. To reduce the costs, to both our allies and ourselves, of equipping our collective forces, by avoiding unnecessary and costly duplicative development programs and by realizing the economies possible from larger production runs.

3. To offset, at least partially, the unfavorable payments impact of our deployments abroad in the interest of collective defense.

Under the policies and goals outlined above, between FY 1962 and FY 1967, the total program has resulted in sales of about \$9.8 billion. In addition, outstanding sales commitments as of June 30, 1967, amounted to approximately \$2 billion. The list of equipment involved has been dominated by sophisticated weapons systems: e.g., F-111's, F-4's, POLARIS equipment, HAWK and PERSHING missile systems, etc. Of the \$11.8 billion of sales and commitments, \$8.5 billion are for cash and \$3.3 billion are credit transactions. Of the latter amount, about \$2.1 billion are being financed by the Export-Import Bank without any Department of Defense guaranty and about \$1.2 billion through a combination of Department of Defense credit sales and guaranty loans.

About 75% of the sales and commitments to date have gone to Europe and Canada, 12% went to the Far East, primarily Australia, Japan and New Zealand, with about 13% distributed among a substantial number of other countries throughout the world.

All important proposals for military sales are reviewed by the Secretary of Defense, with appropriate interagency

coordination, and Presidential decision frequently is required. Decisions to sell equipment are based on a positive determination that it is in the best over-all U. S. national interest to make the sale.

In addition, there have been some instances where U. S. sales have been associated with arrangements under which the purchasing country gains increased access to U. S. military procurement requirements on a competitive basis. From an over-all standpoint, such arrangements at times are desirable, even though they serve in part to increase U. S. foreign exchange expenditures.

Barter and Excess Currency Programs

The Department of Defense also is attempting to achieve maximum feasible use of U. S.-owned excess currencies and barter arrangements as a means of conserving Department of Defense dollar expenditures entering the IBP. In terms of priorities, Department of Defense uses excess currencies before barter for overseas procurements where a choice exists.

Specific policies and procedures have been developed which provide for the use of U. S.-owned foreign currencies rather than dollars for payment of overseas Department of Defense requirements. Where feasible, such items as (1) overseas allowances, (2) travel, transportation, per diem and related expenses of Defense personnel, dependents, employees of contractors, and (3) contract procurements, are paid for in excess currencies. It should be noted, however, that the bulk of excess currencies held by the U. S. are currencies of countries where the number of U. S. forces and the magnitude of Department of Defense expenditures are relatively small (in FY 1967 less than 1.5% of all military personnel assigned overseas were stationed in excess or near-excess currency countries, and less than two-tenths of one percent were in excess currency countries). In addition, there are relatively limited possibilities of using excess currencies to meet requirements in other countries, based in part on the nature of existing country-to-country agreements governing use of the currencies.

With respect to barter, where it has first been determined that excess currencies cannot be used and a determination also

has been made under Department of Defense balance-of-payments procurement guidelines that the requirement must be met from an overseas source, an effort is made to use barter procurement, under procedures developed with the Department of Agriculture.

In its initial year, in FY 1964, the Department of Defense barter program amounted to less than \$25 million. In FY 1967, the barter program amounted to slightly over \$200 million (including about \$15 million AEC barter), or about an eightfold increase over the FY 1964 level.

Miscellaneous Actions

During the past several years, the Department of Defense has given continuing attention to improving IBP reporting and management control procedures in an effort to supplement and enhance the various specific balance-of-payments policies. Some examples are as follows:

1. In FY 1964, Department of Defense implemented a revised system for recording and reporting Department of Defense expenditures and receipts entering the IBP. During FY 1967 these reporting procedures were further refined.
2. The Secretary of Defense has assigned balance-of-payments expenditure and receipt targets to various components of the Department of Defense. These targets, which reflect approved actions, provide useful bench marks from which to measure Department of Defense balance-of-payments efforts.
3. As part of the actions and studies undertaken in April 1967, a Department of Defense-wide review of IBP procurement actions and related accounting is underway. These reviews serve to emphasize the need for continuing attention by activities to current IBP procurement policies and to help assure that IBP accounting reports accurately identify and report properly the impact of Department of Defense expenditures entering the IBP.
4. Specific procedures have been included in annual budget reviews which call for the identification of IBP impacts resulting from alternative budget decisions. International balance of payments implications also are required to be submitted for review in connection with basic budget estimates for construction, procurement and research, development, test and evaluation appropriations.

The Outlook for 1968

The Department of Defense balance-of-payments program will receive continuing attention during CY 1968 in keeping with the President's Message on Balance of Payments of January 1, 1968. This emphasis will rest in part on the significant number of policies and practices already in effect which serve to hold down and, where feasible, reduce Department of Defense expenditures entering the IBP. In addition, the IBP Action and Project List, issued in April 1967, sets out for examination additional proposals where there was some possibility of additional IBP savings and/or the need for renewed attention. Decisions on some of the proposals, as noted above, already have been made. Other items on the project list still are under study and favorable decisions in 1968 on certain of these longer-term items may provide additional IBP benefits in the future. In addition, Department of Defense is examining other proposals with a view to reducing further the IBP costs of personal spending by U.S. forces and their dependents stationed in foreign countries, particularly in Western Europe.

In Western Europe also, it is anticipated that these actions will be supplemented by the previously announced planned redeployment of approximately 35,000 U.S. military personnel from the Federal Republic of Germany during CY 1968, with some associated reductions in foreign national employment. This action, based on current plans, will serve to reduce Department of Defense IBP costs by about \$75 million at an annual rate, although substantial IBP savings are not anticipated until the first half of CY 1969. In SEA, the current outlook is for a smaller increase in expenditures as compared to the increases experienced in 1966 and 1967.

Overall, with respect to Department of Defense IBP expenditures, based on present programs and strength levels, significant new savings will be more difficult to achieve. As a result of past efforts, the "easy" reductions have long since been made. For example, under present circumstances the Department of Defense already appears to have reached the borderline, in the procurement area in terms of IBP savings/budgetary cost tradeoffs.

The Department of Defense also will continue to take all steps feasible within existing policies which would serve to increase receipts. Nevertheless, it is currently anticipated that there will be a reduction in Department of Defense cash receipts in CY 1968 below FY 1967 levels. In this respect, however, Department

of Defense data exclude special purchases of securities by other countries and these purchases are expected to be substantial in FY 1968 and CY 1968. For example, as previously announced, the Bundesbank (FRG) has agreed to purchase in FY 1968 \$500 million in U.S. medium-term securities to ease the net IBP impact of stationing U.S. forces in Germany. There may be other actions of this nature which also represent a departure from the more traditional military offset approach. Although these actions would be of benefit to the U.S. balance of payments during this period, they would not be reflected in Department of Defense receipts data. The Department of Defense is participating with Treasury and other U.S. Government agencies in these efforts.

Source: Department of Defense.

U.S. DEFENSE EXPENDITURES AND RECEIPTS ENTERING THE INTERNATIONAL BALANCE OF PAYMENTS ^{a/}
 FISCAL YEARS 1961-1967
 (Millions of dollars)

	<u>FY 1961</u>	<u>FY 1962</u>	<u>FY 1963</u>	<u>FY 1964</u>	<u>FY 1965</u>	<u>FY 1966</u>	<u>FY 1967</u>
EXPENDITURES:							
U.S. Forces and Their Support:							
Expenditures by U.S. Military, Civilians and Dependents ^{b/} ..	\$ 789	\$ 775	\$ 815	\$ 879	\$ 956	\$1,121	\$1,256
Foreign Nationals (Direct and Contract Hire).....	366	396	438	425	408	438	525
Procurement:							
Major Equipment.....	62	67	76	92	78	87	146
Construction.....	157	122	101	94	105	256	396
Materials and Supplies (Includes POL) ^{c/}	562	597	547	474	415	527	642
Operation & Maintenance) (Other) ^{d/}				418	400	491	695
Other Payments ^{d/}	516	517	536	184	174	213	270
Sub-Total.....	\$2,452	\$2,474	\$2,513	\$2,566	\$2,536	\$3,133	\$3,930
Military Assistance Program:							
Offshore Procurement.....	155	122	161	118	75	53	29
NATO Infrastructure.....	105	36	90	61	34	50	53
Other.....	52	64	67	58	59	54	44
Sub-Total.....	\$ 312	\$ 222	\$ 318	\$ 237	\$ 168	\$ 157	\$ 126
Net Change in Dollar Purchased Foreign Currency Holdings.....	-2	+13	-6	-8	+1	+12	+25
Total Expenditures.....	\$2,762	\$2,709	\$2,825	\$2,795	\$2,705	\$3,302	\$4,081
RECEIPTS:							
Cash Receipts ^{e/}	319	899	1,394	1,204	1,253	1,060	1,566
Barter.....	-	-	-	23	69	139	204
Total Receipts.....	\$ 319	\$ 899	\$1,394	\$1,227	\$1,322	\$1,199	\$1,770
Sub-Total.....	\$2,443	\$1,810	\$1,431	\$1,568	\$1,383	\$2,103	\$2,311
OTHER EXPENDITURES:	343	273	250	136	95	50	28
(AEC and other agencies included in NATO definition of defense expenditures).....							
Net Adverse Balance (NATO Definition).....	\$2,786	\$2,083	\$1,681	\$1,704	\$1,478	\$2,153	\$2,339

Footnotes on page 2.

- a/ Data differ somewhat from data on the defense account shown in the Department of Commerce publication Survey of Current Business. Commerce data exclude, on payments side, small amounts representing retired pay, claims and grants and net changes in DOD holdings of foreign currencies purchased with dollars. On receipts side, Commerce data exclude military sales through commercial channels and barter. These data are included in Commerce accounts under other entries.
- b/ Includes expenditures for goods and services by nonappropriated fund activities.
- c/ Beginning with FY 1964, data for materials and supplies include only expenditures for O&M supplies and stock fund purchases.
- d/ Beginning with FY 1964, "Operation & Maintenance (Other)" includes all O&M payments not included elsewhere and "Other Payments" includes expenditures for retired pay, claims, research and development, industrial fund activities, etc.
- e/ Cash receipts data include primarily: (1) sales of military items through the U.S. Department of Defense; (2) reimbursements to the U.S. for logistical support of United Nations forces and other nations' defense forces; and (3) sales of services and excess personal property. They do not include estimates of receipts for military equipment procured through private U.S. sources, except where these are covered by government-to-government agreements, and data are available, i.e., FRG, Iran, Italy and Saudi Arabia.

AID AND THE BALANCE OF PAYMENTS

During the Marshall Plan and most of the 1950's, aid appropriations were generally spent wherever prices were lowest. For the first few years after the war, the United States was the only major source for most of the goods needed by aid recipients. Consequently, most aid dollars were spent in this country even though they were not tied to U.S. procurement.

This situation changed as the revived European economies became increasingly effective competitors for U.S. aid purchases. By 1959 only 40% of our aid dollars were being spent on U.S. goods and services.

Beginning in 1959, in order to improve the U.S. balance of payments we began to limit our policy of worldwide procurement. Today, funds are spent primarily in the United States for goods and services procured in this country. The only significant elements in the A.I.D. program not specifically tied to U.S. goods and services are salaries and payments to A.I.D. overseas personnel and contractors (only part of which is spent abroad) and limited offshore procurement for A.I.D. administrative purposes.

In FY 1968, the U.S. share of total A.I.D. expenditures is expected to reach 92%, with 96% of commodity expenditures being made in the United States. The net impact of the A.I.D. program on the balance of payments in FY 1968, after allowing for repayments of principal and interest, is estimated at close to zero, as compared to \$934 million in FY 1961.

This change has been brought about by the aggressive steps which A.I.D. has taken in recent years to minimize the balance-of-payments costs of its programs. These steps fall into three general categories--(a) expansion of A.I.D.'s tied procurement regulations; (b) measures to improve U.S. export additionality, both in the context of A.I.D. programs and generally; and (c) use of local currencies.

Tightening of Tied Procurement Regulations

Loan Financing. To assure that A.I.D. funds are used for the purchase of goods and services in the United States, A.I.D. has progressively tied all loans to U.S. procurement. Exceptions are possible only if waivers are approved by interagency committees and signed by the A.I.D. Administrator. There are no current exceptions.

Grant Financing. Virtually all grant procurement is also tied to U.S. goods and services -- procurement is limited to the United States and eight Asian and African less-developed countries. These commodities are paid for in local currencies. But arrangements are made to purchase in the United States a dollar-equivalent amount of U.S. goods under Special Letters of Credit. These arrangements are used almost exclusively for security-related foreign procurement for Vietnam and are estimated at about \$70 million in FY 1967.

Local Cost Financing. In some instances, A.I.D. pays part of the local costs of A.I.D.-financed projects. In countries where the United States does not already have available local currency in excess of U.S. requirements, dollars must be used to obtain the local currency to cover any project costs which A.I.D. may finance. Since 1963, A.I.D. has moved progressively to tie these dollars to U.S. procurement by using Special Letters of Credit good only in payment of goods and services originating in the United States.

There are only three elements of the A.I.D. program, then, which still have a significant impact on our balance of payments:

1. Salaries and other payments to A.I.D. overseas direct-hire personnel and contractors. A.I.D. direct-hire personnel and contractors working overseas have to spend money for living expenses and other local costs. Their salaries and payments cannot, of course, be tied to U.S. procurement, but only part of these funds is spent abroad. The estimate for the FY 1968 program is about \$99 million. Little can be done to reduce this amount materially, although A.I.D. is continuing efforts to increase the use of local currencies where they are available.
2. Minimum foreign procurement for A.I.D. administrative expenses. A very small amount of A.I.D. funds (\$7 million of FY 1968 funds) is used to make local purchases of items necessary for administration of the program which cannot be imported from the United States. Here again, available local currencies are used whenever possible.
3. Cash grants. These are still being made in situations where it has been difficult to substitute U. S. goods and services. The item has been reduced drastically in recent years until it includes only the multilateral Foreign Exchange Operations Fund in Laos (about \$13 million) and parts of some grants to overseas educational institutions.

A.I.D.'s Expenditures as Measured by the "Accounting" Method.
One way to measure the impact of A.I.D.'s expenditures on the balance of payments--the way used by the Department of Commerce in preparing its balance-of-payments figures and which might be called the "Accounting" approach--is to look at the direct result of A.I.D. spending. To what extent are aid dollars spent directly in this country, and to what extent are they spent abroad or paid to an international organization? To what extent are offshore expenditures offset by repayments to the United States of principal and interest on prior-year loans?

In FY 1963 A.I.D.'s offshore expenditures totaled \$799 million, including all contributions to the UN and other international organizations and before making an allowance for offsetting expenditures by these organizations in the United States. In that year the Agency made a commitment as part of the U. S. balance-of-payments program to reduce its offshore expenditures to not more than \$500 million by FY 1965. That goal was reached. In FY 1965 they were about \$411 million. Despite the greatly expanded Vietnam program, offshore expenditures were held to \$503 million in FY 1966. As a result of A.I.D.'s further tightening of tied procurement regulations, there was a further reduction in offshore expenditures of \$100 million between FY 1966 and FY 1967. It also became apparent that A.I.D. and the State Department's contributions to international organizations should not be treated as "offshore" expenditures since they were more than offset by the spending of these same organizations in the U.S. 1/

The currently estimated offshore expenditures in FY 1967, therefore, are \$290 million, after allowing for international organization offsets up to the amount of the U. S. contribution. The projected figure for FY 1968 is \$201 million. 2/

1/ The classic example was that of the Indus Basin Development Fund. The U. S. was contributing 44% of the foreign exchange needed by the IBRD to finance the construction of the Indus Basin projects. The entire amount of the U.S. contribution, under the old procedures, was being counted as a drain on the U.S. balance of payments, even though 54% of the foreign exchange costs of the contracts under the Indus Basin Fund had been let to U.S. firms for construction or consultant activities.

2/ If international organization contributions were still treated as 100% offshore disbursements, these last two figures would have been \$403 million for FY 1967 and \$325 million for FY 1968.

These offshore figures are on a gross basis. They do not take into account the fact that each year the United States receives payments on loans made by A.I.D. and its predecessors. Such payments totaled \$173 million in FY 1965 and \$184 million in FY 1966, and are estimated at \$203 million and \$215 million, respectively, in FY 1967 and FY 1968.

In percentage terms, total A.I.D. expenditures for goods and services in the United States rose from 41% in FY 1961 to about 80% in FY 1966. For FY 1967 this percentage was about 84% and for FY 1968 is expected to reach 92%.

Calculated on the basis of expenditures which will result from current commitments, rather than on the basis of current expenditures (made in part as a result of prior-year commitments), total A.I.D. funds recorded as spent in the United States have risen to over 90%, a level which cannot be increased significantly.

The dramatic rise in the proportion of recorded A.I.D. expenditures in the United States is even more apparent when expenditures for commodities alone are examined. A.I.D. expenditures for commodities purchased domestically rose from 44% in FY 1961 to about 90% in FY 1966. A.I.D. commodity expenditures currently being made in the United States are now above 90% and are expected to rise to about 96% in FY 1968 as tightened A.I.D. procurement measures take effect and remaining expenditures from prior-year commitments are liquidated.

This improvement in aid-tying has not, of course, been achieved without cost. Individual commodities financed by A.I.D. and, therefore, produced in the United States, may cost an aid recipient more--including higher transportation costs--than if they were bought elsewhere at world market prices.

Ensuring Additionality of U.S. Exports

The true economic effect on the balance of payments of the A.I.D. program (or of any other program involving overseas expenditures) cannot be determined as simply as the "accounting" method suggests. There are indirect effects not revealed by the direct accounts.

Many dollars contributed under the A.I.D. program to multilateral agencies, for example, come back through regular commercial channels for purchases of U.S. goods. Also, dollars which go out and enter the economy of a less-developed country may later be used by that country to buy needed goods in the U.S. market. Or, they may go through trade channels to a third country which will use them to purchase goods here.

These are examples of the so-called "feedback" or "re-flow" which comes from overseas spending. They demonstrate that the "accounting" method overstates the effect of aid outflows on the U.S. balance of payments, because the outflows are to a considerable extent soon reflected in increased U.S. export sales.

But there is another indirect effect in the opposite direction. When an aid recipient buys U.S. goods financed by A.I.D. under a tying arrangement, it may be buying goods that it would otherwise have bought with dollars it already owns. The latter dollars--free foreign exchange--can then be used for other purchases either in the United States or elsewhere. When purchases are made elsewhere, the U.S. balance of payments may be adversely affected, although (because of the respending effect) not necessarily by the full amount of third-country purchases.

This is the so-called "substitution" effect, meaning that A.I.D.-financed purchases are sometimes substituted for purchases that would otherwise have been made with "free dollars." To the extent that this takes place, the "accounting" method understates the adverse effect of the A.I.D. program on the balance of payments.

Simply tying procurement to U. S. sources may not, therefore, be fully effective in reducing the impact of the A.I.D. program on the balance of payments. Having already gone about as far as possible in tying procurement to U.S. goods and services, A.I.D. has undertaken a wide variety of measures to ensure that A.I.D.-financed exports will be additional to, rather than a substitute for, exports that would have occurred without A.I.D. financing. A.I.D. has included U.S. export promotion as an important factor in selecting capital projects and commodities for A.I.D. financing and has stressed in other ways the urgent necessity of minimizing the impact of A.I.D. programs on the U. S. balance of payments. Moreover, U. S. Embassy commercial staffs in the more important aid-recipient countries have been or are being strengthened.

Project and Commodity Selection Criteria. A.I.D. is paying increasingly close attention to balance-of-payments considerations in selecting projects and commodities which it will or will not finance:

- A.I.D. is placing greater emphasis on projects and products which will ensure not only immediate U.S.

exports but also "follow on" orders for such items as spare parts or specialized intermediate materials.

- A.I.D. also has limitations on financing projects which will compete with U. S. exports.
- Another device A.I.D. uses is to refuse to finance items, such as spare parts or goods in which the United States is strongly competitive, which a recipient will buy from the United States in any event since they are available at reasonable cost only in this country.
- Still another method is to limit the list of goods eligible for A.I.D. financing to those in which the United States does not have a price advantage.

Other Measures to Increase Additionality. It has also been possible in a number of cases for host governments to make A.I.D.-financed loans less costly or otherwise more attractive to importers through surcharge reductions or elimination; waiver of prior import deposits; or favorable terms for bank credit. Other more established A.I.D. procedures include general ineligibility of commodities of which the United States is a net importer (e.g. POL) for A.I.D. dollar financing and tightened provisions covering the application of 50/50 shipping regulations, commodity import component value rules, and rules concerning contractor services.

In addition, A.I.D. Missions are taking a number of steps to make sure that information about U. S. exports is made available, for example:

- officials responsible for public and private procurement are being brought to the United States to meet U. S. suppliers;
- an Afro-American Purchasing Center has been set up in New York and special arrangements made with the National Institute of Governmental Purchasing to improve knowledge and availability of U. S. supplies; and
- the availability of unused Special Letter of Credit dollars in certain African countries is being publicized in International Commerce.

General Measures to Increase U. S. Exports. Finally, in addition to these and other measures taken by A.I.D. to reduce the impact of its own program on the balance of payments, discussions have been held with aid recipients about the difficulties of maintaining current assistance levels in the

face of the U. S. payments deficit and about ways, in light of the deficit, in which U. S. commercial exports, not financed through the A.I.D. program, may be increased. In several instances A.I.D. has obtained agreement from aid recipients on measures, such as liberalization of exchange or trade restrictions, designed to increase their imports from the United States.

Not only can this approach serve to offset any adverse effect that the A.I.D. program in a particular country may have on the U. S. balance of payments, but it can in some cases result in a positive balance-of-payments effect flowing from the existence of the A.I.D. program in that country.

Research. A.I.D. is also continuing research into the indirect effects of the program on the balance of payments--the effects which the "accounting" method does not measure. With the results of this research not yet available, it remains difficult to estimate the size of the feedback, substitution and other effects of aid spending. Only indirect evidence is available. With respect to the question of how much substitution occurs, for example, an analysis of U. S. trade figures does not indicate that a drop-off in commercial trade occurs when there is an increase in aid. On the contrary, there is evidence that commercial trade with less-developed countries is increasing even where aid may in some cases be increasing.

The less-developed countries do not, as a rule, increase their foreign exchange reserves, although some of the developed countries do. Nevertheless, looking at the world as one large trading community with an infinite number of rounds of responding or feedbacks, there can be little doubt that the great majority of the dollars spent abroad under the A.I.D. program ultimately come back to the United States.

Clearly, more work needs to be done on this score. Meanwhile, it seems fair to conclude that the indirect economic effects of the A.I.D. program on the balance of payments roughly cancel out. Even allowing for some variation from time to time, the true effect of the program on the balance of payments would probably not differ very much from the figures shown by the "accounting" estimates referred to earlier.

Use of Local Currencies

Increasing stress has been laid on using local currencies derived from the sale of commodity imports--including P.L. 480 imports--in place of dollars. In all countries where a supply of local currencies is available, these are used for any U. S.-financed local costs of dollar-assisted projects, local salaries, housing allowances and the like. In the so-called excess currency countries--where U. S. holdings of local currency greatly exceed U. S. needs--local currency is used instead of dollars not only for local procurement, pay and allowances, but

also for such items as international air travel of American technicians and foreign participants, meeting international commitments to the Palestine Refugee Program and the Indus Basin Development Fund, and the support of American-sponsored schools and hospitals abroad.

Source: Agency for International Development.

The IET was not designed to halt completely the outflow of private portfolio capital from the U.S. to the countries concerned, but rather to restrain the rate of outflow to a more normal level and thus relieve the pressure on the U.S. balance-of-payments position.

After the adoption of the IET new foreign security issues subject to the tax have virtually ceased. U.S. transactions with foreigners in outstanding foreign stocks and bonds, which had regularly resulted in substantial net U.S. purchases for years prior to the IET, shifted to net sales from the middle of 1963 through 1966. For the first three quarters of 1967, there was a resumption of net purchases but on a very limited scale. Long-term commercial bank loan commitments to foreigners in countries subject to the IET have fallen to a small fraction of the pre-tax level, as compared with only a moderate reduction in commitments to countries not covered by the tax.

On July 31, 1967, the tax was extended to July 31, 1969, and discretion was given the President to alter the rate of tax from zero to a level approximating an annual interest burden of 1.5%. The rate currently established by the President is the equivalent of a 1.25% interest rate. Stricter procedures for determining prior American ownership in the case of transactions in foreign securities among Americans were also established in order to prevent evasion of the tax through false representations as to American ownership.

Commerce Department Program

The Voluntary Cooperation Program for business firms was announced by the President on February 10, 1965, in a special message to Congress. On March 12, 1965, the Secretary of Commerce wrote to the officers of six hundred corporations inviting them to participate in the program and to report regularly on their balance-of-payments transactions. Companies were asked to increase their over-all balance-of-payments contributions by

- establishing a special balance-of-payments ledger for 1964 and to estimate the amount of improvement believed possible for 1965,
- increasing their efforts to expand exports,

Interest Equalization Tax (IET) and Voluntary Programs

The Interest Equalization Tax was proposed in July 1963, at a time when the U.S. balance of payments was continuing to show substantial deficits and the dollar was under pressure in foreign exchange markets. A rapid acceleration in the outflow of private portfolio capital from the United States was occurring, with U.S. purchases of new foreign security issues rising from just over half a billion dollars per year in 1960 and 1961, to \$1.1 billion in 1962 and an annual rate of almost \$2 billion in the first half of 1963.

The major motivation for the increased borrowing by other industrialized countries in the U.S. capital market was the higher level of interest rates prevailing in these countries rather than a need on the part of the foreign borrowers for foreign exchange. The purpose of the IET was to compensate for this interest rate differential by increasing by the equivalent of 1% per year the cost to borrowers from other industrialized countries of raising long-term capital in the U.S. market.

The tax, which became effective on July 19, 1963, (August 17, 1963, for listed securities) was originally imposed on U.S. purchases from foreigners of foreign stocks or foreign debt obligations with maturities of 3 years or more. The tax was applied to outstanding issues as well as to new issues. The principal exemptions from the tax included direct investment abroad, export credits, investments in less-developed countries, and in the new issues of another industrialized country, if the President makes a determination that application of the tax would have such consequences for the foreign country as to threaten the stability of the international monetary system. Discretion was given the President to apply the tax to bank loans, including those with a maturity of one year or more, and this authority was exercised on February 10, 1965.

The original law which was due to expire on December 31, 1965, was extended until July 31, 1967, and foreign debt obligations subject to the tax were defined to include those with a period remaining to maturity of 1 year or more.

- returning more foreign earnings to the U.S.,
- repatriating short-term funds which were held abroad merely to earn a small but differentially higher rate of interest,
- delaying or postponing direct investment expenditures in developed countries when such investments are of marginal importance,* and
- making greater use of funds obtained abroad in order to reduce the amount of U.S. capital outflow into direct investment abroad.

In addition, since the beginning of 1966, each company has been requested specifically to hold its direct investment capital transactions (including reinvested earnings) with developed countries below an established, quantitative target level. The object of the target was not to reduce productive investments in plant and equipment abroad but rather to lessen reliance on capital outflows from the U.S. and the reinvestment of earnings to finance those investments. Companies were urged to cancel or postpone direct investments abroad only when their projects are of marginal importance and do not soon result in higher exports or larger investment incomes.

Between 1964 and 1966, the 708 companies currently participating in the voluntary program increased their over-all contributions to the U.S. balance of payments, as defined under the overall improvement goal, from \$15.1 to \$18.6 billion, or by nearly 23 percent. Mid-year revised projections for 1967 indicated an over-all improvement this year of \$2.4 billion over the 1966 level, compared with the goal of \$2.0 billion originally set for the year. Most of the significant growth expected in 1967 can be attributed to continuing improvement in exports and net direct investment transactions.

* U.S. direct investment abroad which had been well under \$1 billion a year prior to 1956 was close to \$3.5 billion in 1965 (see Table 2). Remitted earnings plus receipts of fees and royalties rose considerably less rapidly.

In 1966, participating companies, as a group, were well under the specific direct investment target. They also expected to remain considerably below the tighter 1967 target.

American plant and equipment expenditures in Europe and Canada, which account for the bulk of U.S. direct investment transactions with developed countries, increased by over 71 percent from 1964 to 1967. During the same period, U.S. direct investment outflows to developed countries, adjusted for the use of funds borrowed abroad, declined by 28 percent. The large expansion in plant and equipment expenditures despite smaller adjusted capital outflows reflects the growing use of funds borrowed abroad as an alternative to capital outflows and reinvested earnings for financing foreign investment. Borrowing abroad by U.S. companies and their foreign affiliates has increased five-fold since 1964. A total of \$3.2 billion was borrowed overseas from 1964 to 1966, and an additional \$1.5 billion is expected in 1967.

Federal Reserve Program

The Voluntary Foreign Credit Restraint Program for banks and other financial institutions also originated with the President's Balance of Payments Message of February 10, 1965. It was designed to restrain the increase of foreign loans and investments by financial institutions which, in the case of banks, had reached a very high level in 1964 and had continued to accelerate during the early part of 1965 (see Table 3).

As in the case of business firms under the Commerce Department program, banks and other financial institutions under the Federal Reserve program were asked to observe target ceilings. The target for 1965 was for banks to keep their outstanding foreign credits and investments within 105 percent of the amount outstanding on December 31, 1964. Within the over-all ceiling, absolute priority was to be given to bona fide export credits to foreign borrowers.

Among nonexport credits, priority was to be given to credits to less-developed countries; and insofar as reductions in other credits become necessary, they were to be made in nonexport credits to developed countries other than those largely dependent on U.S. financing, such as Canada and Japan, or those involved in balance-of-payments difficulties, like the United Kingdom.

For 1966 and, again, for 1967 the ceiling was set at 109 percent of the amount outstanding on December 31, 1964; and quarterly limits on the rate of expansion within the target ceilings were suggested.

Nonbank financial institutions were asked to reduce their holdings of liquid funds abroad to the year-end total of 1963 or 1964, whichever was lower, in an orderly manner. Other foreign assets with original maturities of 10 years or less, and loans and advances to their foreign branches and subsidiaries, were to be held within 105 percent of the amount outstanding at the end of 1964. Long-term credits (exceeding 10 years) to other developed countries were not subjected to an aggregate target but it was expected that increases in the amounts of such credits outstanding would normally be avoided, except in the cases of Canada, Japan, and the United Kingdom. The nonbank financial institutions were requested to observe the same schedule of credit priorities as the banks. Remittance of earnings from abroad to the fullest extent possible was urged.

Both banks, as a group, and nonbank financial institutions, as a group, have remained within the suggested ceilings. As of September 30, 1967, the banks were under their end-of-1967 ceilings by \$783 million. As of June 30, 1967, the nonbank financial institutions were below their end-of-1967 ceilings by \$57 million.

Table 1

New Issues of Foreign Securities Purchased
by U. S. Residents, by Area, 1962-1966
(\$ millions)

	1962	1963		1964	1965	1966	1967 First Half*
		First Half*	Second Half*				
<u>TOTAL NEW ISSUES</u>	<u>1,076</u>	<u>999</u>	<u>251</u>	<u>1,063</u>	<u>1,206</u>	<u>1,210</u>	<u>758</u>
<u>IET Countries:</u>							
West Europe	195	219	53	20	80	15	--
Japan	101	107	57	--	52	4	--
Other ^{1/}	60	17	--	--	--	--	--
<u>Subtotal</u>	<u>356</u>	<u>343</u>	<u>110</u>	<u>20</u>	<u>132</u>	<u>19</u>	<u>--</u>
Of which:							
(i) Subject to IET			--	--	80	9	--
(ii) Exempt from IET:			110	20	52	10	--
Reason:							
a) Commitments made prior to 7-18-63			(110)	(--)	(--)	(--)	(--)
b) U.S. export- related			(--)	(9)	(--)	(--)	(--)
c) Japanese exemp- tion			(--)	(--)	(52)	(--)	(--)
d) Other			(--)	(11) ^{3/}	(--)	(10) ^{4/}	(--)
<u>Other Countries:</u>							
Canada	457	608	85	700	709	922 ^{5/}	497
Latin America ^{2/}	102	13	23	208	37	69	58
Other countries	77	35	33	131	149	120	98
International institutions	84	--	--	4	179	80	104
<u>Subtotal</u>	<u>720</u>	<u>656</u>	<u>141</u>	<u>1,043</u>	<u>1,074</u>	<u>1,191</u>	<u>757</u>

* Not seasonally adjusted.

1/ Australia, New Zealand, South Africa.

2/ Includes Latin American Development Bank issue of \$145 million in 1964.

3/ Issue had maturity less than three years, which was lowest maturity to which tax had applied prior to February 11, 1965.

4/ Issue by United Kingdom subsidiary of Canadian firm.

5/ Before deducting \$162 million of Canadian Government purchases from U.S. residents of outstanding Canadian and other foreign securities in accordance with Canada's agreement not to let its foreign exchange reserves rise as a result of borrowing in the U.S.

Table 2

U. S. DIRECT INVESTMENT ABROAD
(\$million)

	(1)	(2)	(3)	(4)	(5)	(6)
	<u>Book Value</u>	<u>Outflow from U.S.</u>	<u>Earnings (U.S. Share)</u>	<u>(Earnings Remitted to U.S.)</u>	<u>Royalties and fees</u>	<u>Yield a/</u>
1950	11,788	621	1,766	(1,294)	126	17.7
1951	12,979	508	2,236	(1,492)	129	20.1
1952	14,721	852	2,327	(1,419)	130	18.9
1953	16,253	735	2,258	(1,442)	128	16.2
1954	17,631	667	2,398	(1,725)	136	15.6
1955	19,395	823	2,878	(1,912)	158	17.2
1956	22,505	1,951	3,298	(2,171)	229	18.2
1957	25,394	2,442	3,561	(2,249)	238	16.9
1958	27,409	1,181	3,014	(2,121)	246	12.8
1959	29,827	1,372	3,241	(2,228)	348	13.1
1960	31,815	1,674	3,566	(2,355)	403	13.3
1961	34,667	1,599	3,815	(2,768)	463	13.4
1962	37,226	1,654	4,235	(3,044)	580	13.9
1963	40,686	1,976	4,587	(3,129)	660	14.1
1964	44,384	2,435	5,071	(3,674)	756	14.3
1965	49,328	3,418 <u>b/</u>	5,460	(3,963)	924	14.4
1966	54,562	3,543 <u>b/</u>	5,680	(4,045)	1,045	13.6

a/ Computed as earnings (Col. 3) plus royalties and fees (Col. 5) divided by book value of the previous year (Col. 1).

b/ Includes use (\$52 million in 1965 and \$445 million in 1966) of proceeds from bond issues abroad by domestic - based finance subsidiaries of U.S. firms.

Source: Derived from Department of Commerce data.

Table 3

Change in U. S. Banking Claims on Foreigners
(including claims held for customers)

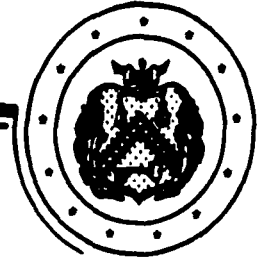
(\$ million)

	<u>Total</u>	<u>Long-Term</u>	<u>Short-Term</u>
1950	-289	-177	-112
1951	-89	-14	-75
1952	-123	-36	-87
1953	261	115	146
1954	-590	-102	-488
1955	-388	-226	-162
1956	-552	-166	-386
1957	-605	-349	-256
1958	-503	-152	-351
1959	-238	-181	-57
1960	-1,148	-153	-995
1961	-1,261	-136	-1,125
1962	-451	-127	-324
1963	-1,535	-754	-781
1964	-2,464	-941	-1,523
1965	93	-232	325
1966	253	337	-84
1967*	-557	206	-763

*First three quarters only, seasonally adjusted.

Source: Commerce Department Press Release, November 16, 1967, and Survey of Current Business, June, 1967.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 18, 1968

FOR IMMEDIATE RELEASE

TREASURY'S MONTHLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$1,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing January 31, 1968, in the amount of \$1,401,412,000, as follows:

274-day bills (to maturity date) to be issued January 31, 1968, in the amount of \$500,000,000, or thereabouts, representing an additional amount of bills dated October 31, 1967, and to mature October 31, 1968, originally issued in the amount of \$1,001,770,000, the additional and original bills to be freely interchangeable.

366-day bills, for \$1,000,000,000, or thereabouts, to be dated January 31, 1968, and to mature January 31, 1969.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Thursday, January 25, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. (Notwithstanding the fact that the one-year bills will run for 366 days, the discount rate will be computed on a bank discount basis of 360 days, as is currently the practice on all issues of Treasury bills.) It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from

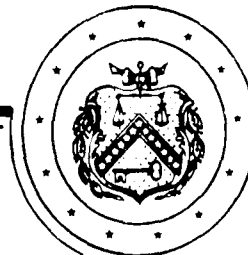
responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on January 31, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing January 31, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 25, 1968

FOR IMMEDIATE RELEASE

TREASURY SECRETARY FOWLER NAMES BLAND W. WORLEY
AS NEW SAVINGS BONDS CHAIRMAN FOR NORTH CAROLINA

Bland W. Worley, Senior Vice President, Wachovia Bank and Trust Company, Greensboro, North Carolina, was today appointed by Treasury Secretary Henry H. Fowler as volunteer State Chairman for the Savings Bonds Program in North Carolina, effective January 25. He succeeds William H. Andrews, Jr., CLU, Jefferson Standard Life Insurance Company, Greensboro.

Mr. Worley is a Director of Blue Bell, Inc., and the Adams-Millis Corporation. He is also a member of the Small Business Committee of the American Bankers Association.

He attended Atlantic Christian College, Wilson, N. C.; received a B. S. Degree from the University of North Carolina in 1938; attended the Graduate School of Banking, Rutgers University, in 1954; and the Executive Program, University of North Carolina, in 1955.

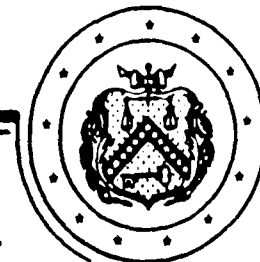
During World War II, he served in the Army in the African and European theaters and was discharged as a Major.

Mr. Worley is a past president and first honorary life member of the Greensboro Chamber of Commerce. His civic activities include posts with the United Fund, Salvation Army, Boy Scouts of America, and Wesley Long Community Hospital. He is a member of the Board of Stewards, West Market Street Methodist Church.

In 1953, he was named Young Man of the Year in High Point, N. C., and in 1959 he was selected Outstanding Young Businessman of North Carolina.

Mr. Worley is married and has three children.

TREASURY DEPARTMENT



WASHINGTON, D.C.

RE RELEASE 6:30 P.M.,
Monday, January 22, 1968.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated October 26, 1967, and one other series to be dated January 25, 1968, which were offered on January 17, 1968, were reopened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

PERCENTAGE OF ACCEPTED NONCOMPETITIVE BIDS:	91-day Treasury bills maturing April 25, 1968		:	182-day Treasury bills maturing July 25, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.728	5.032%	:	97.318 a/	5.305%
Low	98.717	5.076%	:	97.300	5.341%
Average	98.719	5.068% 1/	:	97.303	5.335% 1/

a/ Excepting 1 tender of \$164,000

21% of the amount of 91-day bills bid for at the low price was accepted

1% of the amount of 182-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 29,250,000	\$ 12,813,000	:	\$ 22,708,000	\$ 4,308,000
New York	2,432,910,000	1,142,497,000	:	2,043,229,000	786,395,000
Philadelphia	37,653,000	14,846,000	:	15,096,000	5,136,000
Cleveland	40,395,000	22,848,000	:	44,928,000	23,596,000
Richmond	22,992,000	9,610,000	:	10,093,000	5,093,000
Atlanta	54,187,000	21,173,000	:	28,309,000	10,163,000
Chicago	230,810,000	142,176,000	:	293,327,000	115,038,000
St. Louis	61,037,000	37,137,000	:	40,055,000	13,455,000
Minneapolis	21,692,000	9,092,000	:	18,446,000	3,946,000
Kansas City	27,942,000	19,967,000	:	22,513,000	12,763,000
Dallas	26,030,000	15,130,000	:	19,750,000	9,650,000
San Francisco	232,371,000	56,028,000	:	120,356,000	11,483,000

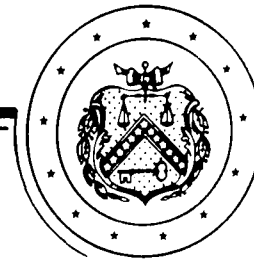
TOTALS \$3,217,269,000 \$1,503,317,000 b/ \$2,678,810,000 \$1,001,026,000 c/

Includes \$254,803,000 noncompetitive tenders accepted at the average price of 98.719

Includes \$138,550,000 noncompetitive tenders accepted at the average price of 97.303

These rates are on a bank discount basis. The equivalent coupon issue yields are 5.22% for the 91-day bills, and 5.57% for the 182-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 21, 1968

FOR IMMEDIATE RELEASE

There have been reports that, during the past week or two, some Canadian subsidiaries of U.S. corporations have been transferring abnormally large amounts of funds from Canada to the U.S. and that these transfers have resulted in some pressure on the Canadian dollar in the exchange market.

The new U.S. balance of payments program does not call for and is not intended to have the effect of causing abnormal transfers of earnings or withdrawals of capital by U.S. companies having investments in Canada. Moreover, the U.S. Government has already made it clear, and now repeats, that Canadian subsidiaries of U.S. corporations are expected to act as good corporate citizens of Canada. The new U.S. balance of payments program covering private capital flows and the Canadian exemption from the Interest Equalization Tax provide scope for continued large flows of capital to Canada.

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F-1140

STATEMENT OF THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
BEFORE THE
HOUSE WAYS AND MEANS COMMITTEE
ON THE PRESIDENT'S FISCAL PROGRAM
MONDAY, JANUARY 22, 1968, at 10:00 A.M.

Mr. Chairman and Members of the Committee:

I appreciate this opportunity at the start of this session to request early enactment of the President's tax recommendations, including a temporary 10 percent surcharge on individual and corporate income taxes. My colleagues and I will try to put these proposals in the perspective of the current situation -- budgetary, economic, and financial.

You are familiar with the tax program itself in view of last year's hearings. Some of the recommended dates have been changed to accommodate to the fact that we are now in 1968.

This tax program is the key part of our fiscal response to a set of major challenges that face our Nation.

In international security affairs we have committed ourselves to repelling Communist aggression in Southeast Asia. Hundreds of thousands of our young men have accepted the burdens of carrying this commitment on the battlefields. It remains for the rest of the population, through the Congress, to accept temporarily increased taxes as the most desirable means of financing a portion of this national effort.

In domestic affairs we have the challenge to government to help meet many problems beyond the scope of individual or private action. Meeting this challenge demands the courage to support cutbacks in government

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expenditures for low priority programs and a willingness to meet the cost of the remaining activities -- in a manner conducive to the maintenance of a stable and strong but well-balanced economy -- in a manner that minimizes the dangers of serious trouble with respect to prices, interest rates, credit availability, and the health of our home-building industry.

In financial affairs we have a national and international responsibility of the highest priority which has grave significance for our economic security and strength and that of the entire free world. It grows out of the role of the dollar in the international monetary system -- as a reserve currency and the principal "transaction" currency of the free world. It is our responsibility under present international monetary conditions, disturbed by the recent devaluation of the British pound and a deterioration in our balance of payments position, to take decisive action to bring our balance of payments to -- or close to -- equilibrium in the year ahead. A tax increase to preserve a stable economy, to protect our trade surplus, and to give the world confidence in our fiscal responsibility in this area, vital to others as to the United States, is the single most important step we can take to fulfill that responsibility.

A proper response to all of these challenges at home and abroad requires that we promptly enact the surcharge legislation.

Developments Since November

Mr. Chairman, the reasons for the surcharge that I gave in August and November have been strengthened by recent developments, particularly developments since we last testified in November. The most significant developments relate to the Federal budget, the balance of payments, the credit markets, and the economic situation.

The Budget and Expenditure Control

When we testified last November, we presented a legislative proposal for reducing obligations below the fiscal year 1968 budget proposals then outstanding. The reduction was to be, for civilian agencies, 2 percent of personnel costs and 10 percent of controllable costs; for defense, it was to be 10 percent of non-Vietnam, new obligation authority.

This measure was enacted by the Congress in December. It is now an operative part of the budgetary situation for fiscal year 1968 and provides a reduced base for fiscal year 1969 projections.

That measure in combination with Congressional action on specific appropriation bills has reduced obligations in fiscal year 1968 by \$10 billion from earlier requested levels. In many cases the reduction of an obligation in 1968 will reduce expenditures in fiscal year 1968. In other cases the expenditure reduction will show up in fiscal year 1969 or later. The expenditure reduction to be achieved in fiscal year 1968 is estimated to be \$4.3 billion.

We have now the dimensions of the President's budget for the fiscal year 1969. Director Schultze will go over these, but I want to bring out some highlights.

The scale of increase in expenditures is less than one-half that of 1967 over 1966 and substantially less than that of 1968 over 1967. The fiscal program provides an increase of budget outlays of fiscal year 1969 over fiscal year 1968 which is less than the expected normal growth in revenues from expansion of the tax base through the rise in GNP. Even if no changes were to be made in existing income and excise tax rates, the budget deficit would thus be lower in fiscal year 1969 than in fiscal year 1968.

But it would not, in the current economic situation, reduce the level of deficit financing to a point consistent with the security and stability of the United States economy.

For this reason it is essential that the Congress enact tax legislation that would increase budget receipts before the end of fiscal year 1968 and maintain this higher level through the fiscal year 1969. The budget deficit for fiscal year 1968 would be reduced by the tax program from \$22.8 billion to \$19.8 billion, and in fiscal year 1969 it would be reduced from \$20.9 billion to \$8 billion.

It is not realistic from a standpoint of timing or amounts to expect to achieve this scale of deficit reduction by cutting expenditures -- as long as military activities at their present level persist in South Vietnam. Outlays in the controllable civilian programs are only slightly higher than the already tight level of 1968, and rise by significantly less than the increase in payments on prior contracts.

Nor is the problem answered by pointing to the increase in budget expenditures in the budget for 1969 over fiscal year 1968 of \$10.4 billion.

Of this total:

- \$3-1/4 billion is for national defense, including the weapons program of the Atomic Energy Commission.
- \$1 billion is for increased interest payments on the public debt.
- \$1-1/2 billion is for the second step of the civilian and military pay increase provided by Act of Congress late last year.
- \$4-3/4 billion is for mandatory payments required by laws passed by the Congress, such as social security, public assistance, and payments to veterans.

The budget will recommend reduction and reforms in various programs which will cut fiscal year 1969 obligations for these programs by almost \$3 billion below the levels appropriated in 1968. Some of the program reductions will be unpopular. The President's fiscal program represents a tough policy, but one which is responsive to important social needs while making the hard decisions to postpone or eliminate some desirable but lower priority items.

We need now to address ourselves to the problem of how to finance this budget. We cannot procrastinate further in a vain hope that a different and substantially lower budget will soon be forthcoming.

Prices and the Economic Outlook

Since our testimony of last November, the economy has developed substantially along the lines that we had predicted at that time. Income has risen sharply, and there has been disturbing price pressure.

The level of unemployment at the end of 1967 was, seasonally adjusted, 3.7 percent and this after an unusually large gain in the civilian labor force of nearly 1.6 million in 1967. In the last half of 1967, however, general prices, as measured by the GNP deflator, rose at the disturbing rate of 3.8 percent a year.

Broadly, one goal of our fiscal program with the tax increase is to hold the growth of demand, that is, the growth of money GNP, to about \$60 billion. As you will see, this will involve some unwelcome price increases. Due to the sharper rise in consumer prices in 1967, it is inevitable that wage increases in 1968 will be somewhat above productivity gains. Thus, somewhat higher prices are in prospect.

Basically, our tax program to check the growth in money demand in 1968 is a matter of assuring that the price increase in 1968 slows down from the rate experienced in the second half of 1967. This will make it possible to move further in the direction of price stability in 1969.

I cannot overemphasize this point. We are not saying merely that a tax increase would be nice because we should have a better price performance than we had in 1967. We are saying more than this, that failure to take action to hold down the growth of money demand in 1968 would lead to a serious, progressive increase in domestic prices. It would lead to larger wage increases, and it would make it still harder to move toward price stability in 1969.

Financial Developments

Let me turn now to developments in domestic financial markets since we last met with this Committee. On balance, financial conditions improved slightly in January, although interest rates at the end of 1967 were extremely high. Both corporate bonds and State and local bonds were yielding rates well above their 1966 highs. The yields on FHA mortgages sold in the secondary market were back to their 1966 highs.

Money and capital markets remain cautious and uncertain. Interest rates and security prices will still gyrate dizzily at apparent changes in the prospects for Congressional tax action. Almost all financial market observers fixed the principal responsibility for the financial pressures in the second half of 1967 on the United States Government's fiscal situation. The prospects of large Federal borrowing in the absence of a tax increase so dominate the financial markets that an investor's outlook at any particular time must be governed by his judgment as to the chance of a tax increase and the prospective Federal deficit. The financial markets received a considerable lift in December on the announcement that this Committee would take up consideration of the tax proposal today.

Then early in January domestic financial conditions were buoyed by two additional elements -- our balance of payments program announced on January 1 -- and press comments suggesting the greater likelihood of peace negotiations with Hanoi.

This market improvement lasted until early last week. Then, interest rates rose sharply again as stories about the possible imminence of peace talks diminished and as our communications media reported somewhat pessimistically on the prospects for a tax increase.

This brief chronology underscores the importance financial markets place on a tax increase. This widespread feeling in financial markets is based on a realistic estimate of the large demands on credit and capital markets -- from private borrowers, State and local governments, and the Federal Government -- that are likely to persist if a tax increase is not enacted. I shall have more to say about likely credit demands in this event later in my remarks.

The Balance of Payments

When we appeared before you on November 29, I said, "Make no mistake about it -- confidence in the dollar and the international monetary system depends on the ability and determination of the United States Government to act responsibly."

Developments in the weeks following the sterling devaluation both before and after the Committee hearings on November 29 and 30 served to place in sharp focus the need for decisive and responsible action on our part. Against the background of a persistent deficit in the United States balance of payments, the British move resulted in a weakening of confidence in currencies and was accompanied by a burst of speculation in the gold markets which led to a loss of over \$1 billion to our gold reserves. In addition, it became evident during this period that our payments position in the fourth quarter had deteriorated sharply, and that for the year as a whole, we would be running a deficit of \$3.5 billion to \$4 billion. The fact that the trade figures for October and November showed a disappointing decline in the trade surplus was quite disturbing. It was clear that new and decisive measures had to be taken to move the United States balance of payments position strongly toward balance.

These measures were announced on January 1 by the President, and you are familiar with them.

In order to give understanding of this Action Program and its importance at this point of time to the people of the United States and peoples everywhere, the Treasury Department issued last week a

report entitled, "Maintaining the Strength of the United States Dollar in a Strong Free World Economy." This document describes in detail the background and reasons for the January 1 Program. It describes what we have done to date and what we propose to do, both over the short and long term, to bring out balance of payments into equilibrium and keep it there, as well as the relationship of this action to the viability of the international monetary system and maintaining confidence in its stability.

The keystone to this balance of payments program is the surcharge proposal you have before you. The other direct measures added in the January 1 Program to the pre-existing effort are like the four fingers of the hand. They cannot be effective in dealing with the problem without the tax proposal which is the thumb, enabling us to get a firm grip on the problem.

As the President said in his January 1 Message:

"The first line of defense of the dollar is the strength of the American economy.

No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus."

The Tax Program

These developments are all in the direction of strengthening our conviction as to the need for a temporary, but substantial, tax increase that would produce, at an annual rate, about \$10 billion. Our program at the rates proposed last August does this, and it also postpones the revenue losses of almost \$3 billion a year that would come from scheduled excise tax reductions. Only the dates have been changed to recognize that we are already in 1968.

Our tax program is this --

- We urge the enactment of a 10 percent surcharge on the income tax of individuals and corporations.
- On individuals the 10 percent surcharge would be effective April 1, 1968, and continue through June 30, 1969. The effective rate on individuals in calendar year 1968 would be 7.5 percent of their present law tax. The surcharge would not apply to about 17 million individuals whose taxable income does not rise above the second bracket.
- On corporations the surcharge would be effective January 1, 1968, and continue through June 30, 1969. This would give an effective rate of 10 percent for corporations in calendar year 1968.
- Corporations should be moved to the same fully current payment basis now applicable to individuals.
- The automobile and telephone excises now scheduled to be reduced April 1 should be extended, at present rates to June 30, 1969.

The specific revenue estimates by fiscal years are given in the following table:

Table 1

Estimated Effect of Proposal on Budget Revenues
(In Millions)

Proposal	: Fiscal year:	Fiscal year
	: 1968	: 1969
Income taxes:		
Proposed surcharge:		
Individual income tax	\$930	\$6,920
Corporation income tax	970	2,880
Acceleration of corporation tax payments	<u>800</u>	<u>400</u>
Subtotal, income tax proposals	2,700	10,200
Excise taxes -- extension of present rates:		
Automobiles	190	1,500
Telephone service	<u>116</u>	<u>1,160</u>
Subtotal, excise extensions	306	2,660
Total revenue under proposals	3,006	12,860

There has been, I think, some confusion as to the magnitude of this surcharge. It is not 10 percent of income; it is 10 percent of the present law tax. In the aggregate Americans pay in Federal individual income taxes about 10 percent of their total income. The surcharge during the 15-month period while it is in effect will be about 1 percent of income.

Another way of putting the size of this surcharge in perspective is to recall that the tax reductions enacted in 1961-65 came to 20 percent of the tax due, or somewhat over 2 percent of the income of Americans. Our proposal is to restore, on a temporary basis, less than half of this cut.

Another way of viewing this surcharge is to look at shares of the national output. In 1963, excluding the largely self-financed social insurance, the trust funds, Federal Government expenditures were about 16 percent of GNP. In 1968, they will be 17 percent even when we include 3 percent for Vietnam. Our total expenditures for other than Vietnam have not grown as fast as the GNP. We are able, therefore, to cover less than half of the war cost out of increased taxes.

As to termination of this surcharge, it will be keyed to our ability to reduce substantially expenditures in Vietnam following a cessation of large scale hostilities. If it occurs before June 30, 1969, the President will recommend early termination of the surcharge.

The Risks of Failure to Act

The issue on any tax increase is not whether we like it or not. Of course we don't like it. The only issue is whether we dislike it as much as we would dislike the consequences of not enacting the tax increase. If you will examine these alternatives with me, you will find the case for a tax increase overwhelming.

I am reminded of the advice of Edmund Burke. On one occasion he incurred the wrath of his constituents in Bristol by his vote on an Irish Shipping Bill. He wrote an open letter to the merchants of Bristol explaining why the bill was really in their interests. He closed with the comment, "I would rather displease my constituents than harm them."

I want to discuss with you the risks that we run through consequences of failure to pass a tax bill. These risks fall in three areas, financial and credit markets, prices and inflation, and the balance of payments.

Financial and Credit Markets

An obvious alternative to a tax increase is tighter credit since high interest rates can curtail demand as does a tax increase although

it curtails the demand of different people. Governor Martin will discuss this consequence with you in greater detail.

I want to emphasize, in the strongest terms, my conviction that it would be a reckless course of action to leave to monetary policy the task of curtailing demand.

Prospects for avoiding strains in money and capital markets in 1968 depend crucially on enactment of the tax increase. Failure to pass the surcharge would mean that the Federal Government would have to continue to tap the securities markets in volume. These Federal demands for funds would be occurring in the context of a more rapid economic expansion in the private sector, which would strengthen the demands for funds by private borrowers. The provision of needed State and local services will also call for larger borrowing by these instrumentalities.

Moreover, in the absence of a tighter fiscal policy, additional monetary restraint would no doubt have to be brought to bear to stem the heightened prospects for accelerating inflation. This would contribute further to upward pressures on market rates of interest. Interest rates on long-term securities would no doubt rise to levels above their recent highs. Shorter term rates might again approach the peaks of 1966.

With this rise in interest rates, and reduced credit availability, some savings institutions and some potential borrowers are bound to get hurt. The net inflows of savings to thrift institutions began to slow in the latter months of 1967 in response to rising interest rates on market securities. Correspondingly, these institutions became increasingly reluctant to continue to commit funds to the mortgage market in the amounts they had earlier.

This trend toward "disintermediation" would step up were market interest rates to rise much further. This would mean that the housing industry undoubtedly again would suffer most, as it usually has when interest rates are high and credit tight. And along with this squeeze in housing credit, one would anticipate a significant curtailment in fund availability to such other borrowers as State and local governments and small businesses.

To refuse to take fiscal action and leave to monetary policy the responsibility for a credit control approach to preventing inflation would be like enacting a special tax that would fall on home buyers, home-builders and suppliers, the savings institutions, State and local governments, and small business -- the groups most affected by credit tightness.

Clearly this is an inequitable alternative to a general tax increase. It will result in an unbalanced pattern of growth. It leaves an inadequate mix of monetary and fiscal policy that is unwelcome to those on this side of the table responsible for both of these elements of economic policy.

Prices and Inflation

There are both limits and risks involved in trying to control inflation through resorting to credit restraint while fiscal stimulus flows from a failure of Congress to enact the surcharge. And the risks are unacceptable if inflation is not restrained in 1968.

I must start with our recent experience with prices. In 1967 we had an appreciable amount of price inflation. Thus the cost of living and the GNP deflator rose about 3 percent. The statistic, however, understates the problem two ways. The overall rise of 3 percent occurred despite generally lower prices for farm goods and for many industrial raw materials. Further, prices rose only a bit over 2 percent in the first half of the year and almost 4 percent in the last of the year. Thus we are going into 1968 with a very fast rate of price increase.

A basic point that I need to stress here is that price changes are closely related to things that have happened in the past. In 1967 wage increases were relatively high in large part due to the price increases that occurred in 1966 and were associated then with rising farm prices. During the first half of 1967 poor market conditions made it impossible to pass on in prices many of the wage increases that were occurring, but these started to be reflected in prices in the last half of the year.

For the first half of 1968 wage settlements will reflect a combination of adjustments to the cost of living increases in 1967 and the completion of multi-stage wage settlements arrived at under long term labor contracts in 1966 and 1967. In addition, farm prices are likely to increase somewhat.

Since we will be at substantially full employment, these wage increases are likely to be passed on in higher prices. In the main, we could say that for the first half of 1968 something like a 3-1/2 percent price increase is nearly assured.

With a tax increase there is every reason to expect that the rate of price increase in the last half of 1968 will be lower than the first half. Under this projection we would be coming out of 1968 with a tapering off of the rate of price increase, and the prospects for moving toward price stability in 1969 would be excellent.

Without a tax increase money demand will continue to grow through the last half of 1968. There will be continuing shortages of labor, particularly skilled labor. These are precisely the circumstances under which we would expect that any cost increases could be passed on and business firms generally would be in a position to raise price margins.

If prices are accelerating at the end of 1968, there will be a lot more at stake than what would appear from the simple statistic that the average price increase for the year was 4 percent rather than 3 percent. What would be at stake is the price pattern in 1969. The

cost of living would be higher and rising. Labor would expect to get wage increases to cover these cost of living increases. The wage increases would push prices up still higher in 1969, and we could be well on the way to a spiralling price inflation.

The risks that we run by tolerating a budget deficit of over \$20 billion for two years in a row and permitting the resulting inflation should be unacceptable.

Balance of Payments

A failure to take this tax action promptly will risk a declining trade surplus. This trade surplus is the mainstay of our balance of payments position. There are both short term and long term dangers to it if there is a failure of fiscal policy.

This short term risk is a flood-tide of imports -- as in late 1965 and 1966 -- induced by an economy running at a very high rate of speed. When our rate of economic growth in money terms expands at a rate of 8 or 9 percent, there is an increased propensity to import. In that situation imports climb relative to our gross national product and our trade surplus evaporates.

As in 1966, excessive increases in income -- especially when we have full employment -- will be quickly translated into higher prices and capacity bottlenecks with a resulting surge in imports and a slow-down in exports. In 1965 and 1966, a period in which GNP growth

exceeded 8 percent per annum, our average rate of growth in imports exceeded 16 percent per annum as compared with 5 percent in 1963 and 9.6 percent in 1964.

Our trade surplus -- the excess of a large amount of exports over almost as large amount of imports -- changes sharply with relatively small changes in imports or exports. If our imports rise 1 percent faster than our exports, we would in one year lose \$300 million of our trade surplus.

The long term threat to our trade surplus to which fiscal action is importantly related is the danger that a continuing spiral of increasing costs and price pressures will undermine the long term competitive position of the United States in markets abroad and at home. With the economy picking up momentum in late 1967 and in 1968, and with cost and price pressures increasing, the risk of no tax increase is for higher prices in 1968 and particularly for a higher rate of price increase toward the end of 1968. The higher money incomes plus the loss of competitive position from rising prices of United States exports could make substantial inroads on our trade surplus.

All other efforts to improve our balance of payments position run the risk of failure unless we avoid the kind of excessive growth that floods us with imports and unless we return to relative price stability and cost competitiveness in the United States economy.

The prompt enactment of the President's tax increase program is the single most important and indispensable step this Nation can take now to improve our balance of trade and payments and protect the dollar and the international monetary system.

The role of the Federal Government in the maintenance of an economic environment in which price and cost stability can be sustained is widely recognized by international financial authorities. The Balance of Payments Adjustment Process Report by Working Party No. 3 of the Organization for Economic Cooperation and Development stated:

"It is agreed that there are certain general principles (or 'rules of prudence') which should be followed by all countries in order to prevent as far as possible the emergence of balance of payments disequilibrium. In the field of demand management, it is agreed that it should be a general object of fiscal and monetary policy to maintain demand at a level which is neither excessive nor deficient, and to promote a continuing expansion of total national expenditure in line with the trend growth rate of productive potential. There is also agreement that, in general, fiscal policy should play a major role in the management of demand."

Over time we must be able to look to our trade surplus to be sufficiently large to finance a large portion of our other expenditures abroad. The sooner we achieve a sustained improvement in our trade surplus, the easier it will be for us to phase out the restrictive measures we have found it necessary to take.

In addition, if it is to be effective, the new balance of payments program requires other nations to make adjustments which in many cases will not be pleasant -- particularly for the surplus countries in

Western Europe where the impact will be sharpest. It will be far easier for them to make these adjustments and not retaliate against our actions, if they know that they are not carrying the whole burden themselves -- but that we, too, are taking difficult measures at home.

Last December the OECD Economic Survey of the U.S. stated:

"An immediate concern of the authorities must be to avoid an excessive increase in demand, which would strengthen cost price pressures and aggravate the balance of payments problem. Given the likely strength of the expansion now developing, this can hardly be achieved without the tightening of fiscal policy proposed by the President."

A United States economist writing for a New York investment counselor last week described the situation as follows:

"The 10 percent tax surcharge has become a symbol of the sincerity of the U.S. Government's determination to defend the dollar. Unless Congress moves promptly to enact the surcharge, Europe will not be impressed with the rest of the balance of payments programs."

This observation squares completely with all the information and impressions we have received through official channels. For example, it was indelibly impressed on Under Secretary Katzenbach and Under Secretary Deming in their recent mission to seven countries to explain the new Balance of Payments Program.

Action on the surcharge is imperative if we are to assure the success of the Balance of Payments Program and maintain the strength of and confidence in the dollar.

Conclusion

Mr. Chairman, one may reasonably ask, however, whether there are risks if we pass the surcharge.

There may be some who say that any increase will halt our economic expansion and push the economy into a stall or even worse. We do not foresee this as a real or substantial risk that is being run. Current and prospective demands are strong. The consensus of private forecasts, which typically have the assumption of a tax increase, agrees on this outlook. If by 1969 things change, both fiscal and monetary policies can be modified. In any event, a new decision will have to be taken since the proposed surcharge is scheduled to expire on June 30, 1969.

There may be some who feel that a temporary tax increase will not remain temporary and that we risk being locked into a higher level of taxation. No one can, of course, say that all things labeled temporary live up to their label. We have had "temporary taxes" that have outlived their "temporary duration." For the surcharge, however, there is solid foundation for confidence in the belief that it will remain temporary.

For one, the surcharge is needed because of hostilities in Vietnam. Its yield is only a portion of those costs. Moreover, the tax reductions of 1964 and 1965, have demonstrated to the country the benefits that flow to our economy and to all in the private sector from the policy of using some portion of the fiscal dividend that comes from economic growth to reduce our level of taxation. This policy will be reinforced at the end of hostilities in Vietnam, which will surely come, by the need to stimulate the private sector to put to peacetime tasks the

resources of men, materials, and facilities that have been used in that effort. Indeed, the enactment of the surcharge now will provide a ready means for a smoother post-Vietnam adjustment through its quick removal.

The clear and present advantages of enacting the tax proposals far outweigh the minimal potential risks involved in taking the action. The prompt enactment of the tax proposal at this session of Congress would:

- Reverse sharply and decisively the trend toward increased deficit financing which began with our increased participation in hostilities in Southeast Asia in the fiscal year 1966.
- Reduce the budget deficits for fiscal years 1968 and 1969 by approximately \$16 billion.
- Take a giant step in providing the confidence and stability in financial markets here and abroad which is based on the strength of the dollar and the United States economy.
- Reduce appreciably the most important source of pressure on our credit markets: the huge over-hang of Federal borrowing which steadily ups interest rates.
- Remove the threat to our housing industry which is in the process of a needed recovery.
- Remove the risk of a credit crunch that will deprive States and local governments and small business of ready access to credit.

- Reverse the trend from a creeping to an accelerating inflation and turn the economy back toward price stability and wage changes more closely related to increased productivity.
- Halt movement toward another disruptive inventory cycle.
- Prevent our returning to the old pattern of "boom and bust."
- Protect, maintain and expand our trade surplus which is the mainstay of our balance of payments position and which is vitally important to the preservation of international confidence in the dollar and the stability of the international monetary system.

Mr. Chairman, I would like to submit for the record a bill incorporating the statutory language to carry out our surcharge proposal and a technical explanation of that bill.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

January 22, 1968

FOR IMMEDIATE RELEASE

Attached is a proposed bill and accompanying technical explanation embodying the recommendations contained in Secretary Fowler's statement today before the House Ways and Means Committee.

Attachment

A BILL

To amend the Internal Revenue Code of 1954 to impose a temporary tax surcharge, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE, ETC.

