between the full year 1965 and 1966, but by only 1.7 percent between December 1965 and 1966, reflecting the downward trend that developed after midyear.

While there were signs that price pressures were abating by late 1966, labor costs per unit of output in manufacturing—and in other major sectors—were drifting upward. This, too, marked a departure from virtual stability earlier in the expansion. As yet, the increases are moderate by comparison with earlier expansions. However, it is essential to achieve an early restoration of cost stability in order to avoid a further push on prices.

We expect the more moderate advance of the economy this year to relieve selective pressures and provide the environment within which a transition to better cost-price performance can proceed. And, the Government will continue its other efforts to relieve cost-price pressures—through its training and employment service program, and in the areas of procurement, stockpile disposal, and farm programs.

But efforts of the Government alone will not be enough. As President Johnson has stated in his economic message, improvement will require the responsible conduct of those in business and labor who have the power to make price and wage decisions.

Before turning to a discussion of the balance of payments, I would like to take note of the recent study by your Subcommittee on Economic Progress entitled "U.S. Economic Growth to 1975: Potentials and Problems." Your committee is extending its record of involvement with important economic issues. As I indicated in my remarks at a Loeb Award luncheon last May, our rate of overall economic growth must increasingly rest almost entirely upon the rate of growth in quantity and quality of new capacity and new manpower. Therefore, your study—and others—of our growth potential is welcome indeed.

Balance of Payments

While full information on last year's balance-of-payments results will not be available for several weeks, I can outline the general picture. Our "liquidity" deficit last year was somewhat over $1.4 billion—roughly $100 million more than in 1965. This minor increase must be viewed against the far greater rise in *direct* foreign exchange costs associated with Vietnam—in the general order of magnitude of $950 million—not to mention the increase in *indirect* balance-of-payments cost in the form of additional imports resulting from higher defense spending at home.

Our "official settlements" balance, in contrast, actually showed a slight surplus of about $175 million on the basis of preliminary figures—the first surplus since 1960 when we first kept figures on this basis. This surplus was attributable to heavy borrowings from abroad by U.S. banks and the consequent accumulation of liquid dollar claims by foreign commercial banks, including foreign branches of U.S. banks. It reflected the tight credit situation in the United States and the unsettled condition of sterling during part of the year.

Ordinarily many of these dollars would have moved into foreign official reserves and some of them would possibly have been converted into U.S. gold. As it was, our gold loss for the year was $571 million, in contrast to $1.4 billion in 1965, excluding the $259 million gold payment in connection with the increase in IMF quotas.