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Comments:

OMB Letter on
Budget Resolution



THE DIRECTOR

EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

June 28, 1995

The Honorable Pete V. Domenici
Chairman
Committee on the Budget
U.S. Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing to transmit the Administration's views on the conference report on H. Con. Res. 67, the concurrent resolution on the budget for fiscal years 1996-2002.

We stand at an important moment in the nation's history. For the first time in recent memory, the President and leaders in Congress have agreed that we must put in place a plan to balance the federal budget. We want to work with Congress on this important goal.

The key question is: How? With this conference report, the American people now have before them two profoundly different approaches -- the President's 10-year plan and the conferees' 7-year plan.

As the Administration has indicated to Congress on many occasions, we have very serious concerns about the approach taken in this conference report. The conferees would balance the budget too quickly and, at the same time, provide a huge tax cut whose benefits would flow disproportionately to the wealthy. To do so, the conferees would cut deeply into Medicare and Medicaid and cut discretionary spending so much that funds for education and training, science and technology, and other priorities that would help raise the living standards of average Americans would be seriously depleted.

If reconciliation and appropriations legislation implementing these policies were presented to the President, I would strongly recommend that he use his veto authority.

The President's plan to balance the budget over a reasonable period of time would protect Medicare and Medicaid, invest in education and training and other priorities, and provide for a targeted tax cut to help middle-income Americans raise their children, save for the future, and pay for postsecondary education.

To reach balance, the President would eliminate wasteful spending, streamline programs, and end unneeded subsidies; take the first, serious steps toward health care reform; reform welfare to reward work; cut non-defense discretionary spending,

aside from the President's investments, 22 percent in real terms in 2002; and target tax relief to middle-income Americans.

From our early analysis of the conference report, we continue to have the same concerns that we expressed about both the House and Senate budget resolutions.

Specifically, I want to express the Administration's deep reservations about the following elements of the conference agreement:

Time frame to a balanced budget. Last fall, Congressional Republicans set an arbitrary goal of balancing the budget over 7 years while providing a huge tax cut whose benefits would flow disproportionately to the wealthy. Then, they had to find the spending cuts needed to reach balance in 2002. That is the wrong approach.

By contrast, the President chose his policies first and let the date to reach balance flow from them. As a result, he was able to cut wasteful spending while protecting vital services.

Tax cuts. The conferees have settled on a \$245 billion tax cut, whose details will be crafted by the congressional tax-writing committees. Such a tax cut is too expensive; it will force unnecessarily deep cuts in Medicare as well as education and other priorities. And, based on the House-passed tax proposal, we remain concerned that the benefits will flow mostly to those who do not need them -- the very individuals who have moved ahead over the last two decades as others stayed in place or fell behind.

The President has proposed a less expensive, targeted tax cut to help middle-income Americans raise their young children, pay for postsecondary education, and save for the future. That is a much better way to help raise average living standards.

Health care. The conferees propose to cut Medicare by \$270 billion by slowing the annual growth rate to an average of 6.4 percent over 1995 to 2002. They propose to reduce Medicaid by \$182 billion, by converting it into a block grant and slowing the annual growth rate to 4 percent by 1998. Such proposals would threaten Medicare beneficiaries, cut Medicaid coverage for millions of children and elderly Americans, and endanger many hospitals, including academic health centers. Assuming a 50/50 beneficiary/provider split, these steps would raise out-of-pocket costs for couples on Medicare by \$5,650 between 1996 and 2002. These severe out-of-pocket increases would not be necessary if the conferees opted for the President's tax cut proposal.

As the President has often said, the key to long-term deficit reduction is controlling health care costs through health care reform. He proposes a serious first step toward reform that would strengthen the Medicare Hospital Insurance

(HI) Trust Fund, ensuring Medicare solvency until at least 2005; expand benefits to families; make insurance more affordable for small business; and reform the insurance market. At the same time, he proposes less than half the Medicare savings and a third of the Medicaid savings as Congress, and would impose no new cost increases on Medicare beneficiaries.

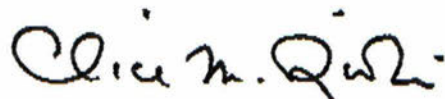
Education and other investments. In attempting to balance the budget over 7 years and finance a huge tax cut, Congress would have to cut virtually everything else, including the very programs that would help raise average living standards. Compared to the 1995 level, the resolution would cut discretionary spending for education and training by \$26 billion over seven years. In addition, the conference report proposes saving \$10 billion in the student loan program, apparently by raising costs to middle- and low-income students.

By contrast, the President proposes to increase discretionary funding for education and training by \$41 billion over the next 7 years. In addition, the President would save money in the student loan program not by cutting in-school interest subsidies and forcing middle- and low-income students to pay more; rather, he would phase in Federal Direct Student Loans quicker, cutting subsidies to wealthy banks, secondary markets, and other intermediaries. That would assist 6 million people a year -- and save money for the government, schools, and students.

In addition, the Administration remains concerned about the size of the proposed welfare cuts; they would cut benefits to poor families, thus punishing children in the process. Congress would increase the tax burden on low-income families by rolling back scheduled increases in the Earned Income Tax Credit, which is designed to reward work by lifting working families out of poverty.

Overall, while the Administration and Congress share the goal of a balanced budget, we have grave concerns about the approach set forth in this conference report. We hope to work with you, as the process moves forward, to find an approach that is acceptable to both the President and Congress.

Sincerely,



Alice M. Rivlin
Director

Identical letter sent to Honorable J. James Exon,
Honorable John R. Kasich, Honorable Martin Olav Sabo

A COMPARISON OF DEFICIT REDUCTION PLANS
(Seven year totals compared to OMB capped baseline, in billions of dollars)

	'96 Budget	House	Senate	President's Plan
Spending:				
Discretionary.....	-198	-463	-522	-200
Defense.....	---	43	-24	-3
Nondefense.....	-198	-506	-497	-197
Mandatory.....	-44	-669	-626	-216
Medicare:				
Extenders.....	-28	-28	-28	-28
Additional savings.....	---	-258	-226	-99
Medicaid.....	1	-187	-176	-54
Health reform (net).....				(-125)
Farm.....	-3	-17	-12	-4
Veterans.....	-6	-6	-10	-6
Civil service.....	---	-3	-7	---
Poverty.....	-4	-131	-116	-38
Spectrum.....	-8	-15	-25	-15
Other.....	4	-23	-27	3
Net interest	-27	-272	-346	-172
Revenues.....	96	340	-9	96
Corporate subsidies.....	---	-25	---	-25

1/ President's plan includes major increases in key education and training programs.

REACH TARGET BY 2005

(In billions of dollars)

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	10-Year Total
Outlays:												
Discretionary:												
Defense.....	272	262	258	255	260	268	276	281	282	283	283	2,709
Non-Defense.....	280	285	287	286	284	281	286	293	297	303	308	2,911
Total discretionary.....	552	547	545	541	545	550	562	574	579	586	591	5,619
Mandatory:												
Health:												
Medicare.....	154	172	186	199	213	227	243	260	282	303	326	2,411
Medicaid.....	88	92	100	109	117	127	138	150	163	177	193	1,367
Other.....	---	---	3	4	4	4	4	5	5	6	6	40
Subtotal, health.....	243	264	290	312	334	358	386	415	450	486	524	3,818
Other.....	508	533	566	594	626	659	690	718	754	791	830	6,760
Subtotal, mandatory.....	751	796	856	906	960	1,017	1,075	1,133	1,203	1,277	1,355	10,579
Net interest.....	234	256	266	272	277	280	282	282	279	277	273	2,745
Total, outlays.....	1,537	1,599	1,667	1,719	1,782	1,847	1,919	1,989	2,062	2,139	2,219	18,943
Receipts.....	1,346	1,416	1,473	1,550	1,626	1,712	1,804	1,904	2,007	2,119	2,236	17,849
Deficit.....	190	183	194	169	156	135	116	85	54	21	-18	1,094

A BALANCED BUDGET THAT PUTS PEOPLE FIRST

Invests in education and training
Balances the Budget by cutting health care costs
Cuts taxes for working families, not the wealthy
Moves people from welfare to work, protects kids
Designed to maintain economic growth

HEALTH REFORM

Realistic Medicare savings of \$130 billion
No new Medicare beneficiary cuts
Responsible Medicaid savings of \$55 billion
Gives states additional flexibility
Protects Medicaid coverage

Specific Elements

6 months of health insurance after job loss
More options for Medicare Managed Care
Down-payment on home & long-term care
Benefits that move from job-to-job
Limits on exclusions for pre-existing conditions
Gives Small Businesses pooling options
Self-employed tax deduction of up to 50%