(a) Short Title.--This Act may be cited as the "Tax Surcharge Act of 1968."

(b) Amendment of 1954 Code.--Except as otherwise expressly provided, whenever in this Act an amendment is expressed in terms of an amendment to a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

SEC. 2. IMPOSITION OF TAX SURCHARGE

(a) In General.--Subchapter A of chapter 1 (relating to determination of tax liability) is amended by inserting at the end thereof the following new part:

"PART V--TAX SURCHARGE
"Sec. 51. Tax Surcharge.

"SEC. 51. TAX SURCHARGE.

"(a) Imposition of Tax.--

"(1) Calendar year taxpayers.--In addition to the other taxes imposed by this chapter and except as provided in subsection (b), there is hereby imposed on the income of every

person whose taxable year is the calendar year, a tax equal to the percent of the adjusted tax (as defined in subsection (c)) for the taxable year specified in the following table:

Calendar Year	Percent	
	Individuals	Corporations
1968	7.5	10.0
1969	5.0	5.0

"(2) Fiscal year taxpayers.--In addition to the other taxes imposed by this chapter and except as provided in subsection (b), in the case of taxable years ending on or after the effective date of the surcharge and beginning before July 1, 1969, there is hereby imposed on the income of every person whose taxable year is other than the calendar year, a tax equal to--

"(A) Ten percent of the adjusted tax for the taxable year, multiplied by

"(B) A fraction, the numerator of which is the number of days in the taxable year occurring on and after the effective date of the surcharge and before July 1, 1969, and the denominator of which is the number of days in the entire taxable year.

"(3) Effective date defined.--For purposes of paragraph (2), the 'effective date of the surcharge' means--

"(A) January 1, 1968, in the case of a corporation, and

"(B) April 1, 1968, in the case of an individual.

"(b) Low Income Exemption.--Subsection (a) shall not apply if the adjusted tax for the taxable year does not exceed--

"(1) \$290, in the case of a joint return of a husband and wife under section 6013,

"(2) \$220, in the case of an individual who is a head of household to whom section 1 (b) applies, or

"(3) \$145, in the case of any other individual (other than an estate or trust).

"(c) Adjusted Tax Defined.--For purposes of this section, the adjusted tax for a taxable year means the tax imposed by this chapter for such taxable year, determined without regard to--

"(1) the taxes imposed by this section, section 871 (a), and section 881; and

"(2) any increases in tax under section 47 (a) (relating to certain dispositions, etc., of section 38 property) or section 614 (c) (4) (C) (relating to increase in tax for deductions under section 615 (a) prior to aggregation), and reduced by an amount equal to the amount of any credit which would be allowable under section 37 (relating to retirement income) if no tax were imposed by this section for such taxable year.

"(d) Authority to Prescribe New Optional Tax Tables.-- The Secretary or his delegate may prescribe regulations setting forth

modified optional tax tables for calendar years 1968 and 1969 computed upon the basis of composite rates incorporating the rate at which tax is imposed by this section. The composite rates so determined may be rounded to the nearest whole percentage point and the tax tables so determined may be rounded to the nearest whole dollar. If the Secretary or his delegate prescribes regulations pursuant to this subsection, then notwithstanding section 144(a), in the case of a taxpayer (whose taxable year is the calendar year) to whom a credit is allowable for 1968 or 1969 under section 37, the standard deduction may be elected for such year regardless of whether the taxpayer elects to pay the tax imposed by section 3.

"(e) Estimated Tax.--For purposes of applying the provisions of this title with respect to declarations and payments of estimated income tax due more than 45 days (15 days in the case of a corporation) after the enactment of this section--

"(1) In the case of a corporation, so much of any tax imposed by this section as is attributable to the tax imposed by section 11 or 1201 (a) or subchapter L shall be treated as a tax imposed by such section 11 or 1201 (a) or subchapter L;

"(2) The term 'tax shown on the return of the individual for the preceding taxable year', as used in section 6654 (d) (1), and the term 'tax shown on the return of the corporation for the preceding taxable year', as used in section 6655 (d) (1), shall mean the tax which would have been shown on such return if tax had been imposed by this section for such preceding taxable year at the rate applicable to the current taxable year.

"(f) Withholding on Wages.--In the case of wages paid after April 1, 1968, and before July 1, 1969, the tax required to be deducted and withheld under section 3402 shall be determined in accordance with the following tables in lieu of the tables set forth in section 3402 (a) or (c)(1).--

Tables to be Used in Lieu of
Tables in Section 3402 (a)
Tables to be Used in Lieu of
Tables in Section 3402 (c)(1)

"(g) Western Hemisphere Trade Corporations and Dividends on Certain Preferred Stock.--In computing, for a taxable year of a corporation, the fraction described in--

"(1) Section 244 (a)(2), relating to deduction with respect to dividends received on the preferred stock of a public utility,

"(2) Section 247 (a)(2), relating to deduction with respect to certain dividends paid by a public utility, or

"(3) Section 922 (2), relating to special deduction for Western Hemisphere trade corporations,

the denominator shall, under regulations prescribed by the Secretary or his delegate, be increased to reflect the rate at which tax is imposed under subsection (a) for such taxable year.

"(h) Special Rule.--For purposes of this title, except as otherwise expressly provided in this section, to the extent the tax imposed by this section is attributable (under regulations prescribed by the Secretary or his delegate) to a tax imposed by another section of this chapter, such tax shall be deemed to be imposed by such other section.

"(i) Shareholders of Regulated Investment Companies.--In computing the amount of tax deemed paid under section 852 (b)(3)(D)(ii) and the adjustment to basis described in section 852 (b)(3)(D)(iii), the percentages set forth therein shall be adjusted under regulations prescribed by the Secretary or his delegate to reflect the rate at which tax is imposed under subsection (a).

(b) Minimum Distributions.--Section 963 (b) (relating to receipt of minimum distributions by domestic corporations) is amended--

(1) by striking out the heading of paragraph (1) and inserting in lieu thereof the following:

"(1) Taxable years beginning in 1963 and taxable years entirely within the surcharge period.--", and

(2) by striking out the heading of paragraph (3) and inserting in lieu thereof the following:

"(3) Taxable years beginning after 1964 (except taxable years which include any part of the surcharge period).--", and

(3) by adding after the table in paragraph (3) the following:

"In the case of a taxable year beginning before the surcharge period and ending within the surcharge period, or beginning within the surcharge period and ending after the close of the surcharge period, the required minimum distribution shall be an amount equal to the sum of--

"(A) that portion of the minimum distribution which would be required if the provisions of paragraph (1) were applicable to the taxable year, which the number of days in such taxable year which are within the surcharge period bears to the total number of days in such taxable year, plus

"(B) that portion of the minimum distribution which would be required if the provisions of paragraph (3) were applicable to such taxable year, which the number of days in such taxable year which are not within the surcharge period bears to the total number of days in such taxable year.

As used in this subsection, the term 'surcharge period' means the period beginning on January 1, 1968, and ending at the close of June 30, 1969."

(c) Clerical Amendment.--The table of parts of subchapter A of chapter 1 is amended by adding at the end thereof the following:

"Part V. Tax Surcharge."

(d) Effective Date.--The amendments made by this section shall apply--

(1) Insofar as they relate to individuals, with respect to taxable years ending after March 31, 1968, and beginning before July 1, 1969.

(2) Insofar as they relate to corporations, with respect to taxable years ending after December 31, 1967, and beginning before July 1, 1969.

SEC. 3 . RAISING FROM 70 PERCENT TO 80 PERCENT THE ESTIMATED TAX WHICH MUST BE PAID IN INSTALLMENTS BY CORPORATIONS.

(a) In General.--Section 6655 (b)(relating to amount of underpayment), and section 6655 (d)(relating to exception), are amended by striking out "70 percent" each place it appears therein and inserting in lieu thereof "80 percent".

(b) Effective Date.--The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1967.

SEC. 4 . PAYMENT OF FIRST \$100,000 OF ESTIMATED TAX.

(a) Requirement of Declaration.--Section 6016 (a) (relating to requirement of declaration of estimated tax in case of corporations) is amended by striking out "\$100,000" and inserting in lieu thereof "\$40".

(b) Reduction of Exclusion from Estimated Tax.--Section 6016 (b) (relating to the definition of estimated tax in the case of a corporation) is amended to read as follows:

"(b) Estimated Tax.--

"(1) Definition.--For purposes of this title, in the case of a corporation, the term 'estimated tax' means the excess of--

"(A) the amount which the corporation estimates as the amount of the income tax imposed by section 11 or 1201 (a), or subchapter L of chapter 1, whichever is applicable, reduced by the amount which the corporation estimates as the sum of any credits against tax provided by part IV of subchapter A of chapter 1, over

"(B) an amount equal to the applicable exclusion percentage (determined under paragraph (2)) multiplied by the lesser of--

"(i) \$100,000, or

"(ii) the amount determined under subparagraph (A).

"(2) Exclusion percentage.--The term 'exclusion percentage' means--

<u>If the declaration is for a taxable year beginning in</u>	<u>The exclusion percentage is</u>
1968	80
1969	60
1970	40
1971	20
1972 or later	0"

(c) Exception from Addition to Tax.--Section 6655 (d)(1) is amended by striking out the phrase "reduced by \$100,000" and inserting in lieu thereof "reduced by an amount equal to the applicable exclusion percentage, determined under section 6016 (b)(2), multiplied by the lesser of \$100,000 or the amount of such tax".

(d) Addition to Tax for Underpayment of Estimated Tax.--Section 6655 (e) (relating to the definition of tax) is amended to read as follows:

"(e) Definition of Tax.--For purposes of subsection(b), (d)(2), and (d)(3), the term 'tax' means the excess of--

"(1) the amount of tax imposed by section 11 or 1201 (a), or subchapter L of chapter 1, whichever is applicable, reduced by the sum of any credits against tax provided by part IV of subchapter A of chapter 1, over

"(2) an amount equal to the applicable exclusion percentage, (determined under section 6016 (b)(2)), multiplied by the lesser of--

"(A) \$100,000, or

"(B) the amount determined in paragraph (1)."

(e) Technical Amendment.--Clause (v) of section 243 (b)(3)(C) is amended by striking out "\$100,000".

(f) Effective Date.--The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1967.

SEC. 5 . POSTPONEMENT OF CERTAIN EXCISE TAX RATE REDUCTIONS.

(a) Passenger Automobiles.--

(1) In general.--Subparagraph (A) of section 4061 (a)(2) (relating to imposition of tax) is amended to read as follows:

"(A) Articles enumerated in subparagraph (B) are taxable at whichever of the following rates is applicable:

"7 percent for the period March 16, 1966, through June 30, 1969.

"2 percent for the period July 1, 1969, through December 31, 1969

"1 percent for the period after December 31, 1969."

(2) Conforming amendments.--Section 6412 (a)(1) (relating to floor stocks refunds on passenger automobiles, etc.) is amended by striking out "April 1, 1968, or January 1, 1969" and inserting in lieu thereof "July 1, 1969, or January 1, 1970".

(b) Communication Services.--Section 4251 (relating to tax on communications) is amended--

(1) By striking out subsection (a)(2) and inserting in lieu thereof:

"(2) The rate of tax referred to in paragraph (1) is as follows:

"Amounts paid pursuant
to bills first rendered -- Percent

"Before July 1, 1969 10
"After June 30, 1969, and
before January 1, 1970 1"

(2) By striking out subsection (b) and inserting in lieu thereof:

"(b) Termination of Tax.--The tax imposed by subsection (a) shall not apply to amounts paid pursuant to bills first rendered on or after January 1, 1970."

(3) By striking out subsection (c) and inserting in lieu thereof:

"(c) Special Rule.--For purposes of subsection (a), in the case of communications services rendered before May 1, 1969, for which a bill has not been rendered before July 1, 1969, a bill shall be treated as having been first rendered on June 30, 1969. For purposes of subsections (a) and (b), in the case of communications services rendered after April 30, 1969, and before November 1, 1969, for which a bill has not been rendered before January 1, 1970, a bill shall be treated as having been first rendered on December 31, 1969."

(c) Effective Date.--The amendments made by this section shall be effective on the date of enactment of this Act.

TECHNICAL EXPLANATION
TAX SURCHARGE ACT OF 1968

This bill, which is entitled the "Tax Surcharge Act of 1968", has four substantive sections:

(a) Section 2 imposes a temporary surcharge on both individual and corporate income tax liabilities at an annual rate of ten percent.

(b) Section 3 raises from 70 percent to 80 percent, the percent of its estimated tax which a corporation may pay by installments without incurring a penalty.

(c) Section 4 eliminates, over a five-year period, the \$100,000 estimated tax exemption presently granted corporations.

(d) Section 5 suspends the schedule for the reduction of the excise taxes on passenger automobiles and telephone service during the period of the temporary surcharge.

There follows a more detailed description of each of these provisions.

SEC. 2. TAX SURCHARGE.

(a) Imposition of tax. Subsection (a) of section 2 adds a new part to subchapter A of chapter 1 of the Internal Revenue Code which consists of a new section 51 imposing a temporary tax surcharge on corporations and individuals.

General Provisions. Subsection (a) of the new section 51 provides for the imposition of the surcharge. The tax is at an annual rate of ten percent of tax liability (adjusted as provided in section 51(c)) and is effective from January 1, 1968, through June 30, 1969, for corporations and from April 1, 1968 through June 30, 1969, for individuals. For taxpayers who report their income on a calendar year basis, the rate of the surcharge for the calendar years involved is as follows:

<u>Calendar Year</u>	<u>Rate of Tax</u>	
	<u>Individuals</u>	<u>Corporations</u>
1968	7.5%	10%
1969	5%	5%

In the case of taxpayers who report their income on a fiscal year basis, the rate will be ten percent for years falling entirely within the effective dates, whereas, in the case of taxable years that straddle either the commencement or termination date, the tax will be prorated depending on the number of days in the taxable year falling within the period the tax is in effect.

Low income exemption. Subsection (b) of the new section 51 provides an exemption from the surcharge for individuals (other

than estates and trusts) whose tax does not exceed that generally applicable to the first two brackets of taxable income. More specifically, the surcharge will not apply to a husband and wife filing a joint return if their tax does not exceed \$290. It will not apply to a head of household whose tax does not exceed \$220, or to a single individual (or a married individual filing a separate return) whose tax does not exceed \$145. In the case of a head of household, the exemption level is determined on the basis of the tax applicable to \$1,500 of taxable income which is midway between the first two tax brackets of a single individual and the first two tax brackets of a married couple filing a joint return.

Tax base on which surcharge is computed. Subsection (c) of the new section 51 provides that the surcharge shall be computed as a percentage of the tax otherwise imposed by chapter 1 of the Internal Revenue Code, with the exception that it shall not be imposed (1) with respect to the 30 percent tax under sections 871(a) and 881 on non-resident alien individuals and foreign corporations receiving income not effectively connected with a business in the United States, or (2) with respect to any increases in tax under section 47(a) (relating to certain dispositions of section 38 property) and section 614(c)(4)(C) (relating to deductions taken under section 615(a) prior to aggregation). In the case of an elderly person who is eligible for the retirement income credit, the surcharge will be computed as a percentage of his tax liability after subtracting his retirement income credit. Similarly, tax liability shall be reduced by the retirement income credit in determining whether such an individual is eligible for the low income exemption. This treatment is afforded the retirement income credit

in order to give it the same effect on the surcharge as the exclusion for social security benefits. Tax liability would not be reduced by any other credits in computing the amount of the surcharge. On the other hand, once the surcharge has been computed, it may be offset by credits to which the taxpayer is entitled and which are not absorbed by his regular tax liability.

Authority to prescribe new optional tax tables.

Subsection

(d) of the new section 51 provides that the Secretary of the Treasury or his delegate may prescribe regulations setting forth modified optional tax tables computed on the basis of composite rates incorporating the surcharge. The tables may be rounded to the nearest whole dollar, and the composite rates to the nearest whole percentage point.

The usual rule that a taxpayer with less than \$5,000 of income may take the standard deduction only if he uses the optional tax tables will be waived in the case of a taxpayer who is eligible for the retirement income credit. This special rule is to reflect the fact that the effect of the retirement income credit on the surcharge cannot be accurately incorporated into the optional tax tables, with the result that those claiming the retirement income credit will almost universally use the regular tax

computation. Under these circumstances, without the special rule, most taxpayers claiming the retirement income credit would be precluded from using the standard deduction.

Estimated tax. Subsection (e) of the new section 51 contains provisions conforming the estimated tax provisions to the new surcharge tax. Under present law, corporations are required to pay estimated tax only with respect to taxes imposed by section 11 or 1201 (a) or subchapter L (relating to insurance companies). The new subsection (e) (1) provides that any surcharge that is attributable to a tax imposed under these sections or subchapter shall, for estimated tax purposes, be treated as a tax imposed under these sections or subchapter and, therefore, subject to estimated tax payments. Paragraph (2) of the new subsection (e) provides that, in the case of the option under which individuals and corporations may pay their estimated tax on the basis of their prior year's tax liability, their prior year's liability shall be adjusted to reflect the surcharge tax at the rate for the current year.

Under the provisions of the new subsection (e), corporations would be required to reflect the surcharge in their first estimated tax payment due more than 15 days after the bill is enacted. For individuals, the surcharge would have to be reflected in the first estimated tax payment due more than 45 days after the enactment of the bill. Fiscal year taxpayers will spread the surcharge ratably over the number of installments remaining in their taxable year. Thus, a corporation with a November 30 fiscal year would reflect the surcharge for its taxable year ending November 30, 1968 in three equal installments on May 15, August 15, and November 15.

New withholding tables. Subsection (f) of the new section 51 will set forth new tables for computing the amount of income taxes to be withheld from wages paid on or after April 1, 1968, and before July 1, 1969. These tables will reflect an increase in the withholding rates of ten percent.

Western Hemisphere Trade Corporations and dividends on certain preferred stock. The following two provisions of the Internal

Revenue Code provide a special deduction with respect to certain income which has the effect of reducing the corporate tax rate applicable to that income by 14 percentage points. These provisions are:

(1) Section 922, relating to the taxable income of Western Hemisphere Trade Corporations; and

(2) Section 247, relating to dividends paid by a public utility on its preferred stock.

Section 244 provides a reciprocal deduction with respect to amounts received as dividends on certain preferred stock of a public utility. In order to maintain the 14 percentage point differential under these sections, subsection (g) of the new section 51 provides that the computation shall be adjusted, under regulations prescribed by the Secretary of the Treasury or his delegate, to reflect in the regular corporate tax rate the surcharge imposed under the new section 51.

Special rules. Subsections (h) and (i) of the new section 51 insure that, under regulations to be prescribed by the Secretary, the surcharge interacts properly with other tax-imposing sections of the Code. Thus, for example, these subsections insure that the provisions of sections 72(n)(3) and 1378(b) (relating to reduction of taxes by certain credits), sections 815(b)(2)(B) and 815(c)(3)(B) (relating to adjustments to the shareholders and policyholders surplus accounts), sections 535(b)(1), 545(b)(1), and 556(b)(1) (relating to adjustments for taxes of personal holding companies), section 852(b)(3)(D)(ii) and (iii) (relating to treatment of undistributed capital gain by shareholders of regulated investment companies), section 1361(a) and (h) (relating to unincorporated business enterprises electing to be taxed as

domestic corporations), sections 1373(c), 1375(a)(3) and 1378 (relating to subchapter S corporations), and sections 515 and 841 (relating to the credit for foreign taxes) will properly reflect the application of the surcharge. (This list is not intended to be exhaustive.)

(b) Minimum distributions by foreign subsidiaries. Subsection (b) of section 2 of the bill amends section 963(b) (relating to receipt of minimum distributions by domestic corporations from their foreign subsidiaries) to provide for the use of a minimum distribution table reflecting the surcharge. The table is to be used for taxable years all or part of which fall within the surcharge period. It is the same table that was applicable for taxable years beginning in 1963 when the corporate tax rate was 52 percent (the present corporate tax rate including the additional surcharge is 52.8 percent). In the case of taxpayers with taxable years falling only in part within the surcharge period, the 52 percent minimum distribution table is to be used on a pro rata basis.

(c) Clerical amendment. Subsection (c) of section 2 of the bill makes a clerical amendment to reflect the addition of the new Part V imposing the surcharge.

(d) Effective date. Subsection (d) of section 2 of the bill provides the effective dates for the surcharge. These dates are explained in the discussion under subsection (a) of section 2 of the bill.

SEC. 3. INCREASE FROM 70-80 PERCENT THE AMOUNT OF ESTIMATED TAX WHICH CORPORATIONS MUST PAY IN INSTALLMENTS.

Under present law, a corporation is not penalized for an underpayment of estimated tax if its payments equal or exceed those which would be required on the basis of estimated tax liability of 70 percent of actual tax liability (less \$100,000). Section 3 of the bill amends section 6655 to raise the 70 percent figure to 80 percent. This conforms the percentage for corporations to that made applicable to individuals beginning in 1967. This change would be effective for taxable years beginning after December 31, 1967.

SEC. 4. PAYMENT OF FIRST \$100,000 OF ESTIMATED TAX.

Under present law, corporations are required to make estimated tax payments only with respect to their estimated tax liability in

excess of \$100,000. They are not required to make any estimated tax payments on their first \$100,000 of estimated tax liability and, if their annual estimated tax liability is \$100,000 or less, they are not required to file a declaration. Under section 4 of the bill, the \$100,000 exclusion would be repealed over a five year period.

More specifically, subsection (a) of section 4 of the bill would amend section 6016 (a) to require a corporation to file a declaration of estimated tax for a taxable year if it can reasonably be expected that its tax liability for the year (after taking into account credits) will exceed \$40. As indicated above, the present exemption level is \$100,000.

Subsection (b) of section 4 of the bill amends section 6016(b) to provide a new definition of "estimated tax" (which is the basic amount subject to payment by installment) reflecting the removal of the existing \$100,000 exemption over a five year period. During the transition period, a corporation, in determining the amount of its estimated tax liability, would be permitted to exclude an amount equal to the applicable "exclusion percentage" multiplied by the lesser of (1) \$100,000, or (2) the amount which the corporation estimates as its income tax for the year less the estimated amount of its credits. The revised subsection (b) of section 6016 would define the term "exclusion percentage" as follows:

If the declaration is for a year beginning in-	The "exclusion percentage" is-
1968	80
1969	60
1970	40
1971	20

In the case of taxable years beginning after 1971, there would be no special exemption.

As an example of the transition rule, a corporation which estimates its income tax less credits for 1968 to be \$80,000 would be entitled to an estimated tax exclusion of \$64,000 for 1968; 80 percent (its exclusion percentage) times \$80,000. Its estimated tax liability would, therefore, be \$16,000. If the corporation estimates its income tax less credits for 1968 to be \$120,000, its estimated tax exclusion would be \$80,000 (80 percent times \$100,000) and its estimated tax liability would be \$40,000.

Subsection (d) of section 4 of the bill amends section 6655(e) to reflect the repeal of the \$100,000 exemption in the provisions for determining whether, and if so, to what extent, an addition to the tax should be imposed for underpayment of estimated tax. The same transitional rules apply. Thus, for example, assume a corporation's tax return for the taxable year ending December 31, 1968, indicates an income tax liability of \$150,000. To utilize the exception provided in section 6655 (d)(1) permitting estimated tax payments to be based on the prior year's tax, such corporation would be required to pay for 1969 an estimated tax of \$90,000, computed as follows:

1968 Income Tax Liability	\$150,000
Less: \$60,000; 60 percent (the exclusion percentage for 1969) times \$100,000	<u>60,000</u> <u>\$ 90,000</u>

Subsection (e) of section 4 of the bill amends section 243 (b)(3)(C) (relating to estimated tax exemption for members of an affiliated group) to reflect the repeal of the \$100,000 exemption.

Subsection (f) of section 4 of the bill provides that the amendments made by this section shall apply to estimated tax payments for taxable years beginning after December 31, 1967.

SEC. 5. POSTPONEMENT OF CERTAIN EXCISE TAX RATE REDUCTIONS.

(a) Passenger Automobiles. Under present law, an excise tax of 7 percent of the selling price is imposed on the sale by the manufacturer, producer, or importer of passenger automobiles. This rate is scheduled to be reduced to 2 percent on April 1, 1968, then to 1 percent after December 31, 1968.

Subsection (a) of section 5 of the bill suspends this schedule of reductions for the period during which the temporary surcharge will be in effect. Thus, the present 7 percent rate will remain in effect until July 1, 1969. A rate of 2 percent will apply to sales between July 1, 1969 and December 31, 1969, with a 1 percent rate

applying to all sales after December 31, 1969. Conforming amendments are made so that floor stocks refunds will apply on the corresponding date of each reduction.

(b) Communication Services. Under present law, an excise tax of 10 percent is imposed on amounts paid for local and long distance telephone service (including teletypewriter service). A reduction of the rate to 1 percent is scheduled to apply to amounts paid pursuant to bills rendered on or after April 1, 1968, with the tax scheduled to terminate entirely as to bills rendered on or after January 1, 1969.

Subsection (b) of section 5 of the bill suspends this schedule of reductions for the period during which the temporary surcharge will be in effect. Thus, the present 10 percent rate will continue to apply until July 1, 1969, at which time the scheduled reduction to 1 percent will take effect. The tax will terminate on January 1, 1970. A conforming amendment makes corresponding changes in the dates applicable under the special rules established under present law to adjust for billing practices.

(c) Effective Date. Subsection (c) of section 5 of the bill provides that the amendments made by this section shall apply as of the date of enactment of the bill.

STATEMENT OF THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
BEFORE THE
HOUSE BANKING AND CURRENCY COMMITTEE
ON LEGISLATION TO REMOVE THE GOLD COVER
TUESDAY, JANUARY 23, 1968, at 9:30 A.M.

Mr. Chairman and Members of the Committee:

I am grateful to you for the opportunity to appear promptly to support the President's recommendation for removal of the gold cover.

On December 15, 1967 the Honorable Wilbur Mills, Chairman of the Ways and Means Committee announced that his Committee would reconvene on January 22 to continue its consideration of the President's surcharge proposals. Chairman Martin and I were alerted to stand by to appear before the Committee on that date, and we accepted the invitation of Chairman Mills.

The Committee will convene at 10 o'clock this morning, and Chairman Martin and I must be there at that time. With the Committee's permission, we will both read our statements for the record and then ask Under Secretary Barr and Governor Robertson, Vice Chairman of the Federal Reserve Board, to answer your questions.

I have assured the Chairman that in the event the Committee feels that it would be desirable after this morning's

session to question Chairman Martin and me directly, then we will be available to come back to this Committee on either January 31 or February 1.

The legislation before you would eliminate the 25% gold reserve requirement from Federal Reserve notes and the \$156 million reserve held against U. S. notes and Treasury notes of 1890.

The Administration believes that prompt action to remove the cover requirement is necessary for three principal reasons:

- Prospective normal increases in currency holdings
- Federal Reserve notes -- by the public will "lock up" more and more of our "free" gold and soon reach a point inhibiting further expansion of our pocket cash. Obviously we cannot tolerate such a situation.
- There should be no doubt whatsoever that our total gold stock is available to insure the free international convertibility between the dollar and gold at the fixed price of \$35 an ounce.
- The world knows as a fact that the strength of the dollar depends upon the strength of the U. S. economy rather than upon a legal 25 percent reserve requirement against Federal Reserve notes, and it is clearly appropriate for this fact now to be recognized in legislation.

Despite these facts, the gold reserve requirement against Federal Reserve notes, instituted at a time when gold circulated freely in the domestic economy, is still part of our law. It should be removed.

The need for prompt removal is apparent from a look at the simple arithmetic of the problem.

The U. S. gold stock is now at \$12 billion -- the cover requirement is approximately \$10.7 billion -- the balance remaining is \$1.3 billion.

The normal increase in notes will absorb over \$500 million annually and a further \$150 million or more will be absorbed each year for domestic artistic and industrial purposes. These two factors taken together mean that about \$700 million a year of our free gold will be absorbed for domestic reasons. There is thus but two years grace at most even if one assumes that no gold at all will be needed for international purposes. Clearly we cannot proceed on such an assumption.

* * *

Since the passage of the Federal Reserve Act more than a half century ago, the function of gold in our monetary system has undergone a fundamental transformation. Gold no longer circulates freely as domestic currency in any major

country in the world. We Americans have not used gold as domestic currency since 1934. Gold belongs in a nation's international reserves. The dollar serves as a reserve currency to the world; the United States' gold supply is available to convert dollars held by national monetary authorities at a fixed price. As such, it is one cornerstone of our international monetary system.

Today, the strength of the dollar is not a function of this legal tie to gold -- a tie which is only applicable to one portion of our total money supply, Federal Reserve notes. The value of the dollar -- whether it be in the form of a bank balance, a coin, or "folding money" -- is dependent on the quantity and quality of goods and services which it can purchase. It is the strength and soundness of the American economy which stands behind the dollar. Balanced growth at home and a strong competitive position internationally give the dollar we use as everyday pocket money its strength.

An expanding United States economy needs an expanding supply of currency. Our main form of currency is Federal Reserve notes. In the years ahead, we can expect increases in Federal Reserve note circulation of about \$2 billion a year. This growth is a normal response to the public's demand for cash in a growing economy. It is basically a

trend development, reflecting a growing population, a growing economy, and a growing number of transactions.

Not to move on the cover requirement at this time would only mean putting off the inevitable. We cannot afford to permit an outmoded provision of our law to impinge on the nation's supply of pocket money.

Removal of this requirement is also of key importance from the viewpoint of the role of the dollar and of gold in the international monetary system. Today, that system relies primarily on gold and dollars -- interchangeable into gold at \$35 an ounce -- as its international reserves. Tomorrow these two key factors will need help from a third -- the new international reserve asset created under multilateral agreement in the International Monetary Fund -- but gold and dollars will continue to play a vital role in the international monetary system.

If this system, which has served us so well in the past, is to continue to facilitate the growth of world trade and prosperity, we must assure that confidence in the system and in the strength of the dollar is maintained. This requires action on four fronts:

- We must continue the long-standing United States' policy of maintaining the gold-dollar relationship at \$35 per ounce. This must not be open to question, and the best way to make continuation of that policy crystal clear is to free our entire gold stock for that purpose.
- We must assure that the U. S. economy grows in an environment of cost and price stability through enactment of the anti-inflation tax and through expenditure controls and appropriate monetary policy.
- We must achieve sustained equilibrium in our balance of payments.
- We and the rest of the free world must put into place the plan for the creation of a new reserve asset agreed upon in Rio last September.

Our policy of maintaining the fixed relationship between gold and the dollar at \$35 an ounce for legitimate monetary purposes is one of the reasons why virtually all countries hold dollars in their reserves and why many of them hold very large amounts of dollars. In addition, of course,

countries hold dollars because, unlike gold, they can invest them in interest earning assets.

The monetary authorities of most of the major industrialized countries understand full well that the link between gold and domestic currencies is no longer a pertinent and relevant fact and that gold is an international asset. Only three other major countries still maintain some link between their domestic currencies and gold. While foreign authorities are aware of the fact that the Federal Reserve can suspend the cover requirement, they find it difficult to understand why the United States, the world's major reserve currency country, still maintains this legal impediment to the free international use of gold.

Thus, legislative action on the cover requirement, by making it clear to the world that the congress as well as the executive branch are committing our total gold stock to international use, is necessary to maintain confidence in the dollar.

Removal of the gold cover will not solve the United States' balance of payments problem nor is it a substitute for the solution of that problem.

The need to achieve sustained equilibrium in our international payments position is essential to confidence in the dollar and the future stability of the international monetary system. The series of measures announced by the President on January 1, with which you are all familiar, are designed to bring us to, or close to, equilibrium this year. It is vital that they be successful. I ask, Mr. Chairman, that the President's message be made a part of the record of these hearings.

Conclusion

I urge you to act promptly on the gold cover legislation before you in order that, domestically, we can continue to be assured that the Federal Reserve will be able to supply appropriate amounts of currency to meet the needs of our growing economy for cash and in order that our policy of maintaining the gold-dollar relationship -- one of the major elements of confidence in the dollar and the international monetary system -- will not be open to question.

MESSAGE TO THE NATION
ON THE BALANCE OF PAYMENTS

JAN 1 1968

Where We Stand Today

I want to discuss with the American people a subject of vital concern to the economic health and well-being of this Nation and the Free World.

It is our international balance of payments position.

The strength of our dollar depends on the strength of that position.

The soundness of the Free World monetary system, which rests largely on the dollar, also depends on the strength of that position.

To the average citizen, the balance of payments, and the strength of the dollar and of the international monetary system, are meaningless phrases. They seem to have little relevance to our daily lives. Yet their consequences touch us all -- consumer and captain of industry, worker, farmer, and financier.

More than ever before, the economy of each nation is today deeply intertwined with that of every other. A vast network of world trade and financial transactions ties us all together. The prosperity of every economy rests on that of every other.

More than ever before, this is one world -- in economic affairs as in every other way.

Your job, the prosperity of your farm or business, depends directly or indirectly on what happens in Europe, Asia, Latin America, or Africa.

The health of the international economic system rests on a sound international money in the same way as the health of our domestic economy rests on a sound domestic money. Today, our domestic money -- the U.S. dollar -- is also the money most used in international transactions. That

money can be sound at home -- as it surely is -- yet can be in trouble abroad -- as it now threatens to become.

In the final analysis its strength abroad depends on our earning abroad about as many dollars as we send abroad.

U. S. dollars flow from these shores for many reasons -- to pay for imports and travel, to finance loans and investments and to maintain our lines of defense around the world.

When that outflow is greater than our earnings and credits from foreign nations, a deficit results in our international accounts.

For 17 of the last 18 years we have had such deficits. For a time those deficits were needed to help the world recover from the ravages of World War II. They could be tolerated by the United States and welcomed by the rest of the world. They distributed more equitably the world's monetary gold reserves and supplemented them with dollars.

Once recovery was assured, however, large deficits were no longer needed and indeed began to threaten the strength of the dollar. Since 1961 your government has worked to reduce that deficit.

By the middle of the decade, we could see signs of success. Our annual deficit had been reduced two-thirds -- from \$3.9 billion in 1960 to \$1.3 billion in 1965.

In 1966, because of our increased responsibility to arm and supply our men in Southeast Asia, progress was interrupted, with the deficit remaining at the same level as 1965 -- about \$1.3 billion.

In 1967, progress was reversed for a number of reasons:

- Our costs for Vietnam increased further.
- Private loans and investments abroad increased.
- Our trade surplus, although larger than 1966, did not rise as much as we had expected.
- Americans spent more on travel abroad.

Added to these factors was the uncertainty and unrest surrounding the devaluation of the British pound. This event strained the international monetary system. It sharply increased our balance of payments deficit and our gold sales in the last quarter of 1967.

The Problem

Preliminary reports indicate that these conditions may result in a 1967 balance of payments deficit in the area of \$3.5 to \$4 billion -- the highest since 1960. Although some factors affecting our deficit will be more favorable in 1968, my advisors and I are convinced that we must act to bring about a decisive improvement.

We cannot tolerate a deficit that could threaten the stability of the international monetary system -- of which the U.S. dollar is the bulwark.

We cannot tolerate a deficit that could endanger the strength of the entire Free World economy, and thereby threaten our unprecedented prosperity at home.

A Time for Action

The time has now come for decisive action designed to bring our balance of payments to -- or close to -- equilibrium in the year ahead.

The need for action is a national and international responsibility of the highest priority.

I am proposing a program which will meet this critical need, and at the same time satisfy four essential conditions:

- Sustain the growth, strength and prosperity of our own economy.
- Allow us to continue to meet our international responsibilities in defense of freedom, in promoting world trade, and in encouraging economic growth in the developing countries.
- Engage the cooperation of other free nations, whose stake in a sound international monetary system is no less compelling than our own.

- Recognize the special obligation of those nations with balance of payments surpluses, to bring their payments into equilibrium.

The First Order of Business

The first line of defense of the dollar is the strength of the American economy.

No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus.

No challenge before business and labor is more urgent than this: To exercise the utmost responsibility in their wage-price decisions, which at home and affect so directly our competitive position/in world markets.

I have directed the Secretaries of Commerce and Labor, and the Chairman of the Council of Economic Advisers to work with leaders of business and labor to make more effective our voluntary program of wage-price restraint.

I have also instructed the Secretaries of Commerce and Labor to work with unions and companies to prevent our exports from being reduced or our imports increased by crippling work stoppages in the year ahead.

A sure way to instill confidence in our dollar -- both here and abroad -- is through these actions.

The New Program

But we must go beyond this, and take action to deal directly with the balance of payments deficit.

Some of the elements in the program I propose will have a temporary but immediate effect. Others will be of longer range.

All are necessary to assure confidence in the American dollar.

1. Direct Investment

Over the past three years, American business has cooperated with the government in a voluntary program to moderate the flow of U. S. dollars into foreign investments. Business leaders who have participated so wholeheartedly deserve the appreciation of their country.

But the savings now required in foreign investment outlays are clearly beyond the reach of any voluntary program. This is the unanimous view of all my economic and financial advisers and the Chairman of the Federal Reserve Board.

To reduce our balance of payments deficit by at least \$1 billion in 1968 from the estimated 1967 level, I am invoking my authority under the Banking Laws to establish a mandatory program that will restrain direct investment abroad.

This program will be effective immediately. It will insure success and guarantee fairness among American business firms with overseas investments.

The program will be administered by the Department of Commerce, and will operate as follows:

- As in the voluntary program, over-all and individual company targets will be set. Authorizations to exceed these targets will be issued only in exceptional circumstances.
- New direct investment outflows to countries in continental western Europe and other developed nations not heavily dependent on our capital will be stopped in 1968. Problems arising from work already in process or commitments under binding contracts will receive special consideration.
- New net investments in other developed countries will be limited to 65% of the 1965-66 average.
- New net investments in the developing countries will be limited to 110% of the 1965-66 average.

This program also requires businesses to continue to bring back foreign earnings to the United States in line with their own 1964-66 practices.

In addition, I have directed the Secretary of the Treasury to explore with the Chairmen of the House Ways and Means Committee and Senate Finance Committee legislative proposals to induce or encourage the repatriation of accumulated earnings by U. S. -owned foreign businesses.

2. Lending by Financial Institutions

To reduce the balance of payments deficit by at least another \$500 million, I have requested and authorized the Federal Reserve Board to tighten its program restraining foreign lending by banks and other financial institutions.

Chairman Martin has assured me that this reduction can be achieved:

- without harming the financing of our exports;
- primarily out of credits to developed countries without jeopardizing the availability of funds to the rest of the world.

Chairman Martin believes that this objective can be met through continued cooperation by the financial community. At the request of the Chairman, however, I have given the Federal Reserve Board standby authority to invoke mandatory controls, should such controls become desirable or necessary.

3. Travel Abroad

Our travel deficit this year will exceed \$2 billion. To reduce this deficit by \$500 million:

- I am asking the American people to defer for the next two years all nonessential travel outside the Western Hemisphere.
- I am asking the Secretary of the Treasury to explore with the appropriate Congressional committees legislation to help achieve this objective.

4. Government Expenditures Overseas

We cannot forego our essential commitments abroad, on which America's security and survival depend.

Nevertheless, we must take every step to reduce their impact on our balance of payments without endangering our security.

Recently, we have reached important agreements with some of our NATO partners to lessen the balance of payments cost of deploying American forces on the Continent -- troops necessarily stationed there for the common defense of all.

Over the past three years, a stringent program has saved billions of dollars in foreign exchange.

I am convinced that much more can be done. I believe we should set as our target avoiding a drain of another \$500 million on our balance of payments.

To this end, I am taking three steps.

First, I have directed the Secretary of State to initiate prompt negotiations with our NATO allies to minimize the foreign exchange costs of keeping our troops in Europe. Our allies can help in a number of ways, including:

- The purchase in the U. S. of more of their defense needs.
- Investments in long-term United States securities.

I have also directed the Secretaries of State, Treasury and Defense to find similar ways of dealing with this problem in other parts of the world.

Second, I have instructed the Director of the Budget to find ways of reducing the numbers of American civilians working overseas.

Third, I have instructed the Secretary of Defense to find ways to reduce further the foreign exchange impact of personal spending by U. S. forces and their dependents in Europe.

Long-Term Measures

5. Export Increases

American exports provide an important source of earnings for our businessmen and jobs for our workers.

They are the cornerstone of our balance of payments position.

Last year we sold abroad \$30 billion worth of American goods.

What we now need is a long-range systematic program to stimulate the flow of the products of our factories and farms into overseas markets.

We must begin now.

Some of the steps require legislation:

I shall ask the Congress to support an intensified five year, \$200 million Commerce Department program to promote the sale of American goods overseas.

I shall also ask the Congress to earmark \$500 million of the Export-Import Bank authorization to:

- Provide better export insurance.
- Expand guarantees for export financing.
- Broaden the scope of Government financing of our exports.

Other measures require no legislation.

I have today directed the Secretary of Commerce to begin a Joint Export Association program. Through these Associations, we will provide direct financial support to American corporations joining together to sell abroad.

And finally, the Export-Import Bank -- through a more liberal rediscount system -- will encourage banks across the Nation to help firms increase their exports.

6 Nontariff Barriers

In the Kennedy Round, we climaxed three decades of intensive effort to achieve the greatest reduction in tariff barriers in all the history of trade negotiations. Trade liberalization remains the basic policy of the United States.

We must now look beyond the great success of the Kennedy Round to the problems of nontariff barriers that pose a continued threat to the growth of world trade and to our competitive position.

American commerce is at a disadvantage because of the tax systems of some of our trading partners. Some nations give across-the-board tax rebates on exports which leave their ports and impose special border tax charges on our goods entering their country.

International rules govern these special taxes under the General Agreement on Tariffs and Trade. These rules must be adjusted to expand international trade further.

In keeping with the principles of cooperation and consultation on common problems, I have initiated discussions at a high level with our friends abroad on these critical matters -- particularly those nations with balance of payments surpluses.

These discussions will examine proposals for prompt cooperative action among all parties to minimize the disadvantages to our trade which arise from differences among national tax systems.

We are also preparing legislative measures in this area whose scope and nature will depend upon the outcome of these consultations.

Through these means we are determined to achieve a substantial improvement in our trade surplus over the coming years. In the year immediately ahead, we expect to realize an improvement of \$500 million.

7. Foreign Investment and Travel in U.S.

We can encourage the flow of foreign funds to our shores in two other ways:

- First, by an intensified program to attract greater foreign investment in U. S. Corporate securities, carrying out the principles of the Foreign Investors Tax Act of 1966.
- Second, by a program to attract more visitors to this land. A Special Task Force headed by Robert McKinney of Santa Fe, New Mexico, is already at work on measures to accomplish this. I have directed the Task Force to report within 45 days on the immediate measures that can be taken, and to make its long-term recommendations within 90 days.

Meeting the World's Reserve Needs

Our movement toward balance will curb the flow of dollars into international reserves. It will therefore be vital to speed up plans for the creation of new reserves -- the Special Drawing Rights -- in the International Monetary Fund. These new reserves will be a welcome companion to gold and dollars, and will strengthen the gold exchange standard. The dollar will remain convertible into gold at \$35 an ounce, and our full gold stock will back that commitment.

A Time for Responsibility

The program I have outlined is a program of action.

It is a program which will preserve confidence in the dollar, both at home and abroad.

The U. S. dollar has wrought the greatest economic miracles of modern times.

It stimulated the resurgence of a war-ruined Europe.

It has helped to bring new strength and life to the developing world.

It has underwritten unprecedented prosperity for the American people, who are now in the 83d month of sustained economic growth.

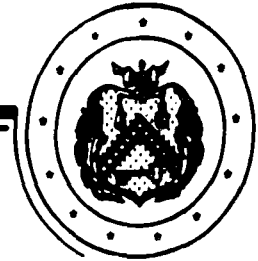
A strong dollar protects and preserves the prosperity of businessman and banker, worker and farmer -- here and overseas.

The action program I have outlined in this message will keep the dollar strong. It will fulfill our responsibilities to the American people and to the Free World.

I appeal to all of our citizens to join me in this very necessary and laudable effort to preserve our country's financial strength.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

January 24, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing February 1, 1968, in the amount of \$2,501,430,000, as follows:

91-day bills (to maturity date) to be issued February 1, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated November 2, 1967, and to mature May 2, 1968, originally issued in the amount of \$999,896,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated February 1, 1968, and to mature August 1, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Monday, January 29, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on February 1, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing February 1, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 25, 1968

FOR RELEASE A.M. NEWSPAPERS
FRIDAY, JANUARY 26, 1968

TREASURY ISSUES REGULATORY CHANGES PERMITTING MARKETING OF NEW TYPE WHISKEY

The Treasury Department today issued regulatory changes which will permit the marketing of a new type whiskey to be produced in the United States.

The new type whiskey, like most imported Scotch, Canadian and Irish whiskies, will be distilled in a relatively high-proof range and stored in used oak containers. It will be known as "light whiskey."

Under the new regulations, members of the domestic distilling industry will be able to market the new type whiskey after July 1, 1972.

Under existing regulations administered by the Internal Revenue Service, the principal American type whiskies, such as bourbon and rye, must be matured in charred new oak barrels. Canadian, Scotch and Irish whiskies are aged primarily in used oak barrels and are generally lighter in flavor than the American types.

In recognition of a growing trend of American consumers toward lighter alcoholic products, several domestic distillers requested that Treasury regulations be amended to permit aging of domestic whiskey in used barrels, and distillation at higher proofs, in order to produce a lighter product which could compete with the imported whiskies.

The views of the distillers and other interested parties were presented to the Internal Revenue Service in formal hearings last September.

The Treasury Department, after careful study, found that it would not be in the best interest of consumers to alter the present requirements for producing those traditional

American type whiskies labeled as "bourbon," "rye," or "straight," since the whiskey produced under the proposed new methods would not have the characteristics which consumers have associated with traditional American types of whiskies for more than 30 years.

However, the Treasury also concluded that the regulations should not operate to prevent the domestic production of a lighter whiskey, intended to meet consumer demand and compete effectively with imported products.

In order to permit the marketing of a lighter type domestically-produced whiskey, while at the same time preserving the long-established standards of identity for the present American-type whiskies, the Treasury regulations have been revised by defining a new standard for a new type of domestic whiskey which will be known as "light whiskey."

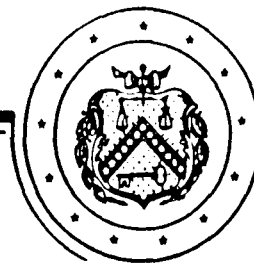
The word "light" describes the distinguishing character of the whiskey and provides the consumer with information to differentiate it from other domestic products. The new product must be distilled at a relatively high proof and stored in used oak containers.

In the interest of equity among members of the domestic distilling industry the new regulations will apply only to whiskey produced subsequent to today's announcement. The Treasury Department also established an effective date of July 1, 1972, for the marketing of the new product. This will provide all distillers a reasonable period for initial aging of the new type whiskey on an equal basis.

The regulations governing the production and sale of alcoholic beverages in the United States are within the jurisdiction of the United States Treasury Department and are administered by the Alcohol and Tobacco Tax Division of the Internal Revenue Service.

The amendments announced today were approved by Stanley S. Surrey, Assistant Treasury Secretary for Tax Policy and Sheldon S. Cohen, Commissioner of Internal Revenue. They are published, together with findings and conclusions on the issues involved, in the Federal Register dated January 26, 1968.

TREASURY DEPARTMENT



RELEASE 6:30 P.M.,
Friday, January 25, 1968.

WASHINGTON, D.C.

RESULTS OF TREASURY'S MONTHLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated October 31, 1967, and the other series to be dated January 31, 1968, which were offered on January 18, 1968, were accepted at the Federal Reserve Banks today. Tenders were invited for \$500,000,000, or thereabouts, of 274-day bills and for \$1,000,000,000, or thereabouts, of 366-day bills. The details of the two series are as follows:

TYPE OF ACCEPTED COMPETITIVE BIDS:	274-day Treasury bills maturing October 31, 1968		:	366-day Treasury bills maturing January 31, 1969	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	96.028	5.219%	:	94.685 <u>a/</u>	5.228%
Low	95.970	5.295%	:	94.576	5.335%
Average	96.001	5.254% <u>1/</u>	:	94.645	5.267% <u>1/</u>

a/ Excepting 1 tender of \$200,000

7% of the amount of 274-day bills bid for at the low price was accepted

12% of the amount of 366-day bills bid for at the low price was accepted

APPLIED TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 522,000	\$ 522,000	:	\$ 30,605,000	\$ 20,605,000
New York	969,608,000	409,848,000	:	1,251,162,000	755,162,000
Philadelphia	4,640,000	640,000	:	10,127,000	2,127,000
Cleveland	20,724,000	15,724,000	:	29,735,000	20,335,000
Richmond	600,000	600,000	:	7,381,000	7,381,000
Atlanta	11,354,000	1,424,000	:	12,816,000	4,056,000
Chicago	114,747,000	44,757,000	:	147,348,000	93,348,000
St. Louis	7,530,000	1,330,000	:	10,710,000	8,710,000
Minneapolis	12,130,000	11,630,000	:	12,740,000	12,740,000
Kansas City	2,380,000	2,380,000	:	8,283,000	8,283,000
Dallas	11,230,000	3,300,000	:	12,100,000	7,100,000
San Francisco	53,765,000	8,015,000	:	71,167,000	60,167,000

TOTALS \$1,209,230,000 \$ 500,170,000 b/ \$1,604,174,000 \$1,000,014,000 c/

Includes \$14,798,000 noncompetitive tenders accepted at the average price of 96.001
 Includes \$43,711,000 noncompetitive tenders accepted at the average price of 94.645
 These rates are on a bank discount basis. The equivalent coupon issue yields are
 5.51% for the 274-day bills, and 5.58% for the 366-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 26, 1968

FOR IMMEDIATE RELEASE

TREASURY TO INVESTIGATE COMPLAINT OF SUBSIDIES ON CANNED TOMATO PRODUCTS FROM ITALY

The Treasury Department announced today that it is issuing a notice of countervailing duty proceeding with respect to imports of canned tomatoes and tomato concentrates from Italy.

The notice, which will be published in the Federal Register of Saturday, January 27, reports that the Treasury is investigating a complaint of subsidization of canned tomato product exports to the United States from Italy. The amount of the subsidy is stated to be 15 to 18 percent of invoice value.

The complainant was Cannery League of California, San Francisco, California.

Under the United States Countervailing Duty Law, if the Treasury Department finds that a "bounty or grant" (within the meaning of the law) is being paid, it is required to assess an equivalent countervailing duty.

The notice of countervailing duty proceeding allows 30 days for submission of data, views, and arguments concerning the existence or nonexistence and the net amount of a bounty or grant.

Canned tomato paste and sauce exports from Italy to the United States totaled more than 22 million pounds during the first 10 months of 1967 and were valued at approximately \$3,700,000. Canned tomato exports from Italy to the United States during this period totaled some 80 million pounds valued at approximately \$6,900,000.

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TREASURY DEPARTMENT
Washington

FOR IMMEDIATE RELEASE

REMARKS BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
AT THE
ANNUAL HARVARD-YALE-PRINCETON CLUBS LUNCHEON
WILLARD HOTEL, WASHINGTON, D. C.,
DELIVERED THURSDAY, JANUARY 25, 1968, 1:00 P.M., EST

The New Year is a fitting time for decisions. This is true not only of individuals but also nations. It is particularly true of the decisions we must make this New Year's period about the U. S. economy and, because of its special role, the economy of the Free World as well.

For the past twenty years, fueled by a strong U. S. economy and a strong U. S. dollar in a viable international monetary system, the Free World has made the greatest strides in trade and development in recorded history. For the past seven years the U. S. economy has enjoyed the longest and strongest and most stable economic expansion in our history.

The decisions the nation is taking in the early weeks of this new year will have much to do with the preservation of that viable international monetary system and that expanding, stable U. S. economy on which it depends.

It is highly important therefore that the nation takes these decisions responsibly -- not avoiding the hard and difficult choices -- not ducking the disagreeable measures -- not waiting for the problems to become unmanageable.

If we do so, we can preserve for many years to come a healthy prosperity and the social and economic progress it makes possible.

Now I realize that preservation of anything is not glamorous or exciting. Indeed, it seems from reading a recent poll by Mr. Gallup that the average American either is taking prosperity for granted or feels a little guilty about enjoying it.

The record-breaking, stable expansion we have experienced during the last seven years has not occurred by accident. It has been made possible by taking decisions to promote the kind of environment in which it can thrive.

This is not a one-way street. When unemployment is high and production low, the environment must be one of encouragement to greater economic activity -- such as the tax reductions of 1962, 1964 and 1965. But prosperity, like many other enjoyable experiences, can develop its own excesses.

The principal excess is running at a rate of speed which puts pressure on resources of labor, materials and plant and results in inflation, imbalances in various sectors of the economy and, if unrestrained, leads to the inevitable bust of the old familiar boom and bust cycle. Thus, when economic activity threatens to accelerate too fast, we must have the courage to hold down public expenditures and raise taxes temporarily -- to use appropriate monetary restraint in the creation of money and credit -- to exercise the utmost responsibility in wage and price decisions which added cost-push inflation to that induced by demand -- to take whatever action is required to preserve the stability of the economy.

It would be a wonderful thing if we could, during the present period of economic pressures, enlarge many of our worthwhile programs for education, health, the war on poverty, desirable public works, and so forth. And yet, as wonderful as these steps would be, they are not as vital as the maintenance of a stable sustained expansion which will keep making all of these things possible, along with more jobs, more wealth and a higher standard of living. Better education and training will mean little if we are pushed into an expansion-wrecking inflation; greater wealth in the extra mileage of highway and buildings which are sought should be compared to the potential loss which can be caused by a decline in economic activity and expansion accompanying a recession.

But holding down the level of desirable and worthwhile expenditures is not enough. Nor is it sufficient to rely entirely on the Federal Reserve System to use high interest rates and tight money as a restraint. We must also have the courage and wisdom to raise taxes and thereby siphon off a potential excess of private demand when this becomes necessary insurance for the preservation of economic stability.

The stake we all have in a stable prosperity transcends our desires as individuals -- as taxpayers, to avoid tax increases -- as investors, to avoid curbs on investment abroad -- as parents and educators, to expand our school systems -- even to press on to the maximum in the war on poverty.

A healthy and stable economy is a prerequisite to almost all of our aspirations whether they be economic, social or cultural.

That is why it is vital in this new year to adapt the policies and to make decisions -- no matter how hard or difficult and unpopular -- rather than to have a relapse back into the recession and inflation-ridden eras that quite a few in this room still can recall.

A strong, stable U.S. economy is the base for a strong dollar, which is the bulwark of our international monetary system.

It has helped bring the greatest economic miracles of all times.

It has not only underwritten unprecedented prosperity for the people of the United States, but it has helped bring back a war-torn Europe and Japan to share that prosperity along with our near neighbors on this continent.

The strong dollar is helping to bring new life and strength and hope to the developing world of Asia, Africa and Latin America. The strength of the Free World economy and the functioning of the international monetary system depend to a large extent on a stable level of economic activity and growth in the United States and the maintenance of a stable dollar -- stable in terms of prices and of exchange rates.

The devaluation of the British pound last November resulted in a loss of confidence in currencies all over the world. It was accompanied by a large international flow of foreign funds seeking safety and a burst of speculative buying of gold. This was a threat not only to the dollar but to the international monetary system as a whole. While the speculation was repulsed by the international financial cooperation of the members of the so-called gold pool, it has underlined the urgency of placing the dollar in an impregnable position.

This means that the time has come when it is necessary and desirable to take decisive measures to eliminate the chronic U.S. balance of payments deficit. While we brought this deficit down, for a brief period in 1965, to the point of equilibrium, and held it at a tolerable point during 1966 despite the increase drain of the war in Southeast Asia, there has been an intolerable deterioration in the wake of the financial crisis accompanying the devaluation of the British pound -- the reserve currency other than the dollar which is widely held.

So, as we in the United States look back upon seven years of relatively stable and satisfactory economic growth at home and 20 years of unprecedented economic progress in the Free World, we find that the new year presents the inescapable challenge to deal decisively with two deficits -- the intolerable deficit in our international balance of payments and a deficit in our national budget of a magnitude that is a highly stimulative factor in an economy already running at an excessive rate of speed accompanied by an unacceptable rate of inflation.

In this new year, the battle of the deficits is on, and fundamental decisions have been and are being taken.

On New Year's Day, the President, in his Balance of Payments message, said:

"The first line of defense of the dollar is the strength of the American economy.

"No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus."

In his New Year's Day message the President also announced a number of measures designed to reduce directly the balance of payments deficit -- measures which are admittedly unwelcome and temporary -- restrictions upon direct investments abroad by American business, a tightening of lending by banks and other financial institutions abroad, a request that Americans

defer non-essential travel outside this hemisphere. In addition, he set in motion new efforts to reduce sharply the balance of payments impact of U.S. Government expenditures overseas for security and development, either by reducing those expenditures or neutralizing their balance of payments effects. The President also directed his representatives to seek to reduce non-tariff barriers that inhibit the development of an adequate U.S. trade surplus and to seek fairer treatment, through negotiation for U.S. goods and services which put our commerce at an unfair disadvantage.

A drastic reduction in our balance of payments deficit is necessary at this time to defend the dollar and insure against a breakdown of the international monetary system. The President's Action Program will achieve this. The Program will entail sacrifices in this country and it will cause difficulties for some foreign countries. In order to assure a fair sharing of these sacrifices, the Program has been widely spread over all sectors of the U.S. economy. In order to minimize adverse effects on the world economy, the Program distinguishes among groups of countries on the basis of their ability to absorb reductions in their foreign exchange receipts. That is in keeping with the agreed philosophy of the balance of payments adjustment process agreed upon for some years between the United States and the principal financial countries whose chronic surpluses must be narrowed if our deficits are to be closed.

The Action Program is designed to deal with an emergency. We do not regard certain aspects of it as consistent with the long-range solution to our underlying balance of payments problem. Restrictive measures are temporary. They are not consistent with the long-term policy of the U.S. which is to support the unrestricted flow of goods, services and capital under a stable international monetary system based on fixed values of currencies defined in terms of gold or the dollar, linked at \$35 an ounce.

An appropriate long-range balance of payments solution for the United States must be based on a substantial and growing surplus in trade and services, including earnings from U.S. foreign investments. The present trade surplus is too small. It must be increased substantially through an expansion of U.S. exports. The Government is taking measures to encourage exports.

The United States is working hard to encourage foreign investment in the U.S. It believes that a building of a two-way flow of portfolio investment into the U.S. from abroad is an important element in the long-term flow of funds which will always include substantial exports of capital from the United States.

The U.S. believes, and the Action Program embodies the concept, that the best long-term solution to the so-called deficit is to increase foreign travel in the United States, and a task force of eminent and informed citizens is hard at work designing plans and programs to facilitate foreign travel in the United States by the private sector working in cooperation with Federal, state and local governments.

But let me emphasize that these direct measures, temporary or long-term, announced in the New Year's Day program, adding to the pre-existing effort, are like the four fingers of a hand. They cannot be effective in dealing with the problem without fiscal restraint, which means the tax bill, which is the thumb enabling us to get a firm grip on the problem.

For all our efforts, direct and otherwise, to improve our balance of payments position, run the risk of failure unless we avoid the kind of excessive growth that floods us with imports, and unless we return to relative price stability and cost competitiveness in the U.S. economy which assures a strong dollar.

The prompt enactment of the President's tax increase program, which has been pending for five months before the Congress, is the single most important and indispensable step this nation can take to insure the achievement of its economic objectives and preserve the expansion and the international monetary system.

That is why the President in his State of the Union Message said, and I quote:

"There are clouds on the horizon. Prices are rising. Interest rates have passed the peak of 1966: and if there is continued inaction on the tax bill they will climb even higher, and I warn the Congress and the nation tonight that this failure to act on the tax bill will sweep us into an accelerating spiral of price increases; a slump in home building; and a continued erosion of the American dollar and this would be a tragedy for every American family."

This is not just the President's view or that of his advisers and the unanimous Federal Reserve Board. This need for a temporary surcharge of ten percent on personal and corporate income taxes -- which average, for the individual, to about one cent on the dollar earned -- is supported by the overwhelming majority of the nation's leading economists, and the country's principal business, financial and labor leaders.

Another way of putting the size of this surcharge in perspective is to recall that the tax reductions enacted in 1961 to 1965 came to 20 percent of the tax due, or somewhat over two percent of the income of Americans. Our proposal is to restore, on a temporary basis, less than half of this cut.

The termination of the surcharge is keyed to our ability to reduce substantially expenditures in Vietnam following a cessation of large scale hostilities. If this occurs before June 30, 1969, the President will recommend an early end of this tax.

On Monday, the Congress will be presented a budget which does include substantial expenditure reductions in 1968, which does represent a tight hold-down in expenditures in 1969, which does devote the requested tax increase to deficit reduction -- not to rising expenditures -- and which does assure that the tax increase is truly temporary, needed only so long as the fighting in Vietnam requires it.

There are those who have maintained for months that the medicine prescribed for the patient is more than he can take

They say tax increases will halt our economic expansion and push the economy into a stall or perhaps worse. There are those who fear that "temporary" means permanent and that the surcharge will become a permanent factor of the Federal tax structure. But given the specific termination, the circumstances and setting of the tax and the need for measures of tax reduction in the wake of cessation of hostilities to stimulate the economy to utilize the resources released by the coming of peace, give assurance that this tax will be temporary.

We are now approaching a period of critical national decision on a very fundamental issue involving the future of the U.S. economy and the world monetary system of which it is a part.

The issue has been roundly debated for five months since the President recommended the proposal last August. It has been examined carefully in hearings on three occasions. Let us look back over the course of the discussion of this issue and see what has happened.

Last year there were some who doubted the economic forecast and were not sure the economy would rise after the slow start in 1967. The economy has risen by \$32.5 billion in the second half of 1967 in contrast with only \$13 billion in the first half.

Last year there were some who doubted there would be an inflationary trend in the absence of a tax increase -- it is clear that we are in a rising price trend, with consumer prices rising at a rate of four percent in the second half of 1967.

Last year we said that our balance of payments position, especially after the British devaluation, would be serious without a tax increase -- it did become serious, we lost a billion dollars in gold, and we had to resort to a new and restrictive program with respect to our balance of payments.

Last year many wanted the 1968 budget expenditures reduced and there was talk of \$5 billion in this area -- the fiscal year 1968 budget has been reduced, with the reductions coming close to \$4.5 billion.

Last year many urged that the 1969 budget increase be held to not more than the rate of increase in the 1967 budget over the 1966 budget -- this has been done, and 1969 budget expenditures, however defined, will rise at a lower rate in 1969 than in 1968 or 1967.

Many wanted us to restrict new programs -- this has been done. They wanted us to cut back existing programs this year -- this has been done.

In all this process we must remember that time is running -- we have already lost \$4.5 billion of the requested tax increase and thus have lost the opportunity to reduce the deficit and the need for Federal borrowing by that amount.

Of course we can debate at length whether the increases in existing programs in the 1969 budget should have been as high as \$3 billion, even though these increases were offset by reductions in other programs. But we must remember as we keep debating that time is still running -- the tax program now comes to \$16 billion over the fiscal years 1968 and 1969 and will reduce the deficit by that amount. I do not see how any amount of discussion can produce a change in the budget expenditures remotely near that figure.

The issue, then, on any tax increase, is not whether we like it or not. Of course we don't like it. The issue on the President's action on various controversial measures on the President's balance of payments program announced on January 1 is not whether we like them or not. Of course we don't like tax increases or restrictive measures on the way we spend our money abroad. The issue is whether we dislike these as much as we would dislike the consequences of not reducing and holding down expenditures, increasing taxes and taking direct measures to curb the outflow of our dollars, while better, longer-term, solutions are being brought to bear upon the international monetary situation.

One often hears the comment that old age is very unwelcome, but the alternative is worse.

So it is with the tax increase and the balance of payments measures if you examine the alternative to a failure to take these actions.

Those of us in public service have a grave and unusual responsibility in dealing with this type of situation.

President Johnson did not like to recommend a tax increase or to exercise the sharp budgetary restraints that characterize the present spending program. But he acted as he had to act in face of a dangerous deficit, rising interest rates and the threat of unacceptable inflationary pressures.

Since that time, the responsible leaders of business, labor, and finance -- who don't like to recommend harmful measures for their constituents and stockholders -- have joined in the President's recommendation. The professional economist -- who is paid to be right more often than he is wrong -- evaluates the economic climate most carefully before he goes down the line for a tax increase. In a way all of these have as much to lose from making a wrong judgment on this question as a member of Congress.

But now the issues presented ultimately will be resolved either by the action or inaction of the Congress.

I can only hope that their decision will be that of the great Edmund Burke, who dealt with an issue not to the liking of a group of his constituents, with the following comment: "I would rather displease my constituents than harm them." It is my sincere conviction that that is the unhappy choice facing the country and the Congress today.

FOR RELEASE AT 12:00 NOON (EST) MONDAY, JANUARY 29, 1968

(THERE SHOULD BE NO PREMATURE RELEASE OF THIS
MATERIAL NOR SHOULD ANY OF ITS CONTENTS
BE PARAPHRASED, ALLUDED TO,
OR HINTED AT IN EARLIER STORIES)

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STATEMENT BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
AT THE PRESS BRIEFING ON FISCAL YEAR 1969 BUDGET
SATURDAY, JANUARY 27, 10:00 A.M. (EST)
AT THE NEW FEDERAL OFFICE BUILDING

The new budget makes plain for all to see that the early adoption of the President's tax increase proposals is a necessary and indispensable element in a sound financial plan for the next 18 months.

Fiscal responsibility is incompatible with back-to-back budget deficits in fiscal 1968 and 1969 exceeding \$20 billion. The early passage of the tax increase proposals is the only way in which these deficits can be reduced in a meaningful measure.

Paying additional taxes is not pleasant to ask of the American taxpayer. But it is necessary if we are going to raise the revenues to pay our bills without excessive borrowing.

Passage of the tax program would produce an additional \$16 billion in revenue over the next 18 months and reduce the deficits for the fiscal years 1968 and 1969 by that total amount -- reducing the current fiscal year deficit from \$22.8 billion to \$19.8 billion and the fiscal year 1969 deficit from \$20.9 billion to \$8 billion.

No amount of discussion and debate is going to produce changes in budget expenditures remotely near those figures.

