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FEDERAL EXPENDITURE POLICIES FOR
ECONOMIC GROWTH AND STABILITY

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OF THE

SUBCOMMITTEE ON FISCAL POLICY

TO THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES



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LETTER OF TRANSMITTAL

JANUARY 23, 1958.

Hon. WRIGHT PATMAN,
*Chairman, Joint Economic Committee,
House of Representatives, Washington, D. C.*

DEAR SIR: Transmitted herewith is a report by the Subcommittee on Fiscal Policy on Federal Expenditure Policies for Economic Growth and Stability. The report presents the subcommittee's findings and conclusions based upon its hearings and study undertaken pursuant to the recommendation of the full committee in its February 28, 1957, Report on the January 1957 Economic Report of the President.

Representative Thomas B. Curtis and Senator Barry Goldwater join me in presenting this report. Senators Paul H. Douglas and Joseph C. O'Mahoney also participated in the planning and formulation of the study and hearings. They have approved the transmission of this report to the committee but could not participate in its preparation.

Sincerely,

WILBUR D. MILLS,
Chairman, Subcommittee on Fiscal Policy.

FEDERAL EXPENDITURE POLICIES FOR ECONOMIC GROWTH AND STABILITY

INTRODUCTION

The Joint Economic Committee, in its February 28, 1957, report to the Congress (H. Rept. No. 175, 85th Cong., 1st sess.) suggested the desirability of a study of Federal expenditure programs in terms of their impact on the level of economic activity and the standards for public expenditures to promote overall economic growth in the long run. In June 1957, the Subcommittee on Fiscal Policy undertook an examination of the fiscal policy implications of the economic outlook and budget developments in fiscal 1958. The subcommittee's report (H. Rept. No. 647, 85th Cong., 1st sess.) pointed up the need for a thorough inquiry into the substance of current Federal expenditure policies in order to appraise their consequences for the economy's growth and stability.

On the basis of these suggestions, the subcommittee initiated its study of Federal expenditure policies and their relationship to the attainment of the Employment Act objectives. In the course of its study, the subcommittee invited and received the assistance of experts from business, labor, research groups, universities, and Government. These participants prepared papers on various aspects of the subcommittee's inquiry, which were printed and distributed to subcommittee members, participants, and the general public in early November. Hearings were held November 18-27, during which participants and the subcommittee developed more fully the problems and issues raised in the printed papers.

The subcommittee has not attempted to make specific recommendations with respect to particular Federal spending programs. Determination of these programs is the function of various legislating committees of the Congress. This statement, instead, sets forth broad principles to assist in the formulation of Federal expenditure policies in the light of the Employment Act objectives.

FINDINGS AND CONCLUSIONS

Meeting the challenge presented by Soviet advances in science and technology emphasizes but does not alter this Nation's basic economic policy objectives. Clearly we must improve our defense efforts. The more fundamental test, however, is to demonstrate our capacity to provide the military competence needed to deter war and the economic competence needed to maintain and improve our standards of living. A high rate of economic growth, unhindered by inflation or recession, is the principal requisite for successfully meeting this challenge.

Increasing emphasis on economic growth necessarily focuses attention on Federal expenditure policies. The Federal Government is the largest industry in the United States. Its direct purchases of goods and services account for a substantial share of the economy's total output; its effects on the amount and character of economic activity are even greater than can be indicated by any such statistic.

In part, these influences stem from the means by which the Federal Government's activities are financed. This subject was extensively investigated in 1955 by the Subcommittee on Tax Policy of the Joint Economic Committee in its study of Federal tax policy for economic growth and stability. The character and extent of the Federal Government's spending activities, however, may be of even greater consequence.

The Joint Economic Committee and its subcommittees, under the mandate of the Employment Act of 1946, must be concerned primarily in all of their inquiries with the impact of Government activity on attainment of the Nation's basic economic policy objective: A high rate of growth in productive capacity with minimum fluctuations in the rate of resource use and in the general price level. The Subcommittee on Fiscal Policy recognizes that many other considerations enter into determination of the scope and character of the Federal Government's activities, and that in many instances such considerations must be ruling. Nevertheless, we cannot ignore the economic consequences of any Government spending policy if we are to be sure that Government will most greatly enhance or least interfere with the conditions requisite for steady economic progress.