EDUCATION AND TRAINING

Preserves investments in education & training
Increases in Head Start, Goals 2000, AmeriCorps,
and student aid
New GI Bill for workers that funds training

TAX CUTS

\$500 tax cut for children under 13
\$10,000 education deduction
IRA for education, health care, or first home

COMPONENTS OF SAVINGS

Medicare savings of \$130 billion over 7 years
Medicaid savings of \$55 billion over 7 years
Welfare reform savings of \$35 billion
Corporate Contribution of \$25 billion over 7 years
Cuts in domestic spending of over 20%

THE REPUBLICAN PLAN

Medicare cuts twice as deep as the President's
Couple would pay additional \$1500-\$2000 a year
Medicaid cuts three times as deep as the President's
Cuts in Education by \$43 billion over 7 years
Cuts Head Start and GOALS 2000 funding
Eliminates or drastically cuts student aid,
AmeriCorps, drug prevention, and job training
Awards \$630 billion tax cut over ten years
Gives \$20,000 tax cut to top 1% of taxpayers
Senate's budget increases taxes on 14 million
working families
One forecast predicts the Republican Plan will:
Slow growth
Increase unemployment to over 8.5%

THE PRESIDENT'S BUDGET

This budget is responsible and pragmatic
Limits a tax cut to working families
Reasonable time path to balance the budget
Does not cut education
No new Medicare beneficiary cuts
Designed to maintain economic growth

PHOTOCOPY
PRESERVATION

James K. Glassman

A Presidential Budget

President Clinton has decided to postpone offering a serious budget—perhaps until the fall, perhaps forever. His cynical advisers think this is a good move politically (he can snipe at the Republican budget without presenting a target of his own). But it's a disaster intellectually and morally. Americans are facing a historic decision, and they deserve two clear choices.

Since the president won't offer a budget, I'll have to do it for him—in something approximating his own words, including the usual heavy reliance on the first-person singular...

My Fellow Americans:

When I took office 29 months ago, I inherited severe and mounting deficits—the legacy of 12 years of irresponsible Republican policies. I immediately took steps to reduce spending by \$255 billion over five years and to raise revenues. As a result, the deficit has fallen for three consecutive years, the first time since President Truman.

In February, I presented my budget for 1996 through 2000. I proposed \$81 billion in additional deficit reductions along with a middle-class tax cut for families with children.

Some have called this a "status quo" budget, and I'll agree that criticism has some merit. But my intention was to let the Republicans, who had just won the congressional elections, show America what they planned to do, then add to my February proposals.

Now, we have seen the Republican budget. It features tax cuts for the rich and spending cuts for the poor and elderly. It shifts costs for many programs onto the states, which ultimately will have to raise taxes or reduce services in order to cope. Today I offer a better way.

Zero Deficit. A balanced budget is an excellent goal, but it should not become a fetish, and we cannot simply slam on the brakes after 30 years of deficits.

I believe we can balance the budget by the year 2005. Why not 2002? Because cutting too quickly would cause great pain and would slow the economy.

The nonpartisan WEFA Group, for example, estimates that the Senate's budget would push the unemployment rate to 8.7 percent. In fact, we are already seeing a contraction of the economy in anticipation of the Draconian cuts in the Republican budget, a "Gingrich recession" if you will.

Taxes. In Republican circles, there is much talk these days about a flat tax. Under such a system, the rich would pay taxes on their income at the same rate as the poor and middle class. I believe that is unfair. But there is an element of the flat tax that would make our current system more equitable: We should limit the tax benefit of itemized deductions to 15 percent for all Americans.

Consider, for example, the effect of a mortgage deduction of \$1,000 under our current system. Such a deduction reduces the tax bill of a rich family by \$396, but it reduces the tax bill of the average working family by just \$150. Instead, I propose that a 15 percent limit on deductions should apply to all.

According to the Congressional Budget Office, this measure would reduce the anticipated deficit by \$72 billion in the year 2000—and by a total of \$293 billion over five years.

Discretionary Spending. The Republicans plan to cut basic research, infrastructure and education. They even want to eliminate the Commerce Department, which has opened up new export markets for U.S. goods. These are precisely the programs that have helped make America the richest and most dynamic nation in the world.

In fact, we need more public investment—in technology, communities and the skills of the present and future work force.

Meanwhile, we have to make our government more efficient by reducing the federal work force. Some programs, which amount to corporate welfare, must go. For example, farm subsidies should benefit only the middle-class, not super-rich agribusinessmen.

Also, defense spending must be pared. The House budget increases the Pentagon's outlays from \$266 billion in 1996 to \$280 billion in 2000. Instead, I propose a reduction to \$250 billion.

Entitlements. The House budget will cut Medicare spending by \$280 billion. How?

The Republicans do not say, but, clearly, the elderly will pay more and benefits will be drastically reduced.

I believe the only way to maintain quality and hold down costs significantly is through a comprehensive reform of the health care system. Congress, however, resists this change.

I hope that, through administrative controls alone, we can hold Medicare costs in the year 2000 to \$250 billion instead of the expected \$288 billion. That is an increase of 40 percent over current levels.

But I have to be honest with you. Trying to control costs in this way may not work. If that becomes clear after two years, I will move quickly to reduce Medicare services and require higher contributions by recipients. Of course, at that point, broad health reform may be accepted as the best alternative.

State and Federal. Similar cost controls would be placed on Medicaid, but the program would not be sent back to the states—nor would welfare. That kind of cost-shifting has no place in a truthful budget.

In addition, while the states are often laboratories for new ideas, the federal government must provide the final assurance that the poor and the helpless in society are protected. Earlier in our history, we saw in the South what happens when such assurances were absent.

In the end, my new budget will offer this great nation a choice. On the one hand, an extreme and risky plan that benefits rich over poor; on the other, a sensible, fair, but tough vision that will help all of us thrive as we greet the 21st century.



BY T. GIBSON

Richard Cohen

Junk Affirmative Action?

Pete Wilson, governor of California and a likely Republican presidential candidate, stood outside a fire station in a drizzle last week and signed an executive order eliminating some affirmative action programs. For the time being, the state college and university system is not affected, although eventually it, too, is supposed to be brought into line. "Today's action starts us down that road," Wilson declared. Wait a minute! Has he seen where that road leads?

Others have—or say they have. They are the admissions officers of California's nine public universities, who have made projections about what would happen if affirmative action were junked. The most elite and the oldest of these institutions is located in Berkeley, which was once famous for pot smoking and other such extracurricular endeavors but which would, without affirmative action, achieve another kind of distinction: It would have almost no blacks.

Berkeley's 1994 freshman class is 6.4 percent African American. (California is 7.75 percent black.) If only academic achievement were taken into account, its chief admissions officer says, the percentage of blacks might be

as low as 0.5 percent. This is only a projection, but as long as we're projecting, let's also assume that once the numbers get that low, even those African Americans who gain admittance would choose to go elsewhere—some place with a vibrant African American community.

Hispanics might want to consider other institutions as well. They are currently 15.3 percent of Berkeley's freshman class. But they might go as low as 3 percent, if admitted purely on the basis of academics. Native Americans would also decline, from 1.2 percent of the frosh to maybe as low as 0.1 which, by my own bad math, comes down to one guy visiting just for the night.

Not surprisingly, white and Asian Americans would be the chief beneficiaries of ending affirmative action. Whites would go from 29.8 percent of the freshman class to as much as 37.3, but Asian Americans would really take off. Now 41.7 percent of the freshman class, they could wind up with 54.7 percent. In other words, 12.06 percent of the state's population would wind up with more than half of the places in that mythical freshman class. At the same time, Berkeley might be almost as free of blacks as a racially segregated school of old.

Is this what Pete Wilson wants? I kind of doubt it. Maybe like me, he's become disenchanted with affirmative action and thinks, overall, that it now does more harm than good. But there are instances where it does some good—and Berkeley is one of those places. After all, the difference between a kid who gets in and one who doesn't is often infinitesimal. If, say, a white kid raised in the bosom of affluence noses out some black kid raised in the ghetto, should we simply ignore backgrounds? Yes, say some critics of affirmative action. This critic, though, is not so sure.

E. J. Dionne Jr.

Dole v. Hollywood

That was strong stuff from Bob Dole about Hollywood last week. "Those who cultivate moral confusion for profit should understand this: We will name their names and shame them as they deserve to be shamed," he declared. Specifically going after the executives of Time Warner, Bob Dole offered us this powerful marriage of Cotton Mather's morals and Ralph Nader's economics: "You have sold your souls," he said, "but must you debase our nation and threaten our children for the sake of corporate profits?"