Therefore, the alternatives are clear -- either accept these dangerous and intolerable deficits over the next 18 months or pass the tax proposals in this budget.

Failure to enact the tax increases proposed, thereby allowing these clearly excessive budgetary deficits to go uncorrected, is to risk fueling a boom that will produce a bust. Already, our deficits and a high rate of expansion are contributing to an unacceptable acceleration of price increases, causing the highest interest rates in 40 years and leading to further credit stringency, and triggering a deterioration in our trade surplus which is very damaging to our balance of payments position.

Unless we put our fiscal affairs in order by the enactment of the President's tax increase proposals, we shall be unable to deal effectively with these problems. We will thereby jeopardize the record breaking seven-year steady and stable expansion in our economy and the 20-year operation of a sound international monetary system that has brought the greatest era of world trade and development in history.

A thorough examination of the budget will reveal that it incorporates a policy of austerity on the expenditure side.

Reduction of the deficits to manageable levels calls for a combination of restraint on expenditures and increased revenues. To reflect this combination called for initially by the President's tax message last August 3, 1967, the budget reflects the joint economy efforts of the President and the Congress in the closing months of the last session. These resulted in nearly \$10 billion of reduced appropriations and \$4.3 billion of reduced expenditures in fiscal 1968.

Moreover, the 1969 budget represents no net increase in controllable civilian program levels, with all increases offset by decreases. This financial plan incorporates national

priorities which have made it necessary to cut back or hold back many programs below desirable levels in order to make room for a few selected increases in very high priority activities.

The increase in the total budget for 1969 over the previous year is far less than the increases in expenditures in 1968 or 1967 over previous years. The total rise of \$10-1/2 billion in projected spending is completely accounted for by higher expenditures for defense, obligatory interest on the public debt, and mandatory payments acquired by recently enacted laws dealing with social security, public assistance, veterans benefits and Federal pay increases.

Increased revenues to be derived in fiscal 1969 from the increased scale of economic activity will be sufficient to more than fund these inescapable increases in expenditures. The total yield from increased taxes would go to a reduction in the deficit, thereby avoiding the fear of many that increased taxes would only go to fund increased expenditures rather than contribute to a declining deficit.

The budget reveals that even with the projected increase in expenditures, but without the proposed tax rise, the deficit

would be considerably less than the \$26 billion of special expenses of Vietnam. This fact gives assurance that the tax increase need only be temporary and can be terminated when a cessation of the hostilities in Southeast Asia relieves the budget pressures from that conflict.

Even with the projected austerity in expenditures and the proposed tax hike, there will still be strong pressures on the economy. An adequate fiscal program, including both expenditure restraint and increased taxes, is necessary to support our security efforts in Asia, keep our economy strong and stable, reverse the trend toward a spiraling inflation, improve our balance of payments, and still provide for some increase in our efforts to improve substantially the plight of our disadvantaged citizens.

In conclusion, this budget presents the issue of an increase in taxes in an unavoidable context. A decision will be taken either by action or inaction. The budget frames it squarely.

Let us review what has happened to the arguments against the President's tax increase proposals.

Last year there were some who doubted the economic forecast and were not sure the economy would rise after the slow start in 1967. The economy has risen by \$32.5 billion in the second half of 1967 in contrast with only \$13 billion in the first half.

Last year there were some who doubted there would be an inflationary trend in the absence of a tax increase -- it is clear that we are in a rising price trend, with consumer prices rising at a rate of four percent in the second half of 1967.

Last year we said that our balance of payments position, especially after the British devaluation, would be serious without a tax increase -- it did become serious, we lost a billion dollars in gold, and we had to resort to a new and restrictive program with respect to our balance of payments.

Last year many wanted the 1968 budget expenditures reduced and there was talk of \$5 billion in this area -- the fiscal year 1968 budget has been reduced, with the reductions coming close to \$4.5 billion. But the deficit is still running at around \$20 billion.

Last year many urged that the 1969 budget increase be held to not more than the rate of increase in the 1967 budget

over the 1966 budget -- this has been done, and 1969 budget expenditures, however defined, will rise at a lower rate in 1969 than in 1968 or 1967.

Many wanted us to restrict new programs -- this has been done. They wanted us to cut back existing programs this year -- this has been done.

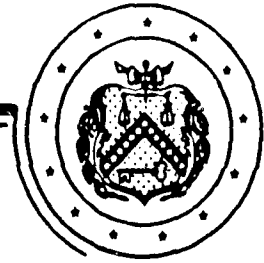
In all this process we must remember that time is running -- we have already lost \$4.5 billion of the requested tax increase and thus have lost the opportunity to reduce the deficit and the need for Federal borrowing by that amount.

Of course there can be unending debate about whether expenditures have been cut enough or too much -- whether additional cuts can or will be made -- whether the proposed cuts can or will be adopted -- whether additional outlays to those proposed in the budget ought to be included in our scale of national priorities. This debate will rage throughout this session of Congress and thereafter into the active political campaigns of this fall, only to be resumed once again next January.

Whatever the outcome of this debate on expenditures, the decision to increase taxes and thereby take \$16 billion

off these back-to-back \$20 billion deficits cannot be put off much longer. It will be taken by affirmative action on the President's tax proposals as proposed or in amended form or simply by failure to act. That is the first and decisive issue presented by the President's budget.

TREASURY DEPARTMENT



WASHINGTON, D.C.

RELEASE 6:30 P.M.,
January 29, 1968.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated November 2, 1967, and another series to be dated February 1, 1968, which were offered on January 24, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$10,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

TYPE OF ACCEPTED TENDER TENDERS:	91-day Treasury bills maturing May 2, 1968		:	182-day Treasury bills maturing August 1, 1968	
	Price	Approx. Equiv. Annual Rate		Price	Approx. Equiv. Annual Rate
High	98.783 a/	4.815%	:	97.515 b/	4.915%
Low	98.767	4.878%	:	97.478	4.989%
Average	98.775	4.846% 1/	:	97.494	4.957% 1/

a/ Excepting 1 tender of \$1,515,000; b/ Excepting 2 tenders totaling \$343,000
57% of the amount of 91-day bills bid for at the low price was accepted
87% of the amount of 182-day bills bid for at the low price was accepted

TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 26,999,000	\$ 12,089,000	:	\$ 7,883,000	\$ 7,883,000
New York	1,873,766,000	1,096,416,000	:	1,474,689,000	738,909,000
Philadelphia	25,649,000	13,591,000	:	16,254,000	8,254,000
Cleveland	31,630,000	31,244,000	:	28,748,000	19,748,000
Richmond	21,069,000	11,069,000	:	10,772,000	6,772,000
Santa	42,986,000	34,236,000	:	30,791,000	20,776,000
Chicago	210,196,000	138,046,000	:	160,038,000	80,998,000
St. Louis	61,008,000	51,849,000	:	39,056,000	33,749,000
Minneapolis	23,405,000	15,548,000	:	17,469,000	9,469,000
Kansas City	27,018,000	23,018,000	:	16,467,000	12,337,000
Dallas	22,407,000	15,407,000	:	19,364,000	14,364,000
San Francisco	103,718,000	57,693,000	:	96,603,000	46,793,000

TOTALS \$2,469,851,000 \$1,500,206,000 c/ \$1,918,134,000 \$1,000,052,000 d/

Includes \$244,389,000 noncompetitive tenders accepted at the average price of 98.775
Includes \$130,119,000 noncompetitive tenders accepted at the average price of 97.494
These rates are on a bank discount basis. The equivalent coupon issue yields are 4.99% for the 91-day bills, and 5.17% for the 182-day bills.

STATEMENT OF THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
BEFORE THE
SENATE BANKING AND CURRENCY COMMITTEE
ON LEGISLATION TO REMOVE THE GOLD COVER
TUESDAY, JANUARY 30, 1968, at 10:00 A.M.

Mr. Chairman and Members of the Committee:

I am grateful to you for the opportunity to appear before you promptly in support of the President's recommendation for removal of the gold cover.

The legislation before you would eliminate the 25% gold reserve requirement from Federal Reserve notes and the \$156 million reserve held against U. S. notes and Treasury notes of 1890.

The Administration believes that prompt action to remove the cover requirement is necessary for three principal reasons:

- Prospective normal increases in currency holdings
- Federal Reserve notes -- by the public will "lock up" more and more of our "free" gold and soon reach a point inhibiting further expansion of our pocket cash, one portion of our domestic money supply. Obviously we cannot tolerate such a situation.
- There should be no doubt whatsoever that our total gold stock is available to insure the free international convertibility between the dollar and gold at the fixed price of \$35 an ounce.

-- The world knows as a fact that the strength of the dollar depends upon the strength of the U. S. economy rather than upon a legal 25 percent reserve requirement against Federal Reserve notes, and it is clearly appropriate for this fact now to be recognized in legislation.

Despite these facts, the gold reserve requirement against Federal Reserve notes, instituted at a time when gold circulated freely in the domestic economy, is still part of our law. It should be removed.

The need for prompt removal is apparent from a look at the simple arithmetic of the problem.

The U. S. gold stock is now at \$12 billion
-- the cover requirement is approximately \$10.7
billion -- the balance remaining is \$1.3 billion.

The normal increase in notes will absorb over \$500 million annually and a further \$150 million or more will be absorbed each year for domestic artistic and industrial purposes. These two factors taken together mean that about \$700 million a year of our free gold will be absorbed for domestic reasons. There is thus but two years grace at most even if one assumes that no gold at all will be needed for international purposes. Clearly we cannot proceed on such an assumption.

Since the passage of the Federal Reserve Act more than a half century ago, the function of gold in our monetary system has undergone a fundamental transformation. Gold no longer circulates freely as domestic currency in any major country in the world. We Americans have not used gold as domestic currency since 1934. Gold belongs in a nation's international reserves. The dollar serves as a reserve currency to the world; the United States' gold supply is available to convert dollars held by national monetary authorities at a fixed price. As such, it is one cornerstone -- and a very main cornerstone -- of our international monetary system.

Today, the strength of the dollar is not a function of this legal tie to gold -- a tie which is only applicable to one portion of our total money supply, Federal Reserve notes. The value of the dollar -- whether it be in the form of a bank balance, a coin, or "folding money" -- is dependent on the quantity and quality of goods and services which it can purchase. It is the strength and soundness of the American economy which stands behind the dollar. Balanced growth at home and a strong competitive position internationally give the dollar we use as everyday pocket money its strength.

An expanding United States economy needs an expanding supply of currency. Our main form of currency is Federal

Reserve notes. In the years ahead, we can expect increases in Federal Reserve note circulation of about \$2 billion a year. This growth is a normal response to the public's demand for cash in a growing economy. It is basically a trend development, reflecting a growing population, a growing economy, and a growing number of transactions.

Not to move on the cover requirement at this time would only mean putting off the inevitable. We cannot afford to permit an outmoded provision of our law to impinge on the nation's supply of pocket money.

Removal of this requirement is also of key importance from the viewpoint of the role of the dollar and of gold in the international monetary system.

I know most members of this committee are well versed in the functions of gold and the dollar in the international monetary system. Rather than take up your time with a description at this point, I would refer you to a Treasury report which was issued two weeks ago, entitled Maintaining the Strength of the United States Dollar in a Strong Free World Economy, and ask that Chapter I, which describes the international monetary system and the role of the dollar, be inserted in the record.

If this system, which has served the entire free world so admirably in the past twenty years, is to continue to

facilitate the growth of world trade and prosperity, we must assure that confidence in the system and in the strength of the dollar is maintained. This requires action on four fronts:

- We must continue the long-standing United States' policy of maintaining the gold-dollar relationship at \$35 per ounce. This must not be open to question, and the best way to make continuation of that policy crystal clear is to free our entire gold stock for that purpose.
- We must assure that the U. S. economy grows in an environment of cost and price stability through enactment of the anti-inflation tax and through expenditure controls and appropriate monetary policy.
- We must achieve sustained equilibrium in our balance of payments.
- We and the rest of the free world must put into place the plan for the creation of a new reserve asset agreed upon in Rio last September.

Our policy of maintaining the fixed relationship between gold and the dollar at \$35 an ounce for legitimate monetary purposes is one of the reasons why virtually all countries hold dollars in their reserves and why many of them hold very large amounts of dollars. In addition, of course, countries hold dollars because, unlike gold, they can invest them in interest earning assets.

The monetary authorities of most of the major industrialized countries understand full well that the link between gold and domestic currencies is no longer a pertinent and relevant fact and that gold is an international asset. Only three other countries in the Group of Ten plus Switzerland, the major industrialized countries, still maintain some link between their domestic currencies and gold. While foreign authorities are aware of the fact that the Federal Reserve can suspend the cover requirement, they find it difficult to understand why the United States, the world's major reserve currency country, still maintains this legal impediment to the free international use of gold.

Thus, legislative action on the cover requirement, by making it clear to the world that the Congress as well as the Executive Branch are committing our total gold stock to international use, is necessary to maintain confidence in the dollar.

Removal of the gold cover will not solve the United States' balance of payments problem nor is it a substitute for the solution of that problem.

The need to achieve sustained equilibrium in our international payments position is essential to confidence in the dollar and the future stability of the international monetary

system. The series of measures announced by the President on January 1, with which you are all familiar, are designed to bring us to, or close to, equilibrium this year. It is vital that they be successful. I ask, Mr. Chairman, that the President's message be made a part of the record of these hearings.

Conclusion

I urge the committee to consider and act promptly on the gold cover legislation before you in order that, domestically, we can continue to be assured that the Federal Reserve will be able to supply appropriate amounts of currency to meet the needs of our growing economy for cash, and in order that our policy of maintaining the gold-dollar relationship -- one of the major elements of confidence in the dollar and the international monetary system -- will not be open to question.

MESSAGE TO THE NATION
ON THE BALANCE OF PAYMENTS

JAN 1 1968

Where We Stand Today

I want to discuss with the American people a subject of vital concern to the economic health and well-being of this Nation and the Free World.

It is our international balance of payments position.

The strength of our dollar depends on the strength of that position.

The soundness of the Free World monetary system, which rests largely on the dollar, also depends on the strength of that position.

To the average citizen, the balance of payments, and the strength of the dollar and of the international monetary system, are meaningless phrases. They seem to have little relevance to our daily lives. Yet their consequences touch us all -- consumer and captain of industry, worker, farmer, and financier.

More than ever before, the economy of each nation is today deeply intertwined with that of every other. A vast network of world trade and financial transactions ties us all together. The prosperity of every economy rests on that of every other.

More than ever before, this is one world -- in economic affairs as in every other way.

Your job, the prosperity of your farm or business, depends directly or indirectly on what happens in Europe, Asia, Latin America, or Africa.

The health of the international economic system rests on a sound international money in the same way as the health of our domestic economy rests on a sound domestic money. Today, our domestic money -- the U.S. dollar -- is also the money most used in international transactions. That

money can be sound at home -- as it surely is -- yet can be in trouble abroad -- as it now threatens to become.

In the final analysis its strength abroad depends on our earning abroad about as many dollars as we send abroad.

U. S. dollars flow from these shores for many reasons -- to pay for imports and travel, to finance loans and investments and to maintain our lines of defense around the world.

When that outflow is greater than our earnings and credits from foreign nations, a deficit results in our international accounts.

For 17 of the last 18 years we have had such deficits. For a time those deficits were needed to help the world recover from the ravages of World War II. They could be tolerated by the United States and welcomed by the rest of the world. They distributed more equitably the world's monetary gold reserves and supplemented them with dollars.

Once recovery was assured, however, large deficits were no longer needed and indeed began to threaten the strength of the dollar. Since 1961 your government has worked to reduce that deficit.

By the middle of the decade, we could see signs of success. Our annual deficit had been reduced two-thirds -- from \$3.9 billion in 1960 to \$1.3 billion in 1965.

In 1966, because of our increased responsibility to arm and supply our men in Southeast Asia, progress was interrupted, with the deficit remaining at the same level as 1965 -- about \$1.3 billion.

In 1967, progress was reversed for a number of reasons:

- Our costs for Vietnam increased further.
- Private loans and investments abroad increased.
- Our trade surplus, although larger than 1966, did not rise as much as we had expected.
- Americans spent more on travel abroad.

Added to these factors was the uncertainty and unrest surrounding the devaluation of the British pound. This event strained the international monetary system. It sharply increased our balance of payments deficit and our gold sales in the last quarter of 1967.

The Problem

Preliminary reports indicate that these conditions may result in a 1967 balance of payments deficit in the area of \$3.5 to \$4 billion -- the highest since 1960. Although some factors affecting our deficit will be more favorable in 1968, my advisors and I are convinced that we must act to bring about a decisive improvement.

We cannot tolerate a deficit that could threaten the stability of the international monetary system -- of which the U.S. dollar is the bulwark.

We cannot tolerate a deficit that could endanger the strength of the entire Free World economy, and thereby threaten our unprecedented prosperity at home.

A Time for Action

The time has now come for decisive action designed to bring our balance of payments to -- or close to -- equilibrium in the year ahead.

The need for action is a national and international responsibility of the highest priority.

I am proposing a program which will meet this critical need, and at the same time satisfy four essential conditions:

- Sustain the growth, strength and prosperity of our own economy.
- Allow us to continue to meet our international responsibilities in defense of freedom, in promoting world trade, and in encouraging economic growth in the developing countries.
- Engage the cooperation of other free nations, whose stake in a sound international monetary system is no less compelling than our own.

- Recognize the special obligation of those nations with balance of payments surpluses, to bring their payments into equilibrium.

The First Order of Business

The first line of defense of the dollar is the strength of the American economy.

No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus.

No challenge before business and labor is more urgent than this: To exercise the utmost responsibility in their wage-price decisions, which at home and affect so directly our competitive position/in world markets.

I have directed the Secretaries of Commerce and Labor, and the Chairman of the Council of Economic Advisers to work with leaders of business and labor to make more effective our voluntary program of wage-price restraint.

I have also instructed the Secretaries of Commerce and Labor to work with unions and companies to prevent our exports from being reduced or our imports increased by crippling work stoppages in the year ahead.

A sure way to instill confidence in our dollar -- both here and abroad -- is through these actions.

The New Program

But we must go beyond this, and take action to deal directly with the balance of payments deficit.

Some of the elements in the program I propose will have a temporary but immediate effect. Others will be of longer range.

All are necessary to assure confidence in the American dollar.

1. Direct Investment

Over the past three years, American business has cooperated with the government in a voluntary program to moderate the flow of U. S. dollars into foreign investments. Business leaders who have participated so wholeheartedly deserve the appreciation of their country.

But the savings now required in foreign investment outlays are clearly beyond the reach of any voluntary program. This is the unanimous view of all my economic and financial advisers and the Chairman of the Federal Reserve Board.

To reduce our balance of payments deficit by at least \$1 billion in 1968 from the estimated 1967 level, I am invoking my authority under the Banking Laws to establish a mandatory program that will restrain direct investment abroad.

This program will be effective immediately. It will insure success and guarantee fairness among American business firms with overseas investments.

The program will be administered by the Department of Commerce, and will operate as follows:

- As in the voluntary program, over-all and individual company targets will be set. Authorizations to exceed these targets will be issued only in exceptional circumstances.
- New direct investment outflows to countries in continental western Europe and other developed nations not heavily dependent on our capital will be stopped in 1968. Problems arising from work already in process or commitments under binding contracts will receive special consideration.
- New net investments in other developed countries will be limited to 65% of the 1965-66 average.
- New net investments in the developing countries will be limited to 110% of the 1965-66 average.

This program also requires businesses to continue to bring back foreign earnings to the United States in line with their own 1964-66 practices.

In addition, I have directed the Secretary of the Treasury to explore with the Chairmen of the House Ways and Means Committee and Senate Finance Committee legislative proposals to induce or encourage the repatriation of accumulated earnings by U.S. -owned foreign businesses.

2. Lending by Financial Institutions

To reduce the balance of payments deficit by at least another \$500 million, I have requested and authorized the Federal Reserve Board to tighten its program restraining foreign lending by banks and other financial institutions.

Chairman Martin has assured me that this reduction can be achieved:

- without harming the financing of our exports;
- primarily out of credits to developed countries without jeopardizing the availability of funds to the rest of the world.

Chairman Martin believes that this objective can be met through continued cooperation by the financial community. At the request of the Chairman, however, I have given the Federal Reserve Board standby authority to invoke mandatory controls, should such controls become desirable or necessary.

3. Travel Abroad

Our travel deficit this year will exceed \$2 billion. To reduce this deficit by \$500 million:

- I am asking the American people to defer for the next two years all nonessential travel outside the Western Hemisphere.
- I am asking the Secretary of the Treasury to explore with the appropriate Congressional committees legislation to help achieve this objective.

4. Government Expenditures Overseas

We cannot forego our essential commitments abroad, on which America's security and survival depend.

Nevertheless, we must take every step to reduce their impact on our balance of payments without endangering our security.

Recently, we have reached important agreements with some of our NATO partners to lessen the balance of payments cost of deploying American forces on the Continent -- troops necessarily stationed there for the common defense of all.

Over the past three years, a stringent program has saved billions of dollars in foreign exchange.

I am convinced that much more can be done. I believe we should set as our target avoiding a drain of another \$500 million on our balance of payments.

To this end, I am taking three steps.

First, I have directed the Secretary of State to initiate prompt negotiations with our NATO allies to minimize the foreign exchange costs of keeping our troops in Europe. Our allies can help in a number of ways, including:

- The purchase in the U. S. of more of their defense needs.
- Investments in long-term United States securities.

I have also directed the Secretaries of State, Treasury and Defense to find similar ways of dealing with this problem in other parts of the world.

Second, I have instructed the Director of the Budget to find ways of reducing the numbers of American civilians working overseas.

Third, I have instructed the Secretary of Defense to find ways to reduce further the foreign exchange impact of personal spending by U. S. forces and their dependents in Europe.

Long-Term Measures

5. Export Increases

American exports provide an important source of earnings for our ~~businessmen~~ and jobs for our workers.

They are the cornerstone of our balance of payments position.

Last year we sold abroad \$30 billion worth of American goods.

What we now need is a long-range systematic program to stimulate the flow of the products of our factories and farms into overseas markets.

We must begin now.

Some of the steps require legislation:

I shall ask the Congress to support an intensified five year, \$200 million Commerce Department program to promote the sale of American goods overseas.

I shall also ask the Congress to earmark \$500 million of the Export-Import Bank authorization to:

- Provide better export insurance.
- Expand guarantees for export financing.
- Broaden the scope of Government financing of our exports.

Other measures require no legislation.

I have today directed the Secretary of Commerce to begin a Joint Export Association program. Through these Associations, we will provide direct financial support to American corporations joining together to sell abroad.

And finally, the Export-Import Bank -- through a more liberal rediscount system -- will encourage banks across the Nation to help firms increase their exports.

6 Nontariff Barriers

In the Kennedy Round, we climaxed three decades of intensive effort to achieve the greatest reduction in tariff barriers in all the history of trade negotiations. Trade liberalization remains the basic policy of the United States.

We must now look beyond the great success of the Kennedy Round to the problems of nontariff barriers that pose a continued threat to the growth of world trade and to our competitive position.

American commerce is at a disadvantage because of the tax systems of some of our trading partners. Some nations give across-the-board tax rebates on exports which leave their ports and impose special border tax charges on our goods entering their country.

International rules govern these special taxes under the General Agreement on Tariffs and Trade. These rules must be adjusted to expand international trade further.

In keeping with the principles of cooperation and consultation on common problems, I have initiated discussions at a high level with our friends abroad on these critical matters -- particularly those nations with balance of payments surpluses.

These discussions will examine proposals for prompt cooperative action among all parties to minimize the disadvantages to our trade which arise from differences among national tax systems.

We are also preparing legislative measures in this area whose scope and nature will depend upon the outcome of these consultations.

Through these means we are determined to achieve a substantial improvement in our trade surplus over the coming years. In the year immediately ahead, we expect to realize an improvement of \$500 million.

7. Foreign Investment and Travel in U.S.

We can encourage the flow of foreign funds to our shores in two other ways:

-- First, by an intensified program to attract greater foreign investment in U. S. Corporate securities, carrying out the principles of the Foreign Investors Tax Act of 1966.

-- Second, by a program to attract more visitors to this land. A Special Task Force headed by Robert McKinney of Santa Fe, New Mexico, is already at work on measures to accomplish this. I have directed the Task Force to report within 45 days on the immediate measures that can be taken, and to make its long-term recommendations within 90 days.

Meeting the World's Reserve Needs

Our movement toward balance will curb the flow of dollars into international reserves. It will therefore be vital to speed up plans for the creation of new reserves -- the Special Drawing Rights -- in the International Monetary Fund. These new reserves will be a welcome companion to gold and dollars, and will strengthen the gold exchange standard. The dollar will remain convertible into gold at \$35 an ounce, and our full gold stock will back that commitment.

A Time for Responsibility

The program I have outlined is a program of action.

It is a program which will preserve confidence in the dollar, both at home and abroad.

The U. S. dollar has wrought the greatest economic miracles of modern times.

It stimulated the resurgence of a war-ruined Europe.

It has helped to bring new strength and life to the developing world.

It has underwritten unprecedented prosperity for the American people, who are now in the 83d month of sustained economic growth.

A strong dollar protects and preserves the prosperity of businessman and banker, worker and farmer -- here and overseas.

The action program I have outlined in this message will keep the dollar strong. It will fulfill our responsibilities to the American people and to the Free World.

I appeal to all of our citizens to join me in this very necessary and laudable effort to preserve our country's financial strength.

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EXCERPT FROM TREASURY DEPARTMENT REPORT, MAINTAINING
THE STRENGTH OF THE UNITED STATES DOLLAR IN A
STRONG FREE WORLD ECONOMY

**I. The International Monetary System and Adjustment
of Payments Imbalances**

The problem of the U.S. balance of payments can be understood and analyzed only against the background of an understanding of the present international monetary system. This paper therefore begins with a description of the complex institutional framework within which world trade and payments are carried out. A second chapter discusses the current problems facing the present system. Subsequent chapters then proceed to analyze the key elements of the U.S. balance of payments problem in detail, the measures previously employed, and the President's new program.

A. The International Monetary System—Why and How It Works

An international monetary system provides means and methods of payments in order to facilitate international trade, capital and other transactions. In a world composed of various countries, each with its own currency, trade and capital movements across national borders have not only to be paid for as they are within any country, but have to be provided with a mechanism to convert one currency into another.

The American exporter to Italy usually wants to be paid in dollars—his currency. The Italian importer has lire. Some mechanism has to be provided to convert the lire into dollars to pay the American exporter. And if credit is involved, there needs to be a financing mechanism that crosses the frontier.

The requirements for handling international payments smoothly are:

- The various currencies should be convertible easily into each other.
- There needs to be confidence in the stability of the exchange rates of the major currencies against each other.
- The various countries need to have international reserves of unquestioned value so that if for a time their outpayments exceed their inpayments they can finance the difference by using these reserves.
- The system works more smoothly if owned reserves as supplemented by credit facilities to tide nations over periods of imbalance.

In a strict sense, the international monetary system is not a system at all. It is a series of arrangements, procedures, customs and

institutions which have evolved over time and which are laced together by a network of formal and informal agreements. It has been partially codified as to objectives, principles and procedures by the Articles of Agreement of the International Monetary Fund (IMF). It has been aided by international cooperation on the part of the important central banks of the world—most notably through the so-called “swap network.” It works partly through correspondent relationships of the major commercial banks of the world. Money and capital markets in the United States and Europe are important factors in making the system work. In recent years it has been strengthened by a series of consultative arrangements undertaken under the auspices of the Organization for Economic Cooperation and Development (OECD).

The system rests on five pillars:

- a dollar convertible into gold at \$35 per ounce;
- other major currencies convertible into dollars at stated rates of exchange—under IMF rules they may vary plus or minus 1 percent from parity;
- adequate international reserves and credit facilities designed to support these relationships;
- a general presumption that a country will over time be in equilibrium in its international position—that surpluses will be offset by deficits on the average;
- in seeking to adjust from deficit to surplus, or *vice versa*, a country will take into account the consequences of its actions on the world community.

B. The Role of the Dollar

In practice, all member countries of the IMF which have convertible currencies operate through their central banks or monetary authorities to keep their currencies in an established relationship to the dollar. For example, the exchange parity of the D-mark is 4 to the dollar, or \$0.25. The IMF intervention limits are \$0.2475 and \$0.2525. In practice, the German Federal Bank intervenes within somewhat narrower limits. When the dollar is strong against the D-mark, the dollar price of the D-mark falls toward \$0.2475. The Bundesbank supplies dollars from its reserves to buy up the excess D-marks. When the D-mark is strong against the dollar, its dollar price rises toward \$0.2525. Then the Bundesbank supplies marks and buys dollars.

Each monetary authority acts essentially in the same way—intervening in its own markets to maintain the price of its currency *vis-à-vis* the dollar within the narrow band of plus or minus 1 percent from its parity.

The United States does not have to carry on operations like this. It fulfills its IMF parity obligations by freely buying and selling

gold for dollars—only with monetary authorities and for legitimate monetary purposes, of course—at \$35 per ounce.

The point is that virtually every country does its market interventions by buying or selling dollars. It does so because the dollar is the major transactions or vehicle currency and is widely used in the payment and receipt transactions of international trade and capital flows. It does so because the dollar is a reserve currency and most countries hold dollars in their international reserves.

The dollar is both a reserve currency and a vehicle currency because:

- it is strong, being backed by a strong economy;
- it can be invested profitably because there exists a big money and capital market in the U.S.;
- it is known and is acceptable as a store of value—that is, it holds its purchasing power better than most other currencies;
- it is in sufficient supply so that there are dollars that can be used or borrowed for transactions; and
- it is convertible by monetary authorities into gold so that they are willing to hold it.

The U.S. did not deliberately make the dollar a reserve currency or a transactions currency. The dollar evolved as such out of its basic strength.

But this strength can be called into question in two ways:

- If the supply of dollars in foreign hands becomes greater than the amount foreign central banks and private holders want to hold, either because of their basic needs or for other reasons.
- If declines in the U.S. gold reserve and consequent unfavorable effects on the relationship between U.S. gold and U.S. dollar liabilities raise questions as to the ability of the U.S. freely to convert outstanding dollars into gold at \$35 per ounce.

It is to prevent such developments that the U.S. must achieve sustainable equilibrium in its payments position. Unless it does so, its liabilities to foreigners increase and its gold reserves decrease, and the monetary system becomes more vulnerable to a shrinkage in overall liquidity that can cause serious financial and business disruption through an international credit squeeze.

Foreign central banks and other official institutions hold some \$16 billion of liquid dollar assets. Private foreigners hold another \$16 billion.

The official holdings are reserves for the rest of the world and constitute nearly 30 percent of such reserves. But so long as they are not withdrawn in the form of gold, they have not reduced our reserves. Thus, our balances of payments deficit, unlike those of a nonreserve currency country, has been only partially reflected in a decline of

gold reserves or in our reserve position in the IMF. A considerable part of our balance of payments deficit has been covered by an increase in our liabilities rather than by a reduction in our reserve assets.

While it is not necessary for a commercial bank to maintain liquid assets to cover all or even a major part of its liquid liabilities, the U.S. as a reserve center is a bank in a rather special sense, and needs to maintain a substantial reserve against its liabilities. It is important that our reserves be adequate to meet demands for conversion, and to maintain confidence in the bank on the part of the official and private dollar holders abroad.

Rising dollar liabilities which constitute reserves for other countries have permitted the world as a whole to build up its reserves more rapidly than would otherwise have been the case. A return of the United States to equilibrium would cut off this growth of reserves for these countries. It has become increasingly clear, therefore, that some other means of providing for the future growth in world reserves will be required. To this end, the members of the International Monetary Fund have now agreed on a plan for the deliberate creation of reserves through multilateral action. When this plan is in effect, the world would no longer be dependent upon gold and the deficits of the United States to provide for the expansion in world reserves which will be needed in the future.

Thus the role of the dollar as a reserve currency has been intertwined with the problem of our balance of payments and has also been related to the general problem of expanding world reserves. Through a multilateral system of reserve creation, we can relieve the dollar of its responsibility to provide for a growth in world reserves, and permit concentration on the balance of payments problem.

The following sections of this chapter set forth the elements of the international monetary system.

C. Exchange Rates

One of the distinguishing features of the present international monetary system is the relative stability of exchange rates. Under the Articles of Agreement of the International Monetary Fund—which since their adoption at Bretton Woods, New Hampshire, in 1944 have embodied the formal principles and procedures which underly the present system—countries undertake to maintain exchange rates for transactions in their currencies within a margin of one percent of a declared par value. This par value may be changed, with the approval of the IMF, in the event of a “fundamental disequilibrium” in a country’s balance of payments. For the most part, however, all the members of the IMF have shown a strong preference for stable exchange rates that are changed only infrequently.

In order to maintain their currencies within a margin of one percent of the declared par value, the monetary authorities of almost all countries other than the United States intervene when necessary in their exchange markets, buying or selling dollars against their own currency. There are a few exceptions to this method of official exchange-market intervention (notably in the sterling area), but for the most part the entire pattern of stable exchange rates is maintained by virtue of the fact that countries “peg” their exchange rates to the dollar.

Since most other countries peg their currencies to the dollar, the United States itself does not need to intervene in the exchange markets to maintain the value of the dollar in terms of other currencies. Although it may at times find it advantageous to do so in order to assure more orderly markets and more efficient and economical use of its reserves, the United States basically maintains its obligations regarding exchange stability in a very different manner: by freely buying and selling gold in transactions with monetary authorities (primarily central banks of other countries) at the price of \$35 an ounce. No country other than the United States freely buys and sells gold. The whole exchange-rate system is therefore pegged to gold only through the commitment of the U.S. monetary authorities to buy and sell gold freely at the \$35 price.

D. Reserves

In order to weather periods of deficit in a system of stable exchange rates, monetary authorities must hold reserves of internationally-acceptable liquid assets. If a central bank had no reserves with which to purchase its own currency at times when its currency was in excess market supply, it would have no choice but to ask the IMF to approve a change in its par value.

Reserves are held primarily in the form of gold and dollar claims on the United States. Because dollars are held so widely in countries' reserves, the dollar is the main “reserve currency” of the international monetary system. Countries in the sterling and franc areas hold part of their reserves in sterling or French francs, and thus—to a much lesser extent—the pound and the franc also function as reserve currencies. Gold and reserve currencies are supplemented by reserve credit available from the International Monetary Fund (see below).

After an initial accrual of dollars resulting from market intervention, the country can either retain its reserve gain in the form of dollars or choose to convert the dollars into another reserve asset, usually gold. Conversely, a country necessarily experiences a reserve loss by the act of selling dollars in its exchange market, thereby reducing its dollar holdings. In order to stand ready to intervene in the market, central banks have to hold at least a working balance in dollars. This

working balance can be replenished as necessary either by selling other reserve assets (such as dollar securities, time deposits, or gold) held by the monetary authorities or by drawing on the IMF or other credit facilities.

Many diverse factors enter into the decisions of central banks when they determine the proportions of their reserves to hold in gold, dollars, and other assets. Some central banks have traditionally held their reserves primarily in gold except for foreign-exchange working balances. Others have historically invested almost all their reserves in dollar or sterling assets. There are many different patterns of behavior in between these two extremes. Moreover, many countries have changed their reserve-composition policies over time.

One important motive for holding dollars is that they can be invested at interest. Gold does not earn any interest and actually costs something to store safely.

It has already been pointed out that the United States maintains its exchange stability obligations in a unique manner. It is equally true that the United States must of necessity have a unique policy with respect to its reserves. Whereas other countries use their reserves by buying or selling dollars in their exchange markets, the United States uses its reserves only to redeem excess dollars acquired by the monetary authorities of other countries.

This structural feature of the international monetary system has another important implication: when the United States does use its reserve assets to redeem outstanding dollar liabilities, this redemption—both in amount and timing—is determined by the reserve-asset preferences of foreign monetary authorities. The amount and timing of U.S. use of reserve assets is therefore not directly subject either to U.S. desires or to U.S. official policy actions. The United States can influence the rate at which it gains or loses reserves only by influencing the attitudes and asset preferences of foreign monetary authorities. One of the major factors influencing foreign official attitudes, of course, is the prevailing appraisal of the strength or weakness of the U.S. balance of payments and reserve positions.

Just as the United States uses reserves in a unique manner, it must *hold* its reserves subject to considerations that are unique. Whereas other countries have a range of assets from which to choose that includes gold, dollars, other currencies, and reserve positions in the IMF, the United States has a much more restricted field of choice. It must hold assets which are acceptable to other countries when they call upon the United States to redeem our outstanding reserve-currency liabilities. While there is some scope for holding other countries' currencies in our reserves, it is clear that in the present system the United States must hold most of its reserves in gold.

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Given the wide extent to which the dollar is used as the “intervention currency” and as a reserve currency, it is clear *that the stability of the entire international monetary system is intimately bound up with the behavior of U.S. reserves.* If a widespread feeling were to develop that U.S. reserve assets might be inadequate in comparison with the size of outstanding reserve-currency liabilities, or especially if U.S. reserve assets threatened to continue to decline simultaneously with a further large expansion of U.S. reserve-currency liabilities, dollar assets might be viewed with increasing distrust by individuals and governments all around the world. The U.S. Government fully appreciates the significance of the fact that the stability of the entire monetary system is interdependent with U.S. reserve and balance of payments policy. This fact and the desire to act responsibly in the face of it have been one of the primary considerations underlying U.S. balance of payments policy since the large payments deficits of 1958–60, accompanied by heavy gold losses, first underscored the existence of a problem.

E. Operations of the International Monetary Fund

In addition to the gold and reserve currencies which countries hold in their reserves outright (sometimes referred to as “unconditional” liquidity since they are usable without any outside institution or government placing conditions on their availability), countries have access to a pool of currencies in the International Monetary Fund. The amount of resources a country may draw from the Fund is governed by its quota, which reflects its economic size and importance relative to other countries. When initially paying in its quota subscription, each country subscribes 25 percent in gold and 75 percent in terms of its own currency. In return for agreeing that the 75 percent balance of its own currency may be drawn upon in case of need to finance other countries’ drawings from the currency pool, countries obtain the right to draw the currencies of others from the Fund themselves under certain stipulated conditions.

The right of a country to draw on its gold subscription (“gold tranche”) is essentially beyond challenge; so also is its right to draw on any credit balance it acquired as a result of other countries having drawn its currency. These two amounts together are described as the country’s “reserve position in the Fund;” it is also a form of unconditional liquidity. Most countries, including the United States, regard their reserve positions in the Fund as an asset fully liquid and usable in case of balance of payments need, and accordingly include the Fund reserve position in their published reserves.

Under circumstances which involve increasingly stringent analysis and discussion of a country’s economic policies, members of the Fund

may draw successive further amounts from the Fund up to 100 percent of their quotas. These further borrowings in a country's "credit tranches" are not comparable to reserves. They are conditional credit facilities (hence sometimes referred to as "conditional" liquidity). They carry specific repayment obligations and interest charges.

The role of the International Monetary Fund in supplying conditional liquidity to governments for the purpose of maintaining stability in exchange rates and the adjustment of payments imbalances has expanded greatly since the inauguration of the Bretton Woods system. The aggregate quotas of all members of the IMF are now some \$21 billion. The appropriateness of quotas is reviewed every five years; the last round of general quota increases became effective in 1966. In addition to expanding the general level of quotas and selectively increasing the quotas of certain countries, the IMF was also strengthened in 1962 by an agreement among the ten main industrial countries (the "Group of Ten") known as the General Arrangements to Borrow (GAB). The GAB is an undertaking by these countries to lend the Fund specified amounts of their currencies (aggregating to the equivalent of about \$6 billion) if the Fund decides that supplementary resources are needed to forestall or cope with an impairment of the international monetary system. The GAB arrangements have been activated several times in connection with large U.K. drawings from the Fund.

The U.S. quota in the IMF is \$5.2 billion, out of total Fund quotas of about \$21 billion. As of the end of 1967, the United States had approximately \$400 million of its "gold tranche" and the full \$5.2 billion of credit tranches available.

F. Other Institutional Arrangements

In 1961, the new U.S. Administration began to foster the development of a new system of international short-term credits in the form of the "swap network" of the Federal Reserve System, and also introduced the so-called "Roosa bonds." Both of these provide a type of exchange protection to the lending country. That is, the lending country is repaid in a constant value in its own currency, and is thereby protected against an exchange adjustment by the borrowing country. The United States, at the center of the swap network, can borrow foreign currencies and sell them in the market in lieu of making gold sales, in the expectation that a subsequent reversal of part of the outflow will reduce the eventual drain on its reserves. In the meantime the swap partner holds dollars with a form of exchange protection. Similarly, the United States has, itself, been able to extend credit and acquire foreign currency with exchange protection when, for example, Italy or Canada or the United Kingdom had an outflow of funds. This network of short-term reciprocal borrowing of reserves, frequently called "a first line of monetary defense," now totals about

\$7.1 billion. It has helped to avoid gold losses resulting from short-term flows that were later reversed. When the United States has been drawn upon, other countries have been provided with dollars to hold their exchange rates stable.

Roosa bonds were designed to provide a longer-term instrument for the investment of dollars accumulated by foreign monetary authorities. Most of them have been denominated in the foreign country's currency as an added attraction to the purchasing country. A total of about \$1.5 billion of these bonds was outstanding as of November 30, 1967.

Since its reopening in 1954, the free market for gold in London has re-emerged as the largest and most important center in the world for free-market gold transactions. During most of the period since that time the flow of gold to the London market, from new production and Russian sales, has exceeded the various demands on it. Accordingly, the residual supply of gold was absorbed by central bank purchases and by the U.S. Treasury at prices varying fairly closely around the U.S. fixed price of \$35 per ounce. For short periods, sudden outbreaks of speculative demand for gold substantially exceeded the supply available to the market. Such a situation occurred in October 1960 when the market price rose to around \$40 and aroused widespread anxieties concerning the international monetary system. The U.S. monetary authorities supported the Bank of England in intervening in the London market to stabilize the price within an acceptable range.

In the following year, after a similar but milder strain on the London market, the U.S. authorities suggested that, in view of the mutuality of interest among the monetary authorities of the major industrial countries in maintaining orderly conditions in the gold and exchange markets, an informal gold selling arrangement be arranged among the group of central banks that are members of the BIS or are associated with it. Under the arrangement, each member of the group (Belgium, France, Germany, Italy, The Netherlands, Switzerland, the United Kingdom and the United States) undertook to supply an agreed proportion of such net gold sales to stabilize the market as the Bank of England, as agent for the group, determined to be appropriate. The U.S. share was 50 percent. This informal arrangement has essentially been continued (without French participation since mid-year 1967 and with the U.S. share at 59 percent since then), both as to purchasing net gold acquisitions as well as supplying net market demand. Representatives of the central banks participating in the "pool" meet periodically at Basle to discuss all aspects of the gold and foreign exchange markets, providing a means thereby to coordinate exchange operating policies as well as to keep fully informed of developments in the London and other gold markets.

G. The Dollar as a Transactions Currency

In addition to its role as the international monetary system's major reserve currency, the dollar is also the primary international means of payment and a major medium for the international investment of short-term funds. This "transactions demand" for dollars has grown greatly over the whole postwar period. In recent years the growing importance of the Euro-dollar market has provided further illustrations of the central versatile role played by the dollar in private international financial transactions.¹

Chart I, entitled "Liquid Liabilities to Foreigners," gives some indication of how rapidly U.S. liquid liabilities to nonofficial foreigners have grown in the recent past. Liquid liabilities to "other foreigners"—foreign commercial banks (including the foreign branches of U.S. banks) and other private foreigners—increased over the period 1957 to 1967 from approximately \$6 billion to about \$16 billion. These liquid dollar assets of foreigners held in the United States are invested in demand and time deposits and money market paper. The secular growth in foreign private dollar holdings can be expected to continue in the future *pari passu* with continued expansion in world trade and other international transactions.

The existence of very large outstanding dollar liabilities, not only to foreign official institutions ("reserve-currency" balances), but also to private foreign individuals and organizations ("transactions-currency" balances) underlines the importance of maintaining confidence in the dollar and, more generally, in the international monetary system itself. The following chapter of this paper, which deals with current problems facing the international monetary system, returns to this important point.

H. Balance of Payments Surpluses and Deficits

When a country consistently loses reserves, it is in balance of payments "deficit." Conversely, if a country consistently gains reserves, it has a "surplus" in its balance of payments.

Strictly speaking, the matter is more complicated than that. "Surplus" and "deficit" are analytical concepts with a variety of possible definitions. For example, it may be appropriate in some circumstances to take into account changes in the foreign assets and/or liabilities of the country's commercial banking system—as well as changes in official reserves—in measuring a deficit.

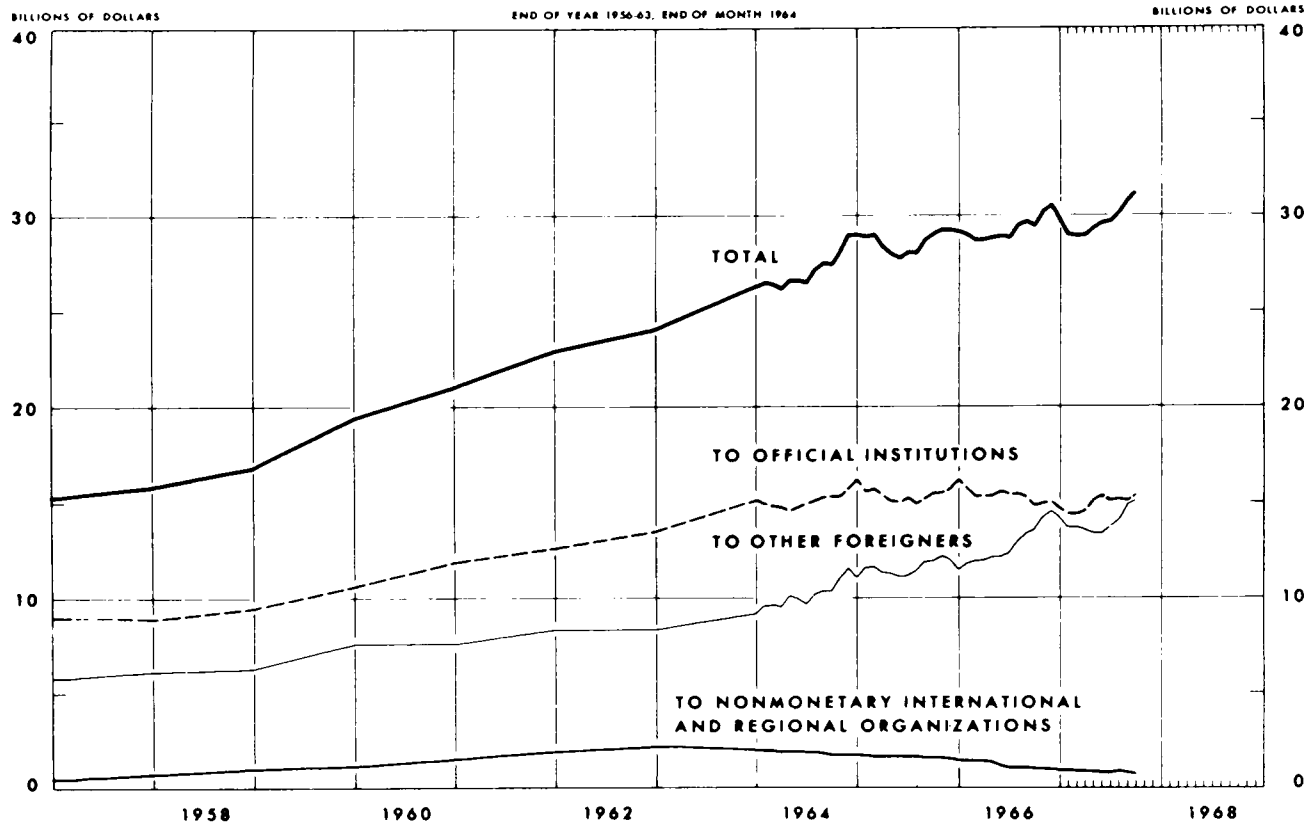
The measurement of the U.S. balance of payments deficit is more complex than for other countries because of the unique position of the U.S. dollar, and was examined by a special review committee.² Fol-

¹ Euro-dollars are deposits in banks outside the United States, principally in European financial centers, that are denominated in U.S. dollars.

² See *The Balance of Payments Statistics of the United States: A Review and Appraisal*, Report of the Review Committee for Balance of Payments Statistics to the Bureau of the Budget (E.M. Bernstein, Chairman), U.S. Government Printing Office, April 1965.

LIQUID LIABILITIES TO FOREIGNERS

Chart 1



Latest Figures Plotted SEPTEMBER

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

lowing this report, the conclusion was reached that no single indicator of surplus or deficit was suitable for all purposes. The primary measure used in this paper is the balance on the "liquidity" basis, although for some purposes reference is made to the balance on the "official reserve transactions" basis.³

Balance of payments surpluses and deficits sometimes are desired. This was the case in the early 1950's, for example, when (on the definitions of surplus and deficit then in use) the European countries undergoing reconstruction had surpluses and the United States had deficits. These deficits and surpluses enabled the European countries to build up their reserves; the declines in the swollen U.S. gold reserves and the increases in our reserve-currency liabilities—representing as they did a redistribution and augmentation of the world's stock of reserve assets—were universally welcomed as such.

On the other hand, *large* and *persistent* payments imbalances, either surplus or deficit, are not sustainable and can give rise to instability in the international monetary system. There is an obvious limit to imbalances of the deficit type: countries can support their exchange rates with their reserves and credit facilities only so long as they have reserves or can arrange further credit. In the case of a reserve-currency country, there are limits to the willingness of private and official holders abroad to accumulate that currency. The limits on the ability of countries to run large and persistent surpluses are much less clear. What is clear, however, is that large and persistent surpluses impose strains on the international monetary system as great as those resulting from large and persistent deficits.

I. The Adjustment Process—Basic Objectives

Each individual country has its own multiple economic and social objectives. These include full employment and a satisfactory rate of growth, reasonable price stability, an equitable distribution of income, and balanced regional and sectoral development. While seeking to attain these objectives, as already noted, countries must also avoid large and persistent imbalances in their external accounts. It is also widely agreed (in the words of the Convention setting up the Organization for Economic Co-operation and Development) that countries should "promote policies designed to contribute to the expansion of world trade on a multilateral, nondiscriminatory basis in accordance with international obligations."

The international monetary system set up at Bretton Woods and based on a pattern of stable exchange rates was then and is now believed by its participants to be the most appropriate system designed to foster

³ For the differences between these two alternative measures of the balance, see Chart VII in Chapter III.

these objectives. The system has evolved over time to meet changing needs and problems. It is once again going through a key evolutionary stage, as the work on proposed amendments to the IMF Articles of Agreement reaches completion, to establish a facility for deliberate reserve creation (see below) and to improve certain rules and practices of the Fund.

The simultaneous achievement of all the economic and social objectives described above, even for an individual country, is far from easy. Governments have only a limited number of policy tools at their disposal. They have not always been able or willing to use these tools in appropriate combinations. Governments in different countries attach different priorities to achievement of various internal and external aims. The nature of imbalances in payments, as well as the appropriate range and mix of instruments required to deal with them, can vary substantially from country to country in line with wide differences in economic and financial structure and in the nature of political institutions.

These difficulties have important implications for the speed and effectiveness with which the adjustment of payments imbalances can be attained. The adjustment process may work somewhat imperfectly, and in any case is apt to be gradual. In a few difficult cases, adjustment of payments imbalances may not take place at all, or will take place only with the costly sacrifice of some of the basic objectives that the system is intended to advance, unless a large measure of multilateral cooperation is brought to bear on the problem.

J. The Adjustment Process—Need for Multilateral Cooperation

The need for multilateral cooperation in achieving and maintaining balance of payments equilibrium has become increasingly widely recognized in the last few years. An understanding of this need has been particularly advanced by an international working group formed under the auspices of the Organization for Economic Co-operation and Development (OECD). The Economic Policy Committee of the OECD established a Working Party in 1961 for the specific purpose of promoting better international payments equilibrium. This group, consisting of senior officials from Ministries of Finance and other key government agencies and Central Banks concerned with balance of payments questions, has met together at approximately six-to-eight week intervals ever since. In 1964, the Ministers and Governors of the ten countries participating in the General Arrangements to Borrow suggested that this OECD working party, known as Working Party 3, make a study of the balance of payments adjustment process with a view toward improving the process of continuing international consultation and cooperation.

The Working Party's report on this subject was issued in August 1966. In addition to endorsing the commonly agreed view that prolonged imbalance in either direction is in general undesirable, the Working Party also noted that "the objectives of international consultation are broader and more general than the mere avoidance of imbalance. The purpose of consultation regarding adjustment policies is to ensure that the policies pursued by individual countries do not hinder others in the pursuit of the general aims of economic policy; more positively, the object is to ensure that as far as possible countries, while avoiding imbalance, collectively support each other in their policies."

The Working Party's report does not fail to point out that there are often inherent difficulties in managing an economy in a way which is consistent with domestic objectives, with the aims of its trading partners, with stable exchange rates, and with the general health of the world economy. But it also recognizes that there is clear room for improvement and that improvement is an urgent order of business. The report describes appropriate methods of dealing with these problems in different circumstances. It refers specifically to the need for clearer formulation of balance of payments aims; early identification and better diagnosis of payments problems; new and more selective instruments of economic policy; more timely action to correct inappropriate demand levels, competitive positions and capital flows; and a further strengthening of the processes of international consultation.

The U.S. Government has strongly supported the Working Party's report and its recommendations. At the recent meeting, November 30 to December 1, of the Ministers of the countries belonging to the OECD, for example, the United States representative, Under Secretary of State Eugene V. Rostow, said:

"We have no doubt that the Atlantic countries can resolve this problem, if they deal with it together, in ways which fortify the world monetary system and permit an early and assured return to growth patterns closer to our full employment objectives. All I am suggesting today is that we recognize that some aspects of the adjustment process require cooperative solutions and that we set about promptly to find them. Cooperation in handling the adjustment process, I suggest, is the next major step after Rio [see below for a discussion of the agreement reached in Rio de Janeiro in September 1967] for us to take in improving our machinery for managing the monetary system."

K. The Adjustment Process—Equilibrium for the System as a Whole

For any country to reduce its deficit or move into surplus, it is generally necessary for other countries to reduce surpluses or increase

deficits. This is simply a statement of what must happen mechanically and statistically if payments imbalances are to be adjusted at all.

This inescapable interdependence of surpluses and deficits makes it very clear that countries must have compatible balance of payments aims if the whole system is not to be working at cross purposes. If all the countries in the system that are in surplus set their policies in such a way as to have continued surpluses, while deficit countries take active measures to eliminate their deficits, then either the deficit countries will still find themselves running deficits or else surplus countries will find that they have not been able to attain their targeted surpluses. All countries together cannot possibly achieve these inconsistent aims; someone is bound to be disappointed.

Virtually all countries take it as their balance of payments objective to be in surplus (and so to have growing reserves) over time. Few if any countries have indicated either a policy or a willingness to have their reserves fluctuate around a fixed level rather than around an upward trend.

It is understandable why countries tend to have this preference for surpluses. The volume of trade and other international transactions has a strong upward trend. It is a reasonable presumption that, because of this trend, the absolute size of imbalances will also increase over time. These facts alone suggest that reserves should likewise have an upward trend if they are to continue to be adequate to support the fixed exchange rate against balance of payments swings. Another factor leading countries not to attempt to reduce their surpluses may be a propensity to discount an existing surplus as partly or wholly "temporary;" it is natural and prudent to conduct affairs so as to prepare for "rainy weather" in the future, and not to presume that current good fortune will continue. Even to the extent that countries aim at a long-run objective of a zero surplus over time, which they tend not to do, they still probably react more quickly to a deficit situation than when they are in surplus (if only because countries in surplus are under much less urgent and intense pressures to act to reduce the imbalance).

Given the set of prevailing attitudes which makes an upward trend in reserves (balance of payments surplus) the targeted long-run "norm" for each country taken individually, the obvious question suggests itself: when, if at all, can the international monetary system as a whole be in equilibrium? Given that it is difficult enough to bring about adjustment of payments imbalances even under ideal conditions where deficit countries take actions to reduce deficits and surplus countries willingly take cooperative actions to reduce their surpluses, how can the system possibly function smoothly when countries in surplus by and large do not want to see their surpluses reduced?

Happily, there is a solution to this dilemma. It is not the case that for every dollar of surplus in the system there must be an exactly offsetting dollar of deficit. When the gross deficits and gross surpluses (consistently defined) of all countries are offset against each other, the sum of the surpluses can exceed the sum of the deficits by the amount of new reserves being added to the system which are not at the same time the liability of a particular country. The key point of this relationship is that if new reserves of the appropriate kind are flowing into the system, it is possible for some countries to satisfy their preferences for reserve increases without necessitating that other countries be in corresponding deficit.

Up to the present time, the only "new reserves" which have allowed this margin to exist have been increases in countries' monetary gold stocks. When newly-mined gold is sold to a monetary authority, that government has a reserve gain without any other country having experienced a deficit. When the dollar component of world reserves increases, on the other hand, this increase in reserves does not allow the system as a whole to have a margin of surpluses exceeding deficits. When the rest of the world adds to its dollar reserves, these new assets are also an increase in U.S. reserve-currency liabilities, and there is therefore a U.S. deficit corresponding to the surplus of the rest of the world. However, gold is not the only reserve asset that is capable of permitting the system to have a situation in which the sum of surpluses exceeds the sum of deficits. Deliberately created new reserve assets, such as the proposed Special Drawing Rights (SDR) described in the next chapter, will serve this function equally well.

Equilibrium for the system as a whole thus requires that new reserves—gold or new reserve assets such as SDR—be added to the system at such a rate that the sum of surpluses can exceed the sum of deficits by a reasonable margin. This condition for "equilibrium" of the system should be thought of as a necessary, but not sufficient, condition. Other considerations, such as the degree to which the system is promoting the achievement of its basic objectives, also need to be taken into account.

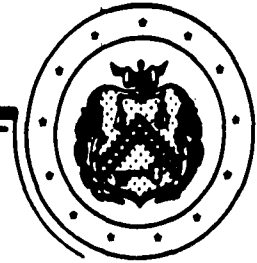
Only under these conditions is there a good chance of making countries' balance of payments aims mutually compatible; only then is there a plausible hope of attaining the objectives the system is intended to promote, including relative freedom from trade and payments restrictions while still getting the adjustment of payments imbalances to proceed smoothly.

What is a "reasonable" margin by which surpluses should exceed deficits? The answer to this question is not fully clear to the financial experts and economists who have studied this question. Broadly speaking, the rate at which new reserves should be added to the system

should probably bear some relationship to the rate at which international transactions are expanding (though the two rates need not be the same and there is no necessity for a precise relationship). The margin should not be too small, and certainly should not be negative. Nor should the margin be an excessive one. At either of these two extremes, one would have to say that the system as a whole was in "disequilibrium."

It is important to be clear on the fact that the above condition for equilibrium of the system, if satisfied, in no way reduces the need for countries to avoid large and persistent imbalances in their external payments. It is still imperative for countries in large or prolonged deficit to reduce their imbalance. And it is just as important as ever for countries with large and persistent surpluses to reduce these surpluses to the point where they are moderate and broadly consonant with the rate at which reserves are growing in the system as a whole. The need for adjustment is not removed. The margin by which surpluses exceed deficits only means that, for each country individually and for the system as a whole, adjustment takes place around an upward trend in reserves rather than around a constant level.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 31, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing February 8, 1968, in the amount of \$2,501,967,000, as follows:

91-day bills (to maturity date) to be issued February 8, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated November 9, 1967, and to mature May 9, 1968, originally issued in the amount of \$1,000,647,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated February 8, 1968, and to mature August 8, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Monday, February 5, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

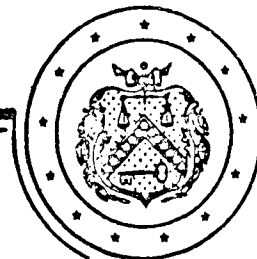
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tender in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on February 8, 1968, cash or other immediately available funds or in a like face amount of Treasury bills maturing February 8, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and the notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained at any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 31, 1968

OR IMMEDIATE RELEASE

TREASURY ANNOUNCES REFUNDING AND CASH BORROWING PLANS

The Treasury today announced that it is offering holders of the note issue maturing February 15, 1968, and the note and bond issues maturing August 15 and November 15, 1968, an opportunity to exchange their holdings for a 5-3/4% 7-year note to be dated February 15, 1968, to mature February 15, 1975.

The Treasury also announced that upon completion of this refunding it will grow about \$4 billion through the offering of a 15-month note. Exact terms will be announced on February 8 with the books open for subscriptions on February 8 and payment on February 20.

The securities eligible for exchange into the 7-year notes are as follows:

5-5/8% Treasury Notes of Series A-1968, maturing February 15, 1968

PREREFUNDING

4-1/4% Treasury Notes of Series C-1968, maturing August 15, 1968

3-3/4% Treasury Bonds of 1968, maturing August 15, 1968

5-1/4% Treasury Notes of Series D-1968, maturing November 15, 1968

3-7/8% Treasury Bonds of 1968, maturing November 15, 1968

The new notes are being offered at par to holders of the February maturities and therefore will yield 5-3/4%. Details for the August and November maturities showing cash and interest adjustments appear in Table 1. Approximate investment yields appear in Table 2. Both tables are attached.

The public holds \$12.1 billion of the securities eligible for exchange, and about \$12.2 billion is held by Federal Reserve and Government investment accounts.

Cash subscriptions for the new 7-year notes will not be received.

The books on the exchange will be open for three days only, on February 5 through February 7, for the receipt of subscriptions. Subscriptions addressed to a Federal Reserve Bank or Branch, or to the Office of the Treasurer of the United States, and placed in the mail before midnight February 7, will be considered as timely. The payment and delivery date for the new notes will be February 15, 1968. Interest on the securities due November 15, 1968, will be adjusted as of February 15, 1968. The new notes will be made available in registered as well as bearer form. All subscribers requesting registered notes will be required to furnish appropriate identifying numbers as required on tax returns and other documents submitted to the Internal Revenue Service. This is a taxable exchange.

7-1150

Coupons dated February 15, 1968, on the securities tendered in exchange should be detached and cashed when due. Coupons dated May 15, August 15 and November 15, 1968, on the securities due on August 15 and November 15, 1968, must be attached. February 15, 1968, interest due on registered securities will be paid by issue of interest checks in regular course to holders of record on January 15, 1968, the date the transfer books closed.

Interest on the new 7-year notes will be payable semiannually on February 15 and August 15.

TABLE NO. 1

Payments due to or by Subscribers in the February 1968 Prerefunding

(In dollars per \$100 face value)

Securities to exchanged	: Payment by : subscribers : on account of : issue price : of offered : notes	: Payment to : subscribers for : accrued interest to : February 15, 1968, : on securities : exchanged	: Net amount to be paid : by subscriber : to subscribe
For the 5-3/4% Note of 2/15/75			
.1/4% Note 8/15/68	.600000	- a/	.600000
3/4% Bond 8/15/68	.850000	- a/	.850000
.1/4% Note 11/15/68	.150000	1.326923	1.176923
.7/8% Bond 11/15/68	1.150000	.979396	.170604

Interest will be paid in regular course.

TABLE NO. 2

Investment returns in the February 1968 Prerefunding

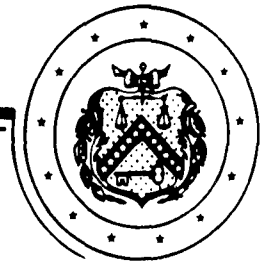
Securities eligible for exchange	: Approximate investment : yield from : 2/15/68 to maturity <u>1/</u>	: Approximate reinvestment : rate of the : extension period <u>2/</u>
.1/4% Note 8/15/68	5.73%	5.77%
3/4% Bond 8/15/68	5.73	5.77
.1/4% Note 11/15/68	5.73	5.79
.7/8% Bond 11/15/68	5.72	5.79

Office of the Secretary of the Treasury

Yields to nontaxable holders (or before tax) on issues offered in exchange based on prices of eligible issues (adjusted for payments on account of issue price). Prices are the mean of bid and ask quotations at noon on January 30, 1968.

Rate for nontaxable holder (or before tax).

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 31, 1968

FOR IMMEDIATE RELEASE

EXCEPTIONAL SERVICE AWARD PRESENTED TO ASSISTANT SECRETARY WINTHROP KNOWLTON

Secretary of the Treasury Henry H. Fowler has presented the Exceptional Service Award to Winthrop Knowlton, Assistant Secretary for International Affairs.

Mr. Knowlton, who leaves the Treasury today, is a former partner of the New York investment banking firm of White, Weld & Company, was cited for his significant contributions "to this country's effort to maintain a stable international monetary position."

"His unusual ability to harness international economic theory and convert it into practical proposals is manifest in Treasury Department policies and programs directed toward achieving a satisfactory balance of payments without impairing our economy or those of friendly nations.

"His creative problem-solving," Secretary Fowler said, "was invaluable in the development and implementation of specific programs. Many of his ideas are embodied in the President's Action Program, announced on January 1, 1968, and described in detail in the Treasury publication, "Maintaining the Strength of the United States Dollar in a Strong Free World Economy."

The award was presented to Mr. Knowlton at a reception January 29 at the Washington Hotel. Secretary Fowler commented that "in addition to bringing to your work -- and thus to the Treasury -- great imagination and perception, your practical experience of working in the international financial community has given you the diplomatic ability to work successfully with many different persons from many different cultures."

Mr. Knowlton has served as Assistant Secretary for International Affairs since August 2, 1966. In that year he had served as Acting Assistant Secretary for International Affairs from June 11 until his appointment as Assistant Secretary.

From June 28, 1965, until June 10, 1966, he was Deputy Assistant Secretary for International Affairs. Previously, he served for a short time in Washington as a consultant with the Office of Education, Department of Health, Education and Welfare.