1. Increasing the effectiveness of our national defense in the years ahead very likely will result in rising defense expenditures

Developments since mid-1957 once more dramatically point up the extremely rapid rate of obsolescence of military plant and equipment. Weapons regarded as highly advanced today become conventional tomorrow and outmoded the day after. Indeed, since considerable time necessarily must elapse between the stages of conception, planning, and production of new weapons systems, the lag between recognition of the type and amount of preparations required to maintain our national security and actual accomplishment always must be substantial. A lag reflecting continuing, rapid progress in science and technology and alertness to the military implications of such advances is evidence of the fundamental strength and soundness of the Nation's efforts to deter war. On the other hand, any lag between conception and achievement stemming from rigidity in planning and programing defense efforts must be regarded as a serious weakness in the Nation's defense preparations.

The Soviet Union has demonstrated not only its capabilities in science and technology but its determination to exploit achievements in these fields for military purposes, regardless of the costs involved in terms of material living standards and amenities for the Russian people. Moreover, the rapid rate of Soviet economic growth (as shown in the study, *Soviet Economic Growth: A Comparison with the United States*, prepared for the Subcommittee on Foreign Economic Policy of the Joint Economic Committee by the Legislative Reference Service of the Library of Congress, July 5, 1957) indicates that such costs may be reduced significantly in the future. Soviet progress in the military applications of scientific and technological advances, rather than domestic considerations, determines the floor under defense efforts in the United States.

Maintaining the superiority, or at least equality, in military capacity upon which the Nation's survival well may depend precludes settling upon any given complex of weapons systems as ultimately satisfying our defense requirements. Research must be expected continually to reveal the obsolescence of weapons even before their production, and indeed should be directed toward that end. To the extent that such research is successful, it should be expected to accelerate the rate of obsolescence and to result in an increasingly complex defense technology. These factors underlie the prospect of rising defense outlays.

2. The prospect of higher levels of defense spending raises no serious questions about the capacity of the economy to meet these demands

In the broadest sense, the amount of resources we can afford to devote to national defense depends on the benefits to be derived compared with the real output for nondefense purposes which must be given up in order to achieve them. The benefits of an adequate defense program lie in prevention of the loss of life and property which would result if a lack of military capability by the United States led to the outbreak of war. Since such benefits are incalculably great, there can be little question that whatever level of defense effort, attainable in real terms, is required to deter aggression is clearly economical.

It is virtually impossible, on the basis of objective standards, to determine the specific limits of defense spending which can be accommodated without major adverse consequences. Our experience during World War II, the Korean crisis, and the entire postwar period has demonstrated the enormous flexibility of the economy and the tremendous reserves of resources which can be mobilized to meet extraordinary demands.

Present defense expenditures, in fact, are absorbing about 10 percent of the Nation's total output. A mere continuation of the postwar trend of growth in real output would alone make possible substantial annual increases in our defense program without materially increasing the proportion of total resources allocated to this end. A 20-percent increase in annual defense outlays, for example, would require less than two-thirds of the annual increase in the economy's total output which we can expect if the postwar rate of growth is maintained. The extent to which our defense preparations can be enlarged and made more effective will be limited, if at all, by difficulties in reallocating resources rather than by inadequate economic capacity.

Maintaining and accelerating our economic growth is thus the basic step required for minimizing over the long run the real costs of increasingly effective defense preparations. An expanding and increasingly diversified productive capacity affords the best assurance that the rapidly changing requirements of national security can be satisfied promptly. The skills and achievements in science and technology upon which our national security depends are also the basis for an increasing capacity to produce a greater volume of more widely diversified nondefense goods and services. Efforts to strengthen the foundations of rapid economic growth and to enhance our defense capabilities are not only consistent, but serve to reinforce each other.

3. National-defense requirements should guide rather than depend upon decisions concerning the level and composition of other Federal spending programs and the evaluation of revenue prospects and requirements

Considerations of economy in our defense programs must originate in the continually changing requirements growing out of our own accomplishments and those of a potential aggressor. Determining defense preparations on this basis calls for a high degree of flexibility in planning and programing which may be seriously impaired by rigid budgetary ceilings on defense outlays.