It is always refreshing to hear a politician speaking eloquently about a serious issue, and this one is. In the case of Time Warner, Dole was jumping on a bandwagon that was already rolling, thanks to the work of former education secretary Bill Bennett and C. Dolores Tucker, the head of the National Political Congress of Black Women and a longtime Democratic Party activist.

Bennett and Tucker had targeted some of the company's rap music line, and they picked a very good target. To call the lyrics in question disgusting is way too mild. It's not just the obscene words, either, or the explicit sexuality. Bennett and Tucker are going after "songs" that degrade women and glorify rape, brutality and violence. As Bennett put it nicely on CBS News's "Face the Nation" Sunday, it's a long way from Elvis's "I want you, I need you, I love you" to "I will slash you, I will cut you into little pieces, I will destroy you, I will kill you."

Bennett and Tucker are entirely right in calling Time Warner to account for putting out this material, and it's important to note that neither of them is talking about government censorship. Bennett explicitly acknowledges the

right of people to say and publish awful things. He and Tucker are simply fighting bad speech with good speech and suggesting that corporate executives should think twice before foisting trash on the marketplace. Tucker's involvement is a reminder to liberals that concerns about the coarsening of the culture are not confined to the Religious Right. "African American women," she told Newsweek, "got tired of their children calling them 'hos, bitches and sluts.'"

But when a moral issue crosses over from being the object of a bipartisan citizens' campaign to being a major tactical move in a presidential campaign, certain questions arise. It was striking, for example, that Dole's campaign staff had a lot of survey data at the ready to explain why this was such a brilliant ploy. "From polling and focus groups, Dole advisers knew the potency of the attack, and to draw additional attention, they beefed up the specifics," Dan Balz and Tom Edsall reported in *The Post*, singling out Time Warner.

Now Bob Dole is hardly the first candidate to conduct polls testing the impact of "themes" and "messages." Nor is he the first to have aides eager to explain all the calculations that went into what on its face looked like a principled stand. But learning these things does take something away from a statement steeped in moral rectitude.

There is also the issue raised by Phil Kuntz in the *Wall Street Journal*: that the butt of Dole's attacks happen to be big-time Democrats—and large contributors to the Democratic Party. Dole conveniently did not mention actors in controversial movies who are major Republicans. And he went out of his way to praise a movie called "True Lies" as "friendly to the family."

Wilson and other politicians have to ask themselves whether blacks, Hispanics and some others will continue to support a higher education system whose most elite components have few of their number. That, though, is a political question and one politicians are uniquely suited to answer. A tougher question has to do with education: Can someone be considered educated if he or she has attended a school that has few Hispanics and almost no blacks?

That, to me, would be an incomplete education, as odd in its way as a single-sex school or one limited to a particular religion. In fact, it seems contrary to the very notion of public education. It neglects the public aspect of its charter—that by taking the public's money, it must contribute to the public good.

A school such as Berkeley has an affirmative obligation to make society better than it has found it. It cannot simply accept the status quo and then graduate it four years later. To take race into account when, really, it ought to be taken into account, is nothing less than good pedagogical practice.

The nature of politics is to trivialize almost all issues, reduce them to sound bites or bumper stickers. This, of course, is precisely what's happening with affirmative action, and Wilson, in his own modest way, has made a unique contribution. His staged event, his chirpy declaration that we are heading toward "a color-blind society," masks how devilishly complicated the supposedly simple issue of affirmative action really is. Wilson's "road," paved with good intentions though it may be, somehow takes us back to where we started so many years ago—institutions with few or no blacks.

As Kuntz noted, "True Lies" was produced by a studio controlled by Rupert Murdoch, a key Republican ally. Yet the movie includes a striptease scene that has been widely criticized as degrading to women. "This is not a family values movie," said Bennett.

This is not just a matter of a little faulty research. The moral issues Dole raised in his speech are genuinely serious and worth talking about. But politicians who want to get into the moral argument had better be in it for more than quick hits. They need to know that a certain consistency will be demanded of them. As Bennett put it, "If you can't criticize a movie because it has a big-shot Republican in it, then your ground is not principle or moral quality, it's something else."

Politicians also have to be consistent about the broader issues involved in criticizing someone else's use of free speech. Can someone please explain to me if there is any objective difference between Gordon Liddy talking about how to shoot an agent of the Bureau of Alcohol, Tobacco and Firearms, and a gangsta rapper who talks about shooting a cop? If you speak out against one, should you not speak out against the other?

The most powerful form of moral witness is when people speak out *against* what are perceived to be their own interests and predispositions—when conservatives criticize Liddy and liberals criticize gangsta rap, when Democrats criticize Time Warner and Republicans criticize Rupert Murdoch. If a big moral debate is destined to be part of the 1996 campaign, that's the test to apply. The rest you can write off as coming out of the polling and focus groups.

THE PRESIDENT HAS SEEN
5.22.95

Lean
Favorable
Tone
need to
discuss
BC

Robert Kuttner

... And the Budget Battle Cry

The details of Republican spending cuts have at last been unveiled—to resounding public disapproval. If there is a popular revolution out there demanding smaller government, the polls certainly don't show it.

A recent Washington Post/ABC News Poll found 56 percent of those interviewed opposed to the Senate Republican plan to slash Medicare, Medicaid and dozens of other programs to achieve budget balance by the year 2002. An even larger majority of 60 percent opposed the House plan, which cuts spending even more severely to finance a \$350 billion tax cut.

Seemingly, this is good news for President Clinton, who has been on an upswing lately. On Wednesday, Clinton explicitly threatened his very first veto, of a Republican bill to cut some \$16.4 billion of money already appropriated for such programs as national service and college loans.

But unless Clinton offers a fundamentally different picture of the government's role in the economy, he will find that the Republicans have set the terms of the larger debate, leaving him to quibble about details. Be-

hind the minutiae of budgetary politics is one central assumption—that the budget ought to be balanced.

Clinton seemed to concede that premise in his State of the Union address when he declared that, "I certainly want to balance the budget," and then challenged the Republicans to say how they would do it. Now that the Republicans have risen to that challenge, Clinton must either match them, cut for cut—or offer a different philosophy of government.

In recent weeks, Clinton's senior White House aides such as chief of staff Leon Panetta and economic adviser Laura Tyson have sounded almost Keynesian. But they have stopped just short of attacking the very idea of budget balance because their boss is sympathetic to it.

In the emerging debate, Senate Budget Committee Chairman Pete Domenici is seen as the moderate, since his budget plan would achieve balance but not exacerbate the task with \$350 billion of tax cuts. A small group of conservative Democrats in the House led by Texas Rep. Charles Stenholm favors the Domenici formula.

If Clinton does not redefine the whole budgetary issue, and soon, he could end up embracing the Domenici-Stenholm approach as the lesser evil—and throwing away hard-won government programs that a majority of voters actually prize.

In fact, there is no good economic reason why the budget must achieve absolute balance, in 2002 or any other year. The real fiscal issue is whether the national debt is manageable relative to the overall economy.

In the 1980s, the debt grew too fast. Supply-siders claimed that you could have tax cuts without spiraling deficits but were proven wrong; debt quadrupled. The accumulated debt held by the public is now equal to about 55 percent of one year's economic output—a level high by recent standards but actually lower than in most industrial nations and half the level that it was right after World War II.

Suppose we agree that the debt ratio should not go any higher. The long-term rate of economic growth has averaged about 2½ percent. As long as the debt grows more slowly than the economy as a whole, that debt ratio will gradually decline. That means deficits are tolerable, as long as they don't exceed 2½ percent of economic output.

That's about \$130 billion in popular public spending that needn't be cut—money for Medicare, college grants, food stamps and the rest. If on the other hand, Clinton joins the budget-balance parade, the Republicans will have set the terms of debate. And whatever cuts Clinton finds will likely be no more popular than the proposed Republican cuts.

At bottom, this debate is not about fiscal probity but about the role government can legitimately play in the national economy. Republicans, in a grand bluff, have interpreted their narrow November 1994 House and Senate wins as a sweeping mandate for radical change. But you'd never know it from the polls.

Speaker Gingrich is a master conjurer. But there is no army of angry citizens demanding steep cuts in social programs, nor absolute budget balance, much less the gutting of environmental protections or another round of supply-side tax cuts. There is public support for moderate budget restraint and for more efficient public services, but this is precisely the course the administration is pursuing. And Clinton has already made significant progress on deficit reduction.

Budget balance has become a Republican hammer for wrecking popular and legitimate programs. Unless the White House calls the Republicans' bluff, the claim of a massive voter revolt against the very idea of government will become a self-fulfilling prophecy. A good place to start would be to challenge the virtue of absolute budget balance.