During his tenure at the Treasury, Mr. Knowlton

- represented the United States during negotiations for a second replenishment of the International Development Association (IDA), attending meetings of Part I countries in Paris in May 1967 and The Hague in November 1967
- headed the U. S. delegation at meetings of the U.S.-Canadian Committee on the Balance of Payments in Ottawa and Washington in 1966 and 1967
- headed the U.S. delegation to the August 1967 (Paris) meeting of Working Party 3 of the OECD
- headed the U.S. delegation to the December 1966 (Paris) meeting of the OECD Group on Export Credits and Credit Guarantees
- served as a member of U.S. delegations to the OECD Ministerial meeting in Paris in November 1966; the Inter-American Economic and Social Council (IA-ECOSOC) meeting in Buenos Aires in March-April 1966; the Inaugural Meeting of the Asian Development Bank in Tokyo in November 1966; meetings of the Economic Policy Committee and Working Party 3 of the OECD in May-June 1967; the meeting of the Joint U.S.-Canadian Cabinet Committee on Trade and Economic Affairs in Montreal in June 1967; the meeting of the Development Assistance Committee of the OECD in Paris in July 1967; the meeting of the Joint U.S.-Japan Subcommittee on Trade and Economic Affairs in Hawaii in January 1968
- served as Temporary Alternate Governor of the International Bank for Reconstruction and Development (IBRD) and the International Monetary Fund (IMF) during their annual meeting in Washington in September 1966 and of the Inter-American Development Bank (IDB) during its annual meeting in Washington in April 1967.

The author of "Growth Opportunities in Common Stock," and author of "A Killing in the Market," Mr. Knowlton is married to the former Grace Daniels Farrar of Buffalo, New York. They live with five children in McLean, Virginia.

Mr. Knowlton attended Lawrenceville School in Lawrenceville, New Jersey, from 1942 to 1948; the University of Nanking in 1948, and Harvard College from 1949 to 1953 where he received his bachelor degree (magna cum laude). He received his master's degree in business administration -- with distinction -- from Harvard Business School in 1955.

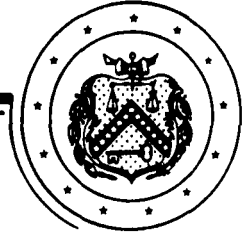
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UNITED STATES SAVINGS BONDS ISSUED AND REDEEMED THROUGH January 31, 1968
(Dollar amounts in millions - rounded and will not necessarily add to totals)

DESCRIPTION	AMOUNT ISSUED ^{1/}	AMOUNT REDEEMED ^{1/}	AMOUNT OUTSTANDING ^{2/}	% OUTSTANDING OF AMOUNT ISSUED
RED				
Series A-1935 thru D-1941	5,003	4,995	8	.16
Series F and G-1941 thru 1952	29,521	29,471	49	.17
Series J and K-1952 thru 1955	3,156	3,106	50	1.58
TURED				
Series E ^{3/} :				
1941	1,870	1,636	234	12.51
1942	8,254	7,243	1,011	12.25
1943	13,281	11,688	1,593	11.99
1944	15,493	13,531	1,962	12.66
1945	12,167	10,439	1,728	14.20
1946	5,506	4,533	973	17.67
1947	5,215	4,126	1,088	20.86
1948	5,384	4,156	1,228	22.81
1949	5,309	4,027	1,282	24.15
1950	4,640	3,464	1,176	25.34
1951	4,016	2,999	1,017	25.32
1952	4,206	3,112	1,094	26.01
1953	4,801	3,454	1,346	28.04
1954	4,890	3,435	1,455	29.75
1955	5,092	3,503	1,589	31.21
1956	4,912	3,322	1,590	32.37
1957	4,618	3,030	1,589	34.41
1958	4,494	2,779	1,714	38.14
1959	4,205	2,543	1,661	39.50
1960	4,207	2,420	1,786	42.45
1961	4,236	2,307	1,929	45.54
1962	4,081	2,160	1,921	47.07
1963	4,540	2,221	2,319	51.08
1964	4,427	2,129	2,299	51.93
1965	4,333	2,001	2,331	53.80
1966	4,652	1,847	2,805	60.30
1967	3,920	978	2,942	75.05
Unclassified	607	737	-129	-
Total Series E	153,353	109,822	43,532	28.39
Series H (1952 thru May, 1959) ^{3/}	5,485	2,952	2,533	46.18
Series H (June, 1959 thru 1967)	6,488	1,182	5,307	81.80
Total Series H	11,973	4,133	7,840	65.48
Total Series E and H	165,326	113,955	51,371	31.07
Series J and K (1956 thru 1957)	596	378	217 ^{4/}	36.41
Series I				
Total matured	37,680	37,572	107	.28
Total unmatured	165,922	114,333	51,589	31.09
Grand Total	203,602	151,906	51,696	25.39

^{1/} Less accrued discount.
^{2/} Net redemption value.
^{3/} Portion of owner bonds may be held and will earn interest for additional periods after original maturity dates.
^{4/} Less matured bonds which have not been presented for redemption.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 1, 1968

FOR IMMEDIATE RELEASE

TREASURY TO INVESTIGATE COMPLAINT OF SUBSIDY ON CANNED TOMATO PRODUCTS FROM FRANCE

The Treasury Department announced today that it is issuing a notice of countervailing duty proceeding with respect to imports of canned tomato paste from France.

The notice, which will be published in the Federal Register of Friday, February 2, reports that the Treasury is investigating a complaint of subsidization of canned tomato product exports to the United States from France. The amount of the subsidy is stated to be 2¢ per pound.

The complainant was Cannery League of California, San Francisco, California.

Under the United States Countervailing Duty Law, if the Treasury Department finds that a "bounty or grant" (within the meaning of the law) is being paid, it is required to assess an equivalent countervailing duty.

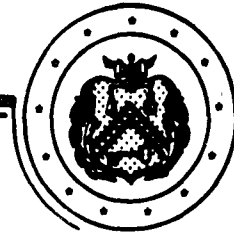
The notice of countervailing duty proceeding allows 30 days for submission of data, views, and arguments concerning the existence or nonexistence and the net amount of a bounty or grant.

Canned tomato paste and sauce exports to the United States from France totalled in excess of four million pounds for the first ten months of 1967 and were valued at approximately \$675,000.

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F-1152

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 5, 1968

IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$10,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing February 15, 1968, in the amount of \$1,459,000, as follows:

91-day bills (to maturity date) to be issued February 15, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated November 16, 1967, and to mature May 16, 1968, originally issued in the amount of \$947,000, the additional and original bills to be freely exchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated February 15, 1968, and to mature August 15, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (minimum face value).

Tenders will be received at Federal Reserve Banks and Branches until the closing hour, one-thirty p.m., Eastern Standard Time, on Friday, February 9, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and enclosed in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of others provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received from deposit from incorporated banks and trust companies and from eligible and recognized dealers in investment securities. Tenders must be accompanied by payment of 2 percent of the face value of Treasury bills applied for, unless the tenders are guaranteed by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on February 15, 1968, cash or other immediately available funds or in a like face amount of Treasury bills maturing February 15, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

STATEMENT BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
BEFORE THE
COMMITTEE ON WAYS AND MEANS
U. S. HOUSE OF REPRESENTATIVES
ON
CERTAIN LEGISLATIVE ASPECTS OF
THE PRESIDENT'S BALANCE OF PAYMENTS PROGRAM
MONDAY, FEBRUARY 5, 1968, 10:00 A.M.

Mr. Chairman, Members of the Committee:

In 1967, the deficit in our international balance of payments increased substantially to reach an intolerable level. On January 1, the President, in a Message to the Nation, announced an Action program to bring our balance of payments to -- or close to -- equilibrium, stating the need for action is a National and international responsibility of the highest priority. I would ask that his Message be made a part of the record.

Shortly thereafter, I released a Treasury Department report entitled "Maintaining the Strength of the United States Dollar in a Strong Free World Economy." This document describes in detail the background and reasons for the Action Program announced by the President. It describes what we have done to date, and what we propose to do, both over the short and the long term. I have asked that copies of this

report be made available this morning to each member of the Committee, because there may be occasions to make reference to it.

We welcome this early opportunity to appear before you to review in general terms the balance of payments program as a background for some important legislative program decisions within the purview of this Committee that call for early action. The areas of particular legislative concern to this Committee relate to improving our trade surplus as the mainstay of our balance of payments situation, both short-term and long-term, and action to deal with our so-called travel deficit, which is one of the sources of increasing weakness in our balance of payments situation. I shall discuss both the trade surplus and the travel deficit and measures to deal with them. Ambassador Roth, the President's Special Representative on Trade Negotiations, is here to present a statement for the information of the Committee concerning a particular aspect of the trade problem which is dealt with specifically in the President's January Message under the heading, "Nontariff Barriers."

I. The Balance of Payments Problem -- What It Is
and How To Resolve It

Before I go into detail concerning the areas with which this Committee is directly concerned, it will be useful to discuss the broad question of the United States balance of payments problem and our strategy -- both the short- and long-term -- to deal with it. In essence, I raise here, and attempt to answer, five questions:

- Why is there a problem with our balance of payments?
- Why do we have to take such drastic action now?
- What are our long-term prospects?
- What will be the world impact of the present program?
- How will the rest of the world respond to it?

The Balance of Payments Problem

Even today, many of our citizens are not fully aware of the urgent necessity of restoring a balance in our international payments. The United States economy is strong and prosperous. Foreign transactions of the United States, while very large in terms of the international economy, are small relative to our total production, consumption, and investment --

relatively smaller than for almost any other country. Why should the United States, or the world, be disturbed about a balance of payments deficit that is only a fraction of one percent of our output of goods and services?

Despite the magnitude of our domestic economy, the foreign transactions of the United States are important to our economic well-being and indispensable to the free world. Imports of foodstuffs, raw material, and finished goods are essential for our production and our high standard of living. The overseas expenditures of the United States Government for foreign aid and defense are vital to our objectives of world peace and security. U. S. private foreign investment is profitable to our banking and business institutions and important for economic growth and development in many other countries. And travel enhances international understanding.

The cost of imports, travel abroad, security and aid expenditures overseas, and foreign investment must be paid for by exports of goods and services. The earnings of our foreign loans and investments, travel and investment by foreigners in the United States and other foreign exchange receipts.

In 1966 our total international payments amounted to \$49 billion, while our foreign receipts were nearly \$48 billion. The resulting deficit in our balance of payments amounted to \$1.4 billion. This increased to more than \$3.5 billion last year.

When our total foreign payments are more than our foreign receipts, some, or all, of the excess dollars received by foreigners are sold to their central banks, which can use them in a variety of ways -- including holding them as reserves or buying gold from the United States. The result tends to be a deterioration in the liquidity position of the United States, as the ratio of its reserve assets (e.g., gold) declines relative to its liquid liabilities (e.g., dollars held by foreigners).

The United States is the major international banking center holding large deposits both for monetary authorities and for private banks, corporations and individuals. The dollar functions as the principal international currency. Its liquidity position must remain strong, like that of any bank, to retain the confidence of its depositors.

The U. S. deficit was welcome when it first developed in the early postwar years. Then, as now, the deficit consisted

of capital outflows -- both public and private -- that exceeded the U. S. surplus on goods and services. It supplied reserves to foreign countries -- principally European -- which had drawn them down to finance the war and postwar reconstruction. More basically, the U. S. capital flow to Europe contributed to the European economic miracle and the smooth transition to European economic unity.

In the late 1950's, however, United States deficits began to become a source for concern. Not only did the size of the deficits rise, but they were financed more by sales of gold and less by foreign accumulation of dollars than in prior years. Some foreign central banks had what they considered to be adequate supplies of dollars in their reserves. Many countries, however, still had small reserves and were still eager to add to their dollar reserves. Thus, there was still no high urgency about restoring balance to our international accounts. Nevertheless, President Eisenhower instructed the Department of Defense and other Government agencies to economize on their foreign exchange expenditures. With three years of large deficits culminating in a speculative outbreak in the London gold market in October, 1960,

new measures were called for. President Kennedy proposed measures to increase exports and other receipts, intensified efforts to cut Government balance of payments costs, and later introduced the Interest Equalization Tax to hold down U. S. purchases of foreign securities. A sharp rise in United States capital outflows in 1964 made it necessary for President Johnson to introduce a voluntary program for holding down direct investment and bank loans abroad.

The rationale behind these measures was as follows:

- First, while the rising outflow of U. S. capital was moderated, U. S. international balance would be restored by the growth of the U. S. surplus on non-capital transactions.
- Second, modestly restraining the increase in U. S. foreign investments, particularly those in Western Europe, would have only a small effect on world economic growth -- in sharp contrast to other alternatives -- and would yield satisfactory balance of payments results over time.

From the 1958-60 period to 1965, we made good progress in reducing our payments deficit because of the growth of

our exports of goods and services relative to our imports, because of the rise in earnings from our foreign investments, and because of the reduction in capital outflow in 1965.

In 1965 and 1966, we reduced our liquidity deficit by almost two-thirds from the average deficits of 1958-60 and one-half from the average of 1961-64. As this period progressed, however, the accelerated expansion of the U. S. economy and the war in Vietnam placed renewed pressure on the balance of payments. The boom resulted in an extraordinary increase in imports. The costs of our forces in Vietnam added substantially to our foreign payments.

Despite this the dollar was strong. After France ceased in October, 1966 its regular monthly purchases of gold initiated early in 1965 to absorb the dollar surpluses it had accumulated, the drain on the U. S. gold supply dried up to a trickle.

There was retrogression in the first three quarters of 1967 because the foreign exchange costs of Vietnam rose further, private capital outflow increased, net tourist expenditures rose, and the European economic slowdown reduced European imports -- and our exports.

The devaluation of sterling in November, 1967, brought the international monetary situation and our balance of payments problem to an acute stage. The British move resulted in a weakening of confidence in currencies and was accompanied by a burst of speculative buying of gold and a resulting large loss of U.S. gold reserves in November and December. This was a threat not only to the dollar but also to the international monetary system as a whole.

While the speculation was repulsed with the cooperation of most of the members of the gold pool, it underlined the urgency of placing the dollar once more in an impregnable position. The time had come when it was necessary and desirable to take new and decisive measures to move the United States payments position strongly toward balance.

What was the best way to achieve this? Depressing the American economy is as unacceptable a solution to our imbalance of payments to most other nations of the world as it is to the United States. The United States **occupies a** unique role in the world economy. It is by far the largest exporting and importing country. It is the principal source of international capital. It is the largest donor of aid.

Military forces stationed abroad are indispensable to the security of many countries -- including the United States. For all these reasons, the entire world is affected by the U. S. economy and the U. S. balance of payments. The volume of international trade, the prices of basic commodities, the cost of money, and even the level of production and employment abroad respond to the U. S. economy. The United States must seek a solution to the payments imbalance through the expansion of the world economy, rather than the severe contraction of its own, and, consequently, the world economy.

The action program announced by President Johnson on January 1 avoids deflation, while underlining the urgent need for prompt enactment of an anti-inflationary tax increase, along with proper control of public expenditures, appropriate monetary policy, responsible wage and price decisions on the part of business and labor, and other measures to increase our export surplus and avoid any deterioration through excessive growth accompanied by inflationary trends that will weaken the United States competitive position in world markets.

Because the need to cut the United States payments deficit is urgent, the program also includes new and stringent temporary restraints on outflows of U. S. private capital. We are here today to recommend a program to curtail, temporarily but sharply, the amount of foreign travel expenditures by Americans. Indeed, it is upon these uncongenial measures that we must rely for the largest immediate effects. These measures are taken reluctantly as an emergency matter. How soon they can be relaxed will depend greatly upon our own efforts to increase our trade surplus, reduce or neutralize Government expenditures abroad, and encourage foreign travel and investment in the United States.

International Monetary System

It is the relationship of the U. S. dollar and the U. S. payments position to the international monetary system that makes this program both a national and international responsibility.

The international monetary system requires adequate monetary reserves to enable countries to meet payments deficits while they take measures to adjust their balance of

payments. The monetary reserves of the world consist mainly of gold, U. S. dollars, and other currencies. As world trade and payments grow, the need for additional monetary reserves also grows. Since 1950, less than half of the increase in monetary reserves has been in the form of gold. More than half of the increase has been in the form of U. S. dollars acquired by the central banks of other countries. Without the growth of dollar reserves, the growth of world trade and payments would have been severely restricted and the world economy might have been subjected to serious deflationary pressures and instability.

In actual fact, the international monetary system has worked well. This is evident from the enormous expansion of world trade from \$55 billion in 1950 to about \$200 billion in 1967. The expansion of trade and payments and the stability of the international monetary system have been buttressed not only by growth of reserves but also by enlargement of international credit facilities. The resources of the International Monetary Fund were increased in two steps from over \$9 billion in 1958 to \$21 billion at present. A network of reciprocal currency agreements was established by the central

banks of the large financial centers for swaps of each other's currency; the United States has such swap arrangements totaling \$7.1 billion with 14 central banks and the Bank for International Settlements. In order to help maintain confidence in the equivalence of gold and currencies at stable values, a number of countries formed a gold pool to maintain the orderly character of the London gold market.

These various measures helped the international monetary system to function effectively. Even so, it became evident that a more basic reform was necessary. The world can no longer depend entirely upon increases in gold and dollars to provide an assured and satisfactory growth of monetary reserves. The amount of newly-mined gold available will not provide for an adequate increase in world reserves. And it is not desirable from the point of view of the United States or the rest of the world that the growth of U.S. liabilities, in the form of dollar reserves abroad, should continue as in the past. A steady increase in U. S. liabilities, while its reserves decline, exposes the international monetary system to the threat of instability.

The Rio resolution for the creation of Special Drawing Rights (SDR) represents a landmark in the evolution of an international monetary system responsive to the needs of the modern world. When this system is in operation, the growth of monetary reserves can be adequate without depending either on the uncertainties of gold mining and gold hoarding or on persistent deficit in the U. S. balance of payments.

The early availability of SDR removes one of the concerns as to the impact of the U. S. balance of payments program -- namely, a slowing of reserve growth and a consequent adverse effect on world trade and income. Early activation of the SDR plan can maintain an adequate growth of world reserves together with restoration of U. S. balance of payments equilibrium.

Strategy for Payments Improvement

The key resources which give the United States the strength to deal with its underlying long-range payments problem constructively and sensibly are:

- a strong economy with a Gross National Product in excess of \$800 billion, representing 40-45 percent of world output;

-- a large stock of foreign assets with powerful earnings potential. Gross assets abroad -- public and private -- total more than \$110 billion. Our net long-term asset position -- approximately \$70 billion -- has increased every year for 20 years. Private overseas assets alone now generate annual earnings of about \$6 billion.

-- a basic trade surplus, on which we must build;

-- a strong reserve position (nearly \$15 billion, or about 20 percent of world reserves), even after losses of the past few years.

We can build on these elements of strength and move toward balance of payments equilibrium through short- and long-range measures vigorously implemented. Furthermore, the passage of time will ameliorate forces that presently exacerbate the balance of payments deficit and hide the fundamental progress achieved.

Ideally, the United States would solve its balance of payments problem through a gradual, long-range approach in which there was no interference with the free movement of goods and services, capital, or people. Over the long run,

the United State is, in fact, dedicated to just such an approach.

However, the situation that confronts the United States today requires prompt and major corrective action. Long-term measures alone that take hold gradually over time are not sufficient.

The President's Action Program

President Johnson's program is designed to bring about a sharp reduction in the United States payments deficit in the year ahead, bringing it into -- or close to -- equilibrium. The program consists of general and specific measures, short- and long-range actions.

The first and essential requirement is stability in the United States economy. I will deal with this matter in more detail later in this statement, along with foreign travel and the trade surplus. Here I shall touch briefly only on three remaining parts of the Action Program, not of direct concern to this Committee:

1. Direct investment.--By Executive Order and regulations issued under the Banking Law, a mandatory limit has been placed on direct investment by United States companies

in foreign affiliates. The program, together with its accompanying provisions on the repatriation of foreign earnings, is expected to reduce the payments deficit by \$1 billion in 1968.

2. Banks and other financial institutions.--Revised guidelines have been issued by the Board of Governors of the Federal Reserve System for reducing foreign credits from United States banks and other financial institutions. The new guidelines are designed to bring a net inflow of at least \$500 million in 1968. The program is voluntary, although the President has given the Federal Reserve Board standby authority to invoke mandatory controls.

3. Government expenditures overseas.--The commitments for aid and defense, on which free world security depends, necessitate very large expenditures abroad. These costs have risen sharply because of the Vietnam War. Over the past three years, a stringent program has substantially reduced these foreign exchange costs. The President has, nevertheless, set a target of a further reduction of \$500 million in the foreign exchange impact of such programs in 1968.

Negotiations will be initiated promptly with our allies in Europe and in the Pacific to minimize the foreign exchange costs of our military spending abroad. They can help, as they have, by purchasing in the United States more of the equipment for their defense needs. They can also offset the adverse effects of our military expenditures on the balance of payments by investing part of their foreign exchange receipts in long-term U. S. securities. The Department of Defense has been instructed to find ways to reduce further the foreign exchange impact of personal spending by U.S. forces and their dependents. The President has instructed the Director of the Budget to find ways to reduce the number of American civilians working overseas. AID has been directed to reduce its foreign exchange costs by at least \$100 million in 1968.

Long-Range Aspects of the Balance of Payments Program

A drastic reduction in our balance of payments deficit is necessary to defend the dollar and to insure against a breakdown of the international monetary system. The action program will achieve this. The program will entail sacrifices in this country and it may cause difficulties for some foreign

countries. In order to assure a fair sharing of these sacrifices, the program has been widely spread over all sectors of the U. S. economy. In order to minimize adverse effects on the world economy, the program distinguishes among groups of countries on the basis of their ability to absorb reductions in their foreign exchange receipts.

The action program is designed to deal with an emergency. We do not regard certain aspects of it as consistent with a long-range solution to our underlying balance of payments problem. Restrictive measures are temporary. The policy of the United States is to support the unrestricted international flow of goods, services, and capital under a stable international monetary system based on fixed values for currencies defined in terms of gold or the dollar, linked at \$35 an ounce. The world economy can operate most effectively only with a balanced pattern of international payments, achieved without restrictions. The international monetary system can function effectively only if monetary reserves can grow steadily at an appropriate rate without depending, as in the past, on a large infusion of dollar reserves derived from a payments deficit of this country.

An appropriate long-range balance of payments solution for the United States must be based on a substantial and growing surplus in trade and services, including earnings from U. S. foreign investments. The present trade surplus is too small. It must be increased substantially through an expansion of U. S. exports. The Government is taking measures to encourage exports. U. S. producers will be able to benefit from these measures only if they strengthen their position in world markets by maintaining competitive prices and costs.

The United States is eager -- and working hard -- to encourage foreign direct investment in this country and investment in United States corporate securities. Foreign companies whose products are already familiar to United States buyers would find direct investment very profitable. We have an enormous market, efficient labor, and easy access to advanced technology. The attractiveness of U. S. corporate securities has been enhanced by the Foreign Investors Tax Act of 1966. The benefits granted by this legislation, as well as other factors, should result in a moderate but steady inflow of investment funds from abroad.

Responsibilities of Our Trading Partners

The United States recognizes its responsibility for adjusting its own balance of payments, and it does not intend to shirk this responsibility. At the same time, it must be recognized that the United States balance of payments is part of a world pattern of payments. The counterpart of the deficits of some countries is the surpluses of other countries. Countries in surplus have a responsibility for adjusting their balances of payments and thereby facilitating the progress toward international equilibrium that the U. S. action program makes possible. They can meet these responsibilities by reducing their barriers to trade, by increasing their aid to less-developed countries, by sharing adequately in the cost of common defense, by encouraging capital outflows, and by maintaining a satisfactory pace of domestic economic expansion. As part of this vital adjustment effort, we should be able -- indeed, we must find ways -- to work constructively with our allies on forms of bilateral and multilateral financial arrangements designed to neutralize the foreign exchange consequences of the locations of our troops and those of our allies. The arrangements should be long term and provide financial viability to our alliances.

The growth of reserves of the rest of the world will be sharply affected by the reduction in the United States deficit. Yet many countries will wish to see a gradual increase in their reserves as their international transactions expand. Therefore, it is important to implement as speedily as possible the plan agreed in outline last September to create new international reserves in the form of Special Drawing Rights in the International Monetary Fund.

II. Travel Proposals

In his message on New Year's day the President pointed out that the travel deficit in our balance of payments this year will exceed \$2 billion. To reduce this deficit by \$500 million he asked the American people to defer for the next two years all non-essential travel outside the Western Hemisphere. He also asked me to explore with the appropriate Congressional committees legislation to help achieve this objective. After some informal exchanges with the Chairman and ranking Minority Member and a good deal of collaborative staff work by the Treasury staff and the staff of the Joint Committee on Internal Revenue Taxation, I am here to present some proposals to this committee which, if adopted, will help achieve this objective.

In addition to the President's request to forego non-essential travel outside the Western Hemisphere for two years, we will seek to reduce the travel deficit by two approaches:

A. Through a program to increase the number of travelers coming to the United States. This is the permanent part of our program. It will make possible a continued increase in international travel. This is in the interest of the United States and all other nations; and

B. Through customs proposals and temporary tax measures that would induce a reduction of United States tourist expenditures abroad with the least possible impact on the number of travelers. We are also recommending an extension of the existing domestic ticket tax to international travel. We would hope that a portion of the revenues produced by this extension would be made available to finance the promotion of foreign travel to the United States.

A. Measures to Increase Travel to the United States

The Johnson and the Kennedy Administrations have both recognized

- that the long-term solution to the travel deficit should not be found through restrictive measures but must be sought through the expansion in the number of foreign visitors to the United States.
- that the United States has unique attractions which, when adequately promoted, will attract far larger numbers of foreign visitors.

With these thoughts in mind, President Kennedy in 1961 proposed, and Congress passed, the International Travel Act which established the United States Travel Service. The USTS has over the years made a major contribution through its

promotional activities abroad and has acted as a catalyst in advertising and sales promotion cooperation between Government and industry.

As part of his February 1965 balance of payments program, President Johnson asked Vice President Humphrey to form a Committee which would enlist the continuing efforts of high-level Government officials to increase coordination of activities affecting our travel receipts.

Concurrent with the establishment of this Committee, "Discover America", Inc., was formed as a private non-profit organization to bring the elements of the United States travel industry together in an all-out effort to increase the size of the tourism market. This organization worked closely with the Vice President's Committee on Travel.

As an intensification of these efforts, President Johnson on November 16 announced the appointment of an Industry-Government Special Travel Task Force under the chairmanship of former Ambassador Robert M. McKinney. The Task Force is now hard at work in developing a whole series of recommendations to increase the flow of foreign travel to the United States. In particular, the objectives of the Task Force are

- to determine practical steps which can be taken quickly to produce early improvement in the travel sector of the balance of payments;
- to determine medium and long-term measures to bring U. S. travel expenditures and receipts into better balance, with recommendations on the necessary steps that should be taken in both the private and government sectors to accomplish this objective; and
- to determine how best to help foreign visitors improve their knowledge and understanding of the United States and the American people through first-hand experience, thus providing a new bridge of understanding through tourism between the United States and other countries.

To facilitate a thorough investigation of the many facets of the problem, the Task Force has been divided into 12 working parties -- eight dealing with suggestions geared toward private industry and four concentrating on efforts which the government might contribute. I am attaching as

an exhibit a copy of the release issued by Ambassador McKinney at the time of the organizational meeting of his Task Force describing the personnel and terms of reference of these working parties.

Ambassador McKinney informs me that that Task Force has received the enthusiastic cooperation of Federal, State and local governments and of private industry, both foreign and domestic.

Through the Task Force's imaginative recommendations and the concrete steps suggested, Ambassador McKinney feels confident that travel costs to the United States will be substantially reduced, inhibitions on travel removed and promotion of the United States as a tourist center more effectively achieved.

These steps should make a trip to the United States economically and otherwise feasible to hundreds of thousands of potential visitors who have not, as yet, had an opportunity to visit our shores.

Recommendations from the 12 working parties have been completed and are now under review by the parent Task Force, which will submit its report to the President by February 19.

Ambassador McKinney's report will include an action program some elements of which have already gone into effect and others of which will go into effect during the next few months. We expect the program to increase the number of travelers to the United States and U. S. receipts from travel. It will have a substantial impact this year and a growing impact in future years.

While the long-term success of this program to increase receipts from travel to the United States should remove the necessity for making permanent the short-term temporary tax measures to be proposed, it will take some time for this program to be fully effective.

B. Measures to Reduce U. S. Travel Expenditures

The benefits of foreign travel need no elaboration by me. The free interchange of people is a basic tenet of democratic life and an ingredient of an expanding free world. But we must be prepared in times when our balance of payments is under the heavy pressure of war, and external circumstances require unusual and temporary measures in other areas affecting our payments, to try to hold down the dollars we spend abroad in travel as well as promoting increased tourism to the United States -- particularly while the latter program is getting under way.

The number of Americans traveling abroad has been expanding at a high rate. For example, the number of United States travelers to Europe and the Mediterranean areas has grown from 637,000 in 1958, the year when our large recurrent balance-of-payments deficits began, to 1,570,000 in 1966. The figure was undoubtedly higher last year, although the exact number will not be known for some months.

In only one year during the period 1958 through 1966 did the increase in the number of travelers fall below 10 percent and that was in 1961 when the Berlin crisis deterred United States travel to the European area. Excluding that year, the average annual rate of increase in number of U. S. travelers was 14 percent.

The objective in the travel area, as in other parts of the balance-of-payments program, is to forge an effective device which, as far as feasible, avoids an undue burden either on those United States citizens or on those foreign countries least able to bear it.

With these general considerations in mind, I would like to describe the specifics of our proposal.

1. General Description of Tax Proposals

The travel tax proposal contains two basic elements --

a. A permanent extension of the present 5 percent ticket tax on the cost of domestic airline travel to cover the cost of all airline transportation, whether within or without the United States, purchased in the United States and also a temporary extension of the tax to cover the cost of water transportation to a destination outside the Western Hemisphere.

b. A temporary graduated tax on the expenditures incurred in connection with a trip outside the Western Hemisphere. Expenditures would not include the cost of transportation to and from the traveler's foreign destination -- which it is proposed be taxed under the expanded transportation tax mentioned above.

The expenditure tax would generally apply to each traveler's expenditures in excess of \$7 per day of travel -- with the first \$8 of the excess taxed at a 15 percent rate and the remainder at a 30 percent rate. The tax would apply only to trips undertaken during the period after the legislation is enacted and before

October 1, 1969. Thus, it would apply to the 1968 and 1969 travel seasons.

Some general description of overseas travelers^{*/} will be helpful in understanding why we are recommending this particular tax structure.

Twenty-four percent of these travelers are going on business, 45 percent on vacation, 5 percent to study or teach, 18 percent "visiting", and 8 percent in miscellaneous categories. The visiting classification is made up of people, frequently foreign-born, visiting friends and relatives abroad.

The average length of stay is 33 days. The average daily expenditures are \$16.73 per person. However, averages are misleading. When the length of stay is analyzed by family income, we find that the lowest income travelers by far stay the longest, 51 days for those with under \$5,000 income. It is 26 days for those with over \$20,000 income. However, the amount spent per day varies as one might expect according to income. In the under \$5,000 group, it is \$9.63

^{*/} The following statistics relate only to travelers to Western Europe and the Mediterranean area, the only group for whom statistics are available. These travelers, however, represent 85 percent of all non-Western Hemisphere travelers.

per day, on the average, and in the over \$20,000 group on the average \$25.39 per day. These two factors, the variation in length of stay and the variation in per diem expenditures, produce the result that in the whole income group up to \$20,000, expenditures per trip are about the same in total. It is only over the \$20,000 level that expenditures per trip increase significantly.

The average cost of a trip to Europe is \$1,000, made up of a \$450 fare for the transportation over and back and \$550 expenditures while in Europe. A significant number of travelers, however, have over \$1,000 of expenditures, in addition to the transportation fare, while abroad. In fact, roughly one-half of the total travel expenditures are made by the travelers with over \$20,000 income -- one-third of all travelers.

Considerations in Adopting this Particular Program

In developing this tax program, we carefully considered many alternatives. We believe that the particular package we are recommending will achieve the desired restraint in the most equitable manner. Let me list for you some of the principles we followed.

First, I have already mentioned, the ideal program would be one which achieved the balance of payments savings with a minimum of trip cancellations. This, of necessity, requires that the tax not fall heavily on those with modest incomes or those of any income level who choose to travel modestly in this period.

The proposed tax program -- by being directed primarily at spending over a modest level -- is consistent with this objective. The \$7 per day exemption, graduated rate, and the low rate of tax on transportation fare will all combine to keep the tax at a modest level for one traveling inexpensively. One spending \$15 per day would pay an expenditure tax of only \$1.20 each day. For a trip of 30 days, this tax (\$36.00) when combined with an average ticket tax, would produce a total tax bill of under \$60 -- about 6.5 percent of the \$900 cost of the trip. On the other hand, the exercise of restraint on each dollar of spending above this amount would be encouraged by a 30 percent tax.

For the low income traveler -- students and foreign born visiting relatives and friends -- who spend on the average about \$10 a day, the expenditure tax would be only 45 cents

per day. Even for a 50-day trip the expenditure tax would be only \$22.50. When combined with an average ticket tax, the total would be \$45, or less than 5 percent of the cost of the trip.

Other forms of taxes -- such as a flat tax per trip, a relatively high ticket tax, or a flat tax per day -- which require every traveler to pay a specified amount regardless of his expenditure level, necessarily have their greatest impact at the lower income levels where the amount of tax is a proportionately higher percentage of the total funds available for expenditure than at higher income levels. They would achieve the necessary expenditure reduction primarily by causing large numbers of the less affluent to cancel their trips and would have little impact on the expenditures of the more affluent. On the other hand, the proposed \$7 per-day exemption, together with the lower tax rate proposed on the next \$8 of expenditures per day are specifically designed to achieve the reduction of expenditures without substantial trip cancellations.

Moreover, since those in the lower income range tend to take longer trips and spend less per day, the proposal avoids graduating the tax on the basis of the length of stay.

A second principle followed in developing the tax program was that any tax restraint on foreign travel expenditures should continue to apply as the expenditures increase. An expenditure tax of the type we are recommending meets this objective by applying the deterrent on each dollar spent over a basic exemption level. In other words, each time a traveller contemplates making an expenditure, the tax will be a factor which he must weigh in making his decision. A flat tax per trip, or even per day, does not have this continuing effect on marginal spending.

The graduated rate of the tax is designed to achieve deterrence at all income levels. Under the proposal each dollar an individual spends above the level of \$15 per day would be subject to a 30 percent tax rate -- double that applicable to amounts spent up to that figure.

A third principle which we have followed is that the tax program should be structured so as to preclude the necessity for providing numerous exceptions. We can all think of particular types of trips which we would not want cancelled. If the tax were in the form of a certain amount per trip regardless of the traveler's expenditures, it would inevitably have to be imposed at such a level as to act as a

financial deterrent to large numbers of trips, particularly by lower income travelers. This, in turn, would create immediate pressure for exemptions involving very difficult judgments as to what constitutes a trip worthy of exemption. Moreover, specific exceptions produce complexity and administrative burdens.

The program we are recommending obviates the necessity of numerous exemptions, since the impact of the tax will be small on individuals who travel modestly.

These are the general principles we have followed in structuring our tax program. By meeting them, we believe that this program will accomplish its objective of reducing foreign travel expenditures with the least impact on the number of Americans traveling overseas and without, as the President put it in his State of the Union Message, "unduly penalizing the travel of teachers, students, business people and American people who have relatives abroad whom they want to see."

Let me now turn to a more detailed description of the tax proposals:

Tax on Transportation

Existing law imposes a 5 percent excise tax on the cost of air transportation. Generally, this tax does not apply to international travel. Our proposal would permanently extend this existing air ticket tax to all amounts paid for transportation where the tickets are purchased within the United States. The tax would also be extended temporarily to water transportation between the United States and a point outside the Western Hemisphere.

While the temporary travel tax is in effect this tax, rather than the ticket tax, would apply to expenditures for air and water transportation outside the Western Hemisphere after the traveler has reached his first stop scheduled for more than 12 hours. For example, the 5 percent ticket tax would apply to a flight from the United States to the first European stop and from the last European stop to the United States. All travel within Europe between arrival and departure would be treated as an expenditure, and taxable under the temporary travel tax. Moreover, where a ticket for transportation to the United States is not subject to the ticket tax because purchased outside the United States, it

would be subject to an equivalent tax of 5 percent collected as part of the travel tax.

Tax on Travel Expenditures

The travel tax would, with few exceptions, apply to all who travel outside the Western Hemisphere, and would apply to all expenditures made in connection with the trip except transportation to and from the United States, which as I explained above, would be covered by the ticket tax.

Each traveler would be entitled to an exemption of \$7 of expenditures times the number of days he is abroad. The next \$8 of expenditures times the number of days abroad would be taxed at a rate of 15 percent. All expenditures in excess of this amount would be taxed at a rate of 30 percent.

Thus, an adult traveler going abroad for 30 days and spending \$700 in addition to the cost of transportation from the United States would be subject to a tax of \$111 computed as follows -- the first \$210 would be exempt (30 days x \$7.00); the tax on the next \$240 would be \$36 (30 days x \$8.00 x 15%); and the tax on the remaining balance of \$250 would be \$75 (\$250 x 30%).

In the case of a non-business traveler, the tax would apply to all expenditures -- meals, lodging, entertainment, purchases of tangible personal property, and transportation not part of a continuous trip to or from the United States.

In the case of a business traveler it would apply to all expenditures for meals, lodging, entertainment and travel as above but would not apply to other types of business expenses nor to the purchase of business assets, such as inventory.

Exemptions from the tax would be limited to the following:

1. Individuals (and their families, transferred or going abroad in connection with their trade, business, profession, or education, and remaining abroad for more than 120 days.
2. Individuals who establish residence outside the United States.
3. All United States Government travel.

With respect to U. S. Government travel, on January 18 the President directed the heads of all the Departments and Agencies to reduce official travel overseas to the minimum

consistent with orderly conduct of the Government's business abroad. The Bureau of the Budget will issue instructions this week to the agencies calling for approval by the Department of State of each Government-sponsored trip to international conferences abroad. By March 15 agencies will report to the President specific measures they have taken to curtail overseas travel. Thereafter, they will report quarterly on progress in achieving the President's objective.

The mechanics of the expenditure tax would be relatively simple. Before embarking on a foreign trip, each individual would deposit at his port of departure an amount of money equal to the tax he expects to owe. Rather than keep an itemized account of all expenditures he would compute the tax on a "net worth" basis. To do this he would file a statement indicating how much money and traveler's checks he is taking with him. On his return, he would make a corresponding statement of the amount of money and traveler's checks he has with him and leave this with the Customs officials at his port of entry. His formal tax return would be required to be filed with the Internal Revenue Service within 60 days after his return and any tax due would be paid.

There would be special provisions to take care of expenses paid or facilities furnished by employers.

For the ordinary tourist, the tax base would be an amount equal to the difference between the money he left the country with and the money with which he returned, plus any expenses he prepaid or charged on a credit card during his trip and the amount of any personal checks issued abroad. This method of computing the tax will eliminate the necessity of any traveler having to keep a detailed record of his expenditures while abroad.

When a family travels abroad together, they would be permitted to file a joint return aggregating all their expenditures as well as their exemptions.

Enforcement of the travel tax would be carried out by the Customs Service and the Internal Revenue Service. It is fully expected that the tax will be both effective and enforceable. The formal return will be associated with the traveler's income tax return for audit purposes.

In summary, we are proposing a tax program aimed at encouraging travelers outside the Western Hemisphere to reduce their expenditures in 1968 and 1969. The balance of

payments savings for this measure has been estimated in the neighborhood of \$250-\$300 million.

2. Customs Measures

a. Duty-Free Tourist Exemption

The estimated value of articles acquired abroad and brought into the United States during 1967 by United States residents returning from countries other than Mexico and Canada and the Caribbean area totaled approximately 200 million dollars. One hundred ten million dollars of this amount was brought in under the present \$100 Customs duty-free exemption granted to returning residents. A substantial reduction in this duty-free exemption would achieve a significant reduction in the value of articles brought into the United States by returning United States residents.

b. \$10 Gift Exemption for Parcels Arriving by Mail

An estimated 11,000,000 packages arriving by mail during 1967 were admitted duty-free under the existing exemption for gifts valued at less than \$10. In addition, many other parcels, presently being admitted without payment of duty, would have duty owing if there

were adequate Customs manpower available to assess the duty. The elimination of the \$10 gift exemption, and a more intensive processing by Customs of packages arriving from abroad by mail would bring about a decline in the shipment of such parcels to the United States. Since many such parcels are purchased by United States residents this would result in a significant balance of payments saving.

Summary of Proposals

In order to reduce foreign expenditures by returning United States residents and thereby achieve a balance of payments savings, we propose:

a. Reduction of Tourist Exemption

The present \$100 duty-free exemption granted to returning United States residents should be reduced to \$10 for persons returning from countries other than Canada, and Mexico and the Caribbean area.

b. Modification of Gift Exemption for Parcels Arriving by Mail

The \$10 duty-free gift provision for articles arriving in the mail from abroad should be reduced to \$1.00.

This will be accomplished administratively under existing law. No change is proposed in the present \$50 gift exemption law applicable to gift parcels arriving from United States servicemen in combat zones.

c. Modification of Duty Assessment Procedures Applicable to Returning United States Residents and to Certain Noncommercial Parcels

In order to minimize the increased Customs workload implicit in the changes described above, the following flat rates should be made applicable:

1. A flat 25 percent rate of duty on all dutiable articles accompanying arriving travelers, provided their aggregate value does not exceed \$500 wholesale.

2. A \$2 charge on all dutiable noncommercial parcels arriving by mail which are valued at \$10 or less retail. Articles valued at \$1 or less will continue to be free of any duty or charge.

3. A flat 25 percent rate of duty on all noncommercial importations of dutiable articles arriving by mail, railway express and other means of transportation, which are valued at more than \$10 retail but less than \$250 wholesale.

The new simplified rates proposed above reflect an average of the duty rates assessed currently under the Tariff Schedules on importations of the types under consideration. Without such a simplified duty assessment procedure, the changes recommended with respect to tourists' baggage and mail parcels would impose a staggering burden for the Bureau of Customs.

d. Resulting Balance of Payments Savings

It is estimated that implementation of all the above recommendations will achieve a balance of payments savings of about \$100 million.

Implementation of the above measures will entail increased administrative costs for the Customs Service and the Internal Revenue Service; and also for the Post Office Department to the extent its expenses in collecting the duty on parcels arriving by mail cannot be covered by postal handling charges because of the ceiling set under the Universal Postal Union Convention. Their ability to execute these measures is dependent upon the establishment of an adequate mechanism for reimbursement of these costs to the agencies involved.

This completes the outline of the measures which we propose be taken to effect a \$500 million savings in the balance of payments deficit resulting from foreign travel. This is intended to be a cooperative program involving the Congress, the Executive, and the American people. The problem is clear; the need for quick action is imperative; I urge you to give it your immediate attention.

III. Achieving An Adequate Trade Surplus

The keystone of a sound international financial position for the United States and the dollar is a substantial trade surplus.

It is natural and desirable for a rich country like the United States to export investment capital abroad, to give foreign aid, to provide its share of the common defense, and to have large numbers of its citizens traveling abroad. But all of this is possible only if, in addition to incomes from foreign investments, the United States trade surplus is large enough to finance such expenses.

The United States has consistently had a trade surplus -- an excess of exports over imports. In 1950-55 the surplus averaged \$2.2 billion; in 1955-60 it averaged \$3.8 billion; and in 1960-65 it averaged \$5.2 billion. It reached an all-time high of \$6.7 billion in 1964, but it narrowed in 1965 to \$4.8 billion and dropped much further in 1966 to \$3.7 billion, the lowest point since 1959.

There was some strengthening of our trade surplus in the first three quarters in 1967 but a sharp deterioration

in the fourth quarter eliminated the anticipated gain in
*
1967.

The question naturally arises: What happened to the fourth quarter trade figures?

Our best answer from the information available to date is that there was an upsurge of imports, more than any real worsening of our export picture, which produced this sharp decline in our fourth quarter trade surplus.

For the first three quarters of 1967, our quarterly trade surpluses were averaging about \$1.082 million. In the fourth quarter however this rate of surplus deteriorated to only \$357 million, with nearly three-fourths of the deterioration on the import side and one-fourth on exports.

Basically the upsurge in imports, which became particularly noticeable in November and December, reflects the further ~~war~~ warming-up of the domestic economy. It was just this development which we were trying to anticipate in the President's Tax Message last August.

* The figures used are calculated on the so-called balance of payments basis. On a census basis the 1967 trade surplus was about \$4.1 billion, up less than \$300 million from the previous year. The primary difference between these two sets of figures involves the ways in which certain military exports are handled.

While some special factors were at work affecting fourth quarter trade, we cannot avoid the fact that we have again moved into a situation where the rapid growth in our Gross National Product in money terms will almost inevitably bring a more than proportionate rate of increase in our imports. This was the process which, as you will recall, brought in 1965-66 the increases of from 15 to 20 percent per annum in our imports as contrasted with 9.6 percent in 1964 and 5 percent in 1963.

But the problem is not limited to imports alone. Starting with the fourth quarter of 1966 and extending through the second quarter of last year our rate of export growth over the same periods a year earlier was averaging about 7 percent. In the third quarter of last year, the rate fell to 3-1/2 percent and in the fourth quarter to less than one percent. The fact that this decline was mainly attributable to reduced exports of agricultural products does not lessen the need for a greater intensified effort to achieve and maintain a much higher rate of export growth.

Moreover, these are only the most immediate types of adverse impact on our trade from an expansion that is highly inflationary in character. In addition, wage and price

increases of the kind we are already experiencing, accentuated by the further push of a new outburst of demand, could seriously undercut our long-term competitiveness in world markets if allowed to continue into a spiraling inflation.

Thus, very dramatically the events of the last quarter of 1967, underscored by a dwindling trade surplus, provide proof positive of earlier assertions of the important relationship of the tax surcharge to our balance of trade and payments and the international position of the dollar.

In his Tax Message of August 3 last year the President stated that failure to act on his tax proposals and to restrain unnecessary spending could have the most serious consequences including: "An excessive expansion of domestic markets could again quicken the flow of imports to the United States, while rising costs and prices cut into our exports. The position of the dollar as the key element in the world's financial system could be impaired."

This proposition developed in my previous appearances on August 14, 1967, November 29, 1967 and January 22, 1968 in connection with the surcharge must be again developed in any discussion of our overall balance of payments situation and what we propose to do about it.

The keystone to the entire balance of payments program is the surcharge proposal you have before you, or some variation. The other direct measures added in the President's January 1 program to the pre-existing effort are not going to be as effective in dealing with the balance of payments problem unless these tax proposals coupled with expenditure controls, appropriate monetary policy, and a more effective voluntary program of wage-price restraint, are combined to stem the inflationary pressures which now threaten our trade surpluses, both long-term and short-term.

Let no one assume that this recent experience is an isolated phenomenon, unrelated to the past.

In the mid-1950's Europe and Japan were rapidly regaining their economic strength. Between the recessions of 1954 and 1958, the United States had a consumption and investment boom during which our price level for metals and machinery rose 20 percent (from the end of 1954 to the end of 1957). By the end of 1959 those prices -- particularly important in determining our international competitive position -- were nearly one-fourth higher than in 1954. With Europe and Japan steadily increasing their ability to produce goods for export,

conditions were being created that would make it more difficult than before for the United States to achieve an adequate surplus in the current account of balance of payments -- that is a current surplus sufficiently large to cover the flows of U. S. private and government capital to the rest of the world. In 1959 our trade surplus dwindled to less than \$1 billion and it was only with the recession of 1960 that it rebounded to a more normal range.

Again in 1965 and 1966 the decline in our trade surplus from the peak level reached in 1964 can be related to the very high rate of growth of those years. Indeed, had we held in 1965 and 1966 the trade surplus level reached in 1964 there would have been substantial balance of payments surpluses in both of those years.

Hence, our balance of payments deficits in the last three years strongly suggest that the trade surplus has been inadequate. To determine what should be done about increasing it we must examine the basic forces affecting U. S. trade.

United States exports and imports are strongly influenced by the pressure of United States domestic demand, by changes

in the U. S. competitive position, and by economic growth and policies in our major overseas markets.

What impact do these interrelated factors have on our trade?

1. U. S. Competitive Position in World Markets.--As can be seen in Table 1, in the 1960's, United States unit labor costs in manufacturing declined slightly while those of our major European competitors rose significantly. If changes in relative costs were the only determinant of export performance, then we should have noticeably increased our relative share of world markets.

Table 1.—Unit labor costs in manufacturing for selected industrialized countries since 1961¹

Country	1962	1963	1964	1965	1966 ²
United States-----	99	98	98	97	99
Canada-----	99	100	100	95	99
France-----	107	112	118	119	116
Germany-----	107	111	111	117	123
Italy-----	108	118	124	122	118
Japan-----	108	113	111	118	125
United Kingdom-----	104	102	103	109	114

1. Ratio of wages and salaries (and including supplements) to production; national currency basis.

2. Preliminary.

NOTE.—Data relate to wage earners in Italy and to all employees in other countries.

Sources: Department of Labor and Council of Economic Advisers.

In point of fact, the U.S. held its share of world trade between 1961 and 1964, as Table 2 shows.

Table 2.—U.S. Share (%) of Total World Exports of Manufactures

Year	
1961-----	25.6
1962-----	26.5
1963-----	25.6
1964-----	25.8
1965-----	23.6
1966-----	23.5

Notes.—1. An adjustment for declassified U.S. special category exports was made by subtracting \$1.0 billion from U.S. and world totals in 1965 and 1966. 2. Excludes intra-EEC and intra-EFTA trade.

Source: United Nations Monthly Bulletin of Statistics November and December 1967.

In 1966 and probably in 1967, the U.S. competitive position was eroded by increases in U.S. labor costs. Another important reason for the decline in the U.S. share of world exports in the past two years has been the sharp difference in rates of economic expansion in Europe and the U.S.

2. Impact of Differences in Economic Expansion in the United States and Europe.—The experience of the first half of the decade indicates the vital importance of sound domestic economic policies to growing U.S. trade surpluses. This is most clearly seen in an examination of the relationship of U.S. imports to the pace of U.S. economic expansion, as illustrated below:

Table 3.—U.S. GNP and Foreign Trade, 1960 - 1967

	<u>GNP (current prices)</u>		<u>Imports</u>			
	<u>\$</u> <u>billion</u>	<u>%</u> <u>change</u>	<u>\$</u> <u>billion</u>	<u>\$</u> <u>change</u>	<u>%</u> <u>change</u>	<u>As %</u> <u>of GNP</u>
1960	503.7	4.1	14.73	-.58	-3.8	2.9
1961	520.1	3.3	14.51	-.22	-1.5	2.8
1962	560.3	7.7	16.19	1.68	11.6	2.9
1963	590.5	5.4	16.99	.81	5.0	2.9
1964	632.4	7.1	18.62	1.63	9.6	2.9
1965	683.9	8.1	21.47	2.85	15.3	3.1
1966	743.3	8.7	25.51	4.04	18.8	3.4
1967	785.1	5.6	26.89	1.38	5.4	3.4
Av. 1961-64		(5.9)		(.97)	(6.2)	(2.9)

As the annual growth rate in GNP (current prices) moves up, imports climb more than proportionately. In 1965 and 1966, a period in which GNP growth exceeded 8 percent per annum, our average growth in imports exceeded 16 percent per annum.

Clearly, it was not only the rate of increase of GNP that was the causal factor, but also the fact that the economic slack which had existed in the early 1960's was being taken up in 1965 and was completely eliminated in 1966. In short, if the United States can maintain a non-inflationary pace of economic expansion, the growth in imports is likely to be much more moderate than in 1965 and 1966.

What happens in our major markets is obviously of great importance in determining the level of U. S. exports. When foreign economies -- principally Western Europe and Canada are expanding, total world markets are likely to be strong and U. S. exports are likely to rise with a general increase in world trade. Where expansion is weak -- as it was when it slowed markedly in Western Europe in 1966 and 1967 -- world trade and U. S. exports suffered. From 1960-63 to mid-1967, European industrial production increased only 26 percent

while U. S. industrial production rose 36 percent -- U. S. growth being more than a third faster. This was a major factor in the \$1.7 billion decline in the U. S. merchandise trade surplus from 1961 to 1966.

3. Foreign Trade Policies.--Trade policy of foreign governments has an important impact on the U. S. trade accounts. The Kennedy Round, just completed, which will result in substantial reduction of barriers to trade, will strengthen national economies through expansion of both exports and imports. But, as far as we can now determine, this expansion will not basically alter the trade balance of any major country.

Other changes in trade policy, however, are not neutral in their impact on trade balances. In particular, recent changes in border tax adjustments -- taxing imports and remitting taxes on exports -- of some European countries, while consistent with the existing international rules of the General Agreement on Tariffs and Trade, will have an adverse effect on the U. S. trade balance.

The above discussion shows the crucial importance to the United States trade balance of maintaining a noninflationary expansion in the United States. As in 1966, excessive increases in income -- especially when we have full employment -- will be quickly translated into higher prices and capacity bottlenecks with a resulting surge in imports and a slowdown in exports. We need the fiscal action proposed by the President on August 3, 1967 -- expenditures restraint and tax measures, including surcharges on corporate and personal income taxes. The performance of our trade account in the last few years underscores the need for responsible financial management by the Executive Branch, the Congress, management and labor.

With the economy picking up momentum in 1968, and with cost and price pressures increasing, we are faced not with the assurance of a continued improvement in our trade surplus but the threat of another downward movement.

All other efforts to improve our balance of payments position will be undermined unless we avoid the kind of excessive growth that floods us with imports and unless we return to relative price stability and cost competitiveness in the United States economy.

Business and labor also have an important responsibility to protect our trade surplus by

- keeping wage demands and price decisions consistent with national productivity performance; and
- avoiding work stoppages or the threat of work stoppages in industries vulnerable to import or export competition at a time when our balance of payments position is under pressure.

Efforts to return to the price and cost stability that characterized the first five years of the decade require business and labor to exercise the utmost responsibility in their wage-price decisions. These decisions directly affect our competitive position at home and in world markets.

Accordingly, the President has directed the Secretaries of Commerce and Labor and the Chairman of the Council of Economic Advisers to work with the leaders of business and labor to make more effective the voluntary program of wage-price restraint.

The prompt enactment of the President's tax increase program is the single most important and indispensable step this nation can take now to improve our balance of trade and

payments and protect the dollar and the international monetary system.

The Committee will recall that in my appearance before you on November 29 and again on January 22, after noting the impact of devaluation of the British pound on the international monetary system and the ensuing disturbances in the gold and foreign exchange markets, I stressed the high responsibility we bear for the maintenance of a stable international economic and monetary system and the need to take steps designed to assure confidence and stability in markets here and abroad.

I stressed then and I emphasize again both the real and psychological importance of achieving a meaningful reduction in our budget deficit by reducing expenditures and a tax increase as essential elements of responsible financial policy. Since that time a national policy of expenditure control has become manifest in the enactment by Congress of the Continuing Appropriations Act last December. The President's budget is responsive in terms and in fact to this prevailing attitude in the Congress.

But there has been no tax increase. Once again, I repeat that the tax increase is the single most important symbol of

this nation's determination to exercise fiscal discipline.

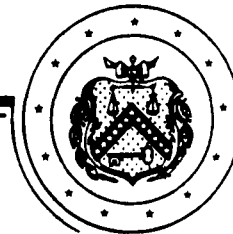
However, this is by no means the whole story on an intensified effort to achieve and maintain an adequate U. S. trade surplus. In addition to soundly managing the U. S. economy to keep it competitive and stable, we must work through international negotiating machinery, multi-lateral and bilateral, to keep world markets open by implementing the tariff reductions negotiated in the Kennedy Round and avoiding the unilateral imposition of statutory import quotas, which could lead to retaliatory action to which our trade surplus is uniquely vulnerable.

We must strive at home through improved export financing and export promotion measures to make U. S. industry more export minded and facilitate its export operations. In this connection, I should like to ask that there be made a part of the record the material in the last two paragraphs on page 69 and pages 70, 71 and 72 of the Treasury Report referred to earlier, which develop in some detail the background for the recommendations on export financing and promotion contained in the President's January 1 Message.

Finally, we must strive through international negotiations, both multilateral and bilateral, and, where necessary, through legislative measures to keep our exporters and importers in a fair competitive position in world markets. Ambassador Roth, the President's Special Representative on Trade Negotiations, is with me this morning to present a statement for the information of the Committee concerning this last aspect of the problems surrounding our trade surplus which is dealt with specifically in the President's January 1 Message under the heading "Nontariff Barriers."

Attached to my statement are technical explanations of the travel tax program and the proposed changes in the Customs rules recommended today before the Committee.

TREASURY DEPARTMENT



WASHINGTON, D.C.

January 11, 1968

FOR IMMEDIATE RELEASE
THURSDAY, JANUARY 11, 1968

McKINNEY OUTLINES TASK FORCE ON TRAVEL WORK PROGRAM AND ANNOUNCES APPOINTMENT OF COMMITTEE CHAIRMEN

Robert M. McKinney, chairman of the Industry-Government Special Task Force on Travel, today listed 12 areas of study the Task Force will pursue before submitting recommendations to the President on how to attract more visitors to the United States, and reduce our balance of payments deficit. He also announced the appointment of the chairmen who will head the 12 working parties.

Objectives of the Task Force, Mr. McKinney said, are:

- (1) to determine practical steps which can be taken quickly to produce early improvement in the travel sector of the balance of payments;
- (2) to determine medium and long term measures to bring U.S. travel expenditures and receipts into better balance, and to recommend the necessary steps that should be taken in both the private and government sectors to accomplish this objective; and
- (3) to determine how best to help foreign visitors improve their knowledge and understanding of the U.S. and the American people through first-hand experience, and to provide a new bridge of understanding through tourism between the U.S. and other countries, including Eastern European and developing nations.

The 12 committee chairmen and the areas of activity each committee will study are:

COMMITTEE ONE -- Chairman, William D. Patterson,
The Saturday Review

Provide statistical information, including projections of U.S. travel receipts and expenditures in 1970 and 1975, under various assumptions. Submit an analysis of factors which tend to limit or impede travel or which would be advantageous to build upon. Recommend the most promising major markets for rapid expansion of visitor travel, and analyze current travel trends within the United States.

COMMITTEE TWO -- Chairman, E. O. Cocke, Trans World Airlines

Evaluate the effectiveness of present American travel promotional programs by U. S. private industry, including sources of funding; target areas and objectives, and scale of efforts. Analyze potential new target areas; magnitude of efforts required; methods for financing new programs; new government-industry roles; ways to increase assistance from travel-related industries, and the possibility of cooperative participation by federal, state and local governments with private industry. Recommend how better to mobilize the travel industry, both in the U. S. and foreign countries, and new promotional programs most likely to produce significant response.

COMMITTEE THREE -- Chairman, Howard L. Clark,
American Express Company

Consider solutions to problems currently encountered in creating and selling tours within the United States. Recommend measures required to design and produce tours which can compete successfully with tours offered in competing travel areas outside the U.S.; ways to increase student and educational travel; travel for purposes of conventions, conferences, and incentive programs, and how to enlist the cooperation of U.S. international corporations and organizations.

COMMITTEE FOUR -- Chairman, Willis G. Lipscomb,
Pan American World Airways

Report what new efforts should be asked from the transportation industry -- including airline, bus, railroad, shipping, car rental, sightseeing, automobile, tire and petroleum companies.

COMMITTEE FIVE -- Chairman, Edward E. Carlson,
Western International Hotels, Inc.

Report on what new efforts should be asked from hotels and potential providers of other accommodations (e.g., youth hostels, college dormitories). Seek new government efforts for improving services and facilities in federal, state, and local parks, monument areas, etc.

COMMITTEE SIX -- Chairman, George Moore,
First National City Bank of New York

Report on what new efforts should be asked from banking, credit card, and insurance companies.

COMMITTEE SEVEN -- Chairman, Frank N. Ikard,
American Petroleum Institute

Suggest new efforts which would assist in increasing travel to the U.S. through better visitor information, services, and host programs. Consider travel attractions, museums, sightseeing services, guides, interpreters and host programs in major cities and resorts, as well as guide books, maps, travel brochures, and news media in formulating recommendations. Seek new ways to help foreign visitors improve their knowledge and understanding of the U.S. through first-hand experience with our way of life, attitudes, and aspirations.

COMMITTEE EIGHT -- Chairman, Winston V. Morrow, Jr.,
Avis Rent a Car Service

Advise on ways and means of reducing costs of travel to and within the U.S. and of acquainting potential travelers with such lowered costs. Consider the cumulative impact of costs of transportation to and within the U.S., accommodations, meals, shopping, sightseeing, travel attractions, accident, and medical insurance, etc.

COMMITTEE NINE -- Chairman, Donald G. Agger,
Department of Transportation

Examine domestic and international transportation policies of the federal government as they affect the balance of payments. Study federal policies on rates, including rate differentials and "directional fares" -- fares, making travel to the U. S. attractive -- for international travelers, carrier certifications, bilateral and multilateral transport agreements, U.S. and foreign regulations impeding competition by U.S. carriers, special arrangements for group travel and other methods of reducing cost of transportation to the U.S. Suggest ways of assisting U.S. flag carriers to obtain a larger share of international travel.

Consider ways of simplifying and facilitating frontier formalities (visas, customs, immigration, agriculture inspection, public health, etc.). Consider how better to mobilize federal programs and resources affecting tourism, including the role of a national tourist office. Consider possible relief from indirect and direct taxes for visitors and/or the travel industry. Consider anti-trust matters related to coordinated domestic programs of the tourist and travel industries (common special rates for foreign tourists in hotels and restaurants, pooling of language and other special service resources, etc.).

COMMITTEE TEN -- Chairman, Frank Hildenbrand, Texas
Tourist Development Agency

Explore new ways for state and local governments to assist through tax incentives, promotional programs, facilities development, host activities, and other measures. Seek ways of increasing cooperation with federal and/or travel industry promotion and other programs -- including possibilities of the government matching private promotional funds.

COMMITTEE ELEVEN -- Chairman, John Black,
United States Travel Service

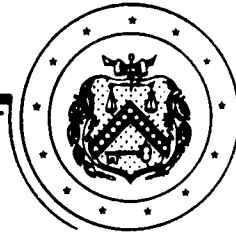
Report on what can be learned from other governments and governmental entities about methods of improving visitor earnings. Explore means of reducing barriers imposed by foreign governments which impede travel to the U.S. (Such as currency restrictions, travel restrictions, free entry provisions, etc.). Consider ways of increasing travel from Eastern European and developing nations to the U.S.

COMMITTEE TWELVE -- Chairman, Stuart Guy Tipton,
Air Transport Association

Draft a new national travel policy in line with the objectives of the Task Force and leading to intensified travel within the U.S. by both U.S. citizens and foreign nationals through: new services and technologies in the travel industry; new facilities and attractions so designed and located as to have maximum impact in attracting and serving foreign visitors; new methods of cooperation between travel and travel-related industries and the federal government; new relationships between federal, state, and local government, and new legislation and/or regulatory and administrative practices designed to make the U. S. more competitive in the international tourist market.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

February 5, 1968

FOR IMMEDIATE RELEASE

Attached are technical explanations of the travel tax program and the proposed changes in the Customs rules recommended in Secretary Fowler's statement today before the House Ways and Means Committee.

Attachments

TECHNICAL EXPLANATION
TRAVEL TAX PROGRAM

The travel tax program consists of two major proposals:

- (1) A permanent extension of the tax on transportation fares to cover international air transportation and a temporary extension of the tax to cover certain international water transportation, and
- (2) A temporary graduated tax on expenditures in connection with travel outside the Western Hemisphere.

Transportation of Persons by Air or Water

Present Law.--Section 4261 now imposes a tax upon the amount paid in the United States (the States and the District of Columbia) for taxable air transportation as defined. Taxable air transportation means generally air transportation which begins in the United States or in those portions of Canada or Mexico which are not more than 225 miles from the nearest point in the continental United States ("the 225 mile zone") and ends in the United States or the 225 mile zone and certain portions of other trips if the portion begins and ends in the United States. There is at present a partial exclusion for trips to Alaska and Hawaii generally for that portion of the transportation which is over Canada or the Pacific Ocean.

Thus, under present law if the ticket for air transportation is purchased in the United States, a trip from:

New York to Chicago	--	is taxable.
New York to Montreal	--	is taxable.
Montreal to Toronto	--	is taxable.
Montreal to Monterrey Mexico	--	is taxable.
Miami to Los Angeles via Panama	--	is taxable (regardless of length of stopover in Panama).*
Miami to Los Angeles via Caracas	--	is not taxable.*
New York to Puerto Rico	--	is not taxable.
San Francisco to Honolulu	--	taxable only on a small portion.
San Francisco to New York to London (with a 3 hour stopover in New York)	--	is not taxable.
San Francisco to New York to London (with a 7 hour stopover in New York)	--	is taxable on the San Francisco to New York portion.

* Since the trip from Miami to Los Angeles does not involve a change of direction it is considered to be a single trip which begins and ends in the United States regardless of the length of the stopover in Panama. However, once a traveler departs from the Northern portion of the Western Hemisphere (which area is defined not to include any part of South America) his trip is considered at an end even though he does not change direction. Therefore, neither the Miami to Caracas leg or the Caracas to Los Angeles leg both begin and end in the United States and therefore neither is taxable.

General Description of Proposed Change

Air Transportation.--The proposal would eliminate this inconsistent pattern of taxation and impose a tax at the domestic rate on all amounts paid within the United States (including not only the States and the District of Columbia but also Puerto Rico and all United States possessions) for air transportation both within and without the United States (including all trips described above as well as other trips between two points within the Western Hemisphere, e.g., Buenos Aires to Lima).

Certain amounts paid for air transportation would also be subject to the expenditure tax. This category includes amounts paid for transportation between two points outside the Western Hemisphere which is not part of uninterrupted transportation, which begins or ends in the Western Hemisphere. (Transportation is considered uninterrupted when the scheduled interval between the end of any segment and the beginning of the succeeding segment of such transportation is not more than twelve hours.) In these situations, the ticket tax will not be imposed in order to avoid a double tax. However, when the expenditure tax expires, amounts paid for this type of transportation will become subject to the ticket tax.

Water Transportation.--As a corrolary to imposing the transportation tax on air travel to points outside the Western Hemisphere (at lower than the expenditure tax rate), the ticket tax would

also be temporarily extended to apply to amounts paid within the United States (including Puerto Rico and the possessions) for uninterrupted transportation (as defined above) by water of a person between a port within the Western Hemisphere and a port outside the Western Hemisphere. The tax base would include amounts paid for sleeping accommodations in connection with such transportation and, if no separate charge is made, amounts paid for food and services.