A flexible budget approach to defense spending does not imply relaxation of efforts to increase efficiency in defense preparations. The prospect of rising defense costs, on the contrary, emphasizes the necessity for (1) eliminating superfluous activities of the Defense Department, particularly those which private enterprises can as efficiently undertake; (2) improving the organization of defense activities, particularly in the research and development areas in order to eliminate wasteful duplication of effort and competition for highly specialized research resources and to assure greater continuity in effort; (3) improving procurement practices to assure minimum-cost production of defense materiel; and (4) revision of personnel policies to minimize costly turnovers. Specific positive efforts along these and similar lines offer far greater assurance of achieving greater efficiency in the defense program than do rigid budget ceilings on outlays.

4. Proposals for fiscal action to offset currently developing slack in employment and plant and equipment use should take account of the possibility of a delayed increase in defense outlays

Under present circumstances, expansion and improvement of the Nation's defense efforts may not be fully and immediately reflected in estimated budget expenditures for fiscal 1959. Development of new weapons, upon which we increasingly must concentrate, requires a substantial investment of time as well as of the most highly skilled and specialized human and material resources. The bulk of the rise in actual defense spending, therefore, may be delayed, but should not be disregarded in formulating fiscal policy.

Although present economic conditions appear to call for relaxation of fiscal and monetary restraints, the effects in 1958 of expansion of defense efforts and defense-associated activity in the private sectors of the economy on total employment and production cannot yet be clearly ascertained. Moreover, the overall budgetary effect of the changes to be made in other Federal spending programs, in response to changing defense demands, is similarly unclear at this time.

Until these trends can be appraised more clearly, economic stabilization policy should rely on expansionary monetary and credit actions which can be quickly reversed should inflationary pressures again become dominant. Tax reductions enacted prior to determination of budgetary and economic trends well might require at a subsequent date tax increases or reimposition of severe monetary restraints to prevent further sharp rises in the general price level. Should it appear, upon appraisal of these trends, that monetary action alone is inadequate to contain persistent recessionary pressures, tax reduction would be in order. The extent of any such reduction should give due consideration to revenue needs to meet projected outlays, and to provide some surplus, at income levels which may be expected when the present slack in employment and production is eliminated.

5. Whether or not tax reduction will be called for, tax revision always is timely.

Emphasis in any tax-revision program should be on eliminating or restricting those provisions of the tax laws which tend to offset the resource-allocating signals of the market mechanism. Preferential provisions in the Internal Revenue Code which substitute tax considerations for those of the market place result not only in inefficient resource use, but also in increasing complexity and unfairness in assignment of tax burdens. Constructive tax revision aimed at greater neutrality in the impact of our revenue laws on the ways in which taxpayers use the resources at their disposal has become more urgent than ever in light of the new challenges currently confronting the Nation.

Improvements in the Federal tax system, along the lines suggested by the Subcommittee on Tax Policy of the Joint Economic Committee in its report, *Federal Tax Policy for Economic Growth and Stability* (S. Rept. No. 1310, 84th Cong., 2d sess.), should be one major objective of fiscal policy aimed at improving the conditions for economic growth. An equally important objective should be revision of Federal spending programs in light of the demands originating in changing defense and defense-related activities and the changing conditions and opportunities for economic growth. Whether or not nondefense spending by the Federal Government can or should be reduced to match increases in defense outlays is of secondary importance compared with efforts to attain the greatest possible economy in Government.

6. In view of the increasing importance of expanding productive capacity as the foundation for more effectively meeting our requirements for national security and leadership of the free world, economic growth consequences should be a major criterion in the formulation of Federal expenditure policies

The impact of Federal spending programs on the availability of resources to other sectors of the economy has significant consequences for the rate and direction of overall economic growth. In applying the economic-growth criterion, therefore, the basic test is whether some or all of the resources required by a Federal expenditure program would contribute more to the economy's total product in some alternative use. Since not all of the products, benefits, and costs of many Federal spending programs are immediately and directly realized, the long-run and indirect consequences of these programs, as

well as the more immediately observable effects, should be carefully evaluated.