THE WALL STREET JOURNAL

THURSDAY, DECEMBER 1, 1994

In for a Dime . . .

Budget cutting is a parlous exercise, Democrats are fond of lecturing the nation. Last week, they internalized the dangers.

Labor Secretary Robert Reich tried to score some rhetorical points by referencing some "corporate welfare" reductions that a generally sympathetic think tank, the Progressive Policy Institute, proposed examining last January. He suggested the Republicans should chew on those a bit.

However, the first gnashing of teeth came from his Clinton administration colleagues, including Treasury Secretary Lloyd Bentsen. After all, Mr. Bentsen and his former congressional colleagues spent years legislating many of the breaks and giveaways that make up the PPI list.

We had a more positive reaction. Although about half of PPI's \$225 billion in subsidy cuts (over five years) come from eliminating tax deductions instead of cutting spending—thus reflecting the liberal presumption that income in the private economy belongs to government until proven otherwise—we're happy to see this as an opening ante in the 1995 frugality hand.

PPI's Robert Shapiro, a onetime Clinton adviser, included a host of energy schemes benefiting traditional and "alternative" sources of power. Great. We'd go further and eliminate the Energy Department, and by that we don't just mean transferring it lock, stock and oil barrel to Bruce Babbitt at Interior.

Mr. Shapiro listed \$21 billion in "agribusiness" cuts. Considering that the USDA will spend about \$300 billion during the span—less than half of it for food stamps—this is too

modest. But he planted a good seed.

Projects for planes, trains, ships and automobiles came in for an additional \$32 billion in possible excisions—\$10 billion more if you add the space station. Well, it's nice to see Democrats going after mass-transit and Amtrak operating subsidies. Unlike PPI, however, we're unwilling to concede that the capital expenditures, by contrast, are public investment; some, like the billions going into the Los Angeles subway, are just waste.

As we noted, half of Mr. Shapiro's list is really tax increases. Some of the write-offs he targeted are indeed suspect, and we'd be glad to trade their elimination for lower tax rates, but only then. A budget-cutting exercise is not the place for enlarging the share of the economy going to government.

Plus, there's a hint of familiar class warfare in Secretary Reich's use of the "corporate welfare" term, but where would an old Democrat be without that handle? Besides, it's expandable. As Scott Hodge of the Heritage Foundation notes, "HUD is corporate welfare—most of its subsidies go to public-housing authorities and developers." Only \$900 million of that nonsense made Mr. Shapiro's list.

While welcoming all New Democrats to make their bids, we must note that PPI is only a beginner at rooting out fiscal favoritism. Groups such as Heritage and the Cato Institute may lack friends in the current Cabinet, but they've found quite a bit more to cut—often using recommendations made by Alice Rivlin and Leon Panetta in their previous congressional incarnations.

Parlous poker, yes. But let's see how big we can make the pot.

The New York Times

TUESDAY, JANUARY 17, 1995

Go After Corporate Welfare

Republicans will have to cut over \$1 trillion out of the Federal budget over seven years in order to pay for their promise to cut taxes and balance the budget. If Social Security and defense are exempted, as many Republican leaders insist, that means the remaining programs must be cut by 30 to 40 percent. This benighted pledge, if fulfilled, will wreck Government programs, good and bad.

The damage could be mitigated by requiring defense to absorb its fair share of the cuts, as this page has urged — and by eliminating the huge, unjustified Federal subsidies and tax breaks doled out every year to wealthy companies and other special interests.

Republicans have already declared war on Aid to Dependent Children and other forms of welfare — including food stamps, housing assistance and child nutrition — that cost about \$50 billion a year. Secretary of Labor Robert Reich challenges them to go after another form of welfare, equally large or larger, which he mockingly labels "Aid to Dependent Corporations." Corporate welfare, according to a meticulous though partial list drawn up by the Democratic Leadership Council, exceeds \$40 billion a year. The Leadership Council estimates that a thorough search would turn up between \$60 billion and \$75 billion a year.

That pile of wasteful giveaways should provide plump pickings for John Kasich, the forthright head of the House Budget Committee, and other G.O.P. budget cutters. By going after corporate welfare they can invest more in training, education, infrastructure and scientific research as well as preserve help for the needy — even as they proceed with their frenzied attack on Federal spending.

Some Federal handouts are justified. Government should underwrite basic research, for exam-

ple in biotechnology or materials science, that has the potential to enrich society even if any one company is unlikely to translate its discovery into large profits. Government also has a responsibility to provide housing and health care to the poor. But a quick scan of the Federal budget shows scores of subsidies that amount to little more than payback to politically powerful constituents.

A Leadership Council think tank lists 68 tax and spending programs that cost more than \$40 billion a year but that, it argues, do little to benefit the economy. A few items on the list can be defended, but most cannot. For example, taxpayers spend billions subsidizing the sale of food to foreigners (to bail out growers) and of timber (to bail out loggers). Washington pays dairy farmers and sugar growers to keep prices high and pays oil companies to drill hard-to-reach wells. Congress subsidizes private utilities that serve rural areas long after electrification of those areas, the original purpose of the program, has been achieved.

None of the beneficiaries of these Federal handouts will relinquish their subsidies without a ferocious fight. The Leadership Council proposes that a commission be set up — similar to the one that recommended which military bases to close — to draw up a plan to cut corporate welfare, which Congress would then vote upon without amendment. Even without such a commission, the G.O.P. promises to bring to a vote a menu of cuts that, as Mr. Kasich has promised, exempts "no Federal program, agency or department." But the Republicans seem allergic to closing corporate loopholes.

The G.O.P. owes America more than budget balancing and tax cuts. Despite its anti-welfare rhetoric, it has a duty to protect vulnerable minorities. It must invest in the economy. It must not sacrifice one set of welfare recipients while protecting the fortunes of another.

This strategy also depends on identifying current spending and tax provisions that weaken the economy by reducing the competitive pressures that drive firms and workers to make the most of their private and public investment. These programs weaken these incentives by artificially supporting a favored industry's rate of return in several ways:

- 1) **Spending subsidies**, such as those for agribusinesses or inland-waterway operators;
- 2) **Tax subsidies**, such as those for energy producers and exporters;
- 3) **Free or below-market-rate services**, such as grazing on public lands or tourism services;
- 4) **Trade protections**, such as those for textiles and machine-tools.

Our current policies also reduce productive investment by imposing economic regulations that restrict competition in certain industries, such as those for segments of telecommunications and finance, and through the non-economic application of legitimate health and environmental regulation. These must be reformed as well.

In a global economy, these domestic subsidies, protections, and regulations cost America jobs and growth. Not only do they reduce normal competitive pressures to innovate for foreign competition, but they also place industries not receiving favored treatment at a domestic disadvantage by effectively raising their capital and labor costs relative to the subsidized or protected sectors.

The result: Tens of billions of dollars a year are transferred from taxpayers and consumers to the shareholders of companies in subsidized industries. And in the end, the industries receiving the subsidies become less productive and competitive, while those denied them have incentives to take advantage of globalization and move some of their operations to countries where labor costs are lower or special subsidies are available.

As a growth-oriented fiscal policy, *Cut-and-Invest* does *not* dictate an end to every instance of special-sector spending, tax treatment, or regulation. In some cases there are overriding social goals, such as childhood immunization or broad home ownership. Further, some subsidies and regulations offset *genuine market failures*. National productivity requires that we phase out those provisions that artificially raise the rate of return in industries with political clout, *for no overriding social or economic purpose*.

Cut and Invest also offers a sound alternative to a rigid balanced-budget requirement that would disable macroeconomic policy. Instead, the budget should be formally divided into public investments and all other spending, and the annual deficit should be limited to no more than net new public investment. In addition, total government spending should be allowed to grow no faster than the private economy.

Finally, in order to break the hold of special interests, Congress and the President should establish a Commission on National Competitiveness and Industry Subsidies modeled on the Base Closing Commission. This body would identify spending and tax provisions that provide anti-productive transfers to particular industries and recommend an annual package of reforms. The President would submit the package, and Congress would have to vote on it, up or down, without amendment.

In the end, Americans control their economic future. The choice is clear: Maintain the budget policies of the Washington establishment and accept high deficits and stalled living standards, or enact a cut-and-invest strategy for higher U.S. productivity and growth.

Cut-and-Invest

A Budget Strategy for the New Economy

by Robert J. Shapiro

Policy Report No. 23

As the battle lines over the budget are drawn for 1995, the real struggle is turning out not to be between Democrats and Republicans but between the promises of *both parties* and the basic requirements of economic growth.