Amounts Paid without the United States.--As indicated above, the ticket tax on foreign travel will not apply to transportation actually purchased outside the United States. (The present tax applies to such purchases only if transportation begins and ends in the United States and this rule will be retained.) This is provided in view of the administrative difficulty of collecting the tax as part of the purchase of the ticket in this situation. However, if the ticket tax would apply to transportation to or from a point outside the Western Hemisphere except for the fact that the ticket was purchased outside the United States, the expenditure tax (at a 5 percent rate) would apply to such purchases for the period this tax is in effect. Moreover, it is not expected that many travelers will seek to avoid the tax with respect to intra Western Hemisphere travel by purchasing their return tickets outside the United States since to do so would require forfeiting a round-trip discount which in most situations is worth at least as much as the tax avoided on the cost of the incoming leg.

Exemptions

The exemptions now applicable to the tax on amounts paid for domestic flights will continue to apply to the tax as extended.

Thus, payments for transportation furnished to the American National Red Cross or an international organization (section 4263 (b)), to State and local governments (section 4292), to the United States, if the Secretary of the Treasury makes a determination that the tax will cause a substantial burden to the United States which can be avoided by granting tax exemption, (section 4293), and to certain non-profit educational organizations (as defined in section 4294(b)) will remain exempt.

Payment of the Tax

The rules concerning payment of the tax will in general remain unchanged. Thus, while the tax is imposed on the person paying for the transportation, it will ordinarily be collected and remitted to the Government by the airlines or ship operators.

Revenue from the tax collected in Puerto Rico, the Virgin Islands, and Guam will be covered into the respective treasuries of these areas in keeping with present excise tax rules.

Effective Date

The expanded tax on air and water transportation will be effective with respect to amounts paid more than 10 days after date of enactment. However, if a ticket for transportation outside the Western Hemisphere, which would otherwise be subject to the new tax, is purchased before such effective date for a trip which is subject to the expenditure tax, the tax will be collected through the expenditure tax. The tax on water transportation will terminate with respect to transportation beginning after September 30, 1969.

Tax on Expenditures

Under this proposal, a temporary graduated tax would be imposed on certain expenditures made by a United States person in connection with a taxable trip he takes outside the Western Hemisphere or in connection with such a trip taken by another United States person. The rate of tax on these expenditures would generally be as follows: The first \$7 per day would be excluded from the tax base; the next \$8 of expenditures per day would be taxed at a 15 percent rate; and the excess would be taxed at a 30 percent rate. The cost of transportation to and from the traveler's foreign destination would be taxed at a 5 percent rate--either as part of the expanded transportation tax described above or, if that tax is not applicable, as part of the expenditure tax. The application of the exemptions and rate schedule in the case of families traveling together is discussed in a subsequent part of this memorandum.

United States Person.--The tax applies to expenditures made by a United States person in connection with his own trip or the trip of another United States person. Thus, amounts paid directly by an employer for meals and lodging of an employee while on a taxable trip would be taxable foreign travel expenditures of the employer; if the expenditures are made by the employee (even though he was reimbursed), they would be his taxable foreign travel expenditures.

If a student travels abroad during the summer on funds given to him by his parents, he is taxable on his expenditures of the trip. On the other hand, if his father pays certain of his expenses directly, the father would be taxable on those expenditures and would pay the tax either with an annual return or, if he so elects, by filing a joint return with his son.

A United States person means:

- (a) Any individual who is a resident in the United States,
- (b) A corporation or a partnership engaged in trade or businesses in the United States,
- (c) An estate or trust which is considered a United States person within the meaning of section 4920(a)(4) (relating to the Interest Equalization Tax),
- (d) The United States or any agency or instrumentality thereof,
- (e) A State including the District of Columbia, Puerto Rico and the possessions, a political subdivision or any agency or instrumentality thereof, and
- (f) A foreign corporation not engaged in trade or business in the United States which is directly or indirectly controlled by a United States person except that any expenditures made by such corporation shall be deemed to be made by the person in control. Control means the ownership of 50 percent or more of the value or voting power of the outstanding stock.

United States.--For this purpose, the United States includes the States, the District of Columbia, the Commonwealth of Puerto Rico and all possessions. Thus, residents of Puerto Rico, the Virgin Islands, Guam, and American Samoa, will be subject to the expenditure tax on their travel outside the Western Hemisphere. A tax on expenditures by such residents while traveling abroad is consistent with the fact that the foreign expenditures of these areas are considered in United States balance of payments. On the other hand, there would be no tax imposed upon expenditures made while traveling in any of these areas.

Thus, these areas would be treated in the same manner as the continental United States. Any revenue collected under the expenditure tax from residents of Puerto Rico, the Virgin Islands or Guam will be covered into the treasuries of those areas.

Taxable Trip.--Only those expenditures in connection with a "taxable trip" would be subject to the expenditure tax.

Commencement and Conclusion of a Taxable Trip.--A taxable trip of an individual shall in general commence with the individual's departure from a port or station in the United States, including the possessions and Puerto Rico. However, since trips within the Western Hemisphere are not subject to the expenditure tax, if

the individual after leaving the United States stops at a port or station in the Western Hemisphere for a scheduled interval of more than twelve hours, the taxable trip shall not begin until his departure from the last such port or station in the Western Hemisphere. The taxable trip shall end when the individual returns to a port or station in the United States; or, if he makes a prior stop at a port within the Western Hemisphere, at that time provided the stop is for a scheduled interval of more than twelve hours.

The tax will only be applicable to taxable trips beginning more than 10 days after the date of enactment of the legislation. The tax will terminate on September 30, 1969, which marks the end of the European travel season. If a person is on a trip on the termination date, he would pay tax only on the part of his trip falling within the term of the tax.

Western Hemisphere.--The Western Hemisphere means the area lying west of the 30th meridian west of Greenwich, and east of the 160th meridian west of Greenwich.

Certain Trips Excepted

Individuals establishing foreign residences.--An individual who, after his departure from the United States, establishes his residence in a foreign country would be considered on a non-taxable trip.

Students.--An individual (and his dependents) would be considered on a non-taxable trip if he spends at least 120 consecutive days--

1. Enrolled as a student in a full course of study at an educational institution outside the Western Hemisphere, or
2. Engaging on a full-time basis in educational activities which are directly related to a course of study leading to a degree he is undertaking in an educational institution in the United States.

Trade or Business.--An individual (and his dependents) shall be considered on a non-taxable trip if he is outside the Western Hemisphere for at least 120 consecutive days while engaged on a full-time basis in a trade or business or profession. This category of exceptions will cover the case of an employee who is transferred abroad by his employer for more than 120 days, an individual who goes abroad to teach on a full-time basis in a foreign school, and a professor on a sabbatical abroad who is doing research on a full-time basis in connection with his trade or business.

If the student, teacher, employee, or businessman, does not spend a total of more than 14 days outside the Western Hemisphere

before and after the period he is carrying on exempt activities, his entire trip would be exempt. If he stays longer than 14 days, thus converting his trip to a partial vacation trip, he (and his dependents) would be considered on a taxable trip, but would be permitted to exclude all expenses incurred during the period he is engaged in the exempt activities.

If the student, teacher, employee, or businessman does not stay abroad for the prerequisite 120 consecutive days, his trip would be taxable unless he could not have reasonably foreseen the circumstances which caused him to cut his trip short.

Military. A member of the armed services (and his dependents) who is transferred to a duty station outside the Western Hemisphere would be considered on a non-taxable trip during his tour of duty at that station. Any trips he makes back and forth to the Western Hemisphere during that tour would also be exempt.

Other United States Employees. An individual employed by the United States traveling in his official capacity will be considered on a non-taxable trip. If he combines his trip with a vacation, only the expenses during the period he is on official business would be excluded from the expenditure tax.

Crew Members of Ships or Airlines. An individual would not be considered on a taxable trip while he is serving as a member of a crew of a facility providing transportation to or from a port or ports outside the Western Hemisphere provided that the portion of the trip outside the Western Hemisphere does not include any period of layover longer than normally provided in similar situations.

Taxable Foreign Travel Expenditures.--In general, unless specifically excluded, the tax applies to all expenditures which are made by a United States person in connection with his own taxable trip or the taxable trip of another United States person. They include not only the traveler's own living expenses, but also those which he pays for other members of his family who are on the trip, as well as the cost of any entertaining he may do and any gifts or other purchases he may make. Expenditures for the use or maintenance of property while on a taxable trip, such as rent for an apartment or automobile, are taxable foreign travel expenditures. If an item of property (such as an automobile) is both purchased and sold during the same taxable trip, the loss, if any, would be considered an expenditure for the use of property, and therefore a taxable foreign travel expenditure. However, only expenditures made for facilities or services to be provided on the taxable trip would be considered made in connection with the trip. Thus, any expenditures for pre-trip facilities or services, such as taxi fares to the airport in the United States, costs incurred during the trip, such as in connection with the traveler's house in the United States while he is gone, or the cost of work done after the traveler's return to repair damages occurring on the trip would not be taxable foreign travel expenditures.

Expenditures of a taxable trip are taxable whether paid before, during or after the trip. For example, hotel bills and transportation fares are taxable foreign travel expenditures whether prepaid to a travel agent, paid in cash or by check while on the trip, or charged and paid for after return.

Consistent with the rules on deductibility for income tax purposes of ordinary and necessary business expenses, the expenditure tax imposed on amounts deductible as business expenses would itself be deductible.

Purchase of Property.--In general, amounts spent while on a taxable trip for the purchase of tangible personal property (other than property held for investment or property to be used in a trade or business) would be taxable. Moreover, the cost of property purchased for delivery to an individual on a taxable trip would be taxable. Thus, for example, if a person purchases a European automobile (whether before leaving or while on a taxable trip) and takes physical delivery while on that trip, the purchase price would be a taxable foreign travel expenditure. Or conversely, if a person purchases the automobile while outside the Western Hemisphere for delivery after his return to the United States, the purchase price would be subject to this tax, in addition to the normal custom duty.

Business Expenses.--In the case of an individual traveling on a taxable business trip, his business expenses, other than for transportation, meals, lodging, gifts and entertainment, would be excluded from the expenditure tax base.

Rate of Tax

The taxable foreign travel expenditures made by a United States person in connection with a taxable trip of such person or another United States person shall be subject to tax at the following rates:

Transportation to the first stop outside the Western Hemisphere or from the last stop outside the Western Hemisphere.--The expenditure tax will in general not apply to the cost of transportation to the first and from the last scheduled stop outside the Western Hemisphere of more than 12 hours. The cost of this transportation, if paid for in the United States, will be subject to the expanded transportation tax described above. If the ticket is purchased outside the United States or before the effective date of the expanded transportation tax, for a trip taxable under the expenditure tax, the expenditure tax will apply but only at a 5 percent rate.

Amounts paid for food and services (where no separate charge is made), and seating or sleeping accommodations, during the period transportation is subject to the 5 percent tax rate shall also be taxed at the lower 5 percent rate. Thus, if a United States person takes a 30-day cruise which makes no stops within the Western Hemisphere and which makes its first stop outside the Western Hemisphere of more than 12 hours on the 5th day and makes the last such stop on the 25th day, one-third of the cruise fare plus any separate charge for sleeping accommodations will be subject to tax at a 5 percent rate either under the transportation tax (if paid for in the United States) or the expenditure tax. The remaining two-thirds of the cruise fare and separate sleeping accommodations' charge and any additional expenditures (such as for sightseeing or food) not covered by the basic fare will be subject to the expenditure tax at the regular rates. As another example, if an individual flies from New York to Paris and, after a scheduled two-hour stopover, continues to Rome, the entire cost of the transportation from New York to Rome would be taxed at 5 percent. However, if his stopover in Paris is scheduled for longer than 12 hours, only the cost of the transportation from New York to Paris is taxed at 5 percent and the remainder would be taxed at the regular expenditure tax rate.

All Other Taxable Expenditures.--All other taxable expenditures will be taxed on the following basis:

(a) Exclusion from tax.--Each traveler is entitled to a \$7 daily exclusion from the expenditure tax base. The amount excludible under this provision for a taxable trip shall be computed by multiplying the number of days during any part of which the individual was on such taxable trip by his exclusion rate.

(b) 15 percent rate.-- Expenditures in the excess of the amount excluded under the above provision shall be subject to tax at the rate of 15 percent to the extent they do not exceed \$8.00 multiplied by the number of days during which such individual was on such taxable trip.

(c) 30 Percent Rate.--The remaining expenditures shall be subject to tax at the rate of 30 percent.

Where expenses are paid for a traveler by another person, they will be taxed to such other person at the 30 percent rate unless the payor joins with the traveler in filing a joint return in which case any unused benefit from the exemption or lower rates may be claimed by the payor.

For example, if a corporate employee goes to London on business for 10 days and spends \$200 for taxable expenditures (whether or not he is reimbursed by his employer) he would pay a tax of \$27 computed as follows:

					Tax Rate	Tax	
Exclusion	\$7	X	10 days	=	\$70	0	-0-
15% rate	8	X	10 days	=	80	15%	\$12
Remainder - 30% rate					50	30%	15
					<u>\$200</u>		<u>\$27</u>

If in addition to his plane fare to London, the employer directly paid for the employee's hotel bill of \$200, the employer would pay a tax of 30 percent on this amount, or \$60.

As another example, assume an individual traveling in Europe has his transportation and hotel arranged for in advance and paid for by his parent. If the parent files a separate return, he will be taxable at 30 percent on the entire amount so paid and the child will be entitled to the exclusion and the 15 percent rate on his own expenditures. However, if any part of the benefit of the exclusion or the 15 percent rate would otherwise be lost, the parent may file a joint return with the child covering all expenses of the dependent's taxable trip and apply the exclusion and the 15 percent rate to their combined expenditures.

Computation of the Tax

In order to preclude the necessity of travelers having to keep detailed records of their expenses, taxable foreign travel expenditures would be computed, to the greatest extent possible, by a travel net worth method. For many people this would involve merely subtracting the money with which they returned from the cash and traveler's checks with which they left and adding this to the amounts paid before the trip began.

More specifically, the first step in the computation for all travelers would be to determine the cash expenses of the trip. To do this, the amount of money with which a person returns from a taxable trip would be subtracted from the sum of the amount of money with which he departed plus all amounts received while on the taxable trip. Amounts received while on the trip must be included regardless of their origin. Thus, withdrawals from domestic or foreign banks, money sent from home, compensation for services received while abroad or money received from the sale of property, would be included.

The second step in the computation would be to add to the cash expenditure figure, the amounts of expenditures in connection with the taxable trip paid before the taxable trip began, the amounts charged while on the taxable trip, and the amount of checks cashed while on the taxable trip. These are all amounts of which the traveler will have a record, e.g., credit card statements, personal check stubs. The resultant figure would represent the tax base for most travelers, and would be taxed according to the graduated rates of 15 and 30

percent or, in the case of certain transportation, the 5 percent transportation tax. For others, a further reduction would be made for expenses specifically excludible from taxable foreign travel expenditures (such as the cost of business inventory). The figure resulting from these reductions would represent their taxable foreign travel expenditures.

In the case of a return filed by a person who paid the expenses of a traveler (such as an employer), the taxable foreign travel expenditures would be itemized (rather than computed on any travel net worth method). However, since expenditures in connection with the taxable trip of another person are likely to be for major items, such as airline tickets and hotel bills, itemization should not be burdensome, and, in any event, must be done for income tax purposes if they are business expenses.

Estimated Tax

Every individual, at his point of departure from the United States for a period during which he reasonably expects to be on a taxable trip, and whether or not he plans to make a stopover in the Western Hemisphere, would be required to make a declaration of his estimated tax with respect to that taxable trip and pay the amount of the estimate to the Internal Revenue Service. He would include in his declaration a statement of the amount of cash (and traveler's checks) he is taking on the taxable trip. This figure is necessary in order to utilize the travel net worth method for computing cash expenditures. Appropriate procedures will be developed for filing the declaration so that compliance with the requirement may be verified before the traveler's departure.

The accuracy of the cash statement would be subject to verification at the point of departure by customs officials or other Treasury officials.

If a United States person departs on a taxable trip from a port in the Western Hemisphere outside the United States, and he did not make the required declaration and statement upon leaving the United States, he will be subject to penalty unless he can show such departure was not expected. In any event, the declaration or statement, if not previously filed, would be filed at this time.

Any individual returning from a taxable trip would be required to make a statement of his incoming cash (and traveler's checks) at the time he is processed through United States Customs. This statement would provide the incoming cash balance from which the travel net worth would be computed, and the accuracy would be subject to verification by a customs official.

Returns and Payment of Tax

A tax return for a taxable trip, together with payment of any balance due, would be required to be filed with the Internal Revenue Service by the traveler within 60 days after his return. This will allow the taxpayer adequate time to receive all necessary credit card and banking records for preparation of the return. Of course, the return may be filed immediately upon arrival. A husband, wife, and any of their dependent children who travel together on a taxable trip may make a single taxable trip return jointly with respect to such trip. Such a return may be filed even though one

or more of such individuals has no taxable foreign travel expenditures. A joint return would allow a family to utilize the full per diem exemption and graduated rate schedule available to each traveling member without requiring that each have separate expenditures to absorb them.

A United States person who paid a portion or all of the expenses of another United States person's taxable trip, and was not on that taxable trip himself, would be required to file an annual tax return covering all such expenditures during the taxable year or in lieu thereof he may join in the taxable trip return filed with respect to the expenses of that taxable trip. Liability for tax shown on a joint return would be joint and several.

Administration and Procedure

Generally the administrative and procedural requirements applicable to other excise taxes would be applicable to this expenditure tax. Thus, for example, the general provision for penalties for failure to file returns, requirements for claims for refund, assessment and collection procedures, and statutes of limitations would apply to the administration and procedure of this tax.

Two new provisions would be added to insure compliance with the requirements for declaration and payment of estimated tax.

A flat penalty of \$200 would be imposed for failure to ~~make~~ a declaration of estimated tax and statement as to cash on hand, as required at the time of departure from the United States unless it were shown that such failure were due to reasonable causes. Thus, if an individual flew from New York to Europe without making a declaration and statement, a \$200 penalty would be imposed for failure to ~~make~~ the declaration in New York. A significant penalty is necessary because of the importance of having an individual establish his outgoing cash figure for purposes of computing the tax base. An underestimation penalty would be imposed of 10 percent of the underpayment of estimated tax. The amount of the underpayment would be the difference between the estimated tax payment ~~and~~ 80 percent of the tax shown on the taxable trip return. The purpose of this 80 percent rule is to allow some leeway for errors in estimation.

TECHNICAL EXPLANATION

PROPOSED CHANGES IN CUSTOMS RULES RELATING TO TOURIST EXEMPTIONS AND PROCESSING OF CERTAIN NON-COMMERCIAL IMPORTATIONS

The proposal is intended to reduce noncommercial expenditures of dollars abroad where such expenditures would further adversely affect our balance of payments. It would do this in several ways. It would lower the duty exemption allowed returning residents. It would provide for a flat rate of duty on articles brought in by travelers and in the mail or otherwise within certain monetary limits. This would ease the administrative burden of handling noncommercial mail importations. At the same time the proposal would not interfere with the legitimate business interests of manufacturers or sellers abroad, or of American businessmen in the import trade.

The proposal would not assess any duty or charge on articles which are themselves free of duty under existing provisions of the Tariff Act. Most of such articles would be works of art, paintings, books, American goods returned, United States origin personal effects of residents abroad and similar items.

The Reduced Tourist Exemptions

The present tourist exemptions granted to returning U. S. residents permit the importation duty free of foreign acquisitions not exceeding a total retail value of \$100. This exemption is granted to American residents who have been abroad for more than 48 hours and may be used only once each 31 days (in the case of persons arriving from Mexico the time limit is waived). The resident is permitted to include

within this exemption one quart of alcoholic beverages. This exemption is applicable to residents returning from any area or country. However, a special exemption is granted to residents arriving from the Virgin Islands and other U. S. insular possessions. This special exemption permits the importation of acquisitions up to a value of \$200, of which not more than \$100 may be acquired outside the Virgin Islands or other insular U. S. possessions, and may cover not more than one gallon of alcoholic beverages of which not more than one quart may be acquired outside the Virgin Islands or other insular possessions.

The proposal would reduce the duty-free exemption to \$10 for U. S. residents returning to the United States from any place other than Canada, Mexico, and the Caribbean area. The continued maintenance of the \$100 exemption for residents returning from Canada, Mexico, and Caribbean area countries is based on the special relationship between the United States and those countries. The definition of Caribbean countries or areas excludes the Virgin Islands of the United States since they are given special treatment and also excludes Cuba because of our trade restrictions against that country.

The new \$10 tourist exemption would be based on the retail value and would be available only after an absence of 48 hours and could be used only once each 31 days. The present privilege permitting the inclusion of one quart of alcoholic beverages would be retained.

Foreign acquisitions accompanying the returning U. S. resident valued in excess of the \$10 exemption would be dutiable at a flat

25 percent of the value of the wholesale merchandise, but articles otherwise free under the Tariff Schedules would be exempt from the application of the flat duty rate. The 25 percent rate would be applied on articles accompanying the resident for noncommercial use up to an aggregate value of \$500 wholesale. Such articles exceeding \$500 in value would be dutiable at the standard rates of duty. In addition to any customs duties, all articles would, of course, be subject to any applicable Internal Revenue taxes.

Consistent with the reduction in the duty-free allowance for tourists, the special exemption applicable to the Virgin Islands and certain other United States insular possessions would be partially changed so as to limit duty-free acquisitions outside Canada, Mexico and the Caribbean to \$10. Articles accompanying returning residents intended for commercial use would be assessed duty at standard rates.

Mail Shipments

At present all arriving mail parcels undergo a preliminary screening to identify parcels supposed liable to duty. Such articles as newspapers or low-value items (under \$1) are stamped "passed free" and returned to the Post Office Department for delivery. The same "passed free" status is given to articles identifiable as gifts valued at less than \$10 and to gifts valued at less than \$50 for servicemen in combat areas.

Nondutiable personal effects of U.S. citizens abroad and other items obviously free of duty are returned immediately to the Post Office Department for delivery.

The \$50 gift exemption for servicemen in combat areas would be retained. The \$10 duty-free exemption for all gift parcels, including those mailed by military personnel stationed abroad in non-combat areas, would be reduced to \$1 retail by regulation. The retention of the exemption for articles valued at \$1 or less is believed necessary since it would be impracticable to assess duty on such articles which comprised approximately 25 million parcels received during 1967. The value of such articles is extremely low -- estimated to average approximately 40 cents a piece.

On dutiable mail shipments valued at over \$1 and \$10 or less retail, the proposal would require collection of \$2, in lieu of any other duty or tax. This \$2 would approximate the average duty and tax on such articles. Dutiable noncommercial mail shipments valued at over \$10 but not over \$250 wholesale would be assessed at the flat rate of 25 percent ad valorem. Dutiable commercial mail shipments valued at over \$10 and not over \$250 would be assessed at the rates of duty provided under the Tariff Schedules. In addition to the above amounts, the Post Office Department would continue the present practice of charging a 50 cent handling fee on all mail parcels on which it collects duty.

All shipments arriving in the mail valued in excess of \$250 wholesale, would require formal entry and would be assessed at the rate of duty provided under the Tariff Schedules.

Shipments Valued At \$250 or Less Which Arrive Otherwise Than in the
Mails or Accompanying a Person

No duty or charge would be imposed in connection with the arrival of articles which are themselves free of duty under existing provisions of the Tariff Act.

Dutiable noncommercial shipments valued up to \$250 wholesale would be assessed at a flat rate of 25 percent. Dutiable commercial articles would be assessed duty under the Tariff Schedules.

Determination of the 25 Percent Flat Rate of Duty

An analysis of present duty rates applied to articles typically arriving by mail and in passengers' baggage indicates that a 25 percent flat rate of duty would approximate the average duty which could be expected to be collected on merchandise affected by this provision. The flat rate would be in addition to the internal revenue taxes otherwise applicable.

Estimated Foreign Expenditure Reductions

During 1967, the total value of foreign acquisitions made by returning U. S. residents arriving from all foreign countries was estimated to be in excess of \$362 million. Of this total, persons arriving from Canada, Mexico and the Caribbean countries (including Caribbean cruise passengers) accounted for slightly over \$162 million. The value of articles acquired by returning U. S. residents arriving from other countries was approximately \$200 million. Approximately

\$110 million was brought in by persons whose purchases totaled less than \$100 per person, while approximately \$90 million was brought in by persons whose foreign acquisitions exceeded the present duty-free exemption.

The total reduction in foreign acquisitions to be achieved by reducing the tourist exemption to \$10 is estimated to be approximately \$50 million.

We estimate that the value of foreign acquisitions by persons now bringing in less than \$100 each will be reduced by \$45 million or approximately 40 percent of the total purchases made by this group.

The effect on foreign acquisitions by the approximately 200,000 persons who now exceed our duty-free exemption and pay duty would be much less drastic. If we can assume that the foreign acquisitions by these persons will be reduced by an amount roughly equivalent to the additional duty (\$23) which they would have to pay, the total reduction in foreign acquisitions by U. S. residents would be nearly \$5 million.

It is estimated that the total value of the 55 million mail parcels which arrived in the U. S. during 1967 was approximately \$500 million. Of this 55 million total, an estimated 11 million parcels were gifts or purported gifts said to be valued at less than \$10; 4 million were gifts valued at less than \$50 from servicemen in combat areas; and 25 million were "flats," newspapers, periodicals, samples, and shipments of insignificant value. Of the remaining 15 million parcels duty was

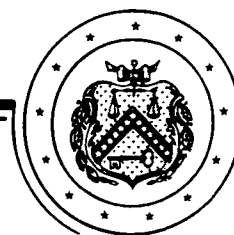
assessed on 1,600,000 parcels. However, our studies indicate that approximately one-third of the 15,000,000 parcel total would have been dutiable if adequate manpower was available to properly handle them.

Certain parcels now included in the present \$10 gift exemption are bona fide gifts mailed from nationals of foreign countries to persons in the United States. While elimination of this privilege with respect to such parcels will not affect expenditures of U. S. dollars abroad, it is nevertheless believed necessary to eliminate this free-gift privilege entirely because it is subject to widespread abuse and because, in practice, it would be difficult to distinguish between gifts from foreign nationals and those from U. S. tourists.

Of the 11 million gift parcels under \$10, we estimate approximately 4 million from U. S. tourists would be discouraged if the existing gift exemption were eliminated. The average value of these parcels is estimated to be \$7. Therefore, foreign expenditure curtailment of approximately \$28 million would be achieved. The application of a flat rate of duty to the remaining noncommercial shipments, by simplifying Customs' administrative task, would allow it to assess duty on an appreciable number of packages which now escape duty because Customs manpower cannot cope adequately with the number of packages involved. Closing this loophole will probably deter the sending of a number of these packages. (Of course, this increased efficiency

would be somewhat offset by the need for additional manpower to process the gifts which would become dutiable. Even the relatively simple assessment of a flat \$2 involves more work than the present practice of passing such gifts free.) It is a conservative estimate that approximately an additional \$12 million in duty collections and a reduction in foreign acquisitions of about \$40 million will result from the above-proposed changes in the Customs processing of foreign mail parcels.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 5, 1968

FOR IMMEDIATE RELEASE

INDUSTRY-GOVERNMENT SPECIAL TRAVEL TASK FORCE TO MEET FEBRUARY 12 AND 13

The industry-Government Special Task Force on Travel will meet in Washington on February 12 and 13 to consider its report to the President, Task Force Chairman Robert M. McKinney announced today.

The report, to be submitted to the President by February 19, will detail specific immediate steps and outline longer term steps which can be taken to encourage a substantial increase in the number of foreign visitors to the United States, Mr. McKinney said.

At the first meeting of the Task Force on January 11, 12 committees were formed to study the various aspects of the Task Force's mission -- eight working parties dealt with actions in the private sector and four dealt with actions by federal, state, and local governments.

Recommendations of the 12 committees will form the basis of the Task Force's report to the President, Mr. McKinney said.

The 14 members from private industry are: William Bernbach, president, Doyle, Dane and Bernbach, New York, N.Y.; Professor Daniel J. Boorstin, History Department, University of Chicago, Chicago, Ill.; John A. Burns, Governor of Hawaii, Honolulu, Hawaii; Edward E. Carlson, president, Western International Hotels, Seattle, Wash.; Howard L. Clark, president, American Express Company, New York, N.Y.; Arthur Frommer, president, Arthur Frommer, Inc., New York, N.Y.; Frank Hildebrand, executive director, Texas Tourist Development Agency, Austin, Tex.; Frank N. Ikard, president, American Petroleum Institute, New York, N.Y.; John H. Johnson, president and editor, Johnson Publishing Co.; Chicago, Ill.; Willis G. Lipscomb, retired senior vice president and director, Pan American World Airways, New York, N.Y.; Winston V. Morrow, Jr., president, Avis Rent A Car System, Garden City, N.Y.; William D. Patterson, vice president and associate publisher, Saturday Review, Inc., New York, N.Y.; Gerald Shapiro, vice president and general manager, Hertz Rent A Car Division, New York, N.Y.; and Lew R. Wasserman, president MCA, Inc., Universal City, Calif.

The six members from government are: Donald G. Agger, Assistant Secretary for International Affairs, Department of Transportation; John W. Black, Director, U.S. Travel Service, Commerce Department; Governor Andrew F. Brimmer, Board of Governors, Federal Reserve System; Charles S. Murphy, Chairman, Civil Aeronautics Board; Harry M. Shooshan, Deputy Under Secretary for Programs, Interior Department, and Anthony M. Solomon, Assistant Secretary for Economic Affairs, Department of State.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

February 7, 1968

FOR IMMEDIATE RELEASE

UNITED STATES-NETHERLANDS ESTATE TAX TREATY DISCUSSIONS TO BE HELD

The Treasury Department **announced today that** discussions will be held in Washington in late March between representatives of the United States and the Netherlands on an estate tax treaty between the two countries to eliminate double taxation of estates and inheritances.

Presently, there is no estate tax treaty between the two countries.

Persons who have an interest in such an estate tax convention and who wish to offer comments or suggestions may wish to consult existing United States estate tax treaties, such as those with Canada, Italy, or Japan, which have been published by the Department of State in the series called "United States Treaties and Other International Agreements". They may also wish to consult the "Draft Double Taxation Convention on Estates and Inheritances", a report published in 1966 by the Fiscal Committee of the Organization for Economic Cooperation and Development (OECD).

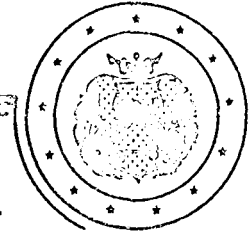
Comments and suggestions in connection with the United States-Netherlands negotiations should be submitted by March 15, 1968 to Assistant Secretary of the Treasury Stanley S. Surrey, United States Treasury Department, Washington, D. C. 20220

F-1157

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TREASURY DEPARTMENT

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WASHINGTON, D. C.

February 8, 1968

FOR IMMEDIATE RELEASE

TREASURY ANNOUNCES \$4 BILLION NEW CASH BORROWING

The Treasury Department announced today that it is offering for cash subscription \$4 billion, or thereabouts, of 15-month 5-5/8% Treasury Notes of Series B-1969 at par.

The notes will be dated February 21, 1968, will mature May 15, 1969, and will be issued in registered and bearer form. Interest will be payable on May 15 and November 15, 1968, and May 15, 1969.

Subscriptions will be received for one day only, on Tuesday, February 13. Any subscription, with required deposit, addressed to a Federal Reserve Bank or Branch, or to the Treasurer of the United States, Washington, D. C. 20220, and placed in the mail before midnight February 13, 1968, will be considered timely.

The payment date for the notes will be February 21, 1968. Payment may be made through credit to Treasury Tax and Loan Accounts.

Subscriptions from banking institutions for their own account, Federally-insured savings and loan associations, States, political subdivisions or instrumentalities thereof, public pension and retirement and other public funds, international organizations in which the United States holds membership, foreign central banks and foreign States, dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions with respect to Government securities and borrowings thereon, and Government Investment Accounts will be received without deposit. Subscriptions from all others must be accompanied by payment of 2 percent of the amount of notes applied for, not subject to withdrawal until after allotment.

Subscriptions from commercial banks, for their own account, will be restricted in each case to an amount not exceeding 50 percent of the combined capital (not including capital notes or debentures), surplus and undivided profits of the subscribing bank.

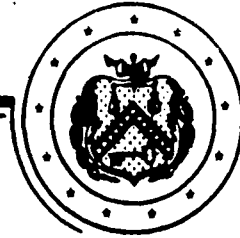
The Secretary of the Treasury reserves the right to reject or reduce any subscription, to allot less than the amount of notes applied for, and to make different percentage allotments to various classes of subscribers. Subject to these reservations subscriptions in amounts up to and including \$200,000 will be allotted in full and subscriptions over \$200,000 will be allotted on a percentage basis but not less than \$200,000.

F-1158

Commercial banks and other lenders are requested to refrain from making unsecured loans, or loans collateralized in whole or in part by the notes subscribed for, to cover the deposits required to be paid when subscriptions are entered, and banks will be required to make the usual certification to that effect.

All subscribers are required to agree not to purchase or to sell, or to make any agreements with respect to the purchase or sale or other disposition of the notes subscribed for under this offering at a specific rate or price, until after midnight February 13, 1968.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR RELEASE 6:30 P.M.,
Friday, February 9, 1968.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated November 16, 1967, and the other series to be dated February 15, 1968, which were offered on February 9, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, or thereabouts, of 91-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	91-day Treasury bills maturing May 16, 1968		:	182-day Treasury bills maturing August 15, 1968	
	Price	Approx. Equiv.: Annual Rate		Price	Approx. Equiv.: Annual Rate
High	98.734	5.008%	:	97.354	5.234%
Low	98.720	5.064%	:	97.326	5.289%
Average	98.726	5.040%	1/:	97.333	5.275% 1/

58% of the amount of 91-day bills bid for at the low price was accepted
11% of the amount of 182-day bills bid for at the low price was accepted

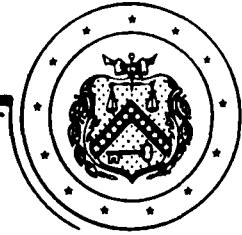
TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 19,842,000	\$ 9,842,000	:	\$ 23,063,000	\$ 12,063,000
New York	1,957,657,000	999,517,000	:	1,627,511,000	712,591,000
Philadelphia	28,528,000	11,409,000	:	18,147,000	10,058,000
Cleveland	40,374,000	36,374,000	:	60,281,000	19,474,000
Richmond	9,500,000	9,500,000	:	4,655,000	4,032,000
Atlanta	52,900,000	43,900,000	:	41,667,000	17,815,000
Chicago	268,318,000	190,958,000	:	255,575,000	141,606,000
St. Louis	50,820,000	45,520,000	:	40,621,000	27,463,000
Minneapolis	17,778,000	8,778,000	:	16,201,000	5,756,000
Kansas City	29,640,000	29,220,000	:	20,662,000	10,422,000
Dallas	30,491,000	22,071,000	:	19,488,000	9,288,000
San Francisco	111,802,000	93,038,000	:	89,903,000	29,453,000

TOTALS \$2,617,650,000 \$1,500,127,000 a/ \$2,217,774,000 \$1,000,021,000 b/

Includes \$222,575,000 noncompetitive tenders accepted at the average price of 98.726
Includes \$117,373,000 noncompetitive tenders accepted at the average price of 97.333
These rates are on a bank discount basis. The equivalent coupon issue yields are
5.19% for the 91-day bills, and 5.51% for the 182-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR IMMEDIATE RELEASE

February 9, 1968

PRELIMINARY RESULTS OF TREASURY REFUNDING

Preliminary figures show that \$5,116 million, or 21.0% of the \$24,331 million securities of the five issues eligible for exchange have been exchanged for the new 7-year 5-3/4% notes offered in the current refunding. This includes \$3,836 million, or 31.8%, of the eligible securities held outside the Federal Reserve Banks and Government accounts.

Of the total securities exchanged, \$2,162 million, or 82.0% were exchanged by holders of the \$2,635 million of the notes maturing February 15, 1968, and \$2,954 million or 13.6%, were exchanged by holders of the \$21,696 million note and bond issues maturing August 15 and November 15, 1968.

Of the total securities held outside the Federal Reserve Banks and Government accounts \$1,241 million, or 72.4% of an aggregate of \$1,713 million, of February 15 maturities and \$2,595 million, or 25.1% of an aggregate of \$10,347 million, of August 15 and November 15 maturities were exchanged.

Following is a breakdown of the securities eligible to be exchanged (amounts in millions):

<u>Security</u>	<u>Date Due</u>	<u>Amount</u>	<u>Total Exchanged</u>	<u>Unexchanged Amount</u>	<u>%</u>
5-5/8% notes, A-1968	2/15/68	\$ 2,635	\$2,162	\$ 473	18.0
<u>PREREFUNDING</u>					
4-1/4% notes, C-1968	8/15/68	6,444	487	5,957	92.4
3-3/4% bonds, 1968	8/15/68	3,747	1,117	2,630	70.2
5-1/4% notes, D-1968	11/15/68	9,913	916	8,997	90.8
3-7/8% bonds, 1968	11/15/68	1,592	434	1,158	72.7
Total prerefunding maturities		<u>\$21,696</u>	<u>\$2,954</u>	<u>\$18,742</u>	<u>86.4</u>
Grand Total		<u>\$24,331</u>	<u>\$5,116</u>	<u>\$19,215</u>	<u>79.0</u>

Details by Federal Reserve Districts as to subscriptions will be announced later.

F-1160

REMARKS OF THE HONORABLE ROBERT A. WALLACE
ASSISTANT SECRETARY OF THE TREASURY
BEFORE THE ROTARY CLUB OF CHICAGO
SHERMAN HOUSE, CHICAGO, ILLINOIS
TUESDAY, FEBRUARY 13, 1968, 1:00 P. M.

THE PERILS OF PROSPERITY -- 1968

A PERSON WHO ACHIEVES A PROSPEROUS CONDITION IS SAID TO BE ON "EASY STREET." YET, AS A NATION ENTERING THE EIGHTH YEAR OF OUR LONGEST EXPANSION IN HISTORY, WE HAVE LEARNED THAT THE PATH OF PROSPERITY IS NOT "EASY." IT IS, INSTEAD, RATHER BUMPY AND DIFFICULT. BUT IT BEATS BEING STUCK IN THE MUD BY A COUNTRY MILE.

PROSPERITY'S PROBLEMS -- AND VALUES

READING ABOUT U. S. ECONOMIC AND FINANCIAL PROBLEMS ONE MAY WELL ASK WHY WE HAVE THEM. THE FACT IS THAT THESE ARE THE WORRIES OF PROSPERITY. WE COULD QUICKLY BANISH THEM WITH AN OLD-FASHIONED RECESSION SUCH AS OCCURRED THREE TIMES IN THE SEVEN YEARS BEFORE THE PRESENT EXPANSION BEGAN. A RECESSION WOULD DRASTICALLY CURTAIL INFLATIONARY PRESSURES AND PROBABLY PROVIDE A QUICK REDUCTION IN OUR BALANCE OF PAYMENTS DEFICIT. BUT FEW OF US WOULD WILLINGLY PAY THE PRICE OF WIDESPREAD UNEMPLOYMENT, SLOW SALES, SHRINKING PROFITS, AND LOST PRODUCTION. THUS, THE BETTER WAY TO DEAL WITH THE WORRIES OF PROSPERITY IS WITH SELF-DISCIPLINE.

THE PRIMARY PERIL OF PROSPERITY IS THAT INFLATIONARY IMBALANCES MIGHT DEVELOP AND KNOCK US INTO A RECESSION -- THE OLD BOOM AND BUST SYNDROME. AVOIDING THIS WILL REQUIRE FISCAL RESPONSIBILITY. WHAT DO WE MEAN BY FISCAL RESPONSIBILITY? AS A DEMOCRATIC NATION, WE MUST IMPOSE ON OURSELVES THE COMPARATIVELY SMALL PRICE OF GOVERNMENT EXPENDITURE RESTRAINTS, MODEST TAX INCREASES, AND BALANCE OF PAYMENTS RESTRICTIONS. THIS WILL NOT BE POPULAR, BUT IT IS NECESSARY IN ORDER TO PRESERVE THE VASTLY GREATER GOOD -- A STABLE PROSPERITY.

OF COURSE, THE PRESSURES ON OUR ECONOMIC SYSTEM STEM VERY LARGELY FROM THE COSTS OF VIETNAM. THE REASON THESE COSTS, PER SE, ARE BURDENSOME, HOWEVER IS THAT THEY HAVE BEEN PILED ON TOP OF AN ECONOMY ALREADY VERY NEAR FULL EMPLOYMENT, WITH LITTLE SLACK TO ABSORB THE EXTRA DEMANDS ON OUR PRODUCTIVE CAPACITY. SO WE MUST HOLD DOWN THE GROWTH OF OTHER DEMANDS -- BOTH IN THE GOVERNMENT AND IN THE PRIVATE SECTORS -- IN ORDER TO ACCOMMODATE OUR VIETNAM NEEDS.

IN SOME RESPECTS, MANY AMERICANS MAY HAVE COME TO FEEL A LITTLE GUILTY ABOUT ENJOYING PROSPERITY. IT SEEMS SO SELF-INDULGENT AND EVEN SELFISH. IT IS TRUE THAT PROSPERITY PRODUCES ITS OWN BRAND OF EXCESSES. IT PROBABLY BREEDS SMUGNESS AND SLOTH AS WELL AS GREED AND SOCIAL DISSATISFACTION.

BUT THE PURPOSE OF HIGH EMPLOYMENT IS NOT TO PROMOTE A LA DOLCE VITA KIND OF EXISTENCE -- FAR FROM IT. THERE IS A POSITIVE AND UNSELFISH SIDE OF AN EXPANSION WHICH MAKES ITS PRESERVATION THOROUGHLY WORTHWHILE. FOR ONLY SUCH AN ENVIRONMENT PROVIDES THE JOB OPPORTUNITIES NEEDED FOR THE POOR AND THE DISADVANTAGED TO ESCAPE THE TRAP OF GRINDING POVERTY. ONLY IN A GROWING ECONOMY DO YOUNG PEOPLE REALIZE THEIR FULL ECONOMIC POTENTIAL. ONLY A HIGHLY PRODUCTIVE NATION PROVIDES ITS SOLDIERS WITH THE GOODS AND SERVICES THEY NEED. ONLY IN THESE SURROUNDINGS CAN OUR CORPORATIONS HAVE THE NECESSARY INCENTIVES FOR INVESTMENT SO IMPORTANT TO RISING LIVING STANDARDS AND SCIENTIFIC ADVANCEMENT. ONLY DURING SUCH A PERIOD DO FUNDS FLOW FREELY TO SCHOOLS, COLLEGES, HOSPITALS, HEALTH RESEARCH, AND OTHER VALUABLE PURSUITS.

A STABLE AND THRIVING U. S. ECONOMY IS THUS A SINE QUA NON FOR THE SUSTAINED ADVANCEMENT OF SOCIETY, WHETHER IT BE SOCIAL, SCIENTIFIC, OR CULTURAL.

CONSIDER, FOR A MOMENT, THAT IN THE PAST SEVEN YEARS OF UNBROKEN EXPANSION:

- MORE THAN 12 MILLION AMERICANS HAVE MOVED OUT OF THE POVERTY CATEGORY.
- THE OVERALL RATE OF WORKERS WITHOUT JOBS HAS BEEN CUT IN HALF, FROM 7 PERCENT TO 3-1/2 PERCENT. THE NON-WHITE JOBLESS RATE HAS DROPPED FROM 12-1/2 PERCENT TO 6-1/2 PERCENT. AND, IN THE PAST FOUR YEARS, 35 PERCENT MORE NEGROES HAVE FOUND PROFESSIONAL, TECHNICAL, AND MANAGERIAL JOBS.
- MIDDLE INCOME FAMILIES HAVE ALSO IMPROVED THEMSELVES. DURING THIS SAME SEVEN-YEAR PERIOD, 8 MILLION MORE FAMILIES HAVE ACHIEVED YEARLY INCOMES ABOVE \$10,000, MORE THAN DOUBLING THE NUMBER ENJOYING SUCH PAY IN 1960.

THESE GAINS REFLECT SUBSTANTIAL PROGRESS BY THOSE WHO NEED IT MOST, AND WE SHOULD FEEL PROUD THAT OUR SYSTEM HAS MADE IT POSSIBLE. WE MUST CONTINUE THIS KIND OF ADVANCEMENT WHICH IS INDISPUTABLE EVIDENCE OF THE ECONOMIC SUPERIORITY OF CAPITALISM OVER COMMUNISM.

PROSPERITY'S BENEFITS EXTEND FAR BEYOND OUR SHORES. THE PEOPLES OF OTHER NATIONS ALSO HAVE A STAKE IN THIS SAME STABLE EXPANSION. WERE WE TO PERMIT OUR ECONOMY TO STAGNATE OR SLIDE INTO A RECESSION, IT WOULD DESTROY A SUBSTANTIAL PORTION OF THE WORLD'S MARKETS AND, ALONG WITH IT, IMPAIR ECONOMIC OPPORTUNITIES AND PROGRESS EVERYWHERE. U. S. IMBALANCES -- INFLATION OR RECESSION -- CAN HAVE DISASTROUS ECONOMIC CONSEQUENCES THROUGHOUT THE WORLD.

WE IN THE UNITED STATES THUS HAVE AN OBLIGATION TO PROVIDE THE KIND OF ECONOMIC ENVIRONMENT WHICH IS A PREREQUISITE TO THE WELL-BEING BOTH OF OUR OWN CITIZENS AND THOSE OF OTHER NATIONS. WHETHER OR NOT WE AS INDIVIDUALS HAVE "EVER HAD IT SO GOOD" IS BESIDE THE POINT.

PRESERVING OUR STABLE EXPANSION

THE RECORD-BREAKING STABLE EXPANSION WE HAVE EXPERIENCED DURING THE LAST SEVEN YEARS HAS NOT OCCURRED BY ACCIDENT. IT HAD TO HAVE THE RIGHT KIND OF ENVIRONMENT IN ORDER TO THRIVE. WHEN UNEMPLOYMENT IS HIGH AND PRODUCTION LOW, WE NEED MEASURES TO ENCOURAGE GREATER ECONOMIC ACTIVITY, SUCH AS THE HUGE TAX CUT OF 1964. ON THE OTHER SIDE OF THE COIN, WHEN ECONOMIC ACTIVITY THREATENS TO ACCELERATE TOO FAST, WE MUST HAVE THE COURAGE TO HOLD DOWN FEDERAL EXPENDITURES AND RAISE TAXES TEMPORARILY IN ORDER TO RESTRAIN DEMAND, EASE PRICE PRESSURES AND PRESERVE THE STRENGTH OF THE DOLLAR.

PRESIDENT JOHNSON'S NEW BUDGET HOLDS ALL CIVILIAN PROGRAMS BELOW LEVELS THAT WOULD BE MORE DESIRABLE, IF WE COULD AFFORD THEM. A FEW EXTREMELY HIGH PRIORITY PROGRAMS, MOSTLY RELATED TO THE NEEDS OF OUR LARGE CITIES, ARE SLATED FOR MODEST INCREASES -- MANPOWER TRAINING, CONTROL OF CRIME, POLLUTION CONTROL, AND MODEL CITIES ARE GOOD EXAMPLES -- BUT EVEN THESE ARE BEING HELD BELOW AMOUNTS THAT MOST OF US WOULD PREFER. MEANWHILE, LOOK FOR CONSIDERABLE DISSATISFACTION WITH THE CUTBACKS THE PRESIDENT PROPOSES FOR MANY POPULAR ACTIVITIES, SUCH AS EDUCATION, HEALTH, CONSTRUCTION, SMALL BUSINESS AND FARM PROGRAMS AS WELL AS FOR SPACE EXPLORATION. NEVERTHELESS, WE MUST BE WILLING TO MAKE THESE SACRIFICES TO PRESERVE OUR STABLE EXPANSION.

IT WOULD BE A WONDERFUL THING IF, DESPITE THE ECONOMIC PRESSURES, WE COULD GREATLY ENLARGE OUR ANTIPOVERTY PROGRAMS, MAKE VAST NEW EXPENDITURES FOR EDUCATION,

ADD TO OUR NATIONAL WEALTH BY INCREASED CONSTRUCTION OF HIGHWAYS AND POWER PROJECTS, AND SO FORTH. YET, EDUCATION FOR BETTER JOBS WILL MEAN LITTLE IF TOO MUCH SPENDING PUSHES US INTO AN EXPANSION-WRECKING INFLATION AND CONCOMITANT SHRINKAGE OF ECONOMIC OPPORTUNITIES; GREATER WEALTH IN THE NUMBER OF ROADS AND DAMS PALES WHEN COMPARED TO THE LOSS OF WEALTH CAUSED BY THE RISING UNEMPLOYMENT AND LOST PRODUCTION OF A RECESSION.

BUT HOLDING DOWN THE LEVEL OF EXPENDITURES IS NOT ENOUGH. WE MUST ALSO HAVE THE COURAGE TO RAISE TAXES WHEN THIS BECOMES NECESSARY FOR THE PRESERVATION OF ECONOMIC STABILITY. THIS STEP IS NECESSARY NOW.

IT IS IRONIC TO THINK BACK TO JANUARY 1961 WHEN THE EXPANSION FIRST BEGAN. AT THAT TIME, WE CONFRONTED OUR THIRD RECESSION IN SEVEN YEARS -- WIDESPREAD UNEMPLOYMENT AND SHRINKING PRODUCTION AND A BALANCE OF PAYMENTS DEFICIT OF NEARLY \$4 BILLION, STILL THE HIGHEST ON RECORD. WE WORKED SEVEN DAYS A WEEK TRYING TO GET THE COUNTRY MOVING AGAIN. OUR GOAL? TO MOVE THE UNEMPLOYMENT RATE BELOW FOUR PERCENT, DEFINED AS "FULL EMPLOYMENT." OH, WE THOUGHT, WOULDN'T EVERYTHING BE WONDERFUL IF WE COULD JUST REACH FULL EMPLOYMENT? WE MADE IT.

BY MID-1965, BEFORE THE VIETNAM ESCALATION, UNEMPLOYMENT HAD DROPPED TO 4-1/2 PERCENT AND WAS MOVING DOWNWARD. BY THIS TIME, THE NATION'S ECONOMY HAD ACHIEVED THE LONGEST AND STRONGEST UNINTERRUPTED PEACETIME EXPANSION IN HISTORY. WE REACHED OUR 4 PERCENT UNEMPLOYMENT GOAL BY THE END OF 1965, BUT THEN WE CONFRONTED AN ENTIRELY NEW SET OF PROBLEMS -- HOW TO DEAL WITH AN ECONOMY MOVING TOO FAST RATHER THAN TOO SLOW -- HOW TO AVOID INFLATION RATHER THAN STAGNATION.

CONSIDERING THE MULTI-BILLION DOLLAR IMPACT OF VIETNAM, I THINK THE ECONOMY HAS ACHIEVED A REMARKABLE RECORD. CONSUMER PRICE INCREASES IN BOTH 1966 AND 1967 WERE HELD BELOW THREE PERCENT, A BETTER RECORD OF PRICE STABILITY THAN MOST OF THE OTHER INDUSTRIALIZED COUNTRIES OF THE WORLD, DESPITE OUR VIETNAM PRESSURES ON TOP OF A FULL EMPLOYMENT ECONOMY.

THE FISCAL MEASURES WHICH CONTRIBUTED TO THIS RECORD OF STABILITY INCLUDED EXPENDITURE RESTRAINT, A SPEEDUP IN TAX COLLECTIONS, AND A POSTPONEMENT OF SCHEDULED REDUCTIONS IN CERTAIN EXCISE TAXES. WE AVOIDED ANY INCREASE IN TAX RATES, BUT WE CANNOT CONTINUE INDEFINITELY TO CARRY THE HEAVY BURDEN OF VIETNAM WITHOUT RAISING THESE RATES.

PRESIDENT JOHNSON'S FISCAL PROGRAM

PRESIDENT JOHNSON'S PROPOSED TAX HIKE WOULD APPLY A TEMPORARY 10 PERCENT SURCHARGE TO INDIVIDUAL AND CORPORATE INCOME TAXES. LET ME EMPHASIZE THAT THIS SURCHARGE IS 10 PERCENT OF THE INDIVIDUAL'S OR CORPORATION'S TAX, NOT 10 PERCENT OF TOTAL INCOME. THE REAL ISSUE THEN IS WHETHER WE ARE WILLING TO TAX OUR NATIONAL INCOME AN AVERAGE OF AN EXTRA ONE PERCENT -- A PENNY ON THE DOLLAR -- TO FINANCE THE COSTS OF VIETNAM RESPONSIBLY. ARE WE WILLING TO TAKE THE NECESSARY STEPS TO PRESERVE A STABLE ECONOMY AT HOME AND THE SOUNDNESS OF THE DOLLAR ABROAD?

YOU WILL HEAR DEMANDS THAT WE CUT EXPENDITURES INSTEAD OF RAISING TAXES. IN OUR OPINION, FEDERAL EXPENDITURES HAVE ALREADY BEEN DRASTICALLY HELD DOWN. STILL FURTHER REDUCTIONS MAY GET THROUGH CONGRESS, BUT NO AMOUNT OF DISCUSSION AND DEBATE CAN POSSIBLY PRODUCE CUTS IN BUDGET EXPENDITURES BY ANYTHING LIKE THE \$16 BILLION FIGURE WHICH THE TAX PLAN WOULD PRODUCE DURING THE NEXT 16 MONTHS.

THE PRESIDENT'S TAX PROGRAM WOULD CUT THIS FISCAL YEAR'S BUDGET DEFICIT FROM \$23 BILLION TO LESS THAN \$20 BILLION AND THE FISCAL YEAR 1969 DEFICIT FROM \$21 BILLION TO \$8 BILLION. WITHOUT IT, THE DEFICIT WOULD DECLINE ONLY SLIGHTLY AND WOULD REMAIN FAR TOO LARGE. FISCAL RESPONSIBILITY IS SIMPLY INCOMPATIBLE WITH BACK-TO-BACK BUDGET DEFICITS OF OVER \$20 BILLION EACH.

PRESIDENT JOHNSON KNEW IT WOULD BE VERY UNPOPULAR TO ASK THE AMERICAN TAXPAYER TO PAY MORE. I THINK THE POLLS SHOW LESS THAN 25 PERCENT SUPPORT FOR HIGHER TAXES. BUT FAILURE TO ENACT THE TAX INCREASE WOULD KEEP THE BUDGET DEFICIT AT LEVELS WHICH OVER THE NEXT 16 MONTHS WOULD RISK FUELING A BOOM THAT COULD PRODUCE A SERIOUS RECESSION. BUDGET DEFICITS AND A HIGH RATE OF EXPANSION HAVE ALREADY CONTRIBUTED TO AN UNACCEPTABLE ACCELERATION OF PRICE ADVANCES. ALTHOUGH PRICE INCREASES IN 1967 WERE LESS THAN THREE PERCENT, THEY ROSE AT AN ANNUAL RATE OF NEARLY FOUR PERCENT IN THE SECOND HALF OF THE YEAR, IN CONTRAST TO A RISE OF LESS THAN 2-1/2 PERCENT IN THE FIRST HALF.

HIGHER PRICES BRING DEMANDS FOR WAGE HIKES IN EXCESS OF PRODUCTIVITY INCREASES. THIS PUSHES UP COSTS, CAUSING STILL HIGHER PRICES. THEN HIGHER PRICES CAUSE DEMANDS FOR STILL HIGHER WAGES, ETC. THESE COST AND PRICE INCREASES TEND TO BECOME PERMANENT FIXTURES IN THE ECONOMY. ONCE A WAGE-PRICE SPIRAL GETS UNDER WAY, IT BECOMES VERY DIFFICULT TO CHECK WITHOUT STALLING THE ECONOMY IN THE PROCESS. THEREFORE, WE MUST APPLY FISCAL RESTRAINT NOW.

IF WE DO NOT RAISE THESE EXTRA REVENUES, THERE WILL BE AN EXCESSIVE AMOUNT OF FEDERAL BORROWING. THIS WILL THROW A HEAVY LOAD ON THE MONEY AND CAPITAL MARKETS, WHEN INTEREST RATES ARE ALREADY AT THE HIGHEST LEVELS IN DECADES.

BUDGET DEFICITS AND A HIGH RATE OF EXPANSION ALSO HURT OUR BALANCE OF PAYMENTS. OUR TRADE SURPLUS STRENGTHENED IN THE FIRST THREE QUARTERS OF 1967, BUT AN UPSURGE OF IMPORTS CAUSED A SHARP DETERIORATION LATE IN THE YEAR. THE PRESIDENT'S TAX

PROPOSALS OF LAST AUGUST WERE INTENDED TO HEAD OFF JUST SUCH A DEVELOPMENT. FAILURE TO ACT ON TAXES HAS CONTRIBUTED TO A RAPID EXPANSION OF THE ECONOMY AND THIS EXPANSION, IN TURN, IS BEING REFLECTED IN A VERY SHARP RISE OF IMPORTS. EVENTUALLY, IF WAGE AND PRICE INCREASES ARE ALLOWED TO RISE UNCHECKED, OUR BASIC INTERNATIONAL COMPETITIVE POSITION WOULD OBVIOUSLY SUFFER.

BOTH DOMESTIC AND INTERNATIONAL CONSIDERATIONS REQUIRE THAT WE PUT OUR FISCAL AFFAIRS IN ORDER BY PROMPT ENACTMENT OF THE PRESIDENT'S TAX PROPOSALS. FAILURE TO ACT WOULD JEOPARDIZE NOT ONLY OUR RECORD-BREAKING ECONOMIC EXPANSION BUT ALSO THE FUTURE OF AN INTERNATIONAL MONETARY SYSTEM THAT FOR 20 YEARS HAS BROUGHT THE GREATEST ERA OF WORLD TRADE AND DEVELOPMENT IN OUR HISTORY.

CAN WE AFFORD A MODEST TAX INCREASE TO HELP FINANCE VIETNAM?

IS A 10 PERCENT SURCHARGE TO HELP FINANCE VIETNAM ASKING TOO MUCH OF AMERICANS HERE WE SHOULD BEAR IN MIND TWO POINTS:

1. PRESIDENT JOHNSON'S TAX REDUCTION PROGRAMS OF 1964 AND 1965 WILL REDUCE OUR 1968 TAX PAYMENTS BY ALMOST \$24 BILLION. A 10 PERCENT SURCHARGE WOULD TEMPORARILY REDUCE THIS TAX SAVING TO \$13-1/2 BILLION. WELL OVER HALF OF THE TAX CUT WOULD REMAIN IN FORCE. ALL OF IT WOULD BE RESTORED WHEN OUR VIETNAM REQUIREMENTS HAVE ABATED.
2. AMERICANS ENJOY THE LOWEST TAX BURDEN OF ANY OF THE MAJOR INDUSTRIAL COUNTRIES OF EUROPE, AND THIS INCLUDES TAXES LEVIED AT ALL LEVELS OF GOVERNMENT -- FEDERAL, STATE AND LOCAL. ESTIMATES BASED ON DATA OF THE ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT SHOW THAT AS A PROPORTION OF TOTAL NATIONAL PRODUCTION FRENCH CITIZENS PAY 38-1/2 PERCENT

IN TAXES; GERMANY, 34-1/2 PERCENT; ITALY, 29-1/2 PERCENT;
GREAT BRITAIN, 28-1/2 PERCENT; AND THE U. S., LESS THAN
27 1/2 PERCENT.

THESE FIGURES ARE NOT CITED TO IMPLY THAT AMERICANS ARE HAVING IT EASY.
THE MAIN PURPOSE OF THE 1964 AND 1965 TAX CUTS WAS TO PERMIT THE PRIVATE
SECTOR OF OUR ECONOMY TO FLOURISH BY ALLEVIATING THE BURDEN OF HIGH TAXES.
BUT THE FIGURES DO SHOW THAT WE CAN AFFORD TO PAY FOR OUR RISING DEFENSE COSTS
AND KEEP OUR ECONOMY HEALTHY.

FUTURE ECONOMIC PROGRESS AT STAKE

UNLESS TAXES CAN BE USED TO RESTRAIN THE ECONOMY IN A PERIOD OF INFLATIONARY
PRESSURES, FUTURE ADMINISTRATIONS AND CONGRESSES MAY BE UNWILLING TO REDUCE
TAXES TO STIMULATE ECONOMIC ACTIVITY WHEN THIS IS CALLED FOR. THIS WOULD, OF
COURSE, FURTHER REDUCE THE FLEXIBILITY OF TAX POLICY AS A COUNTERCYCLICAL WEAPON.
WHEN, IN THE FUTURE, THE ECONOMY NEEDS STIMULATION, WE WOULD THUS BE LIKELY TO
GET HIGHER SPENDING RATHER THAN REDUCED TAXES.

OUR POSITION AS LEADER OF THE FREE WORLD AND THE SOLUTION OF OUR PRESSING
DOMESTIC PROBLEMS ARE AT STAKE, AND THEY BOTH DEMAND THAT WE HAVE A HEALTHY AND
GROWING ECONOMY CHARACTERIZED BY FULL EMPLOYMENT AND PRICE STABILITY. IF WE
ARE TO PRESERVE THE STABLE EXPANSION WHICH WE HAVE ENJOYED FOR SEVEN YEARS,
THE PROGRAM OF TEMPORARY FISCAL RESTRAINT WHICH THE PRESIDENT HAS PROPOSED MUST
BE ENACTED.

BEYOND THIS, OUR FUTURE PROSPERITY IS DEPENDENT ON THE ACTIONS OF ALL THE
DIVERSE SEGMENTS OF OUR SOCIETY -- BUSINESS, AGRICULTURE, LABOR, AND GOVERNMENT
AT ALL LEVELS -- COOPERATING, UNDERSTANDING, AND REASONING TOGETHER AND CONTRIBUTING
TO THE COMMON PURPOSE OF A STRONG AND PROSPEROUS AMERICA.

THANK YOU VERY MUCH.

TREASURY DEPARTMENT
Washington

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WEDNESDAY, FEBRUARY 14, 1968

REMARKS BY THE HONORABLE STANLEY S. SURREY
ASSISTANT SECRETARY OF THE TREASURY
BEFORE THE
DALLAS CHAPTER OF THE
FINANCIAL EXECUTIVES INSTITUTE
CHAPARRAL CLUB, DALLAS, TEXAS
TUESDAY, FEBRUARY 13, 1968, 7:15 P.M., EST

TAXES AND THE FEDERAL BUDGET

Our Federal Budget, on a unified basis for the first time, approaches the \$200 billion level in receipts and outlays. Together its revenues and expenditures play a significant part in shaping the economic and social health of the United States, in safeguarding its national security, and in maintaining strength and stability in its international relationships. There are many facets to the interaction of the tax side of the Budget with the expenditure side. I propose to comment tonight on two aspects that are of current concern -- one involves a quantitative relationship and the other a structural relationship.

The Tax Increase and The Deficit

First, as to the quantitative relationship. All of you are surely familiar with the fact that the Congress is being urged by the Administration to increase tax revenues. Why? The answer lies in the traditional reason for tax increases and goes to the essence of what tax systems are for -- to raise the revenues needed to maintain our Government. The Federal Budget for the coming fiscal year without a tax increase would involve a deficit of over \$20 billion. We would end the fiscal year 1968 with a deficit also over \$20 billion.

Quite clearly, looking at all of the risks and problems that we face, \$20 billion deficits back to back is not the hand we want to play.

The President's tax recommendations involve revenue increases of about \$16 billion for the two fiscal years -- \$3 billion in fiscal 1968 and \$13 billion in fiscal 1969. These tax increases would reduce the fiscal 1968 deficit to under \$20 billion and the fiscal 1969 deficit to \$8 billion, clearly a far more manageable situation.

The need for these tax increases is even stronger than these figures demonstrate. I have said that a \$20 billion deficit for 1969 is too large for our well-being. But there is even no guarantee that without a tax increase we would be facing the prospect of a deficit of this risky size and no more. For even a \$20 billion deficit would contain within it no margin for error -- there would, at that level, still be no cushion to absorb a sudden shock. Yet, in the troubled world of today, there are certainly many chances for careful calculations to be suddenly and greatly altered.

No nation, even in peace, is the unilateral master of its fortunes. A nation engaged in hostilities certainly cannot predict future events with confidence, or foretell with sureness the financial costs of those hostilities. At home we face the uncertainties of our urban problems -- uncertainties that grow out of a profound concern to obtain solutions for those problems but uncertainties nevertheless. These uncertainties are the headlines of the domestic news on our front pages -- but the financial pages also have their headlines of doubt. Our credit markets are unstable, being unable to read the future and yet knowing that some of the possibilities can mean a severe credit crunch in which some sectors are bound to be hurt, and could call for assistance.

Military question marks are not the only international uncertainties that we face. The size of our deficit has a direct bearing on our international financial position. We can say with confidence that the shock waves set in motion by the British pound have fully subsided, and that the speculators have finally decided not to take another whirl to see whether anything else can come unstuck.

International financial confidence is not a cup that can be won and then retired in comfort and ease. With a huge volume of dollars in foreign hands, our fiscal health is constantly and minutely watched the world over. Nor are all of the watchers dedicated to the maintenance of that health.

So the future is taut and risky -- and our resources, large though they may be, will nevertheless be stretched thin in relation to our goals and problems. Given all this, it is all the more unwise and imprudent to run the risks of a \$20 billion deficit -- to run the risks inherent in a deficit of that size and to run the risks of that deficit suddenly being forced higher.

Fortunately, there is no need for our nation to incur these risks. The tax increase that is sought will give us the fiscal strength to avoid the risks. And we -- individuals and corporations alike -- are well able to shoulder this tax increase. Even after the tax surcharge that is involved, individuals will still be paying significantly less than in 1963 before the tax reductions of 1964 and 1965 -- and corporations less than they were paying before the reductions that commenced for them in 1962 through the investment credit and depreciation reform. Moreover, low income groups are not subject to the surcharge.

Nor, realistically, do we face the prospect that a tax increase now, though fully intended to be temporary, will nevertheless lock us into a permanently higher level of taxation. For certainly we must view our hostilities in Vietnam as temporary in the panorama of events, and the tax increase is needed because of those hostilities. We must remember our tax system now produces through normal growth of the economy increases of revenue of around \$12 billion annually. Once the pressure of military demands is removed, a very large sum will thus be available annually both to meet our expenditure needs and permit tax reduction. Even in the fiscal 1969 budget, despite this pressure of hostilities, the increase of expenditures over fiscal 1968 is less than this normal growth in revenues.