7. Economy in Government should be measured by the relative benefits and costs of each program rather than by reference merely to amounts spent

The subcommittee has found no necessary relationship between the amount of Federal expenditures and the rate of economic growth over the long run. A far more important factor appears to be the character of Federal activities and their impact on the setting in which private economic activity must take place. Economy in Government, therefore, involves changing priorities in Federal Government activities, at times requiring expansion of some Federal programs while reducing others, in response to changing circumstances. Based on the test of alternative-resource use, this is a major means through which the Federal Government can contribute to the Nation's economic growth.

Evaluation of many Federal spending programs aimed at broadly expressed social and political objectives on the basis of their comparative benefits and costs is admittedly difficult. The distinguishing characteristics of these programs is that their benefits cannot be fully measured by objective standards such as those provided by the market mechanism. While the costs of these programs can be readily ascertained, their relative values must be determined through the political process by those invested with responsibility for formulating and enacting Federal spending programs. These value judgments should be based on as full awareness as possible of the indirect as well as direct economic effects of the programs, whether or not these effects are immediately related to the program's objectives, and to the greatest extent possible should be arrived at in the light of the comparative costs of all expenditure programs. Broad social objectives frequently are referred to as "needs," but it should be clear that needs are relative rather than absolute. Determining the priority of programs to meet these objectives must give careful consideration to their relative costs.

Other Federal programs, such as those in public works and natural-resource and regional development, should present far less difficulty in measuring benefits. Such programs long ago were established as appropriate activities of the Federal Government where their objective is to eliminate barriers to or provide the stimulus for fuller, more effective resource use and where the means required for realizing these objectives exceed the financial capacity of immediate beneficiaries. Whether any specific project is to be undertaken, however, should be determined by appraisal of measurable economic benefits in comparison with the project's cost. A project which does not promise a rate of return at least equal to that available on the average throughout the economy cannot be justified on economic grounds. The use of lower interest rates in benefit-cost analysis results in a higher level of Federal public works expenditures than would be justified on the basis of most effective resource use. Uneconomical use of resources also results from including in expected benefits those which represent merely transfers from existing facilities, rather than net additions to total productivity.

8. *Federal programs aimed at supporting or improving the economic position of particular groups or industries should be constantly reevaluated in the light of changing circumstances*

Whatever their initial justification, subsidy programs should be so contrived as to eliminate the necessity for their continuation. The broad changes which must be expected in our economy require frequent revision in the scope and character of these programs if they are to achieve their purposes. Failure to adapt the substance of subsidies to changing demands and opportunities may be expected to prevent most efficient use of resources in the subsidized activities as well as in other types of economic endeavor. Where this is the case, the subsidy not only fails of its immediate objective but also imposes real costs on the entire economy over the long run.

Preferential tax provisions and provision of Government services at less than cost, no less than direct Federal outlays, serve to subsidize the activities involved. Frequently, however, neither the cost nor the benefits sought by this type of subsidy can be readily determined. An important basic step for improving these programs, therefore, is to provide for the clearest possible exposition of their purpose and substance.

9. *The alternative-resource-use test also should be applied to Federal programs which involve no significant Federal expenditures*

Federal enterprise activities and programs for insurance and guaranty of private loans generally involve very little net budget expenditures but may, nevertheless, exert a powerful influence on the ways in which resources are used in the private and State and local government sectors of the economy. Rigorous analysis and appraisal of these influences is all the more important in determining the scope and character of this type of Federal program since they are not significantly subject to the budgetary discipline.

Elaboration and refinement of statistical materials and procedures can make a major contribution in improving the accuracy and completeness of benefits and cost measurement. In this respect, favorable action on the recommendations made to the Joint Economic Committee's Subcommittee on Economic Statistics in its hearing October 29 and 30, 1957, on the national economic accounts of the United States, would represent a low-cost investment promising a very high rate of return measured in greater economy in the Federal Government.