The Republican majority insists that the key to prosperity lies in the discipline of a balanced budget amendment, yet the GOP offers no path to achieve it even with drastic cuts in social programs. The Administration calls for smaller deficits and new government priorities, yet its proposed budget fails to cut spending for any significant constituency or raise new revenues from any source. Instead, many Democrats sit back and wait for the Republicans to do what they will promptly criticize them for. All sides can agree only to use any spending cuts not to reduce deficits or shift priorities, but to finance tax cuts.

These political tactics neglect the real challenge: Use every tool of fiscal policy to make the United States more productive and, ultimately, to help restore mass upward mobility. The first step toward this goal is to reform scores of special spending and tax programs that subsidize influential industries and actually weaken the economy; the second step is to redirect these resources to productive public and private investment. We call this strategy **Cut-and-Invest**.

This report outlines *savings of \$265 billion over five years* generated by ending or reforming 120 special spending and tax subsidies—\$131 billion in spending, and \$134 billion in tax breaks. The ultimate goal of this program is to ensure that American workers and firms have the means to be more productive and competitive in the global economy. To do so, the budget must cut the deficit in order to allow *private* investment to increase rapidly, while simultaneously expanding *public* investments in worker education and training, basic research for new technologies, transportation and communications systems that link firms and customers to markets, and economically sound strategies for welfare reform. Therefore, we provide a blueprint that would dedicate about 57 percent of the \$265 billion in savings to reducing the deficit. Another 24 percent of the savings are redirected to specific new forms of public investment, and the remaining 19 percent of the savings could be used to provide targeted tax support to moderate-income families with children.

The success of this strategy depends on maintaining a clear distinction between public investment and other government spending. All genuine public economic investment serves only one purpose: *To expand the private economy's capacity to create wealth.* Moreover, genuine public investment is required only in those areas where markets invariably fail to generate enough private investment—the areas of human, technological, and physical capital, through the investments in education and training, research, and economic infrastructure.

CUT-AND-INVEST II, Add One

The current impasse can be broken and both spending and projected deficits can be substantially reduced—without a general tax increase or Social Security cuts—if the President and Congress "are willing to eliminate or reform scores of special spending programs and tax provisions narrowly targeted to subsidize influential industries."

"Cut-and-Invest II" identifies 120 such subsidies that can be cut or reformed. The savings would total \$265 billion over five years: \$131 billion from spending programs and \$134 billion from tax provisions. These programs, the report stresses, serve to "provide taxpayer subsidies to powerful industry groups."

The report also provides a detailed plan for redirecting these savings. It calls for earmarking 57 percent for deficit reduction; 24 percent for new forms of public investment—education and training of workers, primary economic infrastructure, basic research, and social reforms to reduce welfare dependency and teenage pregnancy—and 19 percent to provide targeted tax support to moderate-income families with children.

But attacking special interest subsidies will require taking on the Washington establishment. "This is a particular challenge to the Republican party, which thus far has proposed cutting only social programs while leaving benefits for high-income constituencies undisturbed," the report says.

To overcome these difficulties, the report calls for a nonpartisan commission modeled on the Military Base Closing Commission. This commission would examine all industry-specific tax and spending provisions and recommend a package of reforms that Congress could only vote up or down without amendment.

Ironically, Washington's current reluctance to take on powerful constituencies may enhance the prospects for a "cut-and-invest" budget strategy, the report concludes. With both parties taking entitlement reform off the table, "industry spending and tax subsidies are the only significant area of public resources left for reducing the deficit or expanding public investment. They are the last stop before tackling entitlements, and therefore the next stop for the budget process."

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***NEW "CUT-AND-INVEST" REPORT IDENTIFIES \$265 BILLION IN SUBSIDY
CUTS, OFFERS DETAILED PLAN TO USE FUNDS
FOR DEFICIT REDUCTION, PUBLIC INVESTMENT AND TAX RELIEF***

WASHINGTON, D.C. -- The Progressive Policy Institute today released a new version of its budget strategy, "Cut-and-Invest," that recommends cutting \$265 billion in special-interest spending and tax subsidies, and provides a detailed plan for redirecting the savings to deficit reduction, public investment, and family tax relief.

The report, *Cut-and-Invest: A Budget Strategy for the New Economy*, by PPI Vice President Robert J. Shapiro, updates his original 1994 plan for ending unproductive business subsidies and using the funds to support greater private and public investment as a means of spurring economic growth. In a global economy, Shapiro argues, these industry subsidies weaken our economy in 3 ways: They claim scarce resources from productive investment; they create an uneven playing field that disadvantages every unsubsidized firm and industry; and they reduce healthy market pressures on subsidized firms to make themselves more efficient, innovative, and productive.

Shapiro sees the 1995 budget debate as a key opportunity to enact an authentic economic growth program. He sharply criticizes Republicans and Democrats for failing to work on a fiscal program that raises U.S. living standards and seriously tackles changing global circumstances.

"To Americans demanding a new economic strategy that can help revive their prospects, both parties offer promises and rhetoric that add up to little more than business as usual," Shapiro writes.

-- more --

Robert J. Samuelson

The Second Coming of Keynes?

His ideas won't cure the middle-aged fatigue of modern economies.

John Maynard Keynes (1883-1946) was the 20th century's most influential economist. His ghost animated government policies for 25 years after World War II, and these led to ruinous inflation and budget deficits. It is curious then that Keynes is enjoying an intellectual revival. The American Prospect, a liberal journal, recently put him on its cover under the headline "THE SECOND COMING." And in a new book, economist Paul Krugman writes: "[T]he rebirth of Keynesian economics . . . has been oddly ignored." Huh?

Keynes is not a man for our times. What afflicts most advanced societies is a sort of economic middle age. The largely invisible and spontaneous process by which companies and individuals create new products and jobs has become less vibrant. In the 1960s, the world's richest nations averaged about 5 percent annual economic growth; in the 1980s, that was 2.7 percent. Europe suffers from astronomical unemployment. In 1970, the European Community had a jobless rate of less than 3 percent; now it's 11 percent.

But these problems do not stem from too little spending—or, in Keynes's vocabulary, insufficient "demand." In the 1980s, consumers in most wealthy nations went on spending sprees; the personal-savings rate in the countries that belong to the Organization for Economic Cooperation and Development fell from 13 percent of disposable income in the late 1970s to 10.5 percent in the 1980s. Nor has government spending been restrained. In OECD countries, it rose from 36 percent of economic output in 1978 to 42 percent in 1993. If economic vitality depended only on spending, there would be no problem.

Something else has gone awry; in truth, we really don't know what. But one source of trouble lies with government policies that encourage "structural slumps," in the phrase of economist Edmund Phelps of Columbia University. This applies especially to Europe. High payroll taxes (which raise labor costs) and tight employment regulations (which do the same) hurt hiring. They also deter business startups and doom marginal firms. The climate for job creation and risk-taking degenerates.

A few remedies are obvious. Last week the OECD issued a report concluding that "the private sector would create more jobs if there were fewer barriers to hiring." It cited high payroll taxes (our Social Security tax and others like it) and minimum wages. The dilemma is that cutting these would help the economy only slowly, while instantly provoking a political firestorm. In France, the government proposed lowering the minimum wage for younger workers to 80 percent of the regular minimum. After massive street protests, the proposal was withdrawn. All modern democracies face the problem of reconciling their long-term economic health with short-term political pressures.

But traditional "Keynesian" policies of larger budget deficits or looser credit do not defeat the dilemma. Although they may temporarily boost growth, large improvements require changes in how people and firms behave. If governments try to spend their way to faster growth, they risk colliding with the "natural rate of unemployment"—a concept conceived by Phelps and economist Milton Friedman. Unemployment could not be pushed below this "natural rate," they argue, except by a continuous rise of inflation. Stiff competition for scarce workers would push up wages and prices. This happened in the 1960s and 1970s.

Unfortunately, the "natural" unemployment rate may have risen in many countries. In practice, it's not "natural." It reflects government policies (how much does it cost to hire people?) and population patterns (are groups with higher jobless rates increasing?), among other things. If these change adversely, the natural rate rises. For example, Phelps thinks France's natural rate is 8.5 percent, up from 2.5 percent in 1970. (France's actual unemployment is now about 12 percent.) Phelps puts the U.S. "natural rate" at 6.5 percent. If true, the economy already faces higher inflation; other estimates, however, are lower.

All this is far from Keynes. What makes him a cultlike figure was his undeniable brilliance and his impatience with orthodox ideas. He is a model for anyone contesting the status quo. But to invoke Keynes now is misleading on two counts. First, we don't know whether Keynes would have endorsed many of the ideas now labeled Keynesian. Postwar Keynesianism was "by no means wholly Keynes's," as Robert Skidelsky writes in a new biography.