And so our people can bear these tax increases and in so doing can see reasonable assurance that their burdens should be temporary. Moreover, our economy is fully able to absorb the restraint on demand that would be involved under the tax increase. Indeed, the forecasts in the absence of that restraint predominantly point to the considerable dangers of an increasing inflationary trend that can send us next year into another round of cost and price increases. And those who watch the thermometer of the international dollar, be they the Finance Ministers or central bankers of other countries, or speculators, or the career officials of the international financial institutions, all are of one voice that our external financial stability depends on our moderating that inflationary trend.

The case for a tax increase is thus solidly grounded in the stark realities of the risks our nation runs under the large budget deficits that are the alternative course. A sober appraisal of those risks, and of the two courses we must choose between, points the way to the needed reduction of the deficit to a far safer level. Moreover, the 1968 and 1969 Budgets are tight Budgets on the expenditure side, and have been revised and built to meet a strict expenditure hold down. But even if we accept the view that any budget can be cut more, the Budget for 1969 cannot be cut \$13 billion, or anywhere near \$13 billion -- the amount of the tax increase for 1969. Thus, only a tax increase can provide the sums required to achieve a safer level. It is this case that awaits the judgement of the Congress.

Social Welfare -- Tax Incentives -- And The Budget
Business and Our Social Goals

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A tax system that will raise revenues of around \$165 billion, including the tax increase, deserves careful handling to maintain its effectiveness and fairness and to prevent distortions in the private economy. An expenditure budget of the size needed in the United States equally merits careful attention to preserve its efficiency and to keep it under tight control at all times. These observations require no elaboration before this financially experienced audience -- you appreciate the high premium any business must place on strict budgetary control. Yet today we face possible developments that could seriously impair the needed Federal

budgetary control and seriously impair the effectiveness of our tax system. In the light of these risks, it is all the more surprising that these developments derive in considerable part from attitudes in the business community. And, as a somewhat ironic twist, these attitudes in turn develop from the commendable efforts of the business community to direct its energies and resources to assist in the solution of our social ills.

No informed audience such as this requires of a speaker that he prove the proposition that our nation faces social problems of a staggering magnitude and complexity. Whether the area be urban or rural; whether the interests of a group center on education, pollution, crime, housing, manpower training, employment, or urban congestion; whether its interests concentrate on the underlying causes, poverty, racial discrimination, denial of civil rights, the need for maintaining personal dignity and stability in a world of bewildering technological and material change -- whatever and wherever the focus there is a challenge to be met.

The solutions to these problems represent very large debts that we as a nation owe to our people. But the imensity of the tasks should not blind us to the assets we possess to meet them. We are a wealthy nation, with resources of great talent and abundant materials. We now have a concern at all levels of Government, and more important, in the hearts and minds of most of us, that these resources should be turned to these tasks. And so hopefully we are debating not goals but methods, not ends but means.

The role of the business community in helping the nation reach its social goals is a very crucial part of the means and methods we must consider. It is commonplace today to say that these problems are too large for Government alone to solve and that the solution requires a partnership between business and Government. True -- but of course it also requires a partnership between labor and Government, between the universities and Government, between the private non-profit organizations and Government, for all of the nation must be involved. And even the term "partnership" obscures the nature of the relationship, especially as to business. It is on this relationship that I wish to focus now, especially in its impact on the tax system and the Federal budget.

Business can become involved in the solution of our social problems in two distinct ways. One way lies through the charitable and community instincts of business -- the giving of funds and the voluntary time and talents of its leaders to community projects. This is traditional, commendable, necessary, expected -- but obviously not enough. The other way lies in business functioning as business -- in selling its services and products to produce a profit for its shareholders. For this is the essence of business to earn its profits by meeting human needs. Recognition of the profit motive is fully consistent with meeting our national goals. There were profits to be made out of spanning the continent with railroads when that was a national need, or out of clipper ships when they served a national goal. Those profits assured the success of the task. Today there are profits to be made out of space exploration, and this now serves a national goal.

Business and Tax Incentives

Why does business falter and forget its traditions and functions when it comes to its role in meeting our social goals? Why do we find business leaders and business organizations, in speaking of the needed partnership between Government and business, stressing not fair profits and recompense as the basis of that partnership but tax incentives? Space exploration involves a partnership between business and Government, but that partnership rests on contracts and not tax incentives -- our capsules are not propelled into space by the Internal Revenue Code. Military security involves a partnership between business and Government, but that partnership also rests on contracts and not tax incentives -- our planes and missiles are not launched by the Internal Revenue Code.

Why then do we find, for example, when we talk of the need for business to train the hard core unemployed that businessmen will say they need a tax incentive if they are to take on that task -- that they need a tax incentive to meet their costs of the training and to prevent their stockholders from being penalized by such costs? Why a tax incentive? What is wrong in selling manpower training services to the Government?

Some businessmen say they cannot deal with Government about such matters, that they are reluctant to assume the burdensome paperwork requirements of any Federal contracting procedure that would be involved, that a Government contract will require some loss of management prerogatives because Government may seek to consider the content of the training to be given, and so on. But businessmen deal with the Defense Department and with NASA -- they negotiate at length and write contracts with these agencies, and those contracts contain specifications. Why is it suddenly different if Government now finds it must buy social welfare activities as well as weapons and spacecraft? To turn the talk from fair and appropriate contracts to tax incentives seems a peculiar posture for a business group to take. To find business seeking to imply that profits and reimbursement of costs are ugly words is strange and defeatist -- and wholly unnecessary.

Tax incentives would be much like Congress legislating the price to be paid for Apollo spacecraft. Either the incentive would be too low and we would be relying on business charity to build the craft or it would be too high and thus wasteful.

We are entering into an era in which Government will be seeking to purchase new types of goods and services from the business community -- in manpower training, in housing, in urban development, and so on. There is no reason why Government and business should not seek to utilize and adapt for these fields the experience and techniques developed in achieving successful purchasing programs in defense, space and other areas of Government procurement. The President's recommendations on Hard-Core Unemployment follow this path.

But some businessmen reply that a tax incentive is a simple, automatic and self-enforcing method in contrast with other ways of dealing with the Federal Government. Now, it would be a nice illusion for a Treasury official to believe that dealing with our Department and with the Internal Revenue Service is so tranquil and delightful, and

to hear that businessmen see the Internal Revenue Agent as the paragon of Government officials, all wise and all understanding. I would like to believe this -- but I fear I have been brainwashed. For I have listened to far too many business complaints about what happens when the Internal Revenue Service must administer any tax provision that involves any element of discretion or judgement, be it depreciable lives, the allocation of profits between affiliated groups under Section 482, the unreasonable accumulation of corporate profits, and so on. And so I cannot see just how an Internal Revenue Agent, trained as he is in accountancy and financial matters, can be said to find the going so hard in these tax areas where that experience at least is relevant, but then will suddenly find himself supremely capable of deciding that proper training is being given to the hard-core unemployed who are taken on by business, that their special problems are being adequately solved, and that these and similar prerequisites of a manpower tax incentive are being met. And in turn, if the requirements work out to be unwise or too rigid or impractical, I do not see how the Internal Revenue Service is going to have the wisdom and background to develop needed changes.

The truth is that there is nothing simple and automatic about complex problems. The training of the hard-core unemployed is a difficult task. Some training will, of course, occur through direct business needs for more manpower where employment is tight or as an aspect of the involvement of a business in the communities in which it is located. But more than this is needed. The development of the solutions can best be left to direct dealing between business and the agencies of Government with expertise and responsibility in this field, rather than involving the Internal Revenue Service as an extra wheel in the process. For the Internal Revenue Service could only go back to these other agencies and ask them to undertake the task of certifying to it when a tax incentive has been earned.

We will find the same complexity, and the same inadequacy of any simple, automatic tax incentive solution, wherever we turn in these fields. There is an inherent difficulty in adapting tax incentives to the specific characteristics of these social problems.

Consider a popular tax credit proposal of recent years, a credit allowed for industrial facilities for the control of pollution. All of the proposed bills on this matter have been designed to provide some offset to the capital cost of what we might describe as an end-of-the-line equipment investment intended to clean up waste water or smoke. But if one looks into the technology of pollution control, it turns out very often that efficient pollution control doesn't call for an end-of-the-line capital facility at all. A well-known case is the problem of sulfur dioxide in smoke. The efficient way to control this is to incur the higher operating cost of using a low sulfur fuel. In other cases pollution control may be a matter of maintaining a higher level of quality control on an industrial process. Even in a case where end-of-the-line treatment is called for, the firm may have a choice between treatments, one with a high capital cost but a higher operating cost, another with a lower capital cost but a higher operating cost. If we were agreed on the principle that government should carry some of the cost of industrial pollution control, one could thus hardly think of a more inefficient way of doing this than providing a tax subsidy that would apply only to one method of control. In many cases this subsidy would be an incentive to use the most expensive form of pollution control simply because its after-subsidy cost is lower.

Another popular tax incentive proposal is a credit for plant location in depressed areas, either areas of rural low income or of urban unemployment. Government currently has an agency engaged in this activity, the Economic Development Administration. It has found, as would be expected, that

direct financial assistance to business is only one of an arsenal of devices to be used to help depressed areas. In development plans worked out with knowledgeable local people, about \$200 million of government funds in fiscal year 1967 were directed by EDA to public works to provide the climate necessary for business development. In addition, \$100 million was provided in business loans and \$11 million was spent on technical assistance.

A particularly interesting feature of EDA experience was the decision at the beginning of 1967 to make a simple policy change which was described as "worst first." EDA had found that many areas that originally qualified for assistance had risen out of the depressed category before there had been time for the EDA assistance to show any effect. Obviously communities close to the borderline can be raised out of their depressed status by general economic growth. EDA sensibly concluded that it ought to concentrate its resources on the worst areas, and it believes this policy was highly successful in improving the efficiency of its programs. But a simple automatic tax incentive would not have the ingredients to implement such a policy approach.

In the education field we have moved a long way from the notion that a simple tax credit for tuition would solve all the problems of higher education -- of aiding financially handicapped or otherwise disadvantaged but capable youths to obtain a college education, of easing the burdens on middle income families with children in college, and of enabling the colleges, especially the private schools, to meet the problem of rapidly rising costs.

And so it is with all these fields. Once we pass the phase of urgent stereotyped pleas for a tax incentive, of wrapping up these huge social problems in the paragraph or two, or even the single sentence, of "Let's have a tax incentive," and we move on to the exploration of the problems in depth and of the alternatives available -- when this occurs we then see the beginnings develop of a needed manifold approach.

Business has been misled I think in its approach to tax incentives for social welfare purposes by its experience under the 7 percent investment credit for new machinery and equipment. That credit does work simply and automatically,

for its purpose and concept are far different in nature from the tax incentives now being suggested. The only questions involved under the allowance of the investment credit are whether it is a new machine, what is its cost, and is its depreciable life more than a certain number of years. The answers to all these questions, we must remember, were determined by already existing tax rules.

Internal Revenue Agents do not ask: Is the purpose of the machine to meet a special need in the business, is it being used only for that purpose; is it really effective for that purpose -- the kinds of questions they would have to decide under a pollution incentive.

Agents do not ask: Is the machine to be used in a depressed rural area, or an area of urban unemployment; was it a "run-away" machine from another area; is its operation so automated that it will not encourage significant employment -- the kinds of question they would have to decide for the business as a whole under a tax incentive for location in depressed rural or urban areas.

Agents do not ask: Is this a special type machine; is the machine being properly used and properly cared for; what are its daily maintenance costs; what overhead costs are allocable to it as compared with ordinary machines; did it displace another machine; was it obtained from a qualified supplier; what was being done with it when it temporarily broke down -- the kinds of questions they would have to decide for employees under a manpower training incentive.

The purposes and concept of the investment credit and its relationship to the effect of our tax system on incentives to invest were thus served by the broad, blanket approach of that credit. But no one is prepared to urge that such a blanket approach would be appropriate for these social areas.

There is another important aspect of the tax incentive approach that makes its urging by business groups puzzling. Tax incentives are of help only to concerns that are profitable, and indeed significantly profitable so that they have profits and taxes to be offset by the tax incentive. Clearly space contractors would not waive their contract proceeds if their overall business happened to show a loss for the year.

Then why prefer a recompense for manpower training or locating in a rural area that turns out to be zero if the business runs at a loss for the year? It seems a strange reply, as some have answered, that profitable companies are in the best position to provide meaningful and continuing employment. I wonder if some of our important companies, who happen in a particular year to suffer a loss perhaps as the result of a bad fourth quarter, or who have new managements that are working the company out of a loss position while having the advantage of not paying taxes because of net operating loss carryovers, would accept that answer. I also wonder if the answer makes much sense to a new business locating in a depressed urban or rural area and in so doing recognizes it may have to accept losses for a few years but is still willing to train workers. And certainly it is puzzling to say that Government should give financial assistance, through a tax incentive, to a firm desirous of locating in a depressed area only if the firm proves profitable. For the only firm that would get full benefit from the tax incentive is one that is sure of being profitable -- that is, it didn't really need the assistance of the incentive.

The Budget and Tax Incentives -- Existing Tax Expenditure Programs

When the matter is seen from the Government side, there are very significant disadvantages to the tax incentive approach. Chairman Mills of the House Ways and Means Committee, in a recent statement* spoke decisively and comprehensively of the damage that the tax incentive approach can do to our tax system and to our control over Federal expenditures. He called attention to the "catastrophic loss of revenue" that would result from the tax credit bills now pending before his Committee and recognized that "enactment of these credits would merely whet appetites for a legion of other credits." He firmly pointed out that the use of tax incentives would undercut efforts to maintain the necessary control over our Government expenditures and criticized those incentives as "back door spending":

"I want to point out . . . that the grant of these tax credits has precisely the same effect on the budget as an outright expenditure. The only difference is they appear as a negative receipt rather than as an expenditure. The grant

* Congressional Record of December 13, 1967, p. H 16890

of the additional tax credits increases the size of the budget deficit just as surely as an additional expenditure. That is why I refer to the tax credits as back door spending. That is why it would do us no good to have expenditure control if the advocates of spending programs need only to run around to the back door to achieve much the same result by tax credits. . . .

"As we look ahead to discover ways in which we can keep the budget within reasonable limits, we must not fail to direct a critical eye to the proposals which would give tax credits to those who make certain expenditures. Acceptance of these proposals for back door spending even more than proposals for outright government expenditures postpones the day when it will be possible to travel again down the road of further Federal tax reduction and greater reliance on the private sector of the economy."

We of course do have tax subsidies presently existing in our tax laws. I have elsewhere observed that through deliberate departures from accepted concepts of net income and through various special exemptions, deductions and credits, our tax system does operate to affect the private economy in ways that are usually accomplished by expenditures -- in effect to produce an expenditure system described in tax language. I called these items "tax expenditures," and indicated that the amounts spent -- i.e., the tax revenue lost -- through these tax expenditure programs should be set forth in a meaningful way in the Federal Budget. We would thereby be able clearly to see what are the total Federal funds going to the various activities affected, and not just the amounts shown in the Budget as direct appropriations and expenditures. For these tax expenditures can be classified along customary budgetary lines: assistance to business, natural resources, agriculture, aid to the elderly, medical assistance, aid to charitable institutions, and so on. Moreover, the amounts involved are quite large, reaching in several of these areas into the billions. The appropriate budgetary recognition of these tax expenditure programs is now under study in the Government. Indeed, consideration of the budgetary treatment of these tax expenditures or tax subsidies finds a parallel in the

recommendation of the Report of the Presidents's Commission on Budget Concepts (1967) respecting loan subsidies accorded by the Federal Government:

"Most Federal loan programs contain at least some element of subsidy. In fact, if this were not true, a serious question could be raised about the appropriateness of such activities being conducted by the Federal Government rather than by private financial institutions. To the extent that Federal loans include a subsidy element by lending at more favorable interest rates than the cost of money to the Government (or the even higher cost of money obtained through private sources) they are at least in part grants or transfer payments rather than loans. . . .

"It is the Commission's recommendation that the full amount of the interest subsidy on loans compared to Treasury borrowing costs be reflected and specifically disclosed in the expenditure account of the budget, and furthermore, that it be measured on a capitalized basis at the time the loans are made." /51-2/

Since the tax expenditure programs are imbedded in the revenue side of the Budget and their cost is not disclosed, they go essentially unexamined for long periods, in contrast with direct expenditures. Their efficiency, in the sense of benefits obtained for Government and the public as compared with amounts expended, is thus not compelled to meet the rigid tests we are now developing and applying to direct Budget expenditures. I doubt that any of these special tax treatments could stand the scrutiny of careful program analysis, and I doubt that if these were direct programs we would long tolerate the inefficiencies that such program analysis would disclose.

Moreover, these inefficiencies have serious ramifications apart from the Budget. They have caused some activities, such as building construction and ownership for example, in many cases to be engaged in solely on an after-tax basis. But a

business in which the before-tax profit is low or meaningless and which becomes attractive only because special tax treatment for that business makes the after-tax profit quite attractive must surely rest on an unsound and unsatisfactory foundation. Especially is this so since the after-tax profit is attractive only for those who have income from other activities sufficient to permit full utilization of those special benefits. In large part this situation compounds our problems in the housing field, for it is difficult to achieve efficient use of direct Government assistance for high priority housing programs when the funds represented by special tax treatment continue to subsidize a whole variety of other building activities.

The Individual and Tax Subsidies

When we turn to the impact of these existing tax subsidies on individual incomes, we find there is no overall governor that keeps the rewards of subsidy within reasonable bounds. In our military contracts we recognize that despite proper contracting procedures, some contracts will turn up unreasonably high profits and a renegotiation process is utilized to maintain overall control. In other situations, either in Government purchasing or in private business, unusually profitable rewards of individuals are made subject to our progressive income tax. That tax system stands as a moderating influence that keeps the rewards of our private enterprise system within acceptable levels by channeling an appropriate part of those rewards into tax payments to maintain our Government. But when the rewards are cast in terms of tax benefits and subsidies, then the tax system is itself asked to stand aside. There no longer is any moderating force.

As a consequence, tax benefits and subsidies singly or in combination can permit some individuals to escape their fair share of contribution to the expenses of Government, and indeed in some cases escape paying any tax at all. It is hard to see why the individual who becomes a tax millionaire through the after-tax benefits accorded low income housing or some other tax-benefited activity is really different from the defense contractor, and why the latter is subjected to renegotiation while the former need not meet any overall limits on the rewards of tax subsidies. Or why there should be a mechanism to protect the integrity of the defense contract system but not the integrity of the tax system if we find some tax subsidies to be really necessary in areas where other solutions are not available.

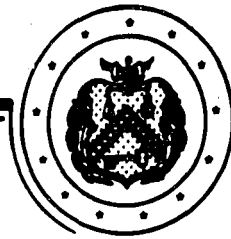
Conclusion

The inherent defects that thus attend the use of tax incentives should not handicap Government or business in a search for useful relationships in solving our social problems. We earlier mentioned the standard process whereby Government obtains goods and services, by simply paying business to supply them. There are, in addition, other alternative financial courses, such as loans, grants, and guarantees. Effective scheduling of Government programs, which would thereby guarantee large scale activity in particular fields over a number of years is another approach, since it would offer business the assurance of continuous activity justifying initial costs.

There are even ways in which tax provisions can be used to accomplish the desired purpose without involving an unnecessary tax subsidy. The President's National Advisory Panel on Insurance in Riot-Affected Areas (January 1968) faced the problem of providing insurance companies with special contingency reserves adequate to meet catastrophe losses which were difficult to measure in advance and at the same time preventing permanent escape from income taxes through the deduction of such large reserves. The Panel recommended the current deductibility of those reserves but with the resulting tax savings to be invested in interest-free U.S. Treasury securities. If the company later incurs losses, these securities can be used to meet them; if not, the securities are returned to income and taxed. There is thus tax deferral that prevents current taxes from depleting these reserves but without the special tax benefits that would otherwise accompany the setting aside of these large contingency reserves. This is the same procedure recommended by the Treasury and adopted by the Congress last year to meet somewhat similar problems faced in the mortgage insurance field.

There thus already exists a considerable variety of methods to provide the means to link business and Government together in solving our social problems. As business itself becomes more involved in these tasks it will undoubtedly develop new methods and arrangements. For innovation has no boundaries and the relationship between business and Government as both proceed deeper into the social field is bound to become more fruitful and more diversified. These are the possibilities that will surely become strong assets for the nation in achieving meaningful solutions to its present ills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 14, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing February 23, 1968, in the amount of \$2,501,490,000, as follows:

90-day bills (to maturity date) to be issued February 23, 1968, in the amount of \$1,500,000,000, or thereabouts, representing an additional amount of bills dated November 24, 1967, and to mature May 23, 1968, originally issued in the amount of \$1,000,010,000, the additional and original bills to be freely interchangeable.

181-day bills, for \$1,000,000,000, or thereabouts, to be dated February 23, 1968, and to mature August 22, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Monday, February 19, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on February 23, 1968, cash or other immediately available funds or in a like face amount of Treasury bills maturing February 23, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and the notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT
Washington

FOR P.M. RELEASE
THURSDAY, FEBRUARY 15, 1968

REMARKS BY THE HONORABLE STANLEY S. SURREY
ASSISTANT SECRETARY OF THE TREASURY
BEFORE THE
NATIONAL INDUSTRIAL CONFERENCE BOARD
AT
THE WALDORF-ASTORIA, NEW YORK, NEW YORK
FEBRUARY 15, 1968 - 9:30 A.M., EST

IMPLICATIONS OF TAX HARMONIZATION
IN THE EUROPEAN COMMON MARKET

The subject of European tax harmonization has evoked a misty glamour in the United States. Any movement that goes by the description of "harmonization" is attractive in these troublesome days. We also hear about a new tax that is sweeping across Europe, the "value-added tax," which has the intriguing, and also disconcerting for us, shorthand label of TVA. Certainly the question, "Is the TVA good for the USA?" can throw one of my generation off stride for a moment, as he wonders if he is back in the 1930's with the shade of Senator Norris of Nebraska and hearing a replay of Senate debates on our Tennessee Valley Authority.

As a consequence, many are apt to believe the Europeans have suddenly discovered a wonderful new tax system and that the rest of the world should rush to emulate them. The reality is quite the contrary. The Europeans for years have

had a serious tax problem on their hands. With the advent of the European Economic Community they have had to face the fact that this tax problem was a serious obstacle to achieving an effective Common Market and the desired economic unity. They have therefore started on the difficult task of correcting that problem.

Background of Tax Harmonization in Europe

What is this serious tax problem? The tax systems of the EEC countries were all characterized by high rate sales taxes, whose structures were extremely complicated, highly discriminatory and economically inefficient. As to rates, France until this year imposed a 25 percent tax on a value-added basis, and the present rate is 20 percent. The other countries had multi-stage, cumulative turnover taxes (also called "cascade taxes") at basic nominal rates of 4 to 6 percent (Luxembourg was at 3 percent, and Italy at 3.3 percent). These nominal turnover tax rates do not tell the whole story, however, since they were levied at each stage of the production and distribution process. Thus, the German 4 percent turnover tax rate was equivalent to an average rate of 12 percent on the value of the final product.

As to complexity, consider, for example, the French system where in addition to the 25 percent value-added tax (TVA) on manufacturers, wholesalers, and some retailers of goods, there was also a retail sales tax covering other retailers and handicrafts at 2.83 percent, and a sales tax on services at 13.66 percent -- along with a whole miscellany of specific excise taxes on such items as entertainment, wines, meat, gasoline, transport. Each tax was characterized by a lengthy list of special rates, exemptions, and options. Thus, the French TVA covered mining and building along with manufacturing -- but not farming and fishing and allied processing, or handicrafts. These complexities of basic rates followed by innumerable special rates and exemptions were characteristic of all the European taxes.

As to discrimination and economic inefficiency, consider, for example, the German system: Its turnover tax of 4 percent applied at each stage of the business process -- producer, manufacturer, wholesaler, retailer. (Hence the descriptive term "cascade tax" applied to these turnover taxes.) And at each stage the tax was built into the price and thus became pyramided and swollen as each sector in turn applied

its markup on price plus tax and then added its own tax. The consequence was acute differences in treatment between vertically integrated and non-integrated industries and concerns, between companies which performed some services for themselves and those which hired the services from others. In the other EEC countries a similar situation prevailed under their turnover taxes.

Sales taxes that run as high as 25 percent, or even 10 to 15 percent, are not to be treated casually or lightly. They have, at such levels, a high potential for economic mischief. But the exigencies of the past, the encrustations that any tax system accumulates, and the lethargy engendered by a familiarity with the status quo produced for the Europeans indirect tax structures that, at these high rates, were seriously defective.

The catalytic agent for change was the formation of the EEC. If Europe was to become a genuine common market in which goods and capital could move freely, a prerequisite was as much uniformity - harmony - as possible among the tax systems of the member countries.

The problem was clear: How to obtain uniformity out of this maze of high but disparate rates and complicated but

disparate structures that characterized the sales taxes of these countries when seen as a whole. The solution chosen was a two-step approach -- find a common sales tax structure that each could adopt and then move to uniformity in rates. The tax changes we are now seeing in Europe are in response to the first step, that of a common structure for these sales taxes.

The Value-Added Tax in Europe

For this first step, the EEC had to answer this question: What type of sales tax structure is best suited in their economies to support a high tax rate? The choices would be among the single stage sales taxes -- a manufacturers tax (Canada), a wholesale tax (Switzerland, Australia, United Kingdom), a retail tax (States in the United States, Norway), or a multi-stage tax of the value-added type (France). The multi-stage turnover type tax was not a possible choice, since it was essentially the villain in the existing picture.

A manufacturers tax has its problem of pyramiding through subsequent markups. It also has its problems of definition -- what is "manufacture" and how far does it reach into assembly, packaging, bottling, etc.? The tax at this stage also discriminates against certain forms of distribution (such as

manufacturers selling at retail), unless complex adjustments in prices are made for tax purposes. A wholesale tax involves many of the problems that beset a manufacturers tax, though in a different degree or form. There is the aspect of pyramiding; the problem of how to handle industries in which retailers perform certain wholesale or manufacturing functions and hence buy at cheaper prices; the problem of wholesalers who also sell at retail or manufacturers who skip the wholesale stage and sell at retail. While these considerations may point to a retail tax, the success of a retail tax can test severely the enforcement capabilities of a country, since the tax offers the largest number of taxpayers to police. In addition, these European countries already had turnover taxes under which each stratum of the economic process was presently being taxed, so that placing a tax at one stage only, say on the retailers, could well arouse difficult political problems.

The Europeans therefore turned to the value-added tax, which essentially is a multi-stage sales tax that achieves the end effect of a retail tax on personal consumption (consumption by households as contrasted with businesses). In

choosing a value-added tax, they desired however to avoid the accumulated complexities of the French approach to a value-added tax -- indeed the French themselves had already started on their own reform. The Germans this year were the first to adopt a new value-added tax to replace their turnover taxes and we can refer to it for understanding of the emerging European picture.

The German tax is imposed at a 10 percent rate (11 percent on July 1, 1968) on almost all sales of goods and services by any business. Let us start with a manufacturer: He applies a 10 percent rate to his total sales to find the preliminary tax due. From this he subtracts the taxes he has paid on his purchases and the net is payable to the Government. In essence, the tax is thus on the "value added" by him as represented by the difference between the value of his total sales and the value of his total purchases.

"Purchases" include all types of goods and services -- components either as raw materials or semi-processed goods; capital goods, such as plant machinery and equipment; goods used up in manufacture; business furniture, etc. The manufacturer, of course, will bill his customer for the 10

percent tax on the sales price of the articles he sells, just as the manufacturer was earlier on his purchases billed 10 percent by his suppliers. The tax is invoiced separately on all sales and is thus not hidden in the sales price.

The process is repeated at the wholesale stage -- the wholesaler pays the Government 10 percent of his sales less the taxes paid previously by the wholesaler on his purchases -- and the wholesaler then bills the 10 percent tax to his customers. But of course no pyramiding should occur since the taxes paid by the wholesaler are kept apart from the price of the goods he purchased and he can subtract this tax cost. The process is repeated once again at the retail stage -- the retailer pays the Government 10 percent of his sales, less the taxes the retailer paid -- and of course the retailer charges his customer for the 10 percent tax. The process ends there if the retail sale is for personal consumption -- food, an automobile, furniture, clothing. But if a business concern buys the article for use in its business -- say an automobile or a desk -- the process begins again as the concern will subtract the tax on the automobile or desk from its tax bill.

There is one additional important facet to note: Under the German system, tax is due each month. Suppose a concern has paid more tax on its purchases than is due on the sales to its customers -- its sales may be slow, for example. The Government here makes a refund each month of any excess tax paid, so that the cost of carrying the value-added tax is not borne by the concern beyond a month or two.

All this adds up to a 10 percent retail sales tax on personal consumption -- the 10 percent value-added levy is designed to be passed along from concern to concern until the consumer is reached and he is left with the tax. The 10 percent tax is not intended to enter into the price structure until that final sale -- until then it is a tax item that accompanies each sale, is kept separate on the books, and is so indicated. If the tax item is not promptly moved along the business chain, the Government refunds it promptly. (If a concern has to finance the tax during this month or two, this cost would enter into the price structure.)

Since the economic effect is that of a retail tax, the distortions due to pyramiding, differential burdens on integrated or non-integrated firms and industries, and

differences in distribution patterns that beset a manufacturers tax or a wholesale tax, are essentially avoided. At the same time the pressure for strong policing at the retail level that would exist under a retail tax is eased, since under the value-added approach the tax will have been partially collected at a prior level. If a retailer evades the tax, the Government has at least taxed the value at the wholesale level. And the chances of retail evasion are lessened, since the wholesaler has notified the Government of his sales to the retailer. Parenthetically, it is quite likely, however, that countries underestimate their capacity to enforce a retail tax. Even some developing countries are finding they can adequately administer such a tax if care is paid to its design and structure.* The Royal Commission (Carter) Report on Taxation in Canada (1966) recommended a retail tax to replace its present manufacturers tax and chose the retail tax in preference to a value-added tax.

The mechanics of the value-added tax are designed to keep the tax from entering into business costs even when a concern buys goods at retail that are used in its business activities. (A retail tax can meet this problem by exempting

* Due, The Retail Sales Tax in Honduras, in Bird and Oldman Readings on Taxation in Developing Countries (Rev. Ed., 1967) 326.

such purchases through a registration system; the value-added tax provides a refund of tax instead of exemption.) Of course, the value-added tax does involve pushing every concern into the act, and there is a lot more bookkeeping, tax paying and tax refunding, and paper passing than would occur under a retail tax. Moreover, the fact that every stage in the production process is nominally taxed can result in pressure drives for rate reductions by industries or groups concerned about their ability to keep passing the tax along. The value-added tax thus has an inherent potential for breeding exceptions and special treatment. But if a country feels it can't efficiently handle a retail tax, then a value-added tax is the next best thing.

The value-added tax is thus a useful solution to the sales tax structural problems that beset the Europeans and blocked their economic unity. As a consequence, Denmark adopted the tax on July 1, 1967; Germany did so on January 1, 1968; the Netherlands and Sweden plan to do so on January 1, 1969, and Austria is also hoping to change on that date; Belgium and Luxembourg will presumably go to the TVA on January 1, 1970; Italy may not be prepared to switch to TVA

by January 1, 1970. The changes in tax structure do not appear for the most part to be designed to bring about significant changes in the total revenue yield of the various tax systems or of the sales taxes themselves. France is reforming its indirect tax structure to achieve a similar application of the TVA.

Hence it is fair to say that the Europeans, by comparison to their present situation, have evolved a far more workable sales tax capable of application at a high rate -- more complicated than is needed where a retail tax would work, but still a workable mechanism. If a country is in the market for a high rate sales tax and if it really believes it cannot handle a retail tax, it should look the European model over. Should the United States be in the market for such a tax?

A Value-Added Tax In The United States?

We can first consider this matter in terms of our domestic tax structure and domestic economy, and then in terms of international aspects.

Certainly we hope that the long-term trend in the United States at the Federal level is not that of tax increase but

of tax reduction. There is indeed justification for us to look forward after Vietnam to being able to use our fiscal dividends -- the increase in Federal tax revenues that comes from growth in the economy -- partly to meet our needed expenditure increases and partly for tax reduction or debt reduction. As a nation we have not, since the Depression, sought to increase our Federal taxes except for fiscal policy reasons in times of hostilities. So we should not want a high rate sales tax on the ground of increasing our tax take.

Do we want it as a substitute for an existing tax? Here there are some -- the Committee for Economic Development for example -- that have for some time urged we should have a sales tax at the Federal level as a substitute for part of the corporate tax. The CED first urged a retail tax and now a value-added tax. Here we reach, of course, a classic split in tax philosophy -- between those who favor maintaining a progressive tax structure at the Federal level and those who would, by shifting to a sales tax, lessen that progressivity. Economists on the whole would agree that the corporate tax is a factor working for progressivity

in our tax system even though, as will be discussed later, there is some difference as to whether part of that tax is shifted forward in price or perhaps backward in wages and raw material prices. And there is general agreement that a retail tax, either of the single stage type or that achieved through a value-added tax, would increase the price level and largely be passed on to consumers, though as will be discussed later there can be uncertainty as to how fully this forward shifting is accomplished. The CED itself states that, "While it is true that the tax burden is distributed differently under a tax system with a value-added tax, we believe that the other effects of the tax are such as to compensate the nation in larger output and more growth.*

There is not the time here to examine in detail the validity of that latter belief, either as to the effect of the tax itself in our economy or the need for further incentives to investment that the statement implies. We must remember that the 7 percent investment credit and

* CED, A Better Balance in Federal Taxes on Business (1966), 28.

depreciation reform operate to provide incentives to investment under our present income tax system. At any event, the literature demonstrates that very many, presumably the majority, of our fiscal economists would disagree with the CED belief that we would be better off with the substitution of a sales tax for a part of our corporate tax. The Conference Report of the National Bureau of Economic Research and the Brookings Institution in 1964 on the subject of "The Role of Direct and Indirect Taxes in the Federal Revenue System" ends with the thought: "It is hard, then, to find much support for more reliance on indirect taxation in the record of the conference, even though some participants came, and left, with a disposition toward this view."

(313) Professor John Due, an acknowledged authority on sales taxes, has concluded:

"On the whole, the sales tax must be regarded as a second-best tax -- one to be employed only if various circumstances make complete reliance on income and other more suitable taxes undesirable. A carefully designed sales tax is not perhaps as objectionable as it was once regarded; it offers definite advantages over widespread excise tax systems, with their inevitable discrimination among various consumers and business firms and their tendency to distort consumption patterns; and it is definitely superior to high rate 'business' taxes

with uncertain incidence and possible serious economic effects. But it must be regarded as secondary to income taxation, in terms of usually accepted standards of taxation."*

Recommendations for a sales tax at the Federal level in the United States generally overlook the fact that the States, supplemented by the cities, are gradually evolving a sales tax structure for the United States, and one at significant rates -- 44 States and the District of Columbia have sales taxes (there are municipal sales taxes in 15 States), the usual rate is presently around 3 percent but some taxes reach to levels of 5 percent and 6 percent (the usual municipal rate is 1 percent), and the trend is of course upwards. While this structure is not at the Federal level, its basic economic consequences are not different from a Federal sales tax.

Recommendations for a value-added tax also gloss over the complexities involved in adding a sales tax to our national system. No one should be misled into thinking a value-added tax is a simple levy, with a few pages of statutory text. It is a highly complex instrument. It is

* Due, Sales Taxation (1957) 41.

** See the discussion by Prof. Francesco Forte on "The Feasibility of a Truly General Value-Added Tax: Some Reflections on the French Experience", 19 National Tax Journal 337 (1966).

considerably better than what most European countries have today -- but no one should ask a country to adopt it unless there is a very clear, real gain to be achieved. Moreover, anyone who thinks a value-added tax sounds simple should just suppose he was back in the past and someone were to say: "Here's a simple way to tax people -- you just add up their total income and then you subtract their total expenses, and then you just tax the difference. It's called an income tax." Well, you know the story of that tax! No mass tax can be a simple tax -- as anyone acquainted with a State retail tax will agree -- and a value-added tax is more complex than a retail tax.

These are among the factors that have in the past kept Congresses, Democratic or Republican, from legislating a national sales tax. If the past is prophesy, a pragmatic view of this question would appear to be that the Congress is not likely to change its course.

One may ask why the Europeans have high rate sales taxes. History plays a very large part. Most of the Europeans mass sales taxes were adopted in World War I or the period just after it, and were borne of financial necessity.

if we subtract the differences between indirect tax levels, so that European indirect taxes would be included at our level, the total tax burdens become: United States 27 percent; United Kingdom 25 percent; Italy 26 percent; Germany 29 percent; France 30 percent; Netherlands 33 percent. If we consider direct taxes alone as a percent of GNP, and thus leave out both indirect taxes and Social Security contributions, the comparisons are: United States 18 percent; United Kingdom 16 percent; Italy 17 percent; France and Germany 20 percent; and the Netherlands 24 percent.

The Europeans have high rate mass sales taxes and as a consequence are countries that impose a heavier tax burden overall on their peoples. The United States does not have sales taxes at those high rate levels, and consequently imposes a lower total tax burden. It is difficult to see why United States taxpayers should urge that we emulate the Europeans.

This is not to say that continued study of the value-added tax is not useful. At the very least we should know what the Europeans are doing. But the studies should be tough-minded and straight-forward. They should not be

content just to admire the outside wrappings and never examine the contents of the package. They should not become bemused with semantics and fail to make clear that the European value-added taxes are in fact sales taxes in their structural design and economic effects. Hence, to substitute a value-added tax for the corporate income tax does not involve just another way of taxing corporations. The issue is not, despite the way it is sometimes put in the United States, of economic and technical judgments over two methods of taxing corporate business. The basic issue still remains that between substituting a sales tax on personal consumption for an income tax on corporate profits. However appealing to some may be the semantic gain, the issue should not be allowed to be blurred by omitting the term sales tax when we discuss the value-added tax.

If we are to study the adoption of a sales tax in the United States we should extend the studies to encompass the retail sales tax as well. The studies should also recognize there are many issues to be explored in addition to that of regressivity and the allocation of the tax burden between consumers and investors. Thus, there are considerable shifts

in burden among the various sectors of the economy when a value-added tax or any sales tax is substituted for a corporate tax: e.g., banks and financial institutions are generally exempted (that is, the tax does not reach their services but may reach their purchases); the activities and profits of foreign investment are not reached; unincorporated business gets swept into the structure of a value-added tax; the tax falls on unprofitable concerns as well as profitable concerns so that if the tax cannot be shifted forward the former concerns will suffer; the coverage of Government-provided services becomes an issue. All in all, there is much more to be studied than the calls for study have generally indicated.

In pursuing such studies we must also remember we already possess a "common market" and economic unity within the United States and so do not have the sales tax problems that the Europeans must solve to achieve their economic unity. As stated above, we do have retail sales taxes in most of the various States, but they do not produce any serious economic distortions or competitive effects. There may be some irritating compliance problems for interstate business, but even these are moving, albeit slowly, to

improvement. Hence we do not have any sales taxes to "harmonize" as do the Europeans.

In this regard the same story may be told for what may some day be the next major step in tax harmonization for the EEC -- the harmonization of corporate income taxes. We in the United States invest and our businesses operate in our "common market" under our Federal corporate rate, which applies uniformly throughout the United States. While State corporate income taxes exist and differ as to rates, their deductibility from the Federal corporate tax greatly lessens their effective rate, although irritating compliance and bookkeeping aspects remain. But Europeans in their common market must invest and operate under as many different high rate corporate tax systems as there are countries involved -- systems that differ both as to rates and structure. So if Europe finally decides on a common corporate tax, it will, as respects economic unity, merely be reaching the stage the United States has enjoyed for many years.*

* Other aspects of harmonization that have a similar consequence may briefly be noted: A common market implies a relatively free flow of capital within the market area
[Footnote continued at bottom of next page.]

European Border Tax Adjustments -- Their Background

Let us turn now to an aspect of the European sales tax systems that has been highlighted in recent years as a result of our balance of payments problems -- the aspect of export rebates and compensatory import taxes that characterize the European sales tax systems. All countries with significant sales taxes or excise tax systems automatically structure those systems to attempt to keep the taxes from affecting external export prices and to ensure the application of the taxes to imported goods. If the tax is a manufacturers tax on the final product --an automobile, a

[Continuation of Footnote:

and will therefore require removal of existing restraints on capital movements. There will be increasing concern among European countries on the extent to which differences in other aspects of direct taxes affect capital flows. Low withholding taxes in a given country would attract portfolio investments from other countries, particularly in the light of the widespread use of bearer shares and bonds. Consequently uniformity in withholding taxes is important. There may also be a reappraisal of attitudes toward the foreign tax credit approach as a means of eliminating double taxation in contrast to the tax exemption approach presently used in many European countries. With more volatile capital movements the consequences of tax exemption of foreign income will appear more serious than in the past. A common market with increased fluidity in capital movements requires the removal of barriers to corporate mergers, reorganizations and the like. Consequently the tax treatment of capital gains, for example, will have to be modified so as to remove a barrier toward integration of industries and reorganizations in line with the emerging needs of an enlarged market area. But again, the United States does not have these problems.

refrigerator, cigarettes, liquor, and so on -- then exports are not made subject to the tax, or if taxed, can secure a rebate. Imported goods, on the other hand, are subjected to the same tax as is imposed on domestic manufactured goods, so that both goods will compete on equal terms in the domestic market in this respect. The United States does this for its few manufacturers taxes; Canada does the same under its 11 percent broad manufacturers tax.

If the tax is imposed at the wholesale stage or the retail stage, such rebates and import taxes are not needed: a manufacturer selling goods whether for internal consumption or export is not subject to these taxes; a wholesaler importing goods will pay the tax on his subsequent sale. The sales for export that a wholesaler or retailer may make will be exempted from tax.

The essential principle under which all these taxes are structured is that sales and excise taxes are intended to be paid by domestic consumers in the form of higher prices -- that is the purpose of the levy and that is the intended distribution of the tax burden. But at the same time it is intended that a country's exports should not be handicapped by these taxes -- and imports into the country should not be favored.

The European turnover taxes followed the same principle but ran into additional complexities. It was simple, of course, to say to a German manufacturing firm that it need not pay the 4 percent turnover tax on an export sale. But what about the 4 percent taxes paid by the manufacturer on purchases from its suppliers of materials of almost every sort -- these 4 percent taxes were built into the costs of the manufacturing operation, just as the 4 percent taxes the suppliers had to pay on their purchases were built into their costs and also passed along as part of the prices charged by the suppliers. For that is the vice of turnover taxes -- they pyramid in prices throughout the economy. The economic effects of these taxes were significant at the high rate levels applied in Europe. The principle of protecting exports therefore required a rebate of these taxes previously imposed in the production chain and which cumulated as costs for the manufacturer on its purchases, or for the wholesaler if he was the exporter. But how much should be rebated? Here these countries had to compute the amount through an estimating procedure, for these high rate taxes were hidden in the price structure and, moreover, their

total would vary with the extent of integration of productive activities in the prior stages. The European countries therefore carefully developed average figures and used them for the rebates. Corresponding figures were used for the import charges.

A common market ideally requires a tax system that does not have complex border adjustments. A common retail tax would accomplish this -- as pretty much occurs in the United States -- if care is taken to keep the tax from applying to purchases for business purposes. Failing that, if border adjustments are to exist, their calculation should be made with as much precision as possible. It is here that the value-added tax provided an extra advantage for the Europeans. For just as the value-added tax eliminated for internal sales the distortions resulting from pyramiding and differences in integration of business activities, it also by the same token and procedure offered a ready measure of the taxes that the exporting firm had to pay because of its purchases. Indeed, under the German value-added tax, a firm is given a "rebate" through refund or credit for all of the taxes it has to pay on its purchases, whether its goods

are sold internally or externally. The structure of the tax thus readily enables the Government to determine the amount of export rebate needed to reflect the exporter's book costs representing the taxes paid on its purchases. And it similarly permits the fixing of the amount of import charge to reflect the taxes paid by domestic concerns.

In time, of course, if Europe can achieve uniform value-added rates, then it could abandon these border adjustments, export exemptions and import charges for intra-EEC trade, and simply go to the rule that the country of origin taxed the sale. It would be a matter of indifference -- within the Common Market -- as far as import and export competitiveness are concerned, whether the exporting country were to grant an exemption or rebate and the importing country impose an identical import equalization tax (the "destination" approach), or whether the exporting country taxed the export and the importing country did not impose its import tax (the "origin" approach). There would be some effect on national revenues to the extent that trade is not in balance, but this would be minor. The border adjustments would, of course, remain applicable to trade by the EEC with other countries.

But the day of uniform sales tax rates will take some time to arrive in Europe. In the meantime the shift to value-added taxes has brought about a precise system of border tax adjustments given the structure of the taxes, and this will facilitate economic unity within the Common Market. In this setting our discussion can turn to the effect on the external trade of the Common Market countries, especially as respects the United States.

Border Tax Adjustments and International Trade

In the German situation, the rebates for taxes paid on goods purchased by the exporter and import charges under the value-added tax are turning out to be higher than the averages used under the previous turnover taxes. This varies, of course, from product to product but the over-all result is higher. In effect, it would appear that some German exporters had presumably not been receiving rebates at the level that their tax costs under the turnover taxes appeared to call for.* Of course German exporters

* As Professor Due has pointed out, German businesses had earlier suspected this: "German firms argue that the failure to obtain full sales tax refund places them at a disadvantage, particularly in competition with American and British firms not subject to a similar tax. . .". Due, Sales Taxation (1957) 62.

presumably had adjusted to that situation and the effect of the undercompensation if it existed could no longer be traced through all the prior history of exchange rate changes, devaluations, and the like. Hence viewed as of today as the starting point in time -- which is the proper way to consider the effects of the change -- this sudden increase in export rebates under the value-added tax, while the internal overall burden of the tax remains unchanged, becomes an advantage to German exporters. And equally, the rise in the import charges can be an added competitive burden to imports.*

What is happening in Germany is, and will be, reflected elsewhere in Europe as the countries shift to value-added taxes. The Netherlands, Austria, Belgium, and Italy are even raising their rebates and import charges under their existing turnover taxes in advance of a later shift to a value-added tax. Sweden is shifting to a value-added tax because it realizes that its previous "retail tax" had been levied on producers' goods and hence was in effect a turnover tax to that extent but it had not been rebated to exporters.

* The Germans assert that these trade advantages are offset by transitory tax arrangements outside the value-added tax affecting investments in plant and equipment, and state that in any event any calculations are to a large extent hypothetical.

As a consequence, European exporters in general will get an added lift in most countries.

There is an additional feature of the shift to a value-added tax that operates to increase this lift to exporters. Countries with a value-added tax seek to achieve as broad a base for the tax as possible, since it operates effectively to prevent pyramiding as compared with specific excises. In France, for example, the reforms of the value-added tax have been in the direction of increasing its coverage and eliminating other taxes. Any commodity previously taxed under a specific excise tax but now swept into a value-added tax immediately falls into the rebate process, under the structure of the latter tax, so that the tax paid on the purchase of the commodity is rebated whether the business concern at that stage is selling internally or abroad. Hence, the result is that a number of hidden, and hitherto unrebated taxes, in effect come to light and now are rebated -- and also included in the import charge.

But what about the rest of the world? The United States does not have a high rate sales tax and therefore only rebates its specific manufacturers taxes on final products. The United Kingdom has a purchase tax at the wholesale level

which over-all does not require rebates for tax costs since essentially it did not apply to business purchases. Canada also does not apply its manufacturers tax to most business purchases and likewise does not need rebates except for any tax paid on the final products that are exported; similarly neither does Japan for its variety of manufacturers excise taxes. Thus, unlike the European countries whose high rate turnover taxes entered into the costs of exported goods through the cost of the goods purchased by the exporter and thus necessitated export rebates and import charges, these countries did not apply their sales taxes to business purchases and thus did not have high sales tax costs imbedded in their exported goods. As a consequence they have not been as rigorous in seeking fully to eliminate indirect taxes from export costs and hence do not have a system of export rebates for tax costs or import charges.

Similarly, the United States has not sought in the past to see how much of the Federal gasoline tax, the passenger motor vehicle tax, the truck tax, the telephone tax, or the alcohol tax, for example, paid by a manufacturer who exports

some of his goods is allocable to those exports and thus increases their costs. Nor has it sought similarly to see what part of State and local sales taxes paid, for example, on office equipment and other goods purchased by a business increase its export costs. In contrast, under the European systems the value-added taxes on such products, since they are all in the base of the tax, automatically are rebated. This was likewise the situation under the turnover taxes, since in large part such goods were under the base of those taxes and figured accordingly in the average rebates. (There are, of course, some specific European excise taxes outside the scope of turnover and value-added taxes that are not being rebated.) The United Kingdom, several years ago, initiated rebates for its special excise taxes -- principally the gasoline taxes, motor vehicle license taxes, and purchase taxes on office supplies -- on goods purchased by its exporters, and essentially used averages to determine the rebates.

In the United States it has been estimated that the costs attributable to our Federal, State and local taxes on goods bought by manufacturers represent on the average

an amount equal to about 2 percent of export sales prices. The impact on product lines differs, of course, with the range running from about 1-1/2 percent to 4 percent of export sales prices. A rebate of these tax costs and a similar import charge, administered through our Customs organization, would reflect for the United States an approach that corresponds to the principle applicable under the value-added and turnover taxes of attempting to keep sales and similar taxes at prior stages of production from increasing export costs and export prices. An approach by the United States to deal with its indirect taxes on a rebate and compensatory import charge mechanism would involve the use of product averages, and this use would be similar to the procedure followed by the Europeans under their turnover taxes. Consideration of this approach in the United States would therefore reflect principles and practices underlying the treatment of indirect taxes in Europe. Moreover, it would parallel the attention to, and consequent changes in, border tax adjustments now generally resulting in Europe from the shift to value-added taxes.

Sales Taxes and International Trade

But the European efforts to stabilize their sales taxes and border adjustments and then to harmonize them raise even larger issues of trade policy interlocked with tax policy. The European practice of rebates and import charges for turnover and value-added taxes reflects the basic assumption that such taxes are passed along through channels of trade so that their burden is borne by households buying goods for personal consumption. This is the assumption behind the exemption of exports from a manufacturers tax. It is the assumption of legislators who enact wholesale or retail taxes or other sales taxes. As a working assumption for domestic legislation and for general judgments on the distribution of the burden of a tax system, or of a new excise or sales tax, it is a useful operational device. But the balance of payments world of today, with its fixed exchange rates and the attention that must be focused on both the over-all balance and its component parts, including the trade portion, requires much more attention to specifics than ever before. This need for such attention is also heightened by the high levels of tax rates that now

obtain under modern tax systems compared with an earlier period, a development that contrasts with the shift to lower levels of tariff barriers that has occurred. If the generality is only a generality and the specific situations show a different posture, then the matter must require a sharper focus.

If sales taxes or other indirect taxes -- whether they be value-added, turnover, retail or other tax forms -- cannot be fully passed on in price, then a manufacturer selling in his domestic market must lower his prices and reduce his profits. But if the full rebate of the tax cost and the exemption of exports from the tax make it unnecessary to change his export prices, then he is not concerned about passing anything along on an export sale, he need not lower his export price, and his export profits would not suffer as would his domestic profits. The business of exporting becomes that much more attractive, and the sales tax system has become an incentive to export activity. Similarly, on the import side, the importer to meet the competition of lowered domestic prices must reduce his price, his profits decline and he is less interested in pushing

those imports. In essence, one gets to the question of tax incidence and whether these sales taxes are fully shifted forward in price or only partly shifted.

Put another way, a value-added tax is carefully structured to pass the tax along in an accounting sense. Its effect on international trade, however, depends on whether the economic effects follow the accounting structure. If the tax is not fully shifted forward in an economic sense, then the international trade of the country using the tax will be favored regardless of the accounting structure.

It is not the levels of rebates per se and the differentials between them that measure the competitive effects of border tax adjustments. If Country A has a value-added tax of 10 percent and rebates to an exporter the total of the taxes, at a 10 percent level, that he has paid on his purchases it is because Country A does not want his tax costs, which are real, to enter into export prices. If Country B has no value-added tax or other sales tax, then there are in this respect no comparable tax costs to rebate to its exporters. But knowing only these facts does not really inform us about trade competitiveness between these

countries. We cannot conclude that Country A grants a 10 percent subsidy to exporters while Country B has no subsidy. Nor can we conclude that the goods of Country A have a great advantage entering into Country B because they face no import charge in the latter country whereas the goods of Country B face a 10 percent charge on entering Country A and hence are a great disadvantage in Country A. If sales taxes were fully shifted forward, then the goods of both countries would, as respects sales taxes and border adjustments, be on an equal competitive plane despite the different levels of adjustment. But if such taxes are not fully shifted, then in this regard the exporters of Country A have been advantaged as against the exporters of Country B -- not necessarily to the full extent of the differentials in border adjustments but only to the extent to which the tax in Country A is not shifted forward.

Of course, questions of incidence can be raised as to other taxes. The working assumption of legislators for domestic legislation when they consider a corporate income tax is that it is borne by shareholders and not passed forward in higher prices or backward in lower wages or lower

raw materials prices. Again, as a working assumption this view of the incidence of the corporate tax is a useful generality. But if it is only a generality and if there is some forward shifting in prices, an exporter has added costs, due to the corporate tax entering into product costs, which are not being rebated and hence which affect his export prices and his external competitive position. Of course, this would be true for an exporter in any country with a corporate tax, including European countries. We should note that the effective rates of corporate income tax in major European countries do not appear to be significantly different from the United States effective rate. Certainly, if a differential does exist between European corporate taxes in relation to the United States corporate tax, it is far less than the differential between European indirect taxes and our indirect taxes. In addition -- though there may be no studies on this point -- the conditions that may influence a shift forward of the corporate tax into prices, if such shifting does occur, would presumably not differ between Europe and the United States.*

* For a discussion of the possible effects, considering the various theories of tax incidence, on the balance of payments of a shift in the United States to greater reliance on indirect taxes and less on direct taxes, and the relationship of those effects to the effects on domestic policies and conditions, see Salant, *The Balance of Payments Deficit and The Tax Structure* (Brookings Institution, Reprint 80) 1964.

These are difficult, intriguing -- and highly important -- questions. This matter of tax incidence and tax shifting is murky, and it has kept economists busy for decades. Their papers have contributed many volumes to the economic literature -- and nevertheless I suspect that the summaries in Economics I are still inconclusive and uncertain. Moreover, one may have to move from incidence and shifting on to levels of taxation and then to levels and allocation of Government expenditures. But clearly the area requires exploration and analysis beyond the generalities.

The problem will become more acute if the Europeans take the next step of harmonizing their indirect tax rates, for this could mean an increase in the value-added taxes -- perhaps to 15 percent or more -- for all countries except France, which today is at 20 percent (on the value of the product excluding tax).

Certainly, to the extent that the generalities are not fully valid, the disparity in indirect tax levels can only be working to the disadvantage of the United States in world trade. The extent of that disadvantage and the extent

to which it has been adjusted for in prior exchange rates and devaluations may be difficult to measure, but the direction is that of disadvantage for the United States.

The Harmonization of Diverse Tax Systems

As a consequence, these basic aspects of domestic tax systems in their international settings require full international discussion and consultation looking to a solution -- a process that is already under way. It is here that we reach an important implication for the United States of European tax harmonization. The premises and rules of GATT with respect to export subsidies and border tax adjustments rest on the generalities of incidence and shifting that I have described. Under those premises and rules the European countries have almost entirely kept their high sales taxes from increasing their export costs and prices. The shift to value-added taxes will underscore this effort and make it easier of accomplishment. In addition, to the extent that the incidence of these taxes in the actual economic world is at variance with those premises and rules, the European tax systems operate in the direction of providing a trade advantage for the Europeans. Looking ahead, most Europeans

countries may well be moving to higher sales taxes in the tax harmonization steps needed to perfect their Common Market. Given European tax harmonization, the larger question becomes that of "harmonization" of their tax systems with those of the United States and other countries in a broad sense. This "harmonization of tax systems" does not, however, mean the uniformity of taxes that harmonization connotes within the EEC. Rather, it means the process whereby national tax systems that may differ both in kind and in burdens imposed can coexist in the world without creating difficulties for each other -- can coexist in harmony. The full exploration of this question within the GATT and in other ways can take us into many facets of international trade, including those of non-tariff barriers. It can take us into the mechanisms for reaching adjustments between countries in a balance of payments surplus position and those in a deficit position.

Clearly such exploration is needed to preserve freedom of action for countries to establish their domestic tax systems and the distribution of their tax burdens in keeping with their notions of economic growth and tax equity without

at the same time prejudicing their international trade position. The essential question is how may countries which desire to rely on a progressive tax structure or countries which do not wish to place heavy overall tax burdens on their peoples, and hence have no need for high rate sales taxes, continue in these domestic goals and still maintain in their international trade full competitiveness with the European countries which have a different domestic tax philosophy? For surely a better answer can be found than that the rest of the world to protect its trade position must simply emulate the Europeans and their domestic tax philosophies, whatever may be the impact of that emulation on the tax systems and internal economies of the other countries.

The United States -- and the rest of the world -- thus has a high stake in a full exploration of these issues -- issues which are made both more pertinent and more important by the process of tax harmonization in Europe.

TREASURY DEPARTMENT
Washington

FOR RELEASE A.M. NEWSPAPERS
THURSDAY, FEBRUARY 15, 1968

REMARKS BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
AT DINNER MEETING OF THE BUSINESS COUNCIL
MAYFLOWER HOTEL, WASHINGTON, D.C.,
WEDNESDAY, FEBRUARY 14, 1968, 7:00 P.M., EST

It is always a pleasure to meet with the members of the Business Council, and to have the opportunity to present to you my views on the nation's fiscal and economic position and to obtain and benefit from yours.

I believe that this meeting of the Council is exceptionally timely and important. It comes at another point in our history when the American people must take hard decisions to meet sharp and inescapable challenges -- not avoiding the difficult choices -- not ducking the disagreeable measures -- not waiting for the problems to become unmanageable.

I refer to the type of decision President Johnson made in his New Year's Day message to the nation on the Balance of Payments.

The manner in which we respond to the challenges facing us -- the choices we make -- will bear heavily not only upon our own security and economic strength but on the security and strength of the entire Free World for many years to come.

In international security affairs, we and our allies are being tested severely in various parts of Asia by open Communist aggression and subversion backed by the threat of aggression. I know this is on all of our hearts and minds every day and night, as our young men fight on -- some never to return.

But tonight let us focus primarily on moves now pending in the field of national and international finance -- hardly less important than those in the field of war.

To a considerable extent the problems of war in Southeast Asia and the financial challenges facing us are interrelated. The war, without question, is a contributing factor to some of our financial strains. We need a tax increase to finance a portion of the costs of that war without an excessive budget deficit or excessive Federal borrowing in the capital markets. And a failure on the financial front could have serious impact on our ability, capacity and will to maintain our national security.

But the war in Vietnam is by no means the sole cause of our economic and financial problems. We had a balance of payments deficit long before Vietnam. And the problem of reconciling price stability, healthy and sustainable economic growth, and full employment has been with us for decades.

In the past twenty years, fueled by a strong U.S. economy and a strong U.S. dollar in a viable international monetary system, the Free World has made the greatest strides in trade and development in recorded history. For the past seven years the U.S. economy has enjoyed the longest, the strongest, and the most stable expansion in our history.

The decisions the nation is taking in the early months of this new year will have much to do with the preservation of that viable international monetary system and that expanding, stable U.S. economy on which it depends. If we make the right decisions we could preserve for many years a healthy prosperity and the social and economic progress it makes possible.

Of course, the preservation of anything worthwhile is not glamorous or exciting. But the issues are clear.

In domestic affairs we are being challenged to act in a financially responsible manner.

The record-breaking, relatively stable expansion we have experienced during the last seven years has not occurred by accident. It has been made possible by taking decisions to promote the kind of environment in which it can thrive.

This is not a one-way street. When unemployment is high and production low, the environment must be one of encouragement to greater economic activity -- such as the tax reductions of 1962, 1964 and 1965. But prosperity, like many other enjoyable experiences, can develop its own excesses.

The principal excess is running at a rate of speed which puts pressure on resources of labor, materials and plant and results in inflation, imbalances in various sectors of the economy and, if unrestrained, leads to the inevitable bust of the old familiar boom and bust cycle.

Thus, when economic activity threatens to accelerate too fast, we must have the courage to hold down public expenditures and raise taxes temporarily -- to use appropriate monetary restraint in the creation of money and credit -- to exercise the utmost responsibility in wage and price decisions which add cost-push inflation to that induced by demand -- to take whatever action is required to preserve the stability of the economy.

Moreover, the right decisions at home on our internal economy are basic and fundamental to the right answers in international financial affairs, where we face the challenge of maintaining a strong dollar as the bulwark of the international monetary system.

The future of our economy and of the international monetary system which is so heavily dependent on it can be preserved if we have the will to act promptly and decisively against the present threats to our economic strength -- against the need for massive Federal debt financing, against the deterioration in our balance of payments, against the inflationary forces that are reducing the value of the dollar at home and weakening confidence in it abroad.

The tax program the President has recommended to the Congress, primarily a temporary increase in personal and corporate income taxes, is a key part of our fiscal response to the major challenges facing the nation.

Let there be no mistake about it -- the prompt enactment of a temporary tax increase is the single most decisive and important action we can take to:

- Reverse sharply and decisively the trend toward increased deficit financing which began with our increased participation in hostilities in Southeast Asia in fiscal year 1966.

- Reduce the budget deficits for fiscal years 1968 and 1969 by as much as \$16 billion.
- Reduce appreciably the most important source of pressure on our credit markets: the huge overhang of Federal borrowing which steadily ups interest rates.
- Remove the threat to our housing industry, which is in the process of a needed recovery.
- Remove the risk of a credit crunch that will deprive States and local governments and small business of ready access to credit.
- Reverse the trend from a creeping to an accelerating inflation and turn the economy back toward price stability and wage changes more closely related to increased productivity.
- Halt movement toward another disruptive inventory cycle.
- Prevent our returning to the old pattern of "boom and bust."
- Protect, maintain and expand our trade surplus, which is the mainstay of our balance of payments position and which is vitally important to the preservation of international confidence in the dollar and the stability of the international monetary system.
- Demonstrate to the world our determination to make whatever sacrifices may be necessary for the maintenance of our economic strength, and through it, the strength of the dollar.

Looking ahead to the days of peace, when we shall need to put to work the men, materials and facilities used in the war effort, the enactment of a tax increase now, specifically related to pay for part of the cost of war, will provide a ready means for a smoother post-Vietnam adjustment through its quick removal.

When a tax increase was recommended by the President last August, there were those who doubted the economic forecasts on which it was based, contrary to the unanimous views of the President's advisers and the near-unanimous forecasts of business and academic economists.

But what is the economic picture today, six months later? It is a picture of an economy that is buoyant, that is already running at excessive speed, and that is still gaining momentum. Because the first half of 1967 was relatively weak, the full extent of the economy's resurgence tends to be concealed in statistics for the full year.

In the second half of 1967, and especially during the closing months of the year following the settlement of major strikes, economic activity advanced at a pace that cannot be sustained without intolerable strains on our resources:

- Gross national product rose by \$32-1/2 billion in the second half of the year, in contrast with a rise of only \$13 billion in the first half.
- Real output grew at an annual rate of 4-1/2 percent from June to December -- at a rate faster than the growth of productive capacity -- and would have been even higher except for major strikes.
- Manufacturing activity, rebounding from the inventory adjustment that had slowed the economy in the first half, advanced at an annual rate of 8-1/2 percent in the second half.
- Payroll employment in nonfarm industry rose 1.2 million in the last 6 months of the year, considerably higher than the sustainable rate of advance under present circumstances.
- Personal income grew \$25-1/2 billion from June to December. By comparison, the largest full-year increase ever registered was \$46 billion between 1965 and 1966.
- In each of the last four months construction contracts exceeded any prior month in history.

There is another and disturbing part of the picture, however, and it is a marked speed-up in inflation -- a speed-up that gives new urgency to the request for early enactment of a tax increase.

In the last quarter of 1967, as in the third quarter, nearly half of the rise in our gross national product was accounted for by inflated prices rather than real growth. Further, the pace of price increases has been accelerating. Wholesale industrial prices, which rose at an annual rate of less than 1 percent in the first half of the year, advanced by more than 2½ percent in the second half.

Consumer prices, rising at an annual rate of 2.3 percent in the first half of 1967, jumped to a rate of nearly 4 percent in the second, and would have been still higher except for a decline in food prices.

Wage increases also were relatively high in 1967, with some very large settlements being reached in the last months of the year.

Thus, we have entered 1968 with a strong and increasing inflationary trend. And if we permit it to continue unchecked, if we fail to restrain demand through a tax increase, then we will clearly risk much -- imbalances in the economy, still higher interest rates and greater credit stringency, and eventually, perhaps, recession. In short, a failure to act will mean risking the future of our economy.

Aside from domestic considerations, we must also be concerned with the international consequences of inaction or delay. Our trade surplus is the most important and most favorable factor in the national balance of payments. We must look to it to finance an increasingly large portion of our other expenditures abroad. And if an increasing price and wage spiral makes it difficult for our products to compete with imports and in export markets, the trade surplus will diminish, not increase, and our balance of payments will suffer. Already, in the fourth quarter of 1967, there was a very disturbing absolute and percentage increase in imports by an economy that has an increasing propensity to import when growth in money terms exceeds 8 percent.

Given the present state of the economy -- expansionary and accompanied by unacceptable inflationary trends -- a highly stimulative Federal budget deficit is inappropriate and even dangerous. The economy needs to be held to a sustainable rate of advance, not propelled by huge Federal deficit financing to still greater speed.

The tax increase the President has again requested, as an essential part of the budget for fiscal 1969, would produce an additional \$16 billion in revenue over the next 18 months. It would reduce the deficit for the current fiscal year from \$22.8 billion to \$19.8 billion, and would sharply reduce the deficit in fiscal 1969, from \$20.9 billion to \$8 billion.