10. *Recognizing that economic considerations may not always prevail in determining Federal expenditure programs emphasizes the need for carrying out these programs at minimum real cost*

Maximizing efficiency provides assurance that, whatever the grounds upon which its priority depends, any Federal spending program will impose the least possible limitation, in terms of availability of resources, on activity in other sectors of the economy. In the interests of increasing efficiency, Federal programs should be channeled, wherever possible, through the market mechanism to take advantage of the objective tests of efficiency in resource use provided thereby. In many cases, more extensive application of operations research and analysis may return substantial dividends in the form of resource-saving methods and improved performance standards.

Greater efficiency in Government operations, however, should not be regarded as a substitute for improvement in the formulation of

programs and their objectives. Highly efficient performance of uneconomical programs will not contribute to the Nation's economic development.

11. *Federal expenditure policies closely geared to the Nation's economic growth objectives must provide for as rapid adjustment as possible in spending programs in response to changing demand and supply conditions*

The essence of a dynamic economy is frequent and rapid change in demands and in methods of production. Such changes result in shifts in the relative value of alternative uses of productive resources. Impediments to prompt change in resource use in response to changing economic opportunities result in loss of efficiency and of total product for the economy as a whole. Rigidities in Federal spending programs may limit significantly the economy's growth potentials.

A considerable volume of evidence showing the inflexibility of many major Federal spending programs was presented to the subcommittee in its hearings in June 1957 on fiscal policy implications of the economic outlook and budget developments and in its November 1957 hearings on Federal expenditure policy for economic growth and stability. A number of these programs have an upward bias as a result of specific features in their statutory authorization, which result in their continuing expansion even under conditions in which decreasing importance is attached to them. Even more adverse consequences result from a fiscally perverse spending program which increases or decreases directly with increases or decreases in earmarked revenues. This type of program adds to inflationary pressures when boom conditions swell tax receipts and accelerates declining demand when receipts shrink under recessionary conditions.

12. *Flexibility in Federal expenditure programs has important implications with respect to the stabilization objectives of the Employment Act*

Periods of boom and recession generally are characterized by changes in the relative economic and social priorities accorded by the economy as a whole to alternative resource uses. Greater flexibility in spending programs, therefore, would permit more expeditious reduction in those public functions of decreasing priority in periods of rapid expansion of economic activity. By the same token, it would more readily permit expansion of those public services and functions subject to increasing demand should a decline in private expenditures serve to free the required resources.

Across-the-board changes in Federal expenditures in response to changing levels of overall economic activity, on the other hand, can be expected to contribute to economic stability only at the cost of misallocation of resources. Changing demand and supply conditions will not uniformly affect the desirable level of every Federal spending program. While minimizing inflationary pressures well may require some—possibly substantial—reduction in Federal spending, it does not follow that each Federal spending program should bear a proportionate part of any overall reduction. By the same token, increasing all Federal expenditures in the same proportion to offset recessionary pressures would result in highly uneconomical or wasteful uses of productive services. The extent to which the Federal Government changes the level of spending for any program during a recession or a

boom, therefore, should be determined on the basis of changes in economic and social priorities.

13. Tax and monetary policy should be relied upon to bear the major brunt of achieving economic stabilization objectives

The effects of many Federal spending programs on levels of total economic activity do not necessarily coincide closely in time with actual expenditures. While adjustments in Federal spending programs are essential in response to long-run changes in economic conditions, they are much less suited to leveling out short-run fluctuations. The subcommittee's hearings in June and in November 1957 confirmed the view that economic stabilization efforts should rely initially on general monetary and credit actions. For major, long-term growth and stabilization requirements, changes in tax rates should be related to changes in levels of Government expenditures by the need for full utilization of growing productive resources and stability in the general price level.

14. The scope and character of Federal spending programs should reflect, wherever possible, the comparative economic advantages of the Federal, State, and local governments and of private enterprise in achieving program objectives

The dynamic qualities in the Nation's political and economic development have resulted in frequent changes in the relationships among the Federal, State, and local governments, and between the public and private sectors of the economy. No clearly established division of responsibility for satisfying changing demands has emerged in this development. This flexibility, while possibly posing the danger of undue concentration of power at the Federal level, also may be a major source of strength in the economy, since it affords assurance that changing demands for services in response to changes in conditions required for economic growth need not be frustrated by institutional barriers.