The second caveat is this: Keynes's theory rests on a huge misunderstanding. He argued that capitalist economies could become trapped in deep ditches of massive unemployment and unused industrial capacity from which they could not spontaneously escape. There wasn't enough "demand." This theory seemed to explain the Depression and discredit the wisdom at the time that economies recover automatically from slumps through adjustments of prices, wages and interest rates. By rejecting this, Keynes justified active government economic management.

The trouble is that the theory doesn't sit well with the facts. What made the Depression so bad was governments' efforts to save the gold standard (maintaining gold to back paper money), as economist Barry Eichengreen has shown. To guard their gold stocks, governments kept interest rates too high. This overwhelmed the economy's normal recovery mechanisms. Once countries left the gold standard (Britain in 1931, the United States in 1933), recoveries began. Between 1933 and 1936, U.S. unemployment dropped from 25 to 17 percent.

It is not that the "free market" is better than government or that economies, left to themselves, always thrive. What we call "the economy" is merely the amalgam of all the institutions, technologies, ideas and popular attitudes that propel production. And that includes government. Its economic intervention—whether by yesterday's gold standard or today's taxes—is inevitable. What we need is wise intervention, which is the hardest kind.

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that population and energy are not still problems – they are. But the forecasts that were made by organizations like the Club of Rome have proven wildly inaccurate. Why? Because things have changed, because social and economic systems have been, at least to some extent, self-correcting.

With respect to the time bomb of pension and medical liabilities associated with the demographic transition, we can count on the fact that there will be many adjustments. We could just wait and allow the adjustments to take place in response to various crises as they emerge. But this would be unwise. There are many possible paths of adjustment for this country. Rather than simply trusting to fate, it is time to take the bull by the horns, and choose some path.

APPENDIX: EDITOR's COMMENTS

Four points can be made which extend Professor Bernheim's comments.

1. Procrastination: The prospects are poor that the U.S. and other G-7 countries will act sooner rather than later in redressing the retirement crisis. The reason is game theoretical in nature: it is *rational* for leaders in both political parties to continue to ignore this problem. For as we demonstrated in our September 1992 essay "Save Us From Ourselves", the games of Presidential and Congressional Election are Prisoner's Dilemma type games.

Their equilibrium points (solutions) are strategies whereby each candidate chooses to avoid a discussion of the entitlements problem or its three possible solutions: large tax hikes, benefit reductions, or postponement of the retirement age. This is true partly because voters do not want to hear the truth, and partly because of the ever-growing proportion of politically organized elderly groups such as the AARP.

2. Baby Boomer Under-Saving: Whereas Bernheim claims Baby Boomers are saving at *one-third* the necessary rate, we compute that they are saving *one-fifth* what they ought to. The reason lies in the significant hike in marginal tax rates that will be necessitated by the very crisis Bernherim describes – a point he concedes.

3. Disarmament: In the longer run, the growth of entitlements spending will necessitate a drastic cutback in military preparedness tantamount to disarmament. This will embolden future Saddam Husseins to act much more aggressively than would otherwise be the case. In our view, it is all but certain that this situation will precipitate sporadic wars.

4. "Fairness": Note, finally, that the legislation that has created this unprecedented and inequitable redistribution of opportunity away from the young to the elderly was wrought in the name of "fairness". This all-too-seductive concept has emerged as the intellectual Venus fly trap of the twentieth century. Enter therein and thou shalt not exit.

Moreover, these immigrants would come from non-traditional sources. Historically, most immigrants to the U.S. have been European. But Europe is also experiencing the same demographic transition as we are. Future immigration would come from the third world, especially India, China, and Africa. And this implies, perhaps, a profound ethnic transition for this country.

Coping with the demographic transition through immigration is certainly an unconventional solution, and I will stop short of actually endorsing it. But nevertheless it may be one of our best hopes for long-run economic prosperity. In the past, immigration waves have fueled American economic growth. Immigrants tend to be special in the sense that they are more motivated and ambitious – historically they have been the cream of the crop. The U.S. has, throughout its history, benefited from the special characteristics and dispositions of immigrants.

Cultural Assimilation Problem: The problem with immigration, of course, is assuring cultural assimilation. While the U.S. has had great success assimilating immigrants from Europe, it remains to be seen whether cultural assimilation will be as effective for other groups. It is also important to remember that the other major developed countries also face the challenges associated with the demographic transition. The United States stands out as the developed country with the greatest potential for effective assimilation of large immigrant populations. Most of our current economic competitors cannot use immigration policy to cope with the demographic transition because they have so little potential for cultural assimilation.

Consider Japan, for example. Japan is a closed society. The Japanese economy cannot be refreshed by new infusions of talent from other cultures. Germany also has limited potential for effective cultural assimilation. We have already seen the kinds of problems that have arisen in Germany with immigration from Eastern Europe, even though Eastern Europeans are far more culturally similar to Germans than third-worlders. The U.S. is unique in the sense that we are a nation of immigrants with a history of assimilation. And therefore there is a possibility that through a strategy of managed immigration and assimilation, the U.S. may remain a vital and preeminent economic power while other current economic powers stagger under the weight of falling dependency ratios.

VI. Conclusion

In conclusion, it is important to keep in mind that historically, cataclysmic predictions rarely come true. Something usually – but obviously not always – happens to avert the most dire consequences of social change. In the 1960s and 1970s people were making all sorts of cataclysmic predictions about the kinds of conditions we would be facing by the mid 90s, concerning, for example, population growth, the depletion of energy resources, and so forth. I do not mean to suggest

A second problem is that it is difficult to fine-tune the retirement age. Remember that the baby boomers are going to have a lot of political power as retirees. If they do not want to retire later, they will use their political power to resist an increase in the age of eligibility for retirement benefits. The existence of disability insurance also makes it difficult to control the retirement age. It is very hard to detect the difference between an inability to work and an unwillingness to work. If we try to push up the normal retirement age, what we are likely to see is more and more people claiming disability as they hit age 63 or 65.

Jobs Adequacy Issue: Another concern associated with the strategy of coping with the demographic transition by raising the retirement age is that if the elderly do not retire, there will not be enough jobs to go around. The significance of this concern has been overstated. It is important to keep in mind the nature of the demographic transition. We will not have to deal with a huge expansion of the labor force. On the contrary, as the baby boomers move into retirement, the labor force will actually shrink. So it will not be necessary to create new jobs to accommodate the working elderly, as long as the adjustment of the retirement age is gradual.

V.C. Increased Immigration

The third, and certainly most daring strategy for coping with the economic implications of the demographic transition concerns immigration policy. Why is immigration policy relevant? The key observation is that the demographic transition is confined to the developed countries. Throughout the developed world, a huge bulge in the population-age distribution is moving steadily towards retirement. In contrast, the developing world has exactly the opposite problem: a huge bulge in the population-age distribution at the very young ages.

When you look at these two distributions on a diagram, they resemble matching pieces of a jigsaw puzzle. *They fit together.* And that phenomenon naturally suggests a strategy for managing the demographic transition. An economist might describe it in blunt terms as follows: "Either we've got to export the old folks or import young folks." Since no one is likely to want our old folks, importing young folks is more feasible. And this is accomplished through immigration policy.

Profound Ethnic Transition: The system may be at least somewhat self-correcting, in the sense that there will probably be increasing economic pressures to liberalize immigration policy, and to allow an influx of foreign workers, as the baby boomers begin to retire and the labor force contracts. But it must also be acknowledged that this strategy would require a major shift in U.S. policy. We would in effect be inviting a major influx of immigrants that would rival the immigration waves that took place in the 1800s and at the turn of the century.

deemphasized. Thus we see that high rates of saving in Japan are not the result of culture. Rather, they are the result of effective policy and conscious choice. In this country we have made the opposite choices.

The fiscal crisis is only one problematic consequence of the demographic transition. It is not clear that the macroeconomic problems associated with the retirement of the baby boom generation will be addressed by encouraging them to save more. After all, for every additional dollar that they put away today, there will be another dollar of dissaving after they retire.

V.B. Raising the Retirement Age

A second strategy for coping with the economic effects of the demographic transition is to raise the average age of retirement. Projections and simulations show that a relatively small change in the average retirement age – by perhaps two or three years – makes an enormous difference in terms of the long-run fiscal outlook. Delayed retirement enhances revenues: people work longer and pay more taxes. It also reduces liabilities because individuals collect benefits for shorter periods of time.

Controlling the Dependency Ratio: If we were free to select the average retirement age, then, in effect, we could control the dependency ratio. Right now the dependency ratio is about three-to-one. Through a gradual increase in the retirement age, we could keep the dependency ratio at three-to-one. Ideally the system would, once again, be self-correcting. Baby boomers should realize that if they are not saving very much, then they won't be able to afford to retire as early as their parents.