There are those -- and I have been one of them -- who have urged, as did the President in his August 3 Tax Message, that along with a temporary tax increase the Congress and the Administration should control and reduce Federal expenditures, civilian and military, to the maximum degree that is consistent with the nation's security and economic soundness. Let us look at the record.

Through a combination of Congressional and Administration actions culminating in the enactment in December of Public Law 90-218, the so-called continuing Appropriations Act, obligations in this fiscal year were reduced by \$10 billion. These reductions will cut back specific expenditures in non-Vietnam defense programs and controllable civilian programs in fiscal year 1968 by \$4.3 billion, and will bring additional savings in fiscal 1969 and later years. These program and expenditure reductions included such items as:

- Cutting back farm operating loans and sewer and water loans;
- Reducing REA loans;
- Canceling some agricultural research projects;
- Closing some agricultural research stations;
- Cutting payments to States for agricultural experiment stations;
- Reducing the small watershed construction projects;
- Cutting agricultural conservation payments to farmers;
- Spreading all of the Corps of Engineers new construction starts voted for 1968 by the Congress over the two years, 1968 and 1969, and holding back on the rate of construction for on-going projects;

- Sharply reducing the higher education facilities grant program;
- Cutting back Hill-Burton hospital grants;
- Cutting back the construction programs for medical schools and other health facilities;
- Reducing the NIH regional medical program by more than one-third;
- Curtailing the impacted area school program;
- Cutting back two major reactor development programs;
- Reducing the Plowshare nuclear excavation experiment;
- Reducing the program for controlled thermonuclear fission.

These reductions provided a reduced base for many of the budget projections for the fiscal year 1969 reported to Congress on January 29.

The increase in the budget expenditures for fiscal 1969 -- \$10.5 billion -- should be compared with increases of \$24 billion and \$17 billion in fiscal years 1967 and 1968, respectively.

This increase in projected expenditures in fiscal 1969 is almost completely accounted for by higher expenditures required for national defense, increased interest payments on the public debt, and mandatory payments required by recently enacted laws dealing with Social Security, public assistance, veterans benefits and Federal pay increases.

The increase in expenditures will be more than offset by the expected normal growth in Federal revenues resulting from increased economic activity in the next fiscal year.

In a few instances, the budget does provide for expansion of a few controllable civilian programs which meet urgent needs -- for example, for job training and urban renewal. But in every case, these increases have been offset by reductions or modifications in other desirable but less essential and urgent government programs.

For example, the President's Budget Message provides on pages 20 through 22 a table of proposed program reductions and reforms which I am appending to the text of my remarks. They touch nearly every major agency in the Federal Government. Affected are Federal construction and construction grant programs, the space program, health, education and welfare grants, agriculture and small business loans, and many other activities that can be deferred in a period when we must relieve inflationary pressures by reducing the deficit. The budget also proposes reforms and modifications to reduce government outlays and increase the effectiveness of certain programs -- in housing, agriculture, transportation and other areas -- and reduce their cost to the taxpayer over time.

These budget reductions and reforms would reduce 1969 obligations and contracts in the affected programs by almost \$3 billion below the levels appropriated for 1968. The reforms would reduce the budget in 1970 by an estimated \$1.4 billion.

I share the general concern that the totals of budget expenditures are increasing. But I must point out that this fact does not diminish the desirability of a tax increase to help finance the war in Vietnam out of current revenues rather than borrowed money.

Our annual expenditures for our efforts in Vietnam amount to about 3 percent of our gross national product. Other outlays, exclusive of social insurance trust funds, have been declining as a share of the nation's income and output in recent years. In 1969 they stand at 13.9 percent. In the last three years of the 1950's they were 16 percent. In 1965 they were 14.6 percent. It is not the rise in regular budget outlays which requires a tax increase but the cost of Vietnam.

Of course, one can debate at length whether the budget outlays in the 1969 budget for controllable civilian programs should be substantially reduced. But we must remember as we keep debating that time is still running, and every day that passes without the tax increase adds about \$33 million to the deficit.

The tax program now comes to \$16 billion over the fiscal years 1968 and 1969 and will reduce the deficit by that amount. It should be passed promptly regardless of the outcome of the long-drawn-out debate on expenditures now beginning. No amount of debate or budget-cutting that is likely to emerge is a realistic alternative to a tax increase for meeting our obligations at home and abroad in that amount.

To sum up on the budget for fiscal 1969 -- it is a responsible financial plan placed on a base of expenditures for fiscal 1968 rigidly scaled down by joint Executive and Congressional action as recently as December 1967. It represents a hold-down in controllable expenditures in 1969; the revenues from the requested tax increase will contribute to the reduction in the deficit, not to rising expenditures; and it does give assurance that the tax increase will be temporary and can and will be removed when hostilities in Vietnam come to an end.

Just as the tax increase is an indispensable element in our domestic financial plan for the year ahead, it is also the keystone of the balance of payments program announced by the President on January 1.

As the President said in his message to the nation that day -- and sometimes this is conveniently overlooked by those who say the direct measures are palliatives:

"The first line of defense of the dollar is the strength of the American economy.

"No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for more than a year. Coupled with expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus."

The direct measures announced by the President to achieve a \$3 billion reduction in our balance of payments deficit this year -- the restrictions upon outflows of funds for direct investments abroad by American business, a reduction in foreign lending by our banks and other financial institutions, actions to reduce our foreign travel expenditure deficit, actions to reduce or neutralize the foreign exchange costs of our government expenditures abroad, actions to encourage increased foreign tourism and investment in the United States -- are necessary and important. Yet they are like the four fingers of the hand. They cannot be effective in dealing with the problem without internal measures, including the tax proposal, which is the thumb that will enable us to get a firm grip on the problem.

For all our efforts, direct and otherwise, short- and long-term, to improve our balance of payments position, run the risk of failure unless we reduce a highly stimulative budget deficit and seek to avoid the kind of excessive growth and inflationary pressures that reduce our trade surplus -- unless we take the course of financial responsibility consonant with continued confidence in the dollar.

Some of the measures the President has proposed to correct the balance of payments deficit, though temporary, are not welcome and are not pleasant -- for the American people or for their government.

We do not like to ask our citizens to forego non-essential travel or to pay additional taxes when their travel expenditures outside the Western Hemisphere exceed very modest proportions.

We do not like to ask American business to curb its outflows for direct investments abroad, and the nation's banks and other financial institutions to reduce their volume of foreign lending.

We ask these measures only because they are essential at this time to deal with an emergency. As a matter of the highest national priority, we must bring our balance of payments to -- or close to -- equilibrium, and place the dollar in an impregnable position.

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You know well the reasons for adoption of the stringent new program: the loss of confidence in currencies all over the world following devaluation of the British pound in November; the speculative buying of gold that cost the United States more than \$1 billion of its gold reserve, threatening not only the dollar but the international monetary system as a whole; the serious decline in our balance of payments in the last quarter of 1967, resulting in a deficit of approximately \$3.6 billion for the year.

These developments made immediate action by the government, and sacrifices by the American people and American business, imperative.

I can assure you that the restrictive elements in the balance of payments program -- like the tax increase that is so important to it -- are of a temporary nature and will be quickly removed when they are no longer needed.

Restrictive measures are not consistent with the long-term foreign economic policy of the United States. We support -- will continue to support -- and will return to as soon as possible -- the unrestricted flow of goods, services, persons and capital under a stable international monetary system.

Moreover, the only appropriate long-range solution to our balance of payments problem lies, not in restrictive measures, but in long-range measures such as those designed to achieve a growing trade surplus, promote foreign investment and travel in the United States, and reduce or neutralize the foreign exchange impact of government expenditures abroad for security and development.

In respect to trade, a principal goal of the new program is to encourage a greater flow of exports through improved programs of export financing, export promotion and fair treatment for our trade in the field of non-tariff barriers.

There is another important aspect of the program, one that is also of particular concern to the members of this Council and to their fellow businessmen. It is the President's request that leaders of business and labor work with the appropriate members of the Administration to make more effective our voluntary program of wage-price restraint and to prevent our exports from being reduced or our imports increased by crippling work stoppages in the year ahead.

While the success of the program will depend largely on the cooperation and support of the American people, it will also be influenced, to a substantial degree, by the cooperation and support of our trading partners, and especially those in Western Europe who have enjoyed chronic balance of payments surpluses which have been the reverse side of the coin of our deficits.

I believe that we should and will have their cooperation and support, for the achievement of equilibrium in our payments is in their own interests as well as ours. Our economies are so interwoven, and the role of the dollar as a reserve and transactions currency so important, that the solution of our payments problem is a common enterprise.

Nor is it surprising or illogical for us to ask and expect assistance in the adjustment process from other countries. International financial authorities clearly recognize that the adjustment process carries responsibilities for both surplus and deficit countries.

Only recently, in a review of the U. S. balance of payments, the 20 member countries of the Organization for Economic Cooperation and Development stated:

"The balance of payments deficit is not only a U.S. problem. The deficit has as its counterpart a surplus in Continental Europe and the responsibility for adjustment must fall on both surplus and deficit countries."

The adjustments we are seeking will not be easy or pleasant -- particularly for the surplus countries in Western Europe where the impact will be sharpest. It will be far easier for them to make these adjustments and not retaliate against our actions, if they know that they are not carrying the whole burden themselves -- but that we, too, are undertaking difficult measures at home.

To the officials of these other countries, the most immediate measure needed is a tax increase to avoid an excessive growth in demand, which would strengthen cost-price pressures and aggravate the balance of payments problem. This viewpoint has been communicated to the United States again and again, and the tax increase has become in fact a symbol of the sincerity of our determination to defend the dollar.

The challenges to the United States -- the commitment we are honoring in Southeast Asia, the responsibility to conduct our financial affairs in a manner that will maintain our economic stability, the safeguarding of the strength of the dollar and of the international monetary system -- are indeed formidable.

The outcome of the test in Vietnam is inevitable -- if we as a nation have the will to remain firm.

The outcome of the test in the field of national and international finance -- hardly less important if less dramatic -- is also inevitable, if we as a nation have the will to act decisively and responsibly.

The decisions are ours. If we make them firmly and responsibly, we will assure our continued security and prosperity and that of the Free World.

Attachment

Table from the Budget Message of the President
for Fiscal Year 1969

BUDGET PROGRAM REDUCTIONS AND REFORMS

[Fiscal years. In millions]

Agency and program	Cuts below 1968 program level, as funded
	1969
BUDGET REDUCTIONS	
Agriculture:	
Farm operating loans.....	-\$50
Rural electrification loans.....	-45
Forest roads and trails.....	-29
Sewer and water loans.....	-22
Water and sewer grants.....	-3
Watershed protection program.....	-17
Flood prevention program.....	-11
Agricultural research.....	-15
Forest protection and utilization.....	-2
Great plains conservation program.....	-2
Other.....	-1
Subtotal, Agriculture.....	-197
Commerce:	
Ship construction.....	-156
Research—Maritime Administration.....	-7
Subtotal, Commerce.....	-163
Health, Education, and Welfare:	
College facility grants.....	-224
Books, equipment, guidance, and testing grants.....	-120
Health research facilities construction.....	-29
School aid to federally impacted areas.....	-17
Medical library construction grants.....	-10
Subtotal, Health, Education, and Welfare.....	-400

BUDGET PROGRAM REDUCTIONS AND REFORMS—Continued

[Fiscal years. In millions]

Agency and program	Cuts below 1968 program level, as funded
	1969
BUDGET REDUCTIONS—Continued	
Housing and Urban Development:	
Grants for basic water and sewer facilities.....	-\$25
Public facility loans.....	-10
Special assistance for market rate mortgages—Federal National Mortgage Association.....	-27
Subtotal, Housing and Urban Development.....	-62
Interior:	
Reclamation program.....	-27
Indian construction programs.....	-22
Road programs.....	-6
Sport fisheries construction.....	-5
Commercial fisheries construction.....	-1
Subtotal, Interior.....	-61
Justice: Elimination of new prison construction.....	-1
State: Educational exchange.....	-1
Atomic Energy Commission:	
Production of special nuclear materials.....	-12
Nuclear rocket program.....	-10
Space electric power.....	-8
Civilian application of nuclear explosives (Plowshare).....	-6
Subtotal, Atomic Energy Commission.....	-36
General Services Administration: Construction.....	-143
National Aeronautics and Space Administration: Manned and unmanned exploration and other programs.....	-447
National Science Foundation: Institutional science programs.....	-31
Small Business Administration:	
Business loans.....	-40
Economic opportunity loans.....	-25
Investment company loans.....	-25
Subtotal, Small Business Administration.....	-90
Total, budget reductions.....	-1,632

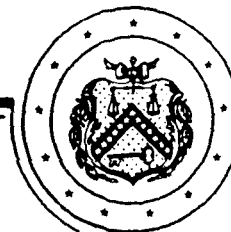
BUDGET PROGRAM REDUCTIONS AND REFORMS—Continued

[Fiscal years. In millions]

	1969	1970
PROGRAM REFORMS		
Agriculture:		
Agricultural conservation program—limit to practices with long-term benefits.....	-\$120	-\$120
Health, Education, and Welfare: School aid to federally impacted areas—tie payments more closely to Federal burden.....		-100
Housing and Urban Development: Private housing—place greater reliance on the private market (requiring change in statutory interest rate ceilings).....	-669	-669
Labor: Institute user charges to recover expenses under Longshoremen and Harbor Workers Compensation Act.....	-3	-3
Transportation:		
Airway services—increase taxes on users.....	-40	-55
Waterways—impose tax on users.....	-7	-14
Highway trucking—increase tax on diesel fuels and apply graduated use tax by weight.....	-239	-250
Subtotal, Transportation.....	-286	-319
Veterans Administration:		
Compensation—eliminate statutory payments for cases of arrested tuberculosis.....	-54	-54
Burial benefits—eliminate duplication with social security.....	-46	-46
Pensions—count railroad retirement benefits as part of income in setting amount of veterans pension.....	-7	-7
Subtotal, Veterans Administration.....	-107	-107
Small Business Administration: Disaster loans—employ more equitable and rigorous criteria.....	-50	-50
Water Resources Projects of several agencies—raise the interest rate used for evaluating projects.....	(¹)	(¹)
Total, program reforms.....	-1,235	-1,368
Grand total, budget program reductions and reforms, 1969.....	-2,867	

¹ While no immediate savings are realized, the long-term effect could be substantial.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR IMMEDIATE RELEASE

February 14, 1968

SUBSCRIPTION FIGURES FOR CURRENT REFUNDING

The results of the Treasury's current exchange offering of 5-3/4% notes dated February 15, 1968, maturing February 15, 1975, open to holders of \$24,331 million of securities maturing February 15, August 15 and November 15, 1968, are summarized in the tables below. Total subscriptions amount to \$5,144 million, including \$2,169 million from holders of the notes maturing February 15 leaving \$466 million, or 17.7%, of such notes for cash redemption.

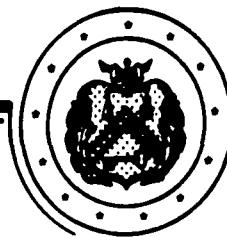
<u>Federal Reserve District</u>	<u>Amount Exchanged</u>
Boston	\$ 143,313,000
New York	2,866,513,000
Philadelphia	121,897,000
Cleveland	224,060,000
Richmond	72,094,000
Atlanta	127,922,000
Chicago	612,107,000
St. Louis	190,138,000
Minneapolis	126,829,000
Kansas City	135,997,000
Dallas	134,983,000
San Francisco	263,249,000
Treasury	125,176,000
Total	\$5,144,278,000

SUMMARY OF AMOUNT AND NUMBER OF SUBSCRIPTIONS BY INVESTOR CLASS

	<u>Amount (millions)</u>	<u>Number of Subscriptions</u>
Individuals ^{1/}	\$ 130	6,381
Commercial Banks (Own account)	2,426	8,057
All Others	<u>1,308</u>	<u>3,230</u>
Total	\$3,864	17,668
Federal Reserve Banks and Government Accounts	<u>1,280</u>	
Grand Total	\$5,144	

^{1/} Includes partnerships and personal trust accounts.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 15, 1968

FOR IMMEDIATE RELEASE

TREASURY'S MONTHLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$1,500,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing February 29, 1968, in the amount of \$3,904,591,000, as follows:

275-day bills (to maturity date) to be issued February 29, 1968, in the amount of \$500,000,000, or thereabouts, representing an additional amount of bills dated November 30, 1967, and to mature November 30, 1968, originally issued in the amount of \$1,000,262,000 the additional and original bills to be freely interchangeable.

365-day bills, for \$1,000,000,000, or thereabouts, to be dated February 29, 1968, and to mature February 28, 1969.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Wednesday, February 21, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. (Notwithstanding the fact that the one-year bills will run for 365 days, the discount rate will be computed on a bank discount basis of 360 days, as is currently the practice on all issues of Treasury bills.) It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders

from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on February 29, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing February 29, 1968. Cash and exchange tender will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

STATEMENT BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
BEFORE THE
JOINT ECONOMIC COMMITTEE
FEBRUARY 15, 1968
10:00 A.M.

Mr. Chairman and Members of the Joint Economic Committee:

It is a pleasure to be with you again this morning. These annual hearings on the President's Economic Report are always an important occasion. They provide us with a valuable opportunity to review the performance of the economy and to chart a course for the future.

In my view this is a year in which economic and financial policy should be directed toward reversing decisively the trend in 1967 to increasing deficits in our internal budget and our international balance of payments. We should move back toward balance in our budget and our international payments -- and thereby assure a balanced economy, properly poised to discharge our national and international responsibilities -- in war or peace -- at home or abroad. With the nation engaged in a costly conflict abroad, we must act at home so as to maintain the stability of the economy and the strength of the dollar.

eliminate their deficits should have the effect of markedly reducing additions to dollar and sterling reserves held by other countries. At the same time the unreliability of new gold supplies as significant additions to the world's monetary reserves has been amply demonstrated. The world's monetary gold stocks may actually have declined by as much as \$1 billion in 1967.

The restoration of a calmer atmosphere in the gold market could ultimately lead to some additions of gold to monetary reserves. But, the world now faces the prospect of a limited rate of growth in reserves. The Subcommittee on International Exchange and Payments of this Committee has taken a leading part in drawing attention to this situation.

The problem of inadequate growth of reserves can be met by creating Special Drawing Rights in the International Monetary Fund, under a plan unanimously approved by the Fund Governors last September. Under the plan, all the participating members would obtain the newly created assets in proportion to their quotas in the Fund. The amount of drawing

We meet after a year in which the domestic economy moved ahead, slowly at first, then at a faster pace -- in fact, too fast a pace to be sustained. Meanwhile, the balance of payments, which had shown sharp improvement in 1965, and held its own in 1966 in face of the mounting foreign exchange costs resulting from the conflict in Southeast Asia, took a sharp turn for the worse in 1967. Prompt measures are needed -- and are being taken -- to cut the payments deficit. But, there is an equally pressing need to cut the Federal budget deficit and bring our domestic finances into better order.

In the domestic economy, real growth resumed at a rapid rate in the last two quarters of 1967 after an anticipated inventory adjustment in the first half of the year, but it has been accompanied by far too strong a rise in costs and prices.

Moderation of the upward pressures on our costs and prices must be a continuing objective in the period ahead. We must reverse the trend toward a spiralling inflation. An economic climate conducive to a return to stable costs and prices -- in the pattern of 1961-1965 -- would protect our trade balance against a short-term floodtide of imports and a long-term deterioration in competitive position. It

would also avoid the risk of an excessive and unsustainable rate of growth that could terminate not in an inventory adjustment like early 1967 but a recession like those of other years.

Since mid-1965, the economy has absorbed nearly a \$25 billion increase in national defense spending levels without resort to wartime controls and without lasting interruption to the economy's advance. This has been a remarkable achievement. But, it has not all been smooth sailing. We have seen how a surge of demand in an economy near full employment can distort financial flows, boost interest rates, lead to excessive inventory buildup, disrupt cost-price stability and touch off a sharp rise in imports. With total public and private spending now rising strongly, that same unwelcome pattern could begin to unfold once again.

As the President stated in his January 1 Message to the Nation on the Balance of Payments: "No business before the returning Congress will be more urgent than this: To enact the anti-inflation tax which I have sought for almost a year. Coupled with our expenditure controls and appropriate monetary policy, this will help to stem the inflationary pressures which now threaten our economic prosperity and our trade surplus."

Prompt application of a degree of fiscal restraint is, indeed, essential for the health of the economy and the soundness of our financial position -- at home and abroad. We dare not allow a highly stimulative fiscal policy to conjoin with increasing demand in most areas of the private sector. Whether fiscal restraint will be applied or whether we will depend exclusively on monetary restraint with its imbalancing impact is, and has been for some time now, the overriding domestic economic policy issue. Fiscal restraint is also the key to the success of our overall balance of payments program and the maintenance of confidence in the dollar and the international monetary system.

The Domestic Economy in 1967

With the President's Economic Report before you, there is no need for me to comment on last year's domestic economic developments in any detail. I will concentrate on a few features of last year's experience that are most important for an understanding of our present situation.

As we find it now, the economy is rapidly gaining momentum, while a year ago that was far from the case. A year ago, it was clear that some adjustment of a temporarily excessive

inventory position would have to take place in 1967. It was important to insure that this adjustment occurred within the context of a generally prosperous private economy. Therefore, it was decided to complement the relaxation of monetary stringency that was already in progress with a degree of fiscal support during the first half of 1967.

Between the end of 1966 and the middle of 1967, the Federal sector of the national income accounts moved from a deficit position of about \$3 billion annual rate to a deficit approaching \$15 billion annual rate. During the same period, monetary policy also moved to a significantly easier position. For example, the level of "free reserves" which averaged more than a minus \$150 million in late 1966 rose near a plus \$300 million by mid-1967.

Contrary to the fears of those who saw recession lurking around every corner, final sales increased strongly in the first half of the year while the inventory adjustment ran its course. This was made possible, in large part, by fiscal and monetary action which had been accurately timed to the needs of the economy.

During the second half of last year, the economy moved ahead briskly, with production interrupted only temporarily by work stoppages and growth in final sales tempered only by a personal saving rate rising to unusual levels. Because the first half of 1967 was relatively weak, the full extent of the economy's resurgence tends to be concealed in statistics for the full year. For example, gross national product in current prices rose at about a 6 percent annual rate between the end of 1966 and 1967. But this is the result of an annual rate rise of a little less than 3-1/2 percent in the first half of 1967 and 8-1/2 percent in the second half. Real output grew at little more than a 1 percent annual rate in the first half of 1967 but at about 4-1/2% in each of the last two quarters of the year.

This rebound has left only a narrow margin of unutilized efficient resources readily available which can be drawn upon to boost this year's rate of growth in output. It may appear that there is still some margin of spare manufacturing capacity with operating rates in the 85% range -- about 6 points below the peak 1966 levels. But much of this unused capacity is likely to be the high cost and less efficient capacity. In any event,

the utilization rate by itself is a very unreliable indication of slack because of the shortage of skilled and semiskilled labor. The overall unemployment rate has fallen to 3-1/2% -- the lowest in 14 years. The rate for adult males is 2.3% also as low as at any time since the early 1950's.

Despite the slow first half of 1967, the resumption of strong growth in the economy during the second half set off a sharp advance in prices. The comprehensive GNP price deflator which had increased at an annual rate of about 2-1/3 percent in the first half of the year advanced at nearly a 4 percent rate in the second half. This second-half advance was the largest in more than a decade despite the fact that farm product prices were falling during much of 1967.

The economy is in grave danger of excessive overheating. Restraint or the risk of spiralling inflation are the alternatives. If we move decisively to apply restraint, we can reduce inflationary pressures and expect a year of stable growth. The economy enters the 8th year of its record breaking expansion in better balance than a year ago. Then there was an inventory overhang and the housing industry was depressed. Now, the rate of inventory accumulation is in better relation to sales and

housing has made a strong recovery. But there is still a serious imbalance domestically that must be removed. That imbalance is in the Federal sector. The Federal budget is in heavy deficit at a time when there is a need, not for steady stimulus, but for a sharp and decisive movement toward fiscal restraint.

Budgetary Policy: The Need for Restraint

In the period from late 1965 to the middle of last year, the Federal fiscal position operated in a consistently stabilizing direction. Opinions may differ as to whether or not fiscal actions were always large enough or precise in their timing. But, the general profile of the Federal fiscal position was appropriately geared to the state of the economy. In the third quarter of 1965, with the Vietnam buildup barely underway, the Federal deficit on National Income Accounts basis was running in excess of \$3 billion annual rate. By the end of the year, rising revenues had pulled the NIA budget to a position of near balance. In early 1966, the rise in payroll taxes for social security and the Tax Adjustment Act, along with the revenues generated by the faster pace of activity, swung the NIA budget into a surplus of \$3 billion annual rate by mid-1966.

By the third quarter of 1966, the NIA budget had moved back to a position of near neutrality. And, by the final quarter, with signs of a possible inventory adjustment appearing, that budget moved further in the direction of stimulus to a \$3.3 billion rate of deficit. As the economy slowed further early in 1967, the budget moved to an even more stimulative position with an NIA deficit which approached a \$15 billion annual rate by the middle of the year.

But the large Federal deficits have overstayed their time. The rate of deficit in the exuberant last half of 1967 narrowed slightly but still averaged in the \$12 billion range -- clearly inappropriate in a high employment economy with private demand strong and rising. Increasingly, the effects of that deficit are being registered in rising prices and a deteriorating trade balance.

As a consequence of the President's proposed fiscal actions, initially proposed last August 3 in his Tax Message and renewed this January, the Federal NIA deficit would be reduced from the \$12.5 billion rate of 1967 to an estimated \$5 billion for calendar 1968. In terms of fiscal years, the reduction would be from \$10 billion in 1968 to \$2.5 billion in 1969.

Without fiscal action, the NIA deficit would remain near its present levels and would be an excessively stimulative influence on our high employment economy. Continuation of deficits on such a scale would greatly increase the risk of more inflation and further short-run deterioration in our trade balance.

Also, with monetary policy now pointed in the direction of restraint, an excessively large budget deficit with a corresponding need for continuing heavy Federal borrowing would tip the odds toward a return to tight money conditions. Interest rates are already at extremely high levels in terms of our historical experience and a move to even higher rates and reduced availability of credit for housing, state and local needs, and small business would be a very unhappy prospect.

The President's fiscal program includes expenditure restraint as well as the proposed tax increase. The expenditure cuts in specific programs totalling \$4.3 billion achieved by joint Congressional and Executive action late last year were in the spirit of the recommendations made by your Committee in its last annual report.

The current budget also proposed program reductions and reforms, totalling \$2.9 billion in fiscal 1969, with the expenditure savings spread over several years. As a result, outlays in relatively controllable civilian programs will be virtually stable between fiscal 1968 and 1969. The net rise of \$0.5 billion is made up of decreases in controllable civilian outlays of \$2.5 billion and increases of \$3.0 billion. About two-thirds of the \$3 billion increase is for payments on prior contracts and commitments.

The total expenditure increase for fiscal 1969, on the unified budget basis, of \$10.4 billion is almost entirely accounted for by rising outlays for defense and for relatively fixed charges under present laws.

While there may be considerable differences of opinion about the choice of priorities, there has been a definite application of priorities. The prompt enactment of the proposed tax program is the only realistic way of assuring the timely reduction in the fiscal 1969 deficit of \$13 billion or any sum approaching that magnitude. And every day that passes without a tax increase adds \$33 million to the fiscal 1968 deficit. Already delay has cost \$4.5 billion in revenues.

Over the years, the activities of this Committee have done a great deal to elevate the level of public discussion of economic issues and have contributed to much more informed attitudes on public policy. With your help we have gone beyond an earlier, and misleading, orthodoxy which did not assign fiscal policy any role in stabilizing the economy. There is a need now to demonstrate that fiscal policy can appropriately be used to restrain as well as to stimulate. Your support of the President's fiscal recommendations -- on the basis of their economic logic -- would be an effective and influential endorsement of the practice, as well as the theory, of stabilizing fiscal policy.

Financial Policies and Debt Management

In the financial area, we look back on a year of strong demand pressures in our money and capital markets. Because of these strong demands, interest rates moved higher despite a larger flow of savings and monetary ease during most of the year. Money market rates did decline in the first half of the year but then moved up rather steadily. Longer-term interest rates dipped only temporarily in early 1967 and rose during the balance of the year.

The financial demands of the private sector were strong even while the economy was moving more slowly in early 1967. Partly in reaction to the credit squeeze of 1966, efforts were made to rebuild liquidity and provide for possible future credit needs. As the year progressed, an upturn in planned business plant and equipment expenditures and a rise in inventory investment were adding to corporate financial requirements. Long-term corporate security offerings and placements (including refundings) reached \$24 billion in 1967, about 36 percent above the sizable 1966 total. State and local issues in 1967 are estimated at \$14-1/2 billion, about 27 percent above 1966. Net additions to mortgage debt at \$22 billion were only slightly above the 1966 total, but were rising throughout the year as savings inflows to mortgage lenders continued in large volume.

With private demands strong all year, the major change was in the Federal fiscal position which swung from debt repayment to heavy net borrowing. In terms of the new budget concept of the Federal sector's net financing demand on the economy, which includes the Federal Reserve System with the private sector, there was a net repayment of \$5-1/2 billion in the

January-June 1967 period. Adding the financing activities of the Federal Home Loan Banks and the Federal Land Banks and subtracting security purchases of the Federal Reserve, there was a net repayment of \$11 billion to the private sectors. In contrast, repayments to the private sectors were only \$2 billion in January-June 1966 and \$4-1/2 billion in January-June 1965.

In the second half of last year, the Federal sector made net credit demands on the private sector of about \$18 billion. This was sharply above the net credit demands of roughly \$5 billion each in the July-December periods of 1964, 1965, and 1966. The combination of strong private and Government demands for credit exerted strong upward pressure on interest rates during the second half of 1967. Fortunately, though, there was no large scale diversion of funds away from the mortgage market last year as there had been in 1966. However, saving inflows at thrift institutions have been slowing down and there is no room for complacency. Prompt tax action is still the best insurance of a continued recovery in housing.

For the current half-year, even with prompt action on the tax bill, the Federal sector, including the Home Loan Banks and the Land Banks, may make a contraseasonal net credit demand of \$5 billion or more on the rest of the economy, including the Federal Reserve.

Borrowing requirements in fiscal 1969 will, of course, depend very much on the outcome of the President's fiscal proposals. In the absence of tax action, the fiscal 1969 deficit on the new unified budget basis would exceed \$20 billion and require roughly that amount of borrowing. To this would be added Home Loan Banks and Land Bank requirements and the amount of FNMA borrowing for secondary market operations in its proposed new private ownership status. The impact of such a volume of Federal borrowing may be judged from the following comparison. In the period fiscal 1961 through fiscal 1967, Federal borrowing averaged less than \$5 billion annually.

Large scale deficit financing in overstrained financial markets diverts credit flows and drives up interest rates. It is not a question of whether or not the Government will get its money -- of course it will. But, in the process, the

cost of all credit is driven up and many private borrowers are knocked entirely out of the market. At the present time, most interest rates are below their end of 1967 levels but they have begun rising again.

Recently the Treasury has undertaken sizable refunding, prerefunding and cash financing operations, all of which have been successful. But the new securities had to carry historically high rates of interest in order to attract investors. Thus, prompt and favorable action is needed on the President's tax proposals to raise \$16 billion in fiscal 1968 and 1969. This would shrink the budget deficits and hold Federal borrowing to manageable levels.

The Need for a Return to Cost-Price Stability

Our overall price record since the current expansion began in early 1961 remains a good one. During this period the average percentage rise in U.S. consumer prices has been less than in any other major country. Even since mid-1965 our record is better than that of most major industrial countries. But there are clear warning signs that this good record is in danger.

One of last year's more disturbing developments was the much faster advance of prices after midyear. The gain in gross national product in the second half of 1967 was impressive -- a rise of \$32 billion despite a sizable loss because of the auto strike. But nearly half of the \$32 billion rise was eaten up in the form of higher prices. By way of contrast, in the period from early 1961 to mid-1965 less than one-quarter of the gain in GNP reflected higher prices. And even from mid-1965 to mid-1967, the proportion of GNP gain attributable to rising prices was less than it has been recently.

Since mid-1965, there have been three fairly distinct periods as far as price changes are concerned. From mid-1965 through September 1966, both consumer and industrial prices rose strongly. The rise was triggered by the burst of demand which quickly carried the economy to near-capacity levels of operation. This set off a process in which wage advances and price increases began to interact. From about September 1966 through the middle of last year, there was some relief from the rapid rate of price advance as the pace of economic advance slowed temporarily, but costs continued to move up. Finally, in the second half of last year, as demand strengthened, the rate of price advance accelerated once more.

We are now at the point where so-called "demand-pull" and "cost-push" factors are threatening to interact with one another in a dangerous manner. Once an inflationary process is well established, any distinction between demand-pull and cost-push breaks down entirely. Rises in costs are reflected in higher prices and money incomes which contribute to increased spending, which drives up costs and prices, and so on. Fiscal and monetary restraint can slow this upward spiral by cutting back demand, but the measures may have to be very severe if the inflationary process is allowed to gain momentum. This we must avoid.

The real risk of recession does not lie in the prospect of too much fiscal restraint from the President's program. Rather it lies in the threat that fiscal inaction and too much demand will aggravate the inflationary pressures that are already all too apparent. The prompt application of fiscal restraint is our best insurance against further inflation and the risk of an eventual return to "boom and bust".

Balance of Payments

As you know, the immediate background of the action program to bring our payments to or close to equilibrium this year which the President announced in his New Year's Day Message included:

- the devaluation of the British pound with its disturbing impact on the international monetary system and the value of currencies;
- a sharp increase in our gold sales during the final quarter of 1967, reflecting the uncertainty and unrest on international foreign exchange markets associated with the devaluation of the British pound; plus
- indications of a very sharp deterioration also, during the fourth quarter, in our payments deficit, following some decline in the second and third quarters from the levels of 1965 and 1966.

The preliminary figures on our fourth quarter and full-year 1967 payments deficit appear in the regular quarterly Department of Commerce press release being issued today. They show:

- A deficit for the year, on the liquidity basis, of \$3,572 million -- which is near the lower end of the

\$3.5 - \$4.0 billion range anticipated in the President's Message but, nevertheless a deterioration of \$2.2 billion compared with the 1966 results. The deficit for the year, on the official settlements basis, was \$3.4 billion.

- A seasonally adjusted liquidity deficit for the fourth quarter alone of \$1,832 million. This represents
 - a rate of deficit more than three times as large as the \$580 million seasonally adjusted average for the first three quarters of the year; and the worst deficit we have experienced in any single quarter, at least since the third quarter of 1950 following the outbreak of the Korean War.
- A sharp deterioration in our merchandise trade account during the final quarter,
 - resulting in a trade surplus for the full-year 1967 virtually identical with that of 1966 in place of the moderate improvement which we had expected on the basis of the experience of the first three quarters.

The details of this increase in our fourth quarter payments deficit will not be available for several weeks. But it is clear that the most worrisome element in the picture was the drop in our trade surplus. Imports rose over \$500 million while exports dropped nearly \$200 million from the January-September averages. Our trade picture thus accounted for more than half of the increase in our liquidity deficit above the levels of the first three quarters.

- A second major development in the fourth quarter was the liquidation by the U.K. Government of the \$570 million remaining balance from its long-term investments in U.S. securities. This action, of course, was taken in connection with the devaluation crisis.
- Unfortunately, as noted earlier, the detail necessary to evaluate other factors simply is not yet available. Such other categories of our international payments for which preliminary figures are now available show generally rather small -- and largely offsetting -- changes as compared with the first three quarters of the year.

Last month I released a Treasury Department report entitled "Maintaining the Strength of the United States Dollar in a Strong Free World Economy." This document details the background and reasons for the Action Program announced by the President. It describes what we have done to date, and what we propose to do, both over the short- and long-term. Copies of this report are available to each member of the Committee.

The President's Action Program underlines the urgent need for a tight lid on expenditures, appropriate monetary policy and a more effective voluntary program of wage-price restraint. As the President's Economic Report points out: "The avoidance of excessive demand in our economy is crucial to the strength of the dollar as well as to our domestic prosperity.

"If we place too much pressure on our resources, U.S. buyers will turn abroad for supplies and our imports will soar. And if our prices rise, we will weaken our export competitiveness and attract even more imports -- not just immediately, but for years to come."

I shall not review in detail the various selective measures through which we seek an improvement of \$3 billion in our balance of payments during the year 1968. They are set forth

clearly in the Presidential statement which appears at the beginning of the Treasury report on the Action Program.

The United States recognizes its responsibility for adjusting its own balance of payments, and it does not intend to shirk this responsibility. At the same time, it must be recognized that the United States balance of payments is part of a world pattern of payments. The counterparts of the deficits of some countries are the surpluses of other countries. Because of the concentration of payments surpluses in Continental Western Europe, it is primarily to this group of countries that we must look for cooperative actions facilitating the progress toward international equilibrium that the U.S. program would make possible. The relationship of the U.S. deficit and the persistent surplus of these countries is examined in Chapter IX of the Treasury report.

We have undertaken both bilateral and multilateral consultations with other countries regarding our action program. Broadly speaking, the response of the Continental European countries has been gratifying. They recognize and accept the fact that their surpluses must fall along with the correction

of the U.S. deficit. There is some concern regarding the more favorable treatment of non-Continental countries in several phases of our program but there is appreciation that a non-differentiated program would have created painful adjustment problems for countries least able to make these adjustments. There are encouraging indications of a general readiness on the part of individual countries to adjust their fiscal and monetary policies to the new situation created by the U.S. program.

The European nations strongly emphasize that the full objectives of the program will not be achieved without the primary and essential component of restraint on the U.S. economy through fiscal and monetary policy, supplemented by intelligent and responsible actions by management and labor to limit the rise in unit costs to a noninflationary level. In particular, action on the tax increase has become a critical and symbolic test, in European eyes, of our ability to control domestic inflationary pressures. It is the acid test of fiscal responsibility and confidence in the future of the dollar in financial circles here and abroad.

International Finance

One of the difficulties faced in discussion of our balance of payments problem is that it is hard to put in terms that are analogous to the familiar financial problems of doing business in the United States. The United States can be likened to a large trader and investor, as set forth on pages 12 and 13 of the President's Economic Report. It also is the most important international banking center. About half of our liquid liabilities of \$33 billion are holdings of foreign monetary authorities, the United States acting as a bank. The official dollar holdings of foreign countries are part, and in many cases a large part, of the ultimate national reserves that foreign nations hold to meet unforeseen contingencies. Thus we have the responsibility that falls upon a bank to maintain at all times the unquestioned confidence of the depositors in its liquidity as well as its solvency.

We need to have reserves that will assure that our depositors can spend their dollars in all the major countries of the world. Some of these countries, notably in Continental Europe, will expect the United States as a bank to pay them, in effect, not in dollars but in gold or in claims on the International

Monetary Fund as they acquire dollars beyond their customary official holdings of dollars. They have the alternative of reinvesting some or all of these dollar receipts in private markets -- and this alternative can be particularly helpful when borrowing demands in the European capital markets are heavy -- but there is likely at times to be some cashing of dollars into gold.

Although the world has come a long way toward accepting dollars as a regular and normal proportion of world reserves, it is still true that gold comprises about \$40 billion of the total world reserves of something over \$70 billion. The gold ratio is substantially higher for some countries, particularly in Europe. And our depositors, in some cases, feel the need of assurance that their reserves in the form of dollars are adequately protected by large and available reserves of gold (or the equivalent in claims on the IMF).

The importance of the factor of confidence in a major currency was demonstrated by the recent experience of sterling. The international monetary system was put to a severe test by the devaluation of sterling and its aftermath. This challenge was met, and the results demonstrated the resilience and the

resistance of the system to a difficult series of political and financial events. The private markets for gold had shown nervousness since the Mid-East crisis in the spring, and the devaluation of sterling triggered a heavy run on gold.

A statement by the gold pool contributors made in Frankfurt the weekend after devaluation served to calm the market substantially. But later, rumors again flooded the market -- the size of the pool's losses, the possible withdrawal of support of the pool and the possibility of limitations of some sort being placed on the market.

A further statement by me as Secretary of the Treasury and by the Chairman of the Federal Reserve Board, made with the support of the other gold pool members, again restored comparative calm. But the factor that brought more enduring strength to the gold market was the announcement on January 1 by the President of a forceful U.S. balance of payments program. With only a few exceptional days the market has been much better balanced in 1968.

The events of 1967 accentuated the need for prompt implementation of the International Monetary Fund plan for multilateral creation of supplementary reserve asset. The strenuous efforts being made by the United Kingdom and the United States to

eliminate their deficits should have the effect of markedly reducing additions to dollar and sterling reserves held by other countries. At the same time the unreliability of new gold supplies as significant additions to the world's monetary gold stocks may actually have declined by as much as \$1 billion in 1967.

The restoration of a calmer atmosphere in the gold market could ultimately lead to some additions of gold to monetary reserves. But, the world now faces the prospect of a limited rate of growth in reserves. The Subcommittee on International Exchange and Payments of this Committee has taken a leading part in drawing attention to this situation.

The problem of inadequate growth of reserves can be met by creating Special Drawing Rights in the International Monetary Fund, under a plan unanimously approved by the Fund Governors last September. Under the plan, all the participating members would obtain the newly created assets in proportion to their quotas in the Fund. The amount of drawing

rights to be created would be determined from time to time, normally for intervals of five years in advance, in such a way as to assure an adequate but not excessive rate of growth in global reserves. There is ample safeguard against excessive use of this authority in the provision that the Managing Director will make a proposal for creation of the new drawing rights only after extensive consultation, and proposals will require the approval of 85 percent of the weighted votes of participating countries.

In order to make sure that the Special Drawing Rights will serve effectively as supplementary reserve assets, countries undertake obligations to accept them up to an amount that will always equal three times the amount of Special Drawing Rights that may be created for them. It is these obligations to accept the new instrument that give it its assured backing; countries may also accept larger amounts voluntarily and will probably do so as the instrument becomes more familiar in the years to come.

I will not go into further detail here on the Special Drawing Rights, but will be glad to submit for the record the outline plan that was approved in September at Rio de Janeiro, and a statement I made before the Subcommittee on International Exchange and Payments of this Committee on September 14.

I am pleased to report that the process of drafting amendments to bring the plan into effect is going forward in the Fund. After their completion by the Executive Board, scheduled for March 31, 1968, by the Resolution at Rio, the amendments will be submitted to the Governors of the Fund to approve, by a simple weighted majority, submission to governments for acceptance. If all goes as scheduled, it will be possible to present the amendments to the Congress for its consideration in the spring of this year.

The plan will become effective in the constitutional sense when the amendments have been accepted by three-fifths of the members of the Fund having 80 percent of the weighted votes. At this stage, which might take place in late 1968 or early 1969, the Managing Director and the members can make a determination that initial activation should take place. This will require the approval of 85 percent of the weighted vote of the participating members.

I should also mention that the Executive Directors will prepare a second report dealing with a number of proposals for amendments directly related to the Special Drawing Rights plan,

put forward for study primarily by the members of the European Economic Community. There are several controversial proposals, and all are under active discussion in the Executive Board of the Fund. A report must be made to the Governors by March 31, 1968, and we do not yet know to what extent some questions may require further consideration after that date. We would strongly hope that the controversial issues in these proposals, if not settled promptly, would not delay ratification of the Special Drawing Rights plan.

Conclusion

The need for fiscal restraint is the dominant feature of our economic situation, combined with less inflationary wage-price decisions and direct balance of payments measures, some short term and some long term. In the present setting, there is no conflict between the policy prescription for both the domestic economy and the balance of payments. Each would be improved by a prompt transition to a less inflationary environment. Both our budget and our balance of payments deficits are far too large and both must be reduced. The action program to shrink the balance of payments deficit by \$3 billion is already in motion. Corresponding action is urgently required on the President's tax program, which would cut our budget deficits in fiscal 1968 and 1969 by \$16 billion over the next year and a half.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 16, 1968

FOR IMMEDIATE RELEASE

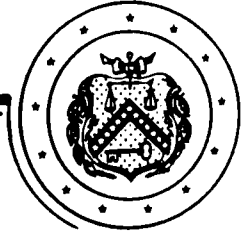
TREASURY MARKET TRANSACTIONS IN JANUARY

During January 1968, market transactions in direct and guaranteed securities of the Government investment accounts resulted in net purchases by the Treasury Department of \$50,378,000.00

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TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR IMMEDIATE RELEASE

February 15, 1968

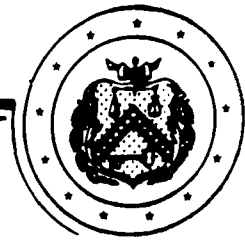
RESULTS OF TREASURY'S CASH OFFERING OF 5-5/8% NOTES

The Treasury today announced a 39 percent allotment on subscriptions in excess of \$200,000 for the current cash offering of \$4 billion, or thereabouts, of 5-5/8 percent Treasury Notes of Series B-1969 due May 15, 1969. As provided in the offering circular, subscriptions for \$200,000 or less will be allotted in full. Subscriptions for more than \$200,000 will be allotted not less than \$200,000. The total amount of subscriptions accepted is about \$4,250 million.

Reports received thus far from the Federal Reserve Banks show that subscriptions total \$9,820 million, of which \$8,550 million were received from commercial banks for their own account and \$1,270 million from all others.

Details by Federal Reserve Districts as to subscriptions and allotments will be announced next week.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 16, 1968

FOR IMMEDIATE RELEASE

TREASURY'S EXCEPTIONAL SERVICE AWARD PRESENTED POSTHUMOUSLY TO SLAIN NARCOTICS AGENT

Treasury Secretary Henry H. Fowler today conferred the Department's Exceptional Service Award posthumously on Narcotic Agent Mansel R. Burrell of Moline, Illinois, who was shot to death on December 19, 1967, in Gary, Indiana, while working on an undercover assignment. The presentation was made to Mr. Burrell's father, Willard Burrell, in the Secretary's office. Agent Burrell's brother, Edsel, also was present.

Secretary Fowler said that "events leading to this young agent's death demonstrate his outstanding courage and show that, on his own initiative, he repeatedly risked his personal safety in the face of danger."

Agent Burrell was 23 years old, a 1966 graduate of Northern Illinois University, and had been employed as an Agent of the Bureau of Narcotics since September 12, 1966.

According to the report given Secretary Fowler by Commissioner of Narcotics Henry L. Giordano, in late October, 1967 the Gary, Indiana, Police Department had requested that the Bureau assist in preparing a case against a narcotics violator in Gary. Agent Burrell was assigned to make an undercover approach and purchase heroin which could be used as evidence.

Commissioner Giordano said Agent Burrell was successful in making a first purchase of evidence on November 28, 1967. Success in prosecution, however, is often substantially greater if there has been more than one "buy." On December 19 Burrell made arrangements to rendezvous for the second purchase. Burrell had been advised that the seller suspected, because of Burrell's manner of speech, that he might be an agent. In addition the place set for a rendezvous was an alley in a crime-ridden section of Gary,

Indiana, and the agent who was to accompany Burrell was out of town on another assignment. Despite the dangers in the situation, Burrell continued with his work.

While all of the facts surrounding the ensuing tragedy are not yet clear, Mr. Giordano said, it appears that Agent Burrell was taken at gun-point from the alley of rendezvous to a wooded area where he was killed. His body was subsequently found in nearby Illinois.

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TREASURY DEPARTMENT

NOTE TO PRESS:

February 16, 1968

MONTHLY STATEMENT OF
RECEIPTS AND EXPENDITURES OF THE UNITED
STATES GOVERNMENT

Major modifications in the format and classification of data for the Monthly Statement of Receipts and Expenditures of the United States Government have been underway, coordinate with the fundamental changes adopted for the President's Budget for 1969. As is widely known, the changes stem from the recommendations of the President's Commission on Budget Concepts which have been adopted.

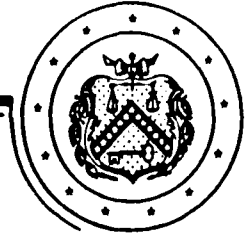
The scope of the changes, including certain new requirements which the Treasury has had to establish for all reports furnished by Government agencies, have inevitably resulted in a longer operating cycle and a consequent reduction in the timeliness of publication of the Government-wide statement.

It is expected that the statement for January 1968, the first statement consistent with the new budget concepts, will be published on or about the last day of February. This publication schedule is expected to prevail throughout the rest of fiscal year 1968. Every effort will be directed toward restoring, as soon as possible, the very timely publication date around the 20th of the month which has prevailed for many years.

Also, for some months to come, the published monthly statement will not be complete with respect to prior year comparative data on the new budget bases. Such data will be developed as soon as possible for publication.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

RELEASE 6:30 P.M.,
Monday, February 19, 1968

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated November 24, 1967, and the other series to be dated February 23, 1968, which were offered on February 14, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,500,000,000, or thereabouts, of 90-day bills and for \$1,000,000,000, or thereabouts, of 181-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	90-day Treasury bills maturing May 23, 1968		:	181-day Treasury bills maturing August 22, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.774	4.904%	:	97.433	5.106%
Low	98.758	4.968%	:	97.411	5.149%
Average	98.765	4.940% <u>1/</u>	:	97.419	5.133% <u>1/</u>

91% of the amount of 90-day bills bid for at the low price was accepted
97% of the amount of 181-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 19,250,000	\$ 9,250,000:	:	\$ 8,721,000	\$ 2,721,000
New York	1,723,742,000	1,110,682,000:	:	1,375,964,000	764,814,000
Philadelphia	24,940,000	12,940,000:	:	14,043,000	5,843,000
Cleveland	29,687,000	29,687,000:	:	39,889,000	23,229,000
Richmond	14,374,000	9,374,000:	:	9,202,000	4,202,000
Atlanta	46,932,000	33,833,000:	:	34,441,000	14,591,000
Chicago	195,209,000	134,370,000:	:	152,949,000	59,599,000
St. Louis	48,005,000	31,588,000:	:	28,607,000	9,007,000
Minneapolis	22,612,000	15,414,000:	:	17,404,000	6,889,000
Kansas City	21,221,000	21,021,000:	:	16,666,000	13,466,000
Dallas	22,013,000	15,623,000:	:	22,497,000	11,397,000
San Francisco	96,111,000	76,661,000:	:	125,801,000	84,251,000

TOTALS \$2,264,096,000 \$1,500,443,000 a/ \$1,846,184,000 \$1,000,009,000 b/

Includes \$223,874,000 noncompetitive tenders accepted at the average price of 98.765
Includes \$122,517,000 noncompetitive tenders accepted at the average price of 97.419
These rates are on a bank discount basis. The equivalent coupon issue yields are 5.09% for the 90-day bills, and 5.36% for the 181-day bills.

TREASURY DEPARTMENT
Washington

FOR RELEASE UPON DELIVERY

REMARKS BY THE HONORABLE HENRY H. FOWLER
SECRETARY OF THE TREASURY
BEFORE THE
INTERNATIONAL RADIO AND TELEVISION SOCIETY, INCORPORATED,
WALDORF-ASTORIA HOTEL, NEW YORK, NEW YORK
WEDNESDAY, FEBRUARY 21, 1968, 1:30 P.M., EST

A TIME OF TESTING FOR INTERNATIONAL FINANCIAL COOPERATION

I am honored to meet with this group of leaders in the field of radio and television.

Your industry is a major medium of entertainment for the people of the United States and other countries. But more importantly, it is also one of their principal sources of information -- a means by which they obtain the knowledge and understanding needed for informed opinions and sound decisions on the great issues and challenges of our time. With the communications satellite and the advances in radio technology, your industry has become an important medium for promoting international communication and understanding of common problems.

Today I want to speak to you about one of these great challenges which is a common problem for the United States and the 106 member nations of the International Monetary Fund. This common problem is the preservation and improvement of the international monetary system -- the promotion of international financial cooperation -- a system and a practice that makes possible the international movement and exchange of goods, services, people and capital.

I ask your assistance in providing increased understanding of the importance of this system and practice to the continued security and prosperity of the United States and the continued economic development of the entire Free World.

The lack of adequate public understanding can be the Achilles heel in the international monetary system. It can lead to weakness in and failure of the system. It can limit the practice of international financial cooperation that is so vital to us all. The last signal failure resulted in the worldwide depression of the early Thirties and the narrow nationalism of that decade which contributed to the rise of Hitler and World War II.

The common problem for discussion is the bringing of the United States balance of payments into equilibrium which, in the words of the President, is "a national and international responsibility of the highest priority."

What we do in this American program is related to our international responsibilities because without a strong dollar, a healthy, stable international monetary system is not possible.

Moreover, this American program must, as a counterpart, involve cooperative actions by and with other nations. Without that cooperation it is not possible to end the damaging deficits in U.S. payments in a manner conducive in the long term to the increased flow of international trade and capital and viable and sturdy arrangements for international security and development. Achievement of balance compatible with these objectives will call for adjustments by America's trading partners as well as by the United States.

It was because of this lack of public understanding that the Treasury Department followed up the President's New Year's Day Message on the balance of payments by issuing a report entitled "Maintaining the Strength of the United States Dollar in a Strong Free World Economy." The purpose of the report was to give some measure of vital understanding to the program and its importance at this point of time to the people of the United States and to peoples everywhere. Given understanding and communication, support of and participation in the achievement of this program will be sure to follow. You can help provide that understanding.

The challenge we face -- the United States and its trading and financial partners -- is to act promptly and decisively to terminate a long series of deficits in the United States balance of payments. This deficit worsened appreciably last year. At the same time the devaluation

of the British pound shook confidence in currencies generally and disturbed the stability of the world's financial gold and foreign exchange markets. Unless we act to eliminate this deficit the preservation of the international monetary system, based in good part on the strength of the dollar, will be in serious danger.

To bring our foreign expenditures and receipts into balance will not be easy. It will require difficult and even disagreeable measures by our nation, temporary sacrifices on the part of some groupings of the American people, and unwelcome adjustments by other countries. But reach the goal we must, if we are to insure a continuation of our own economic expansion and of the unprecedented prosperity the Free World has enjoyed for the past 20 years.

I know that the balance of payments, and the problems we are encountering with it, may seem a complex and mysterious subject to many Americans. Yet it is a national and international financial problem that is much like the financial problems of a family.

When a family spends more than it earns, it has several alternatives -- it must make up the difference by drawing on its bank account or other reserves, it must cut down on its spending, or it must increase its earnings.

That is just about the situation of the United States today in regard to its foreign expenditures and earnings.

For 17 of the last 18 years, our expenditures abroad have exceeded our earnings. We have been able in the past to draw on our reserves to meet these chronic deficits, but the day has arrived when we can no longer afford to do so. Our reserves will not permit it. Instead, we must reduce our foreign spending and increase our earnings abroad.

I recognize also that the urgency of the situation may not be readily apparent to most Americans. The nation's economy is strong, and we have had a stable economic expansion and record prosperity for more than seven years. Our international transactions are small compared with our total production, consumption and investment. Why should the United States or the world be concerned about a payments deficit that at worst has been only a fraction of one percent of ~~of our~~ gross national product?

This is particularly a difficult question when one considers the kind of balance of payments deficit we have.

Typically, a nation incurs a deficit because its imports exceed its exports. However, this is not true of the United States. We have consistently had a trade surplus over the last 17 years, including a surplus of \$3.7 billion in 1966.

Unfortunately, our consistent trade surplus has been more than offset by steadily growing outflows of capital -- government expenditures overseas for security and development, amounts spent by Americans traveling abroad, foreign investments by U.S. businesses, and loans by our banks and other financial institutions.

In 1966, for example, despite the trade surplus of \$3.7 billion, we ended the year with a deficit of \$1.3 billion.

As Rinaldo Ossola, economic adviser and director of the Bank of Italy, pointed out recently in an article discussing the United States balance of payments problem:

"In the 16 years from 1951 to 1966, the United States exported goods and services worth 47 billion dollars more than those imported. Obviously, the country did not live beyond its means. However, the overall balance of payments showed an aggregate deficit amounting to \$35 billion. This was due to the fact that the U.S. exported capital totaling \$82 billion Accordingly, on a broadly approximated basis it can be said that the net capital exports from the U. S. completely offset the trade surplus, and on top of that made it possible to meet the demand for liquidity by foreign businessmen and central banks."

The problem presented by the U.S. balance of payments deficit goes beyond the importance to our economic well-being and national security of the imports of raw materials and finished goods needed for our production and high standard of living; of our overseas expenditures for mutual security and foreign aid; of our profitable foreign investments and loans, of our travel to other lands. It goes beyond our being able to pay for these things -- which we must -- by exports, earnings on our foreign investment, amounts received from foreign tourism in the United States.

The problem of the U.S. deficit transcends these especial considerations of peculiar national concern. It goes to the role of the dollar as the cornerstone of the international monetary system in its fixed relationship to gold, as a reserve currency, and as the "transactions" currency in which much of the world's business is conducted.

When the outflow of dollars exceeds our total foreign receipts, some of the excess dollars received by foreigners are sold to their monetary authorities in return for local currency.

To some extent and for some time, foreign central banks have been willing to add these dollars to their reserves. But now that the accumulation of dollars has been large in amount and has continued for a long time, some central banks are no longer willing to add dollars to their reserves. Instead, they use them to buy gold from the United States.

Primarily because of these purchases, United States gold reserves have declined over the last 10 years from \$23 billion to just under \$12 billion.

The result has been:

- A decline in the ratio of our reserve assets to our liquid liabilities.
- A weakening of confidence in the dollar.
- A consequent threat to the continued working of the international monetary system, of which the dollar is the bulwark.

For a time after World War II, large deficits in our international financial accounts could be tolerated by the United States, and were desirable to other nations. Our deficits provided the reserves that enabled Western Europe and Japan to rebuild their war-shattered economies, and re-distributed the world's gold reserves more equitably.

By the late 1950's, however, the post-war economic recovery was complete, and the continuing drain on United States reserves began to trouble both our own country and others.

Under President Eisenhower, and subsequently under President Kennedy and President Johnson, the United States began steps to end the deficits and bring its payments into equilibrium.

By 1965 we had made good progress, and the deficit had been reduced by two-thirds -- from \$3.9 billion in 1960 to \$1.3 billion in 1965.

In 1966, however, progress was interrupted by changes associated with the expanding military effort in Southeast Asia. The accelerated expansion of the U.S. economy brought a tremendous upsurge in imports, while the increased costs of supporting our forces in Vietnam added substantially to our foreign payments. As a result, the deficit remained at the same level in 1966 as in 1965 -- \$1.3 billion.

Last year, the deficit widened for several reasons:

- The foreign exchange costs of Vietnam rose further.
- U. S. private investments and loans overseas increased.
- Americans spent more on travel abroad.
- Because of a slow-down in the European economies, United States exports to Europe did not grow as rapidly as expected.

You know well the events that, added to those factors, brought the payments problem to an acute stage: the loss of confidence in currencies all over the world following devaluation of the British pound in November; the speculative buying of gold that cost the United States more than \$1 billion of its gold reserve, jeopardizing the dollar and the international monetary system as a whole; the serious decline in our payments account in the last quarter which resulted in a deficit of approximately \$3.6 billion for the year.

These developments made immediate and emergency action on the problem imperative. And President Johnson acted promptly

and courageously in presenting an Action Program to the nation on January 1.

The measures he proposed were developed carefully and responsibly -- mindful of the interests of all of the American people; mindful of the interests of the people of other nations; mindful of the special role of the United States in the world economy as the principal trading and banking nation; mindful of our objectives of world peace, development and security.

The President has recommended a solution to the payments problem that involves both domestic measures and close cooperation with the United States friends and trading partners.

We have no desire to depend, for the ultimate long-range answer to the problem, on narrow nationalistic measures that, while benefiting our own economy, might seriously damage the economies of other nations. The history of developments leading up to World War II -- the failure of the London Economic Conference and of other efforts to achieve international cooperation -- tells the tragic results when nations act only in self-interest.

What we seek, instead, is a cooperative approach to the problem. The progress that has been achieved since the Bretton Woods Conference -- in the strengthening of the international monetary system and the expansion of world trade and development -- has shown clearly how much can be accomplished when nations work together to solve problems that affect all.

Given such cooperation, the United States seeks to achieve adjustment in payments over the longer-term without seriously disturbing economic relations among nations, without placing undue burdens on other countries which also have payments deficits, and without slowing the growth of the developing countries of Asia, Africa and Latin America.

The Action Program is also well-balanced from the domestic standpoint. Its measures apply to each of the most significant elements in our balance of payments. The restraints and sacrifices it asks are distributed broadly across all segments of the U.S. economy, so that none is asked to bear an inequitable share. It includes short-term measures designed to deal immediately with the emergency situation, and longer-term measures aimed at a more desirable and permanent solution of the payments problem.

Our trade surplus is already the mainstay of the balance of payments program. But we must increase it, so that in time it will pay an even greater share of our overseas expenditures. The new program will encourage a greater flow of exports through improvements in export financing and intensification of export promotion. We will also strive for the elimination of non-tariff barriers that place our exports at a competitive disadvantage.

Direct investments abroad are profitable to American business, and a favorable element in the balance of payments. In 1966, income from these investments exceeded the outflow of new direct investment by \$2 billion. Yet as a temporary measure, the United States must moderate the outflow of new direct investments abroad and encourage the repatriation of accumulated earnings of U. S.-owned foreign businesses, thus maximizing the return on present investments.

In the same manner, the new program restrains foreign lending by U. S. banks and other financial institutions, and purchases of foreign securities, so that this element of our balance of payments will be further improved.

We also are seeking to reduce or neutralize the foreign exchange costs of necessary expenditures overseas for mutual security and development assistance.

Over the past four or five years the Defense Department has made substantial savings in the balance of payments impact of U. S. military expenditures abroad. We have reduced the number of troops deployed in Western Europe and taken other measures to cut the foreign exchange costs of defense expenditures.

Since 1959, an increasing share of our assistance to developing countries has been tied to the purchase of American goods and services. This fiscal year, more than 90 percent of our aid expenditures will be made for the purchase of American goods and services.

Under the new program, we will try to accomplish an even greater saving in the foreign exchange costs of defense and development expenditures -- specifically, a \$500 million saving this year.

The Action Program also embodies the concept that the best long-term solution to the travel deficit

in the balance of payments is to increase foreign travel in the United States. A task force of eminent citizens has recommended early this week plans to increase the number of foreign visitors. In the interim, and until we can narrow the deficit, we have asked American citizens to limit temporarily their non-essential travel this year and next to the Western Hemisphere, and we have proposed taxes, temporary in nature, designed to encourage the traveler outside the Hemisphere to hold down his expenditures to modest proportions.

We will also carry on our efforts to encourage foreign investment in the United States inaugurated several years ago and underscored by the passage of the Foreign Ministers Tax Act in 1966. There will always be substantial exports of investment capital from this country. We would like to see, in return, a growing inflow of portfolio investments into the United States from abroad.

Let me assure you that the restrictions contained in the new program are just as they have been termed -- temporary -- and will be quickly removed when they are no longer needed.

Restrictive measures are not consistent with the long-term foreign economic policy of the United States. We support -- will continue to support -- and will return to as soon as possible -- the unrestricted flow of goods, services, persons and capital under a stable international monetary system.

Moreover, the only appropriate and lasting solution to the balance of payments problem will be found, not in restrictive measures, but in long-range steps to build a larger trade surplus, promote foreign investment and travel in the United States, and reduce or neutralize the foreign exchange costs of necessary government expenditures abroad.

There is another urgent and essential factor in the solution of the payments problem -- the proper handling of our own domestic economy to keep it on the path of steady, stable, sustainable non-inflationary growth. This includes the anti-inflation tax increase the President has recommended to the Congress, control of federal expenditures, appropriate monetary policy and responsible private decisions on wages and prices that preserve our international competitive position.

The direct measures designed to reduce the balance of payments deficit by \$3 billion this year are necessary and important. Yet they are like the four fingers of the hand. They cannot be effective in dealing with the problem without the tax increase and expenditure control, which is the thumb that will enable us to get a firm grip on the problem of our internal budget deficit.

For all our efforts, direct and indirect, short- and long-term, to improve the United States balance of payments position, run the risk of failure unless we avoid the kind of excessive growth and inflationary pressures that bring a floodtide of imports, reduce the ability of our products to compete in world markets, and diminish our favorable trade surplus.

Moreover, all these efforts to maintain confidence in the dollar as a lasting component in the reserves of central banks of other countries, will not achieve their objectives if other nations lose confidence in the stability of the economy from which the dollar draws its strength and acceptance as a reserve and transactions currency throughout the world.

While the success of the Action Program will depend largely on the support of the American people, it will also rest, to a substantial degree, on the cooperation we are asking of other nations.

The countries of continental Europe, and particularly the countries of the European Economic Community, have had chronic balance of payments surpluses which have been the main counterpart in the world to the U.S. deficits. In addition, these countries have large amounts of reserves and high per capita incomes. It follows, therefore, that most of the burden of adjustment resulting from the U.S. program must be borne by these countries.

The United States is asking them -- in their own interests and those of the rest of the world -- to accept reductions in their payments surpluses.

We are urging them to adopt policies which will lead to higher domestic levels of activity -- an expansion of their economies -- while maintaining stable prices.

We are asking that they become more receptive to imports from developed and less-developed countries, removing non-tariff barriers that now stand in the way of freer trade.

We want them to accept an appropriate share of the costs of mutual defense and of economic assistance to the developing countries.

We are asking them to encourage greater outflows of capital from their countries, and to stimulate the development of their internal capital markets.

I believe that we should and will have the cooperation and support of European and other countries. The lessons of history are as clear to them as to the United States. They know that economic cooperation benefits the people of every land, and they are aware that a solution to the United States balance of payments problem is so important to the world economy that it is a common enterprise.

Only recently, in a review of the U. S. balance of payments problem, the 20 member countries of the Organization for Economic Cooperation and Development stated:

"The balance of payments deficit is not only a U. S. problem. The deficit has as its counterpart a surplus in Continental Europe and the responsibility for adjustment must fall on both surplus and deficit countries."

Just last month, a subcommittee of the OECD which included representatives of the major Free World nations, agreed that the United States program is desirable, and that there should be close international cooperation to make it succeed. They concluded that their countries should assist -- even if it means a decline in their own payments surpluses and reserves -- by stimulating economic growth to provide expanded markets for imports, and by encouraging greater outflows of capital.