The nature of the problems and objectives giving rise to many Federal programs precludes substantial and effective non-Federal participation. On the other hand, many types of activities performed by the Federal Government also can be and are performed by State and local governments and in the private sectors of the economy. Apart from the generally recognized social and political virtues in minimizing Federal responsibility for such functions and activities, considerations of the economy's growth potential also require Federal programs to be so formulated as to give non-Federal organizations every opportunity to determine whether they can efficiently participate in achieving the desired objectives.

15. Failure of State and local governments and private enterprise to recognize and to respond quickly to new demands must be expected to result in public pressure for the Federal Government to expand its activities

The historical record shows that the public has turned readily to the Federal Government when other agencies failed to meet new or expanded demands, and that the Federal Government has not been able to defer very long taking the action demanded of it. Revision and expansion of educational programs and of basic research efforts are the most important cases in point at the present time. The signifi-

cance of these programs for the Nation's defense preparations and for economic growth has suggested to many the occasion for Federal Government action. The prospect for such pressures was stressed by the Subcommittee on Economic Stabilization of the Joint Economic Committee in its 1955 study of automation and technological change. The subcommittee pointed out, however, that first responsibility for meeting the demands for technical and scientific skills should fall upon local communities and upon the individuals and businesses interested in such competence.

These and similar programs are those in which a major role of the Federal Government, in the past, has been to stimulate activity in the non-Federal sectors of the economy. Whether that role now is to be substantially expanded well may depend on the speed with which agencies other than those of the Federal Government respond to the new and rapidly increasing demands.

16. *Federal participation in activities shared by State and local governments and private enterprise should be aimed primarily at improving the effectiveness of these activities and should avoid merely transferring responsibility for them to the Federal Government*

In the field of education, for example, the basic objective is to improve the quality of curriculum and instruction at all grade levels as well as to increase the number of teachers, classrooms, and enrollments in advanced institutions.

Achieving this objective will require reappraisal and revision of the basic substance of educational programs at the elementary, secondary, and advanced levels. Although these revisions will not be achieved merely by increasing expenditures, they should be expected to result in rising costs, since they will require relatively more and better resources than now are available. In view of this prospect, efforts to improve education programs should seek every possible opportunity to exploit technological advances. The use of television as a means of supplementing present instructional techniques, for example, suggests numerous other low-cost, high-return capital outlays which might well be made, particularly at the secondary and advanced levels of education. More intensive use of existing school plant and equipment may also serve to reduce the real costs of expansion and improvement of the Nation's education programs.

There is no evidence that the extent of the increase in these costs depends significantly on whether responsibility for improving educational programs is assigned to the Federal, State, or local governments or to the private sector of the economy. The role of the Federal Government in this effort, therefore, should be determined on other grounds.

Some of the participants in the subcommittee's study urged greater Federal responsibility for educational programs on the basis that the extra demands on resources in education arise from national rather than local requirements. Whether the national interest in education is greater than, or even different from, that of the States and localities cannot be objectively determined. In any case, since the real costs of the desired improvements will not be materially affected by shifting responsibility, greater financial participation by the Federal Government, if deemed necessary, should avoid obscuring these costs lest

States and localities be encouraged to divert their resources to programs of lower social priority, with a consequent loss to the economy as a whole.

Statutory and constitutional provisions limiting their financial resources may inhibit States and localities from promptly assuming increasing responsibility for public functions. Such limitations cannot be realistically ignored in the formulation of Federal expenditure policies. Where these are the principal constraints faced by State or local governments, however, the efforts of the Federal Government should be directed primarily toward the development of an expanded fiscal capacity at the State and local level.

Very much the same considerations are involved in the case of improving and expanding research activities. The subcommittee's hearings brought out the fact that a major obstacle to more effective research programs is the difficulty in establishing criteria for the allocation of highly limited and specialized research skills and equipment. It is agreed generally that a significant expansion of research efforts is required. Success in this respect, however, depends at the outset on improving the organization of research resources and their allocation into more productive lines of inquiry. Merely providing substantial increases in Federal outlays for these programs may serve only to transfer available research skills and facilities from the private sectors of the economy to the Federal Government, without materially improved results. Such competition may, in fact, disrupt current research efforts in which the Federal Government has a major interest.