Increasing the retirement age is an attractive alternative for a variety of reasons. We have come to think of 65 as the "normal" retirement age, and we rarely stop to think about whether people ought to stop working at age 65. Perhaps it is appropriate to recall that this "normal" retirement age was established by Otto von Bismark, who set up the first Social Security system during the 1800s. Back in the 1800s, those who made it to age 65 were usually not capable of doing much more work. In contrast, the typical 65-year-old today is quite capable of continuing to work for quite a few years. So it is not obvious that the historical reasons for a 65-year-old retirement age are still relevant.

Limitations of Postponed Retirement: The strategy of coping with the economic consequences of the demographic transition by pushing up the retirement age is not without limitations. One problem is that this strategy probably would not affect the overall outlook for health care expenditures. Medical costs would still be problematic because they are driven by the number of elderly people. Late retirement does not do anything to change the number of elderly people, unless we work them to death.

do not change their behavior, their standard of living will decrease drastically after retirement. That is a powerful incentive to save more, and it exists today. How much will tax breaks enhance that incentive? If someone does not understand compound interest, the answer is, "Not very much." Suppose he is trying to decide whether to put one thousand dollars in the bank or spend it this year. If he does not understand compound interest, how will he think about the benefits of receiving, say, an 8 percent return on those funds tax-free? If he just calculate the tax that he saves on the 8 percent return during the first year, it comes out to about two bucks a month. If he is inclined to spend the thousand dollars today, he is not very likely to put it in the bank for an extra two dollars a month, unless of course he understands the long-run advantages of pursuing this kind of an investment strategy.

Need for Promotional Savings Strategies: Nevertheless, there is some evidence that tax incentives do work for the majority of people when they are combined with appropriate promotional strategies. In this country we have seen this principle demonstrated in the context of the IRA program. There is, of course, no consensus about the effectiveness of IRAs. My own view is that the IRA program was successful, in large part because it was a high-profile program that focused attention on the need to save for retirement. In a sense, it raised consciousness on retirement issues. It also provided Americans with a target: two thousand dollars a year. Most Americans who contributed to the program tried to reach that target – in effect, the government gave an official endorsement to the practice of putting away two thousand dollars per year for retirement.

In addition, the IRA program also provided the financial services sector with something to market. That was extremely beneficial because the financial services sector essentially undertook the provision of financial education. IRA accumulation scenarios were regularly tabulated in promotional materials, and the public actually learned something about compound interest.

Experience in Other Countries: There is, in addition, evidence that the combination of tax incentives and non-tax promotional activity has worked in other countries. The most notable precedent is the post-war experience of the Japanese. We sometimes forget that prior to World War II the Japanese actually saved less than Americans. The notion that saving is inherently cultural, and that Asians have deeply rooted proclivities to save, is nothing more than a myth. Japan, Taiwan, and many other Asian countries have experienced dramatic increases in rates of saving during the post-war period.

What happened in Japan? After World War II the Japanese government resolved to shape directly cultural attitudes about saving. They did this through a program that combined powerful tax incentives with aggressive non-tax promotions, including activities like workers' seminars, children's savings banks, and the general distribution of all sorts of promotional materials. The savings rate in Japan increased sharply during the 1960s, despite the fact that this was a decade of Westernization, in which traditional Japanese values were

personally expect to face a financial crisis. *Baby boomers are failing to internalize these issues.* They have not yet recognized that the demographic transition and the associated long-run fiscal crisis have very important implications for their own lives.

V. Preventive Medicine

We could, of course, take active steps to stimulate saving and encourage baby boomers to achieve financial independence before retirement. This would spur capital accumulation, and could well usher in a new period of high real wage growth. One way to encourage saving is, of course, through tax incentives. There are a wide variety of options ranging from narrowly-focused tax-favored accounts, such as Individual Retirement Accounts, to broad-based capital gains tax relief, or even the elimination of capital income taxation through the implementation of a consumption tax. There is also an intense debate over the effectiveness of saving incentives.

My views on this topic are somewhat unorthodox because I do not fall squarely into either of the two well-defined camps. The evidence on the effectiveness of tax incentives is mixed. Moreover, it is mixed for very good reasons. Once we understand these reasons, we can design more effective tax incentives.

V.A. Effectiveness of Tax Incentives

For the minority of Americans who are financially sophisticated and who understand concepts like compound interest, tax incentives are quite effective. It is important to recall that this minority is quantitatively important because they do the bulk of saving. Of course, this is precisely the group of Americans that was deprived of the tax incentives for saving in the 1986 tax reforms.

The majority of Americans, however, are not financially sophisticated. It is important to keep in mind, for example, that the vast majority of Americans cannot correctly calculate the change that they are due on a two-item restaurant meal. More than one-third of Americans believe that if you take a thousand dollars and invest it in the bank for thirty years at eight percent, you'll have less than five thousand dollars. In fact, the correct answer is more than ten thousand dollars. The average American just doesn't understand the power of compound interest.

Reasons for Skepticism: For these individuals, I am skeptical of the claim that tax incentives in isolation – and I emphasize that I am only referring to the use of these incentives in isolation – will have a significant effect on behavior. These individuals already have a compelling reason to save more. They are saving at one-third the rate required to make adequate preparations for retirement. If they

The bottom line from this study was that the typical baby boomer is saving at one-third the rate required to sustain a standard of living after retirement comparable to that enjoyed before retirement. Unless baby boomers triple their rate of saving, they will face precipitous declines in standard of living after retirement. And that's an optimistic calculation, because the simulation model assumes that there will be no reductions in Social Security benefits or Medicare benefits, and no increases in taxes, despite the fact that the status quo is unsustainable.

Even under this unsustainable scenario – a scenario that the baby boomers may be counting on – they are falling far short of what they need to save in order to accumulate sufficient wealth by retirement.

We cannot grow our way out of these problems unless we have a significant increase in saving. And we cannot have a large increase in saving unless the baby boomers significantly alter their behavior. Perhaps the baby boomers will simply start saving on their own at some point in the future. Perhaps as they age and move past the child-rearing years, they will begin to save at higher rates. Then again, perhaps not. I do not have much hope that they will become savers on their own. After all, their parents did not. It is a common myth in this country that the baby boomers are the first generation of big spenders. That simply is not true. The typical parent of a baby boomer didn't save very much for retirement either. Some did, but most did not.

Today's Retirees Got Lucky: The parents of the baby boomers are, by and large, reasonably well prepared for retirement because as a generation they got lucky. They benefited from a huge increase in Social Security benefits, a significant expansion of the private retirement benefit system, and an extended period of high inflation that nearly wiped out the real value of their biggest liabilities, in the form of fixed rate mortgages. They also experienced a huge run up in real housing prices that created huge windfalls for many of them.

So the baby boomer's parents have generally been reasonably well prepared for retirement. But this isn't because they saved a lot. Most importantly, there was no real acceleration in their rates of saving once they completed child-rearing and reached the second half of their working lives. Similarly, any significant acceleration in savings goes undetectable among baby boomers as they move into their mid 40s.

A Collective State of Denial: Perhaps baby boomers will be different. Maybe they will eventually wake up, notice the crisis, realize what the future holds in store for them, and start saving. Then again, maybe not. Unfortunately, the baby boomers tend not to personalize the crisis. Baby boomers are collectively in a state of denial. When contemplating their future financial prospects, they tend to exercise cognitive dissonance. Eighty-six percent of baby boomers say that they believe future retirees will face financial crises. But less than a half say that they

Self-Defeating Increases: If we actually increased taxes by the prescribed amounts, economic activity would decline, and we would once again find ourselves short of revenue and in need of still higher taxes. When one is discussing fiscal shortfalls of such enormous magnitude, attempts to achieve balance through increases in taxation may simply send the economy into a death spiral. I'm not at all convinced that it is even feasible to balance the government's budget in the long run through taxes. In all likelihood, something else must give.

IV.C. Autonomous Solutions?

There are several paths that the economy could take to achieve long-run fiscal balance and to address some of the other problems that will arise as a result of the demographic transition. I want to mention some of these paths and say a few words about their likelihood and their desirability. The first solution is to achieve more rapid growth of real wages. That sounds great – all we have to do is grab the wage-growth knob and crank it to the right. Obviously the question is: how do we accomplish this?

In an ideal world the economy would be at least somewhat self-correcting. If the baby boomers thought hard about the issues that have been presented, and if they realized that our fiscal path is unsustainable, they might well conclude that they are not going to receive sufficient income from Social Security, and that they will, for the most part, have to rely on themselves during retirement. They might respond to this realization by increasing their own saving, perhaps substantially.