The adjustments our Action Program will require of other countries will not be easy or pleasant -- particularly for the Western European countries where the impact will be sharpest. It will be far easier for them to make these adjustments and not retaliate against our actions if they know that they are not carrying the whole burden themselves -- but that we, too, are undertaking difficult measures at home.

To the officials of these other countries, the most immediate measure needed is a tax increase to avoid an excessive growth in demand which would strengthen cost-price pressures, increase imports, and aggravate our balance of payments problem. This viewpoint has been communicated to U. S. officials again and again, and the tax increase has indeed become a symbol of our willingness and determination to defend the dollar.

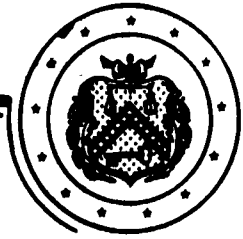
I am confident that the American people, if they have an understanding of the situation, will have that willingness and determination, and that they will meet the present challenge to our economy and to the world economy as they have met so many challenges in the past -- resolutely, promptly and successfully.

I am also heartened and encouraged by the response the United States program has met from the officials of other countries. The real test still lies ahead -- in their actions rather than their words -- but I have every reason to hope that they will continue to work closely with the United States to nourish economic growth, expansion of trade, and a stronger international monetary system.

In the final analysis, success or failure in restoring equilibrium in our balance of payments will depend on public awareness -- in the United States and abroad -- of the importance and urgency of our efforts.

It is here that the radio and television industry can render invaluable service. Informed public opinion is indispensable to progress, in economic as in other matters. Your industry can provide increased knowledge and understanding of the problem, and in so doing help to shape the solution, and with it, the future of the United States and the world economy.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR IMMEDIATE RELEASE

February 20, 1968

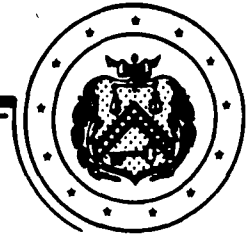
TREASURY ANNOUNCES INCREASE IN WEEKLY BILL AUCTIONS

The Treasury announced today that weekly offerings of 3-month bills will be enlarged by \$100 million commencing with the bills to be auctioned on February 26, and probably running through a full 13-week cycle. This means that weekly bill offerings will include \$1.6 billion of 3-month bills and \$1.0 billion of 6-month bills.

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F-1172

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR IMMEDIATE RELEASE

February 20, 1968

SUBSCRIPTION AND ALLOTMENT FIGURES FOR TREASURY'S CURRENT CASH OFFERING

The Treasury Department today announced the subscription and allotment figures with respect to the current offering of 5-5/8% Treasury Notes of Series B-1969, due May 15, 1969.

Subscriptions and allotments were divided among the several Federal Reserve Districts and the Treasury as follows:

<u>Federal Reserve District</u>	<u>Total Subscriptions Received</u>	<u>Total Allotments</u>
Boston	\$ 495,142,000	\$ 211,826,000
New York	3,031,963,000	1,218,954,000
Philadelphia	392,285,000	168,352,000
Cleveland	724,447,000	308,760,000
Richmond	441,804,000	199,246,000
Atlanta	524,191,000	252,658,000
Chicago	1,479,571,000	658,410,000
St. Louis	407,351,000	202,436,000
Minneapolis	246,807,000	125,341,000
Kansas City	291,708,000	173,643,000
Dallas	310,735,000	142,931,000
San Francisco	1,525,257,000	613,564,000
Treasury	997,000	797,000
Totals	<u>\$9,872,258,000</u>	<u>\$4,276,918,000</u>

STATEMENT OF THE HONORABLE FRED B. SMITH
GENERAL COUNSEL OF THE TREASURY
BEFORE THE SUB-COMMITTEE ON EUROPE OF THE
HOUSE COMMITTEE ON FOREIGN AFFAIRS
FEBRUARY 21, 1968

Madam Chairman and Members of the Committee:

I am here to describe the role of the Treasury Department with respect to East-West Trade.

State Department witnesses already have discussed the overall foreign policy aspects of East-West Trade. Treasury Department operations related to East-West Trade are carefully attuned to these foreign policy considerations.

The Treasury has been given Presidential authority and delegated the function of administering controls over foreign assets and financial transactions where necessary to protect United States national security interests. Determinations with respect to types and amounts of goods which are strategic and the United States position in international consultations on the administration of international controls of such commodities are developed through interagency consultations in the Economic Defense Advisory Committee (EDAC). Where questions of overall U.S. foreign policy arise in connection with the

administering of these regulations, Treasury is largely governed by the views of the Department of State. In instances where any contemplated measures or actions would significantly affect the international financial position of the United States, the Treasury Department would play a major role in the determination of the policy which would apply to such matters.

As a prelude to the remainder of my statement, I believe it would be helpful if I were to indicate the extent of trade between NATO countries and the Communist countries-- to give some idea of the economics affecting the U.S. role in East-West Trade. The trend of trade between 1963 and 1966 indicates that the trade of NATO countries with the Communist countries has remained fairly constant--imports from Communist countries in 1966 were 3.4% of NATO countries total imports and exports to these same Communist countries were 3.7% of the total. NATO countries exports to Communist countries increased by 24.3% in value between 1965 and 1966, while their exports as a percentage of their total exports increased from 3.3% to 3.7%. Their imports from Communist

countries increased 13.7% in value between 1965 and 1966 and their imports as a percentage of total imports increased from 3.3% to 3.4%.

U.S. exports to Communist countries in 1967 were about \$195 million, down from about \$198 million in 1966. Imports were about \$180 million in 1967, down from about \$182 million in 1966. In both years U.S. trade with Communist countries amounted to about 0.7% of total U.S. trade. These amounts indicate that these transactions are not among the most significant which affect the United States balance of payments. While we must seek out every opportunity to improve our payments position, U.S. policies with respect to East-West Trade cannot be motivated primarily by balance of payments considerations; it is important to maintain scrutiny over this trade for national security reasons.

In order to inform the committee of the details of the Treasury Department's role in East-West Trade matters, technical descriptions have been prepared and are attached for the record. I shall summarize here the more significant aspects of the Treasury Department's activities in this important area.

The Treasury Department presently administers three sets of Regulations which have a direct bearing on East-West Trade and which were issued specifically to operate in this national security area. These are the Foreign Assets Control Regulations, the Cuban Assets Control Regulations, and the Transaction Control Regulations, all of which were issued under the authority of the Act of October 6, 1917, as amended, 12 U.S.C. 95a.

The first two sets of Regulations affect East-West Trade by prohibiting, except pursuant to license, all commercial and financial transactions with Communist China, North Korea, North Vietnam, and Cuba or nationals thereof and with respect to their products no matter where located. The Transaction Control Regulations deal with the purchase and sale by Americans and American-controlled firms of strategic commodities located outside the United States if the intention is ultimate delivery to East Europe or the U.S.S.R.

The Foreign Assets Control Regulations were issued on December 17, 1950, to implement the United States policy of a total embargo on all financial and commercial dealings

with Communist China and North Korea, including both exports and imports, except pursuant to license and were amended on May 5, 1964, to include North Vietnam. The control of exports from the United States to these areas is actually exercised by the Department of Commerce which has primary responsibility for the movement of U.S.-origin goods under its export control regulations. Thus the Treasury Department's Foreign Assets Control Regulations contain a general license permitting any export directly to those areas which are licensed by the Department of Commerce. The financial controls contained in Treasury Department regulations serve to supplement Commerce controls over the goods. As a practical matter, under both Treasury and Commerce Department regulations only publications move between this country and Communist China and North Korea.

All imports from Communist China, North Korea, and North Vietnam are prohibited by the FAC regulations the provisions of which also extend to goods regarded as presumptively Chinese. Because of transshipment possibilities, these restrictions affect imports of certain commodities from East Europe and the U.S.S.R. such as certain ores and metals, textiles and animal hair.

The Foreign Assets Control Regulations also extend to American-controlled firms abroad. It is the Government's policy not to license exports by such firms to Communist China, North Korea, or North Vietnam except for overriding foreign policy considerations. The decision on any case which arises in this area is made only in consultation with State (and as appropriate other interested agencies). The general policy followed is based on a 1965 interagency review, headed by the Attorney General, which concluded that the application of the Treasury regulations to U.S.-controlled firms abroad should be continued and that individual cases should be treated flexibly with exceptions to a general denial policy to be made only on the basis of foreign policy considerations. (This basic approach was the same that had been followed in prior years.) American-controlled firms abroad equally may not import prohibited merchandise.

The Cuban Assets Control Regulations, issued on July 8, 1963, are essentially parallel to the Foreign Assets Control Regulations. Thus, trade between the United States and Cuba is limited to exports of publications and

gift shipments of foods, clothing and medicines authorized by the Commerce Department and to licensed imports of publications. However, in the case of Cuba most American-controlled subsidiaries abroad have been authorized for foreign policy reasons to engage in trade with Cuba in non-United States origin goods. As a matter of fact such firms, except for exports of foods and medicines, are not known to be trading in any significant degree with Cuba. The authorization does not extend to U.S. citizens abroad who, as officers or directors, are in a position to control the operations of the foreign firm. Applications for licenses to authorize the participation of such American officers or directors in Cuban transactions are handled in the same manner and involve essentially the same considerations as applications relating to trade with Communist China, North Korea or North Vietnam by American controlled firms abroad, as I mentioned earlier.

The Transaction Control Regulations were issued on June 29, 1953, following policy consideration of the need, primarily in the interdepartmental Economic Defense Advisory Committee (commonly referred to as EDAC), as a part of the

United States efforts in the internationally agreed control of strategic commodities. These controls are in addition to the controls exercised by the Commerce Department over direct exports from the United States to Eastern Europe and the U.S.S.R. The Transaction Control Regulations prohibit, unless licensed, any person within the United States, and foreign firms controlled by such persons, from purchasing or selling or arranging the purchase or sale of strategic commodities located outside the United States for ultimate delivery to the Eastern Europe and the U.S.S.R. The coverage of these Regulations is restricted to those commodities which are listed as strategic by international agreement through the Consultative Group Coordinating Committee (generally known as COCOM). Treasury decisions on requests for licenses are in conformance with the policies reached in the EDAC. A summary of Transaction Control Regulations operations during the past five years is included in the attached technical descriptions.

In 1954, at EDAC's request, Foreign Assets Control Regulations and Transaction Control Regulations were interpreted to apply to patent and technical data licensing

agreements whereby the foreign licensees agreed not to ship anything produced abroad with American know-how to Communist China or North Korea in the absence of a Treasury License. Similarly, the foreign licensees agreed not to ship anything on the internationally agreed strategic lists to Eastern Europe or the U.S.S.R. or North Vietnam in the absence of a Treasury license. This control was transferred to the Commerce Department on April 1, 1964. (Under present Commerce regulations North Vietnam is grouped with Communist China and North Korea.)

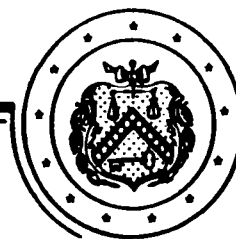
In addition to the foregoing, Treasury, through the Bureau of Customs and the Internal Revenue Service, administers other laws and regulations of secondary importance to East-West Trade.

The major Customs involvement is to assist other U.S. agencies and Treasury's Office of Foreign Assets Control who have the prime responsibilities for carrying out the laws and regulations which are applicable to East-West Trade. Customs assistance comes through the enforcement of import restrictions, statutory rates of duty, and export control laws. Of less importance to East-West Trade

are Customs regular responsibilities for collection of import duties and dumping duties, smuggling control, and restrictions on imports.

Internal Revenue, through the Interest Equalization Tax (IET) is only involved in trade, including East-West Trade, when Americans finance exports through the receipt of foreign debt obligations of one year or more. A series of exclusions is provided to minimize interference with our general export objectives. The IET was principally designed not to deal with trade, but to curtail the outflow of portfolio funds seeking higher rates of interest abroad.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR RELEASE 6:30 P.M.,
Wednesday, February 21, 1968.

RESULTS OF TREASURY'S MONTHLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated November 30, 1967, and the other series to be dated February 29, 1968, which were offered on February 15, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$500,000,000, or thereabouts, of 275-day bills and for \$1,000,000,000, or thereabouts, of 365-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	275-day Treasury bills		:	365-day Treasury bills	
	maturing November 30, 1968		:	maturing February 28, 1969	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	96.021	5.209%	:	94.708 a/	5.220%
Low	95.975	5.269%	:	94.587	5.339%
Average	95.998	5.239% 1/	:	94.646	5.281% 1/

a/ Excepting 1 tender of \$500,000

11% of the amount of 275-day bills bid for at the low price was accepted

28% of the amount of 365-day bills bid for at the low price was accepted

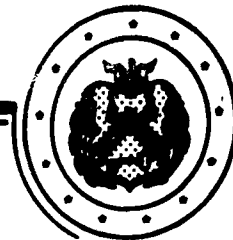
TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ none	\$ none	:	\$ 16,556,000	\$ 5,556,000
New York	1,085,064,000	427,724,000	:	1,142,962,000	741,762,000
Philadelphia	5,063,000	1,063,000	:	8,855,000	855,000
Cleveland	15,409,000	5,519,000	:	34,228,000	34,228,000
Richmond	2,980,000	980,000	:	3,184,000	2,184,000
Atlanta	13,075,000	2,185,000	:	12,979,000	7,539,000
Chicago	128,382,000	39,932,000	:	143,163,000	91,163,000
St. Louis	10,368,000	1,368,000	:	15,518,000	12,418,000
Minneapolis	13,805,000	2,405,000	:	13,649,000	8,649,000
Kansas City	3,969,000	869,000	:	5,287,000	4,287,000
Dallas	11,571,000	1,571,000	:	12,848,000	2,848,000
San Francisco	58,429,000	16,429,000	:	108,550,000	88,550,000

TOTALS \$1,348,115,000 \$ 500,045,000 b/ \$1,517,779,000 \$1,000,039,000 c/

Includes \$15,645,000 noncompetitive tenders accepted at the average price of 95.998
 Includes \$26,398,000 noncompetitive tenders accepted at the average price of 94.646
 These rates are on a bank discount basis. The equivalent coupon issue yields are
 5.48% for the 275-day bills, and 5.58% for the 365-day bills.

TREASURY DEPARTMENT



WASHINGTON, D.C.

February 21, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,600,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing February 29, 1968, in the amount of \$3,904,591,000, as follows:

92-day bills (to maturity date) to be issued February 29, 1968, in the amount of \$1,600,000,000, or thereabouts, representing an additional amount of bills dated May 31, 1967, and to mature May 31, 1968. . . originally issued in the amount of \$900,146,000 (additional amounts of \$500,686,000 and \$1,002,582,000 were issued August 31, 1967, and November 30, 1967, respectively), the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated February 29, 1968, and to mature August 29, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Monday, February 26, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

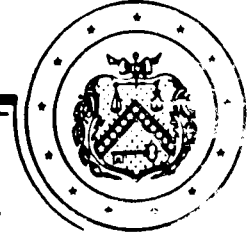
Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on February 29, 1968, cash or other immediately available funds or in a like face amount of Treasury bills maturing February 29, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and the notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained at any Federal Reserve Bank or Branch.

TREASURY DEPARTMENT



WASHINGTON, D.C.

FOR RELEASE 6:30 P.M.,
Monday, February 26, 1968.

RESULTS OF TREASURY'S WEEKLY BILL OFFERING

The Treasury Department announced that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated May 31, 1967, and the other series to be dated February 29, 1968, which were offered on February 21, 1968, were opened at the Federal Reserve Banks today. Tenders were invited for \$1,600,000,000, or thereabouts, of 92-day bills and for \$1,000,000,000, or thereabouts, of 182-day bills. The details of the two series are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:	92-day Treasury bills		:	182-day Treasury bills	
	maturing May 31, 1968		:	maturing August 29, 1968	
	Price	Approx. Equiv. Annual Rate	:	Price	Approx. Equiv. Annual Rate
High	98.721	5.005%	:	97.360	5.222%
Low	98.700	5.087%	:	97.350	5.242%
Average	98.706	5.063% <u>1/</u>	:	97.353	5.236% <u>1/</u>

58% of the amount of 92-day bills bid for at the low price was accepted
41% of the amount of 182-day bills bid for at the low price was accepted

TOTAL TENDERS APPLIED FOR AND ACCEPTED BY FEDERAL RESERVE DISTRICTS:

District	Applied For	Accepted	:	Applied For	Accepted
Boston	\$ 21,859,000	\$ 11,859,000	:	\$ 9,469,000	\$ 9,469,000
New York	1,875,545,000	1,136,705,000	:	1,482,839,000	706,694,000
Philadelphia	35,210,000	17,950,000	:	13,290,000	4,921,000
Cleveland	37,751,000	32,131,000	:	80,020,000	34,691,000
Richmond	8,807,000	8,807,000	:	3,816,000	3,602,000
Atlanta	44,322,000	35,302,000	:	33,766,000	14,084,000
Chicago	248,191,000	184,991,000	:	242,416,000	144,549,000
St. Louis	51,799,000	41,768,000	:	40,606,000	31,226,000
Minneapolis	22,238,000	14,638,000	:	17,018,000	6,543,000
Kansas City	29,085,000	28,085,000	:	15,332,000	10,680,000
Dallas	23,197,000	15,777,000	:	18,208,000	8,618,000
San Francisco	111,993,000	72,515,000	:	95,338,000	25,153,000

TOTALS \$2,509,997,000 \$1,600,528,000 a/ \$2,052,118,000 \$1,000,230,000 b/

Includes \$241,827,000 noncompetitive tenders accepted at the average price of 98.706
Includes \$125,746,000 noncompetitive tenders accepted at the average price of 97.353
These rates are on a bank discount basis. The equivalent coupon issue yields are 5.20% for the 92-day bills, and 5.45% for the 182-day bills.

TREASURY DEPARTMENT
Washington

FOR RELEASE ON DELIVERY

REMARKS BY THE HONORABLE FREDERICK L. DEMING
UNDER SECRETARY OF THE TREASURY FOR MONETARY AFFAIRS
AT THE GREATER SAN FRANCISCO METROPOLITAN AREA
1968 INDUSTRIAL PAYROLL SAVINGS CAMPAIGN MEETING
ST. FRANCIS HOTEL, SAN FRANCISCO, CALIFORNIA
MONDAY, FEBRUARY 26, 1968, 1:35 PM PST

I want to talk to you today about our Savings Bonds program and how it fits into our general program to finance the Federal budget deficit in a sound and non-inflationary manner. And I want to relate the need to reduce our domestic budget deficit with the equally vital need to reduce or eliminate our balance of payments deficit.

We must take strong action on both deficits in order to promote sustainable economic growth at home and to provide for a sustainable international monetary system that will underpin world economic growth.

Let me begin by noting an important fact that seems to be given little attention in much that is said or written about international payments imbalances. That fact is that deficits and surpluses in international accounts today have a different character from those of yesteryear, and policies to resolve them also must have a different and a broader character.

Throughout much of modern history, balance of payments deficits arose when inflation occurred in a country and made the price of goods expensive in that country. This caused the country's exports to fall and its imports to rise. The correction was mainly to deflate the economy and, thus, reverse the export-import situation. In company with deflation would be rising interest rates that would produce equilibrating capital flows which would also reduce the deficit. Surplus countries would export capital and increase imports and produce their adjustments in this way.

Today, the problem is different both in kind and in cure. Sharp deflation is not only unpopular; it is recognized as stunting growth not only in deficit countries but in the world as a whole. And some countries without inflation have had deficits and some of those with inflation have had surpluses. Deficits arising from the foreign exchange costs of world wide defense alliances are not susceptible to reduction by fiscal and monetary policies at home. Tourism is big and growing and is related more to level of income than to costs and prices. Capital flows are not always equilibrating and do not always respond fully to interest rate policies. In a world short of capital and with expanding markets, much capital moves with long-term perspective rather than for short-term gain.

The United States has had balance of payments deficits in 17 of the last 18 years. In that period, our record of price stability was second to none. Moreover, our merchandise trade balance has been favorable in each of those years. It is clear that the situation has become far more complex in an increasingly interrelated world economy. As we search for balance of payments equilibrium, we look not only to our trade account but also to our balance on capital account, our balance on tourist account, the foreign exchange costs of our worldwide military deployment, and the foreign exchange cost of our economic assistance to the developing world.

In the early post-war years, our generous assistance to the wartorn countries of Europe and Asia left us with moderate balance of payments deficits which we were quite prepared to accept. Foreign countries began to restore their depleted international reserves, and we had the foresight to see that restoration of the productive capacity of Western Europe and Japan would benefit ourselves and the rest of the world.

By 1958, it was apparent that Europe and Japan had gone a long way toward restoration of their productive capacity -- and much of that capacity was modern and highly efficient. Despite our good over-all cost and price record, the 1954-57 investment-consumption boom had brought price increases -- particularly in metals and machinery -- in those years, and our competitive position had deteriorated.

We had a small surplus in 1957 -- mainly because of the Suez crisis and the oil situation. Then, for the following three years, our deficits averaged \$3.7 billion.

These deficits were too big. Their financing became troublesome. They supplied too many dollars too fast to be absorbed smoothly into world reserves. A substantial part of those dollars came back for conversion into gold -- and our reserves fell. The need for action to reduce our deficit became obvious.

The first direct actions were aimed at shrinking the foreign exchange costs of Government spending overseas. Net military outlays were reduced both by direct economies and by military offset sales. Foreign aid outlays were cut by tying such aid to purchase of American goods and services. Our movement toward better balance was aided a great deal by the fine record of price stability that extended over the first half of the 1960's. This, in conjunction with high growth rates in foreign industrial areas and expanding demands for our goods, helped to produce substantially larger U. S. trade surpluses.

But, as corrective action came on Government account and the trade account improved, capital began to flow out in increasing volume -- partly because we generated large savings and had large capital markets, partly because of investment opportunities overseas, partly because the long campaign to increase U. S. foreign investment had gradually won many converts

These tendencies were damped somewhat by the Interest Equalization Tax in 1963 and by the voluntary programs to restrain direct investment and foreign lending in 1965.

The arithmetic is instructive here. The 1960 deficit was \$3.9 billion. The 1962 deficit was \$2.2 billion -- mostly due to reduced Government costs and better trade balance. The 1964 deficit was \$2.8 billion -- reflecting one of the best trade balances in our history but also the biggest private capital outflow. In 1965 and 1966, the deficit was cut to \$1.3 billion, as capital outflow was curtailed. It was mostly bank lending which declined -- direct investment continued to grow.

In a sense, it is fair to say that the major reason we failed to achieve equilibrium in our payments balance in 1965 and 1966 was the rising foreign exchange cost of Vietnam and its impact on domestic business activity and our trade balance. The deficits in both these years reflected primarily Vietnam war expenditures. But, in 1967, we could no longer count Vietnam as the principal factor. Our deficit last year was \$3.6 billion; the direct foreign exchange costs of Vietnam were well under half that sum.

As 1967 data were compiled from quarter to quarter, it became apparent that the over-all situation was getting worse.

By the end of September, last year, it was clear that the deficit would be sharply higher. Net military expenditures were somewhat increased, but the largest deterioration was shown in net private capital outflow.

The fourth quarter showed substantial further deterioration and brought the deficit for the year back to the discouraging total of \$3.6 billion. The fourth quarter deficit alone was \$1.8 billion and accounted for half the annual deficit. In one sense, the fourth quarter deficit was not quite as bad as it looked in that it included a one-time exceptional item -- a \$570 million liquidation by the British Government of its portfolio of private U. S. securities. But, in another sense, the fourth quarter deficit was as bad as it looked in that it showed a \$720 million decline from the third quarter in the trade balance. Imports were up \$560 million and exports were off \$160 million from the previous quarter.

Just our own deficit position would have required strong corrective action by us. But the problem became much greater after devaluation of the British pound in November. The entire international monetary system came under savage speculative pressure, which was intensified by the fears that accompany devaluation of a major currency. There were massive currency movements and a rising demand for gold. The U. S. lost \$1.2 billion in gold reserves in 1967 -- most of it in the last six weeks of the year.

A strong -- a drastic -- program was needed. But balance was no less important than strength. The program announced by the President on New Year's Day has both strength and balance -- and is designed to bring us to, or close to, equilibrium in 1968.

First -- and most important -- there is balance between domestic and international measures. The first order of business, the President said, is to enact the tax surcharge now before Congress. The surcharge is essential to contain the domestic economy and to avoid inflationary pressures which would lead to rapid growth in imports. I said earlier that balance of payments problems today have different characteristics from those of former times and, consequently, need different and broader policy approaches. But any corrective program for an economy laboring under too fast and too large cost and price increases must start with containment of these pressures at home. These, in our case, are not the only causes of the deficit. But they are important causes, and it is important to correct them for today's needs and even more important to correct them if we are to attain steady trade growth.

Secondly, there is balance within the selective program -- between the capital restraints and the current account measures -- and between the public and the private sectors. Specific

action to reduce direct investment and further reduction of foreign lending by banks and other financial institutions are designed to bring about a balance of payments improvement of about \$1.5 billion. The remainder of the program deals with current account items. Here, the restraints are applied to Government outlays on both military and civilian account and to tourism. Measures to expand exports are also included -- assigned to the Department of Commerce and to the Export-Import Bank. We are also exploring thoroughly steps to remove -- or counter -- disadvantages to our trade arising from border tax and non-tariff barriers imposed by foreign countries.

Finally, there is a third important sense in which the program is balanced. The selective measures are designed to temper the impact of our own actions on weaker countries abroad. By and large, the Continental European countries have had a balance of payments surplus that has corresponded to the deficits of the United States and the United Kingdom over the years. Consequently, the selective restraints applied in the balance of payments program have -- and should have -- their greatest impact on those countries whose reserves and competitive position are strongest. In this way, the countries in other parts of the world will bear the lightest part of the adjustment burden.

It follows that the reaction of Western Europe to our program is of fundamental importance to its success. I can report with great satisfaction that the reaction of our partners has been highly responsible.

The Continental European countries have, for several years, been concerned by the continuing United States deficits. They have recognized that their own surpluses are the mirror image of our deficits. While they have, of course, raised questions about particular aspects of our program, they have, on balance, accepted the necessity of selective application of our restrictions in such a way that the burden of adjustment would fall on those countries best able to bear it. They recognize, as we do, that the balance of payments adjustments which the United States and the United Kingdom are now making could be highly disruptive to the world economic system unless that adjustment is absorbed by the surplus countries of the world.

As a result, it is now apparent that these European countries will not only seek to avoid actions which might frustrate adjustment but are moving to institute positive policies of expansion which will facilitate the adjustment process. They recognize that expansionary action in Continental Europe would represent an appropriate offset for the dampening effects on demand which will accompany the efforts of the United States and the United Kingdom to eliminate their deficits.

They realize that their efforts to attain higher growth rates in the near future may mean deterioration in their balance of payments positions. They realize also that our measures in the field of capital restraints will increase pressures upon European capital markets. They are, I believe, agreed in principle that they should refrain from measures which would tighten their capital markets or raise their interest rates unduly. On the contrary, they recognize that they should accept and promote capital outflows as an offset to their current account surpluses.

As we do, the European countries place particular importance on that part of our balance of payments program which the President called the "first order of business." They are paying particularly close attention to our efforts to obtain additional revenue through a tax surcharge. They believe, just as we do, that this would be the most efficient way of restraining excessive internal demand in the United States. They place great importance on realization of that balance, which I mentioned earlier, between domestic measures in this country to control demand and the specific international measures in our balance of payments program.

The action program for 1968 is an emergency program and, thus, a temporary program.

At longer range, we seek a sustainable equilibrium not dependent upon these special emergency actions -- one consistent with world economic growth. Three avenues are especially important in pursuing this objective.

- We need to have a rising trade surplus in order to cover our capital investment abroad and to help meet our responsibilities for promoting growth and security in the free world. The first element depends heavily upon managing our own economy without a spillover of demand that would lead to excessive imports. It also depends on our success in avoiding a rise in costs at a more rapid rate than that experienced by our competitors. These two factors are crucial in the longer run. Our relative share of the world market has been falling in recent years. That trend must be reversed. But only a small rise in our relative share should be needed if world trade grows and our imports do not rise too rapidly.
- The foreign exchange cost of forces abroad, engaged in common defense efforts, should be neutralized. This principle should apply to all countries. Common security needs should not be impaired by balance of payments strains which can and should be neutralized.

The demands of assuring the security of the free world weigh heavily on our balance of payments. These burdens are already severe in human costs and in domestic budgetary costs. We are negotiating with our allies and friends with a view to neutralizing this aspect of our international accounts.

-- We have an important long-run positive factor in the rising level of our income on foreign investment. Balance of payments receipts on this account have risen from \$2.8 billion in 1960 to \$5.1 billion in 1966. This is a factor of strength on which we must count in the long run.

The progress made on these three fronts will influence, to a large degree, the speed with which we can dismantle the temporary restraints we have today. We cannot, however, continue to spend more than we receive and pay out the difference at the cost of our liquidity. We need to achieve and maintain equilibrium in our international accounts. We hope to do so in the most constructive way possible. But events will require us to correct the deficit, in one way if not in another.

It is my belief that we are following the best course open to us at present in a world not devoid of troublesome problems. The action program is off to a good start.

A serious incipient financial crisis has been choked off. We have a strong and balanced program of general domestic policy and specific item-by-item correction of the balance of payments. The European response has been constructive and cooperative.

We are behind schedule, however, on the tax surcharge, and I would urge your vigorous support of this measure, to cement our good progress here and good reception abroad.

I said, in opening this talk, that we need to attack two deficits. I have been discussing, in some detail, the attack on the balance of payments deficit and have stressed the importance of the tax surcharge in this connection. But the tax surcharge, itself, is the single most important action that can reduce the domestic budget deficit. It not only is indispensable to containing the economy to a sustainable growth path but will lessen the demands of the Federal Government on the money and credit markets, thereby making more room for private borrowers and moderating pressure on interest rates.

Even with a tax surcharge, the deficit for fiscal 1968, on the new unified budget basis, will be about \$20 billion and, for fiscal 1969, will be about \$8 billion. Deficits of this size require major financing efforts on the part of the Treasury. They need to be financed in a sound and anti-inflationary way, and here is where Savings Bonds make a great contribution.

Savings Bonds held by tens of millions of Americans comprise more than 23 percent of the publicly-held portion of the National debt, and they represent the soundest way of financing our Federal budget deficit available to us. By contributing to the reduction of over-all demand in the economy, increased purchases of Savings Bonds provide important assistance to the eventual elimination of the deficit in our international accounts.

For this reason, I am especially happy to play a part in this occasion, which looks to another period of great achievement for our Savings Bonds Program -- and which sets its sights on greater Payroll Savings accomplishments in 1968.

During the year past -- largely due to the efforts of your fellow Californian, Chairman Dan Haughton, of the 1967 Industrial Payroll Savings Committee -- your nationwide accomplishment surpassed the announced goal. More than 2-1/2 million employees were signed up.

Of those new 1967 bond savers: 2,410,000 are from industry; 388,539 are from the civilian rolls of Government, signed up in the Federal Employees' campaign headed by Postmaster General O'Brien.

Now we are well into a new campaign year. Our 1968 program is fortunate to enjoy the leadership of Bill Gwinn -- the 1968 National Chairman of the Payroll Savings Committee.

Total sales of Savings Bonds and Freedom Shares, during 1967, came to nearly \$5 billion -- a rise of 2 percent over the previous year, and our best year in the past eleven. Gross redemptions, including interest, were down by one percent over the preceding year.

The net result -- the point that means most to us, as far as financing our deficit and adding to the savings of individuals are concerned -- was that the volume of Savings Bonds outstanding increased by over \$1.1 billion during 1967, passing the \$51 billion mark in August and closing the year at nearly \$52 billion.

I believe that those good results are a tribute to the Payroll Savings promotion that volunteer leaders like yourselves stimulate so effectively. I believe that they are also a tribute to the nationwide effort that has brought about the telling of the Savings Bonds story in thousands of plants and places of business; in union meetings and over the counters of banks; in newspapers and magazines; in radio and TV broadcasts; and in motion picture theaters.

Since the inception of the Savings Bonds Program, in 1941, it has enjoyed a remarkable blending of professional and volunteer effort and service. This is nowhere better illustrated than by the presence and by the performance of the members of this audience.

Today, in light of the problems with which we must cope, the Savings Bonds program is of as much importance as at any time since its inception. We must do our best in the year ahead.

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TREASURY DEPARTMENT
Washington
FOR RELEASE UPON DELIVERY

REMARKS BY THE HONORABLE STANLEY S. SURREY
ASSISTANT SECRETARY OF THE TREASURY
BEFORE THE
TAX EXECUTIVES INSTITUTE, INC.
AT THE
SHOREHAM HOTEL, WASHINGTON, D. C.
FEBRUARY 26, 1968 - 12 NOON EST

THE TRAVEL TAX IN PERSPECTIVE

The Ways and Means Committee is now in the middle of two weeks of public hearings on the travel portion of the President's balance of payments program. Of the 67 witnesses scheduled to appear before that Committee, reports indicate that few if any are in favor of this portion of the Administration's program -- which is about par for most tax proposals. It is therefore pleasing to have this audience available to me to express the other side of the picture.

Balance of payments problems, I am sure, may not have the immediacy to you that tax treaties or Section 482 Regulations might have. In fact, balance of payments problems seem generally to have a lack of immediacy to almost everyone. This lack of a feeling of urgency and concern is no doubt due to the esoteric nature of international financial payments. To average citizens, as well as to many well informed citizens, the balance of payments, the strength of

the dollar, and the workings of the international monetary system are remote concepts. They seem to have little relevance to their daily lives. Therefore few come forward, either as witnesses or in public print, to support programs aimed at solving problems in this area.

While the concepts may be difficult to understand, the problems are there and a failure to understand the concepts will not cause the problems to disappear. Unfortunately, people may take the time to understand the concepts and the problems, and therefore the necessity for remedies, only after they find that the problems are adversely affecting their daily lives. The Administration's balance of payments program is aimed to provide remedies now in order to prevent these problems from growing in intensity and having adverse effects later.

This lack of understanding is clearly evident in the nature of the criticisms of the travel tax. Any particular program set forth by the Administration is properly open to debate and to improvement as the result of analysis and criticism. But neither the travel tax proposal nor the solutions to the balance of payments problem are helped by

criticism which lacks perspective or balance or by criticism which offers no realistic alternative.

The travel program has been criticized on several different levels and I would like to address myself to these general categories of criticism. There are those who argue that there is no balance of payments problem and that the Administration is simply "pushing a panic button." But the facts belie this placid view. Our balance of payments deficit last year was over \$3-1/2 billion, and for the last quarter of the year was running at an annual rate of over \$7 billion. Our gold loss in the last two months of the last year, following the British devaluation, was in excess of \$1 billion. These deficits and gold losses certainly cannot continue unabated without seriously threatening the stability of the international monetary system which depends on the dollar as the principal reserve currency. A drastic reduction in our balance of payments deficit is thus necessary now.

Our domestic prosperity depends on a stable currency in terms of which businessmen can plan with confidence and the individual can save with confidence. International prosperity, with which our domestic prosperity is so closely

associated, depends on the same stability. If we do not have a stable currency at home and abroad, uncertainty takes over -- uncertainty on the part of the businessman about whether to invest or employ more people; uncertainty by the individual on how much to spend or save; uncertainty by the Government on how much freedom of international business enterprise, trade and travel it can afford.

For another group of critics -- those who admit that there is a balance of payments problem -- the answer lies totally outside of those areas dealt with by the President's Balance of Payments Action Program. They would, for example, find the answer to the problem in a withdrawal of our military forces from abroad. Besides the delayed balance of payments impact such measures would have, this solution of course raises grave questions of international commitments and national security, and the extent of action in this area must be measured against our whole international posture. The balance of payments program does include steps to reduce substantially the impact of our overseas commitments on our balance of payments. Supplementing substantial other measures long in effect, the President has taken three steps in this regard:

First, he directed the Secretary of State to initiate prompt negotiations with our NATO allies to minimize the foreign exchange costs of keeping our troops in Europe. He asked that our allies help in a number of ways, including:

- The purchase in the United States of more of their defense needs.
- Investments in long-term United States securities.

The President also directed the Secretaries of State, Treasury and Defense to find similar ways of dealing with this problem in other parts of the world.

Second, he instructed the Director of the Budget to find ways of reducing the numbers of American civilians working overseas.

Third, he instructed the Secretary of Defense to find ways to reduce further the foreign exchange impact of personal spending by United States forces and their dependents in Europe.

Others have claimed that the share of American foreign subsidiaries in the Eurodollar pool comes to \$16 billion and that a tax incentive to these subsidiaries to repatriate their accumulated earnings would at one stroke solve our whole balance of payments problem. But the \$16 billion

figure is far above the share of our companies in this Euro-dollar pool. Moreover, the net assets invested in Europe by American companies, including their accumulated earnings, are there in the form of bricks, mortar, machinery and equipment, and not as cash or portfolio investments. They thus do not represent dollars available for repatriation to the United States. The Commerce program provides for at least the maintenance of the same substantial rate of repatriation of current earnings that has characterized our European operations. In addition, to the extent that some companies may have liquid assets available for repatriation, a program of tax incentives to encourage their repatriation would raise serious questions of tax equity. The result would be to tax corporations earning money abroad at a rate lower than that applied to corporations earning their funds in the United States, and in this respect would itself become an incentive for additional investment abroad. Besides, as a practical matter, our corporate tax does not operate as a barrier to repatriation. Most industrialized countries apply corporate taxes about as high as our tax rate and our tax system allows full credit for those taxes

when earnings are repatriated from subsidiaries in those countries.

Other critics, recognizing both the need for action in the balance of payments area and the superficiality of these and other proffered panaceas, nevertheless ask, "Why make the traveler the whipping boy?"

The balance of payments Action Program does not single out the traveler. Travelers are but one group whose activities are being moderated under that program to solve our critical balance of payments problem -- along with Government, investors, banks, and consumers. In fact those sectors have been under a restraint for some time. Under the President's program, a \$3 billion savings in our balance of payments would be achieved as follows:

- A mandatory program to reduce direct investments abroad -- \$1 billion.
- A Federal Reserve Board program to restrain foreign lending by banks and other institutions -- \$500 million.
- Reductions in Government expenditures overseas -- \$500 million.

-- Measures to improve our trade balance -- \$500 million.

-- Reduction in the travel deficit -- \$500 million.

These measures are joined in the Action Program with the 10 percent tax surcharge to restrain inflationary pressures at home, thereby improving our competitive position in world trade.

This Action Program would be incomplete were travel omitted. Our balance of payments deficit arising as a result of travel was about \$2 billion last year. This deficit arose because United States residents traveling abroad spent \$4 billion -- almost 10 percent of this country's gross foreign payments -- while foreign visitors to the United States spent only \$2 billion.

We often hear the argument pressed that travel is an inalienable right. While the value of travel is unquestionable, the fact nevertheless remains that each dollar spent abroad for travel must be offset by an equal amount of foreign exchange earned by this country from travel or other sources. This exchange must be available to finance the exercise of this right to travel. When that exchange

is not fully available, of necessity travelers along with others must curtail their spending.

Establishing the fact that there is a travel problem merely moves many critics to say that a solution restraining travel is negative and that we should instead close the travel gap by increasing tourism to the United States. We fully agree with the proposition that the best long-term solution to moderating the travel deficit lies not in restraining travel by Americans but in increasing travel by foreigners to the United States. This, however, necessarily will take time.

The Task Force headed by Ambassador McKinney has developed a comprehensive program for increasing tourism to the United States. It is clear that this program cannot be entirely implemented this year, and moreover its full effects will not be immediately realized.

The American Travel Association, in its presentation before the Ways and Means Committee, was one of the witnesses which took the position that the solution to the travel deficit lay in increasing tourism to the United States. It said:

"The economic factors are very great. How many more visitors to the U. S. would it take to balance the \$500 million the Administration wants to cut off the equation? A little simple arithmetic will give you a clue. If the visitors brought only \$100 each, we would have to attract 500,000 more people to the U. S. If they spend \$500 each in the U. S. (a more likely amount) it would take only 100,000 more."

However, more accurate, but equally "simple arithmetic", would show that these 100,000 visitors spending \$500 each would help the balance of payments problem by only \$50 million, or only one tenth of the \$500 million travel goal. Applying "simple arithmetic" thus shows that 1 million additional foreign visitors spending \$500 each would be necessary to achieve the needed balance of payments effect. This would represent an increase of about two-thirds in the number traveling to the United States. Perhaps the impossibility of immediately achieving an increase of this size led the Association to its mathematical solution of our difficulties.

Other critics claim that an affirmative program restraining our travel abroad will be ineffective because of the retaliation it will evoke. It is not completely clear, however, just what "retaliation" means in this context. By

"retaliation" these critics may be referring to the fact that the economy of a foreign country is affected by a decline in our tourist business and hence the country might spend less for United States goods and services. This is a distinct possibility. However, for each dollar by which we reduce our balance of payments deficit some other country of the world will have a reduction in their receipts of \$1. If we reduce the cost of our overseas troop commitments, or reduce our direct investment abroad, or reduce lending abroad, or do anything at all to reduce our balance of payments deficit, there is inevitably a reduction in the dollars available to other countries, and therefore the possibility that fewer dollars will be spent by them in the United States. Why there would be more "retaliation" in this feedback sense if the foreign group directly affected are hotel keepers, restaurateurs and the like rather than manufacturers or suppliers of "hard goods" is difficult to see. In essence, there is always some "feedback" in an overall program of this nature, and that feedback enters into the calculation of the overall balance of payments savings.

Another meaning of "retaliation" might be a deliberate effort on the part of a foreign government to offset the

effect of a travel tax by imposing travel restraints on its own citizens. Again, it is difficult to see why such retaliation should occur. The countries of the world with balance of payments surpluses are also the countries of the world having a direct stake in the stability of the dollar and therefore must be willing -- and have the responsibility -- to permit that stability to be reached.

One specific possible area of retaliation pointed to by critics is a reduction in foreign orders for United States aircraft. Close examination does not lend credence to this fear, and the travel program is specifically designed to have the least impact on the number of people traveling abroad. It should thus have the least effect on the airline business of any form of travel restraint and therefore on aircraft orders.

The next group of critics focus directly on the structure of the travel tax and take the position that it is unworkable, unenforceable, unfair and ill-conceived -- to say the least. They say one can't see Europe for \$7 a day, the amount of the exemption under the tax; that the tax will fall heavily on teachers, students and other low income

people; that it will have little effect on "jet-setters;" that it will involve mountains of red tape; and that it will encourage Prohibition-type evasion.

We can consider the defects in these criticisms in a moment. We should note that these critics rarely suggest an alternative form of tax. We suspect the reason for this is they cannot come up with another tax which solves the problems they see in the proposed tax, achieves the necessary balance of payments savings, and yet meets the essential standard of fairness. Certainly other tax approaches could have been devised -- and were considered. A tax of 20 or 25 percent on tickets would have achieved approximately the same balance of payments savings. So also would a head tax of \$100 to \$150. So also would a tax of \$4 or \$5 a day. Taxes of this kind would have been simpler -- and grossly inequitable.

The proposed tax clearly cannot be faulted on equity grounds. The tax exempts expenditures up to \$7 a day, imposes a 15 percent rate on expenditures between \$7 and \$15 a day, and a 30 percent rate on expenditures above \$15. The tax is thus progressive according to expenditures, which,

after all, is the factor contributing to the balance of payments problem. It is designed so that one traveling modestly will incur little tax. On the other hand, the 30 percent rate on expenditures over \$15 per day (which is approximately the average amount spent by tourists) is a significant continuing deterrent to marginal expenditures even by the most affluent traveler. A substantial tax on tickets or a tax on each traveler in a fixed amount or on each day of travel would fall equally on the modest traveler as well as the lavish traveler. Such taxes would therefore represent a far greater proportion of the expenditures of the less affluent and would be no continuing deterrent to the more affluent.

It would be interesting to contemplate the arguments that might have been put forward if one were to propose today an individual income tax for the first time. Certainly the same arguments now being made to the Ways and Means Committee would be made against that proposal. However, having lived with an income tax, we would all agree that the arguments as to complexity and enforcement are arguments applicable only to a very small percentage of taxpayers, and that this is a small price to pay for the equity achieved by a progressive tax measured by ability to pay.

Just as one can argue that there are ways to evade the travel tax, one can argue that there are ways to evade the income tax -- and some people try it. Out of 100 million income taxpayers in the United States, however, and out of 3 million audited returns, there were under 1,000 fraud indictments last year. This clearly demonstrates that the great mass of American taxpayers accept their responsibility to pay taxes -- if not happily, at least honestly. There is no reason to believe the travel tax would not be accepted in the same way.

As to the argument that no one can live for \$7 a day in Europe let us agree, despite the appeal of the book entitled "Europe on \$5 a Day." Probably few if any can live for \$600 a year in the United States, the amount of the income tax exemption. But that exemption is not designed to provide for a moderate standard of living. It is designed to carry out the principle of progressivity, so that one earning a small amount pays little tax. So with the travel tax -- one spending modestly incurs little tax. However, even the traveler spending modestly does contribute to the balance of payments problem and therefore it is necessary that there be some restraint imposed even on his spending. The data indicate

that a modest traveler to Europe can get by on \$10 a day, in which case the tax is 45 cents a day -- certainly a contribution not likely to cause this traveler to cancel his plans. The structure of the travel tax clearly is designed not to interfere with modest travel.

Much of the criticism based on complexity and evasion involves a misconception of the tax. The tax does not require an itemization of every drink in a sidewalk cafe and every tip given to a museum guide. It does not involve the itemization of any expenditures. Therefore the picture presented by some critics of European hotel clerks busily grinding out \$3 receipts for \$25 suites will not materialize. The tax is based on the difference between the amount of money and travelers' checks a traveler leaves the United States with and the amount left when he returns. This will be the extent of the computation for most travelers. For those who use credit cards and personal checks, these amounts would be added. But no one need carry pencils and pads -- or take his accountant -- with him on his trip to Europe.

Others have criticized the requirement of a payment of estimated tax on departure. Estimated tax payments, however,

have long been a part of our income tax system. Nor should there be difficulty in arriving at an estimate. Indeed, most travelers "estimate" the expenses of their trip when they go to their bank and buy their travelers checks.

The final level of criticism is that, even accepting everything we have said about the need for a travel tax and the structure of this proposal, it cannot do the job of effecting a balance of payments savings of \$250-300 million. These critics point to the fact that the tax is applicable only to travelers outside the Western Hemisphere and, moreover, that large groups of such travelers, such as businessmen, persons visiting relatives in Europe, teachers and students, will travel to Europe despite the tax. They therefore contend that the base on which the tax can operate is only vacation travel outside the Western Hemisphere and that a base so limited is insufficient to yield the balance of payments saving we are seeking.

This criticism ignores the structure of the tax. The tax indeed assumes that most travelers to Europe will not cancel their trips but will respond to the tax by reducing their expenditures abroad. It is fair to assume that all

types of travelers will respond in some degree to the tax, either by shortening their stay by a few days or by eliminating some marginal expenses. Indeed, a traveler contemplating spending \$15 a day could absorb the entire tax, including the ticket tax, by cutting only 4 days from a 30 day trip -- if he contemplated spending \$25 a day he could cut his trip by 6 days. If the \$25 a day traveler wanted to spend his full 30 days in Europe, he could offset the tax by reducing his daily expenditure to about \$20 a day. It is therefore reasonable to believe that travelers of all types will examine their spending plans with the tax in mind. On this basis, a \$250 to \$300 million balance of payments saving out of the almost \$2 billion in contemplated travel expenditures outside the Western Hemisphere seems clearly attainable. It would represent only about a 15 percent adjustment in the anticipated 1968 foreign travel payments outside the Western Hemisphere.

It is also reasonable to expect that this will be a real savings and not produce just a transfer of the travel to countries in the Western Hemisphere. There may, of course, be a certain number of travelers who will revise their plans.

But it is clear that the existing tourist facilities in the Western Hemisphere outside of the United States will not accommodate a large amount of additional tourism.

This is the travel tax in perspective. It accepts the imperatives of our serious balance of payments situation. It is an essential part of an overall program which recognizes the need for immediate action in all the important sectors of our expenditures abroad. The tax is designed to meet equitably the need for temporary travel restraint, with due regard to all types of travelers. Its mechanics for the vast majority of our travelers are uncomplicated and can be readily understood and satisfied. It offers an essential and feasible bridge to the time when our longer-range programs to increase tourism to the United States take hold.

Critics of the measure should also accept the imperatives of our situation. The choice is not between a tax and no tax.

TREASURY DEPARTMENT
Washington

FOR RELEASE UPON DELIVERY

REMARKS OF THE HONORABLE FREDERICK L. DEMING
UNDER SECRETARY OF THE TREASURY FOR MONETARY AFFAIRS
AT THE GREATER LOS ANGELES METROPOLITAN AREA
1968 INDUSTRIAL PAYROLL SAVINGS CAMPAIGN MEETING
AT THE AMBASSADOR HOTEL, LOS ANGELES, CALIFORNIA
ON TUESDAY, FEBRUARY 27, 1968, AT 1:35 P.M., PST

I am pleased to play a part in this occasion, which looks ahead to another period of great achievement for our Savings Bonds Program -- and which sets its sights on greater Payroll Savings accomplishments in 1968.

During the past year -- largely due to the efforts of your fellow Californian, Chairman Dan Haughton of the 1967 Industrial Payroll Savings Committee -- your nationwide accomplishment surpassed the announced goal. More than 2-1/2 million employees were signed up.

Of those new 1967 bond savers: 2,410,000 are from industry; 388,539 are from the civilian rolls of Government, signed up in the Federal employees' campaign headed by Postmaster General O'Brien.

Now we are well into a new campaign year. Our 1968 program is fortunate to enjoy the leadership of Bill Gwinn -- the 1968 National Chairman of the Payroll Savings Committee.

Total sales of Savings Bonds and Freedom Shares, during 1967, came to nearly \$5 billion -- a rise of 2 percent over the previous year, and our best year in the past eleven. Gross redemptions, including interest, were down by one percent over the preceding year.

The net result -- the point that means most to us, as far as financing our deficit and adding to the savings of individuals are concerned -- was that the volume of Savings Bonds outstanding increased by over \$1.1 billion during 1967, passing the \$51 billion mark in August and closing the year at nearly \$52 billion.

I believe that those good results are a tribute to the Payroll Savings promotion that volunteer leaders like yourselves stimulate so effectively. I believe that they are also a tribute to the nationwide effort that has brought about the telling of the Savings Bonds story in thousands of plants and places of business; in union meetings and over the counters of banks; in newspapers and magazines; in radio and TV broadcasts; and in motion picture theatres.

Since the inception of the Savings Bonds Program, in 1941, it has enjoyed a remarkable blending of professional and

volunteer effort and service. This is nowhere better illustrated than by the presence and by the performance of the members of this audience.

FISCAL AND FINANCIAL BALANCE

The Savings Bonds Program is an important element in our goal of fiscal and financial balance. The \$52 billion of Savings Bonds and Freedom Shares outstanding -- held by tens of millions of Americans -- represents 24 percent of the publicly held portion of our national debt. We need the Savings Bonds Program to help finance the deficit. We need even more to reduce the deficit that needs to be financed.

Yesterday, at a similar meeting in San Francisco, I spoke of the need to bring our international payments position into sustainable equilibrium -- to eliminate or sharply reduce our balance of payments deficit. Today, I want to speak of the vital need to reduce our Federal budget deficit. We must move strongly on both points if we are to achieve sustainable economic growth at home and expand our trade and financial relationships with the rest of the world.

Fiscal Stimulus and the Economic Outlook

Let me begin by noting the relationship of the Federal

budget to general business activity. There is wide agreement today that the budget should be used as an effective stabilizing force in the economy. For stabilization purposes, the budget should move in the direction of surplus when employment is high, demand is growing rapidly, and inflation threatens. When business is sluggish, a budget moving in the other direction, with the Government spending more than it takes in, tends to provide needed support to private demand and may prevent a recession. During most of the current expansion, the Federal budgetary position has, in fact, been a stabilizing force.

In talking about the Federal budget today, I shall use two different measurements of it: one, the National Income Accounts Budget; the other, the new Unified Budget -- used for the first time in the President's Budget Message this January. The first provides the better picture of the economic impact of the Government's fiscal program; the second, a better picture of the Government's financial needs -- the amount of the deficit that needs financing.

Over time, the NIA Budget tracks the changing course of the Government's fiscal impact -- which both influences, and is influenced by, the pace of private spending and taxable income. On the expenditure side, this Budget includes Federal

Government purchases of goods and services, and other Federal expenditures such as welfare payments and grants-in-aid to State and local governments. In this respect, it closely parallels the expenditure account in the new Unified Budget.

At mid-1965, the NIA Budget was running a moderate deficit -- about \$3 billion at an annual rate. As the economy expanded rapidly, the Budget moved into balance by the end of 1965. Special fiscal measures taken early in 1966, and incorporated in the Tax Adjustment Act of 1966, reinforced an already scheduled \$6 billion rise in payroll taxes for social insurance. Thus, despite a large rise in defense spending, the NIA Budget swung into surplus at better than a \$3 billion annual rate by mid-1966 and helped to restrain the economy. Additional restraint was needed, however, and monetary policy supplied it. In retrospect, the total of fiscal-monetary restraint was about right; but, also in retrospect, the share carried by monetary policy was larger than it should have been.

The NIA Budget moved to a position of near neutrality in the Third Quarter of 1966. Special measures were taken in the early Fall to relieve the pressure in financial markets and to reduce inflationary pressures. By the end of 1966, with an inventory adjustment in process, the NIA Budget was appropriately

moving in the direction of fiscal stimulus. In the First Half of 1967, the effects of a massive inventory adjustment were cushioned by a Federal deficit on National Income Accounts of more than \$13 billion at an annual rate. In combination with monetary ease, the added degree of fiscal support kept the inventory adjustment from cumulating into anything worse.

I believe it fair to say that, from the middle of 1965 to about the middle of last year, the National Income Accounts Budget was closely geared to the state of the economy. In varying degrees, this reflected both the automatic stabilizers that are built into our fiscal system, and discretionary actions on both the tax and expenditure side. I do not contend that the discretionary fiscal actions were always perfectly timed, or precisely regulated. Those critics who are blessed with 20/20 hindsight have no difficulty in pointing to cases where a little more or less, a little sooner or later, would have been better. But, if the recent fiscal record falls short of perfection, the Budget did, in general, exert a stabilizing influence on the economy.

Since mid-1967, however, the budget position has threatened to become a destabilizing influence on the economy and credit

markets. In January 1967, the Administration recommended a tax increase to be effective at mid-1967; it has been pressing vigorously for it since last August. In the absence of action on the proposed income tax surcharge, the NIA Budget is still in heavy deficit at a time when employment is high and private demand is rising. The fiscal stimulus which was needed in the first half of last year was definitely not needed in the second half, and is even less needed now.

Prompt action on the tax increase proposals is needed. Large budget deficits in periods of prosperity and rising prices are not called for by either the "new" or the "old" economics. With the economy expected to move ahead very rapidly this year, a measure of fiscal restraint is clearly required.

With the President's tax program, the NIA Budget deficit will fall to an estimated \$5 billion average for the Calendar Year 1968 and remove much of the expansionary thrust from the Federal sector. In the absence of tax rate increases, the deficit would probably stay near the \$12-1/2 billion rate averaged in Calendar Year 1967. A deficit of this size would give the economy too strong a push from the fiscal side -- a

push that might very well throw it badly off balance.

Even with fiscal restraint, the economy will move ahead briskly -- perhaps too briskly. Business fixed investment is on the rise again. Inventory investment has been picking up. If the availability of mortgage money holds up, residential construction expenditures will rise significantly. State and local governments will be spending appreciably more. And Federal spending will also be up some -- despite close budgetary control.

All things considered, the balance of risk is that the economy will begin to exceed safe speed limits if fiscal restraint is not promptly applied. And, if the pace of the economy does begin to accelerate -- with all that it implies in terms of a more rapid rise in prices and a deteriorating trade balance -- there will have to be restraint of some sort. If it all has to come from monetary policy, the result could be a return to tight money, drastically reduced availability of credit, and imbalanced financial markets.

Financial Prospects

Currently, the cost of borrowed funds to home buyers, state and local governments and businesses, is generally at or above

the peaks reached at the height of the financial crunch in the late Summer and early Fall of 1966. In that period, the Federal Government's credit demands were contributing very little to the stringency in the money and credit markets. Since mid-1967, however, the story is different.

Most observers of the financial scene feel that a major factor in the rise in interest rates in 1967 was the Federal Government's fiscal situation. There was an immediate impact on the financial markets due to exceptionally large Federal borrowing. And participants in the financial markets also look to the future. In the absence of Congressional action on the tax increase, the future looked like "more of the same" -- continued heavy Federal borrowing, more inflation, and renewed monetary restraint.

The levels to which interest rates have risen have already forced postponement of some financial plans. As in any period of lessening credit availability, home financing faces particularly difficult problems. With the rise in yields available on market securities attracting more of the funds of individual savers, the flow of savings to financial institutions has begun to diminish -- particularly inflows of funds to

thrift institutions specializing in the financing of home construction and home purchases.

With the growth in their net savings flows declining, and with the year-end dividend and interest-crediting period approaching, fears of savings institutions mounted late last year of a repetition of the large withdrawal of funds that had occurred in mid-1966. Fortunately, the thrift institutions survived the critical year-end period without suffering massive disintermediation. But the relationship between the interest rate return these institutions can offer, and the yields available on market securities, is at a point where very much of a rise in market rates could trigger significant withdrawals of savings funds from these institutions.

Whenever there is serious concern about future inflows of funds, mortgage lenders are understandably reluctant to increase the volume of new commitments they are making for future mortgage lending. So far, loan commitments seem to have held up pretty well on a national basis, and lending institutions are in a relatively strong position. But this could change. In my opinion, prompt fiscal action to shrink the Federal deficit is still the best insurance of a continued advance in home financing and construction.

As for the general outlook for the credit markets over the months to come, given the projected GNP rise of \$60 billion or so, demands for funds by private borrowers, and state and local governments, are likely to be quite large. Just how large these demands will be will depend, of course, on a variety of factors, including the expectational and psychological climate in the economy and the financial markets. And how much of these demands can be satisfied will depend upon the demands of the Federal Government.

Why should an increase in private credit demands create such a stir in a growing economy? First, this would be an increase on top of a very hefty total last year. Second, monetary policy was relatively easy last year and is now pointed in the direction of restraint. Third, the Federal sector is making increasingly heavy demands in the credit markets and will continue to do so in the absence of fiscal restraint. It is the combination of heavy private and Federal demands for credit that threatens to strain market capacity and push interest rates still higher.

Let me sketch the dimensions of the Federal demands. Here, I am using the new Unified Budget. In the first half of

Calendar 1967, there was actually a large net repayment of debt from the Federal Government -- resulting in a \$11 billion reduction in private holdings of Government obligations (counting in participation certificates and the securities of Federal agencies, including the Federal Home Loan Banks and the Federal Land Banks). The comparable volume of repayments was only \$2 billion in January-June, 1966, and \$4-1/2 billion in January-June, 1965. But, in the second half of last year, the Federal sector made net credit demands on the private sector of some \$18 billion. This was much above the net credit demands of, roughly, \$5 billion each in the July-December periods of 1964, 1965, and 1966. For the current half year, even with prompt action on the tax bill, there will be a contra-seasonal net credit demand of \$5 billion or more.

Prospects for minimizing potential strain on money and credit markets in 1968 depend crucially on the enactment of the tax proposed by the Administration. The tax program would mean an additional \$16 billion in revenues during the remainder of Fiscal 1968 and in Fiscal 1969. Given the outlook for Federal spending, as spelled out in the recent Budget Document, and with enactment of the tax proposal, the 1968 deficit would

be about \$20 billion and, in 1969, it would fall to about \$8 billion in terms of the new Unified Budget.

Needed Federal borrowing to finance this Fiscal 1969 deficit -- including direct Treasury debt, sales of participation certificates in Government-held loans, and borrowing by Federal agencies -- would approximate the amount of the deficit. (It should be noted that under the new Budget concept this total excludes the borrowing needs of the Home Loan Banks and Federal Land Banks, as well as the funds supplied by the security purchases of the Federal Reserve System. It also excludes the financing needs to support the secondary market operation of FNMA after their assumed transfer to private ownership.)

Direct Treasury borrowing for the current half year -- that is, the last half of Fiscal 1968 -- is now largely completed with the recent one-two punch of a \$4 billion combined refunding and prerefunding of publicly held maturing February, August, and November debt with a 4-3/4 percent 7-year note, and a cash offering of a like amount of \$4 billion through issuance of a 5-5/8 percent 15-month note. Assuming the tax increase, the remainder of the Treasury's direct first

half financing needs can probably be met mainly through the additions to our weekly bill sales announced last week.

But, there is other Federal borrowing aside from direct Treasury finance. Thus, there will be some sales of both Export-Import Bank and FNMA participation certificates. The Budget calls for additional participation certificate sales of about \$2.75 billion during the remainder of the current Fiscal Year -- of which probably about \$2 billion would go to the public. In addition, there will also be some new money borrowings by several Federal agencies.

Still, the remaining Federal finance in the markets for Fiscal 1968 is not large and should put little additional pressure on the credit markets.

But, as we look beyond the next few months and into Fiscal 1969, the tax surcharge becomes the single most important factor in the Federal financing equation.

Without the proposed tax program, budget deficits would continue to be excessive from the point of view of both economic stabilization and credit markets. In terms of the new Unified Budget concept, the deficit for the current Fiscal Year would be about \$23 billion without tax action. In Fiscal

Year 1969, without tax action, the deficit might decline only slightly to about \$21 billion. Fiscal responsibility is simply incompatible with back-to-back budget deficits in Fiscal 1968 and 1969 exceeding \$20 billion.

Price Behavior and Inadequate Fiscal Restraint

I have pointed out that a large Federal deficit is inappropriate at a time of high employment and rising demand. Our recent experience with prices has shown how important it will be to keep demand within bounds this year. In 1967, we had an appreciable amount of price inflation. Moreover, the general picture was one of a much faster rate of price increase in the second half of the year, when demand strengthened more than in the first half.

Without a tax increase, there seems little question that demand would grow at an unsustainably rapid rate this year. Labor shortages would become more acute. Cost increases would more readily be passed on in an atmosphere of buoyant demand. The outlook would probably be for continuing price rises this year, but for some acceleration of the rate of advance as the year progressed. This would bode ill for the maintenance of steady and sustainable economic growth next year and after.

Even with a tax increase, the price rise will not be

stopped in its tracks. Price behavior, for a good part of this year, will still be heavily influenced by past developments. But, the tax increase would make a crucial difference by slowing the upward rise in prices and, with fiscal restraint, we should be well on our way to a less inflationary environment by the end of the year.

Conclusion

Now, I conclude by coming back to Savings Bonds. Whatever the Federal deficit will be, we need to finance as much of it as possible out of savings -- and Savings Bonds help greatly in this effort. Thus, it seems to me that our assignment -- here, today, and in the months to come -- is to build on success. That is, to follow through on the momentum built up in the banner year just ended -- in all phases of our program -- but particularly in the area of Payroll Savings, which is the reason for our meeting together.

We have a message of great personal importance to get across to those millions of Americans who are not now signed up for systematic savings plans. That message combines the common prudence of planning for the financing of family requirements, along with the patriotic opportunity to lend a

helping hand to the achievement of the affairs of the Nation.

We are most fortunate to be American citizens. The gift of citizenship endows our lives with privileges that are priceless. But good citizens don't just sit down and hug themselves over how lucky they are to be Americans. They know that it takes a lot of working; sometimes a lot of fighting.

The materiel of modern warfare comes high by the price tag. That's part of the penalty of protecting freedom. That's one of the costs of citizenship.

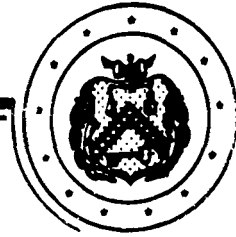
Let's remember that behind the fighting line and the supply line, there's the dotted line -- where we sign up to buy Savings Bonds and Freedom Shares to help support the valor of our servicemen in Vietnam.

As a great public program, our joint venture in U. S. Savings Bonds has become the envy of the world. Nowhere else is there anything quite like the companionship of banking, business, education, Government, industry and labor that blesses our endeavor together.

As a great nation, we've come a long way together, and together we can meet and master any challenge to our integrity, our prosperity and our security.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

February 28, 1968

FOR IMMEDIATE RELEASE

TREASURY'S WEEKLY BILL OFFERING

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$2,600,000,000, or thereabouts, for cash and in exchange for Treasury bills maturing March 7, 1968, in the amount of \$2,501,467,000, as follows:

91-day bills (to maturity date) to be issued March 7, 1968, in the amount of \$1,600,000,000, or thereabouts, representing an additional amount of bills dated December 7, 1967, and to mature June 6, 1968, originally issued in the amount of \$1,000,639,000, the additional and original bills to be freely interchangeable.

182-day bills, for \$1,000,000,000, or thereabouts, to be dated March 7, 1968, and to mature September 5, 1968.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$50,000, \$100,000, \$500,000 and \$1,000,000 (maturity value).

Tenders will be received at Federal Reserve Banks and Branches up to the closing hour, one-thirty p.m., Eastern Standard time, Monday, March 4, 1968. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e. g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve Banks or Branches on application therefor.

Banking institutions generally may submit tenders for account of customers provided the names of the customers are set forth in such tenders. Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guaranty of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve Banks and Branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$200,000 or less without stated price from any one bidder will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank on March 7, 1968, in cash or other immediately available funds or in a like face amount of Treasury bills maturing March 7, 1968. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under Sections 454 (b) and 1221 (5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418 (current revision) and this notice prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve Bank or Branch.

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TREASURY DEPARTMENT



WASHINGTON, D.C.

February 29, 1968

FOR IMMEDIATE RELEASE

The Joint Commission on the Coinage will meet Friday, March 1, at 10:00 a.m. in room 4121 of the main Treasury Building, Washington.

The purpose of the meeting will be to review the coinage and silver situation since the Commission's last meeting on September 18, 1967. It is expected that discussions will include a review of coinage production, inventories of coins and silver, silver prices, silver sales, and the redemption and retirement of silver certificates.

The Joint Commission on the Coinage, created by the Coinage Act of 1965, consists of 24 members, including 12 from the Congress, four from the Executive Branch, and eight public members. Secretary of the Treasury Henry H. Fowler is Chairman.

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