The subcommittee's study brought out clearly the importance of expanding activity in pure research as the basis for continued technological advance and, therefore, economic growth. The study also revealed the limitations on present knowledge concerning the conditions and incentives necessary for long-run expansion of pure research efforts. It seems clear that over much of the period of this Nation's industrial development, the complex of patent laws, the tax system, and other institutional arrangements provided a setting highly conducive to rapid exploitation of applied research and developmental activity. Further study and analysis is required to determine the adequacy of these arrangements under today's conditions, and more particularly, to determine whether these arrangements are consistent with the growing requirements for pure research.

A number of the participants in the subcommittee's study maintained that, in view of the highly uncertain results, it is unlikely that private enterprise can be expected to undertake of its own initiative a major part of these pure research activities. However significant this limitation may be, it does not necessarily follow that merely enlarging research establishments within the Federal Government will achieve the desired objective. A necessary first step is determining the present availability and use of research talent and facilities in business, the universities, private research organizations, and at all levels of government. Federal research programs should seek closer integration and better organization of research activities. Such improvements are fundamental in assuring the greatest possible productivity from any increase in Federal research outlays.

17. *Business-type activities of the Federal Government should be subjected to frequent review to determine the possibilities of their effective performance by private enterprise*

The subcommittee's hearings brought out an extensive inventory of Federal Government activities of an essentially private-enterprise character. The dollar total of the net costs of such programs may be regarded as relatively insignificant when measured against total budget expenditures. The implications of these activities concerning the appropriate relationship between the Federal Government and the private sectors of the economy, however, warrant their careful consideration.

Some of these Federal enterprises were originated during the depression of the 1930's in order to stimulate economic recovery by developing new markets, often through subsidies of a particular type of production or consumption, and by reducing risks for a wide variety of private enterprises. The relative importance of these Federal activities should be assumed to have been significantly affected by the substantial changes in economic conditions occurring during World War II and the postwar period and should be frequently reappraised in light of the Nation's continuing economic development and progress.

Some business-type enterprises of the Federal Government are intended to prevent private monopolization of activities for which the most efficient scale of operation precludes a profitable multifirm industry. Federal responsibility in such cases permits the economy as a whole to realize the benefits of optimum-size enterprise without the dangers inherent in private monopolies. Since these conditions are difficult to determine objectively in advance of actual experience, and since Federal enterprise well may preclude subsequent private participation, Federal ventures in this area should assume the burden of proving their necessity on the grounds of basic economic obstacles to successful, competitive private enterprise.

Another category of Federal enterprise includes those which developed from pilot projects for product or resource development in which private enterprise, either because of lack of knowledge or because of alternative investment opportunities, was not interested. Continuation of Federal participation in such activities after substantial private development has occurred may be justified on the grounds of protecting the public interest, particularly from the danger of undue private concentration of production and distribution control. In such cases, the possibilities of developing a broader private market for the disposition of the facilities or effective regulatory practices which do not require continuation of the Federal enterprise should be explored.

Whether or not the Federal Government should continue or withdraw from any enterprise activity must be determined on the basis of the considerations relevant to each case. The Employment Act objective of promoting vigorous private enterprise, however, calls for continuing reexamination of these Federal functions to minimize any constraints they may impose on opportunities for private enterprise.

18. *Budget procedures should be revised to show more clearly the economic effects and costs of Federal Government programs*

The Federal budget is more than an accounting statement of proposed outlays and anticipated receipts. It is the principal instrument which those responsible for formulating and enacting expenditure policy must use to: (1) evaluate and compare alternative public programs on the basis of a wide range of criteria, including that of promoting economic growth and stability; (2) determine the type of program best suited to meeting public demands; and (3) make sure that those programs which are adopted are carried out in the most efficient manner possible. The extent to which real economy and efficiency can be achieved in the Federal Government, therefore, depends on the effectiveness of the budgetary process.

19. *Effective budgetary procedures should provide adequate information concerning the objectives and substance of the expenditures to be made by the Federal Government*

The regular course of the legislative process very often suffices to develop the salient features of new spending proposed for the Federal Government. In the case of continuing expenditures, however, issues concerning their basic substance and purpose may be obscured by concern with details. Without a clear analysis of the purposes to be served by such expenditures and their past effectiveness in achieving these purposes, there is no basis for informed judgment about their relative value and the consequent priority in command over resources to be accorded them.

20. *The budgetary process should show how the various activities of the Federal Government are related to each other on a program basis, and how these programs are related to similar activities outside of the Federal Government*

Responsible decisions about the desirability of specific expenditures or appropriations requested by any agency of the Federal Government hardly can be made in the absence of information about similar activities elsewhere in the economy. Instances of Federal agencies working at cross-purposes or in duplication of each other's efforts or those of private enterprises, the States, or localities, continually are brought to the attention of the Congress. While considerations of effective administration call for presentation of expenditures on an organizational basis, considerations of economy in Government, calling for budgetary exposition on a program basis, are at least equally important.

Moreover, program analysis should include Federal activities which lie outside the budget. Activities of Federal corporations, trust funds, and those financed by counterpart funds may have important consequences for other Federal programs more explicitly set forth in the budget. Failure to relate these extrabudgetary activities to budget programs can impair the effectiveness of both.

21. *Budget decisions should be based upon a clear recognition of the longer range prospects for Government programs in terms of their costs and objectives*

Current procedures concentrate attention on the single fiscal year covered by the budget despite the fact that most Federal expenditure programs are designed to continue over substantially longer periods

of time. Economy in Government, in the sense used throughout this report, requires evaluation of the long-run resource requirements and benefits of spending programs. The initial-year requirements of many programs may appear to be insignificantly small, although their eventual cost may substantially exceed the benefits to be derived. In the absence of analysis of these long-run prospects, there can be little assurance that alternative programs will be properly weighed.

Greater emphasis in the budgetary process on the long-run costs and objectives of Federal programs would also facilitate determination of the conditions under which programs can be reduced or terminated. Relatively explicit statutory provisions to this effect would, at the least, provide the basis for thorough periodic appraisals of the substance of Federal Government activities.

22. Budgetary procedures should provide an objective analysis of the likely effects of Federal programs on the overall level of economic activity, employment, prices, and opportunities for and limitations upon investment and other growth-generating activities in the private and State and local sectors of the economy

The budget should set forth clearly the types of adjustments which may have to be made if the basic continuing objectives of the Employment Act are to be achieved. It is recognized that economic effects may be of minor significance in determining the relative importance of specific programs. Nevertheless, these factors cannot be ignored in the budgetary process if economic policies of the Federal Government are to be mutually consistent and are to contribute to a high rate of economic growth with minimum fluctuations in the rate of resource use and in the general price level.

In many cases, particularly where long lead-time items are involved, the economic impact of Federal programs is not clearly or accurately reflected by estimates of budget expenditures. In such cases, budget expenditures represent the culmination of the economic activity set in motion by the placing of a Government contract. In the current situation, for example, substantially expanded efforts in the missiles and other technologically advanced defense programs will be reflected only partially in proposed defense expenditures for fiscal 1959, although such efforts may have major immediate consequences for the level and type of activity in important sectors of the economy. Accurate and complete analysis of the economic effects of such Federal programs requires information concerning levels of contract activity as well as expenditures. Budgetary procedures, therefore, should provide data concerning the proposed rate of use of obligational authority. Development of statistical series on the use of obligational authority would materially aid evaluation of the influence of Federal programs on the economy.

23. Budget procedures should describe the plans and methods which are to be used to achieve greater efficiency in carrying out the functions proposed in budgeted programs

In the absence of fairly explicit, positive proposals to this end, there is a tendency to seek greater efficiency through blanket reductions in the amount of funds made available. Such actions, however, run a considerable risk of undermining the effectiveness of spending programs without eliminating the basic sources of inefficiency.

24. *Finally, achieving the economies and increased efficiency in the Federal Government required to meet the challenges now facing the Nation demands vigorous leadership by the executive branch and cooperation by the Congress and the public*

Explicit proposals for revision of specific spending programs should be presented to the Congress in the President's budget message and supporting statements. Such proposals should be supported by a detailed appraisal of the relative merits of existing and proposed programs.