This in turn would increase capital accumulation, and the resulting capital deepening would promote wage growth. Higher saving would alleviate the impending crisis in another respect: if the baby boomers achieve financial independence by making adequate preparation for themselves, they will be less resistant to measures that would achieve fiscal balance through the reduction of Social Security benefits.

Low Baby-Boomer Savings: How likely is this scenario? Will we achieve significant capital deepening and higher real-wage growth as a result of a surge in saving by the baby boomers? Probably not. Most baby boomers simply are not savers. Obviously some are; I don't mean to suggest that none of them save anything. But for the most part baby boomers do not save large fractions of their incomes.

A couple of years ago I undertook a major study of saving by members of the baby boom generation. To conduct this study, I developed an elaborate computer simulation model, which calculated the amounts that baby boomers need to save in order to be prepared adequately for retirement. These prescriptions were then compared with actual saving, which was inferred from a survey of baby boomers conducted in 1992.

mechanism for reducing Social Security benefits is means testing. At some point it may well become politically feasible to single out higher income individuals and to say, "Let's wipe out their benefits because, after all, they don't really need it as much."

Mailed Promises to Pay: I would also point to another development that affects the likelihood of further cuts in Social Security. I consider this to be a rather insidious development because on its surface it seems quite innocent. Beginning in 1995 the Social Security Administration will begin sending unsolicited benefit statements to every wage earner in the country, beginning with older workers. These statements will resemble the statements that you probably receive from your private pension plans. Before too long you will also receive statements from the Social Security Administration that project your benefits after retirement. This policy is not completely new, in that you can currently request the Social Security Administration to prepare a benefit statement for you. But as of 1995 these statements will be mailed out automatically, regardless of whether or not you request them.

This is a disturbing development. In the first place, it is disturbing because it is potentially misleading. These statements will contain benefit projections based on current statutes. Naturally the fine print will contain disclaimers to the effect that the benefits projections are based on current statutes and that they are not guaranteed. But the Social Security Administration is not going to proclaim in large print that "This is not fiscally sustainable and you probably should not count on receiving this much."

Misleading the Populace: So why is the government going to do something that has the potential so fundamentally to mislead the American working population? My understanding is that the benefit statement policy has emerged largely from the efforts of Senator Moynihan. Moynihan believes that by distributing these statements we will stimulate confidence in the Social Security system. We will encourage people to expect their benefits, thereby creating the political clientele necessary to combat efforts to reduce benefits. In other words, Moynihan's objective is to create a self-fulfilling prophesy that protects Social Security benefits from future budget cutters.

IV.B. Tax Increases?

If the prospects for reducing Social Security benefits are slim, what about the possibility of increasing taxes? The simulations and projections that I've talked about don't really capture what would happen if we tried to achieve fiscal balance by increasing taxes. Specifically, the projections do not make any allowance for the fact that higher taxes would depress the level of economic activity. In effect, these calculations hold activity constant, and mechanically calculate the rate of taxation that would be required to balance the government's finances.

Heavy Hit to Bonds: The impending liquidation of the baby boomers' retirement assets should have a similar effect on all asset prices. However, it is worth noting that these retirement assets are tilted more heavily towards bonds than towards equities and other investments. Certainly, Social Security is completely bond-financed. Private pension assets are also tilted heavily towards bonds. It is increasingly common for baby boomers to be covered by defined contribution plans, which provide them with significant control over the retirement investments. They typically exercise this control by investing very conservatively – that is, in bonds, rather than stocks.

Therefore it is quite possible that the liquidation of the baby boomers' retirement assets will have a disproportionate effect on the bond market. In effect, retirement saving by and for baby boomers currently stimulates the demand for bonds relative to other assets, and this pattern may reverse as the boomers retire.

IV. Three Strategies for “Containment”

Throughout this address I have been discussing projections rather than predictions. There is an important difference. The scenarios that have been described are not particularly plausible or sustainable. Something has to give. What radical development might the future hold?

IV.A. Benefit Reductions?

It is possible that we might go the route of reducing Social Security benefits. Cutting Social Security has always been a tough sell politically. Although there have been effective benefit reductions in the past, they have always encountered determined opposition. It will become especially difficult to reduce benefits once the baby boomers retire, because the baby boomers constitute an extremely large segment of the population. If you think that the elderly are a powerful lobby today, just wait until this enormous group of baby boomers reaches retirement age. In addition the baby boomers are not saving very much for their own retirements. As a result, the boomers will be highly dependent on Social Security benefits. If they reach retirement without significant assets of their own, they will certainly use their political power to protect their financial interests in the Social Security system.

A Divide-and-Conquer Strategy: There is, of course, a possibility that we might reduce Social Security benefits prior to the retirement of the baby boomers. If this occurs, it will most likely be the result of a divide-and-conquer strategy. We observed the divide-and-conquer strategy in action when Social Security benefits were last reduced. The essence of this strategy is to identify a subgroup of the population for whom a reduction in benefits is politically feasible. This subgroup tends to be higher income individuals, although the definition of “higher income” has crept steadily towards the middle class. For the future, the most likely

plans dropped steeply. So far, the early 1990s have been a period of extraordinarily low saving, even by the standards of recent history.

What will happen to pension funds during the retirement of the baby boom generation? A recent study by Syl Schieber and John Shoven demonstrates that there will be enormous net outflows from pension funds as the baby boomers begin to retire.¹ If indeed pension funds dictate the rate of private saving, then we may observe negative rates of national saving. Can we rely on capital inflows to finance investment in the U.S. during the retirement of the baby boomers? Will foreign investors bail us out as they did in the 1980s? Probably not. The important thing to remember is that almost all of the developed world is facing a similar demographic transition. Other developed countries will find themselves in a similar situation during the first half of the next century. As a result, there will not be a natural source of funds for capital investment in the U.S., even if we are willing to accept the consequences of widespread foreign ownership of American assets.

Thus there is a serious risk that it will not be possible to finance significant new capital investment during the retirement of the baby boomers. Will the American economy simply grind to a halt due to the lack of capital formation? And what are the implications for asset markets as we move into this period? What will be the effect of liquidating the enormous stock of assets that is going to pay for the retirement of the baby boom generation?

Sharply Rising Interest Rates: The dynamics of the Social Security system are such that, during the first half of the next century, there should be an enormous increase in the net supply of government bonds to the market. That will occur regardless of what happens to the Social Security trust fund. One view is that, over the next 40 years or so, we will accumulate a huge trust fund and then use that trust fund to pay for the retirement of the baby boomers. That would require the government to buy up government securities – they cannot buy other securities – and then sell government securities once the baby boomers retire.

Another view is that the government will succumb to short-run political pressures and fail to accumulate a large trust fund. In that case, it will still have to make good on at least some of its promises to the baby boomers, and that will require it to finance much larger deficits. In either case, the large increase in the net supply of bonds will have the effect of driving bond prices down and raising rates of return. If investors are reasonably forward-looking, that effect will propagate back through time.

¹ Sylvester J. Schieber and John Shoven, "The Consequences of Population Aging on Private Pension Fund Saving and Asset Markets", Center for Economic Policy Research, Stanford University, September 1993.

address real wage growth effectively through policy, but in the absence of rather drastic action, the prospects are not great.

III. Other Macroeconomic Implications – Savings and Interest Rates

We have seen the fiscal implications of the demographic transition. Now some macroeconomic implications will be unveiled. For context, let us start by addressing the current state of our economy, focusing in particular on national saving. As we all know, Americans do not save very much. During the last few years, national saving has averaged around 2% of GNP. Government deficits are often blamed for low rates of national saving. That is not entirely fair. In fact, private saving, and personal saving in particular, have dropped sharply. The decline in personal saving accounts for a large fraction of the decline in national saving. Low rates of personal saving – and not government deficits – also account for the very large differences between rates of national saving in the U.S. and other developed countries.

Lower National Savings Rates: Low rates of saving create serious concerns about the health of the macroeconomy. Saving finances capital accumulation. Capital accumulation is absolutely essential for growth. With low rates of capital accumulation we can expect very little growth, and stagnant standards of living. In the short run our failure to save can be redressed to some extent through international capital flows. Those international capital flows, though, have their own macroeconomic implications. When there is net foreign investment in the U.S., the value of the dollar becomes inflated. This creates a balance of trade deficit, and causes domestic manufacturers to complain about a loss of competitiveness. It is also the case that most countries are intolerant of imbalances in international capital and current accounts, and generally take steps to reduce these imbalances over reasonably short periods of time.

If these are the consequences of our low rate of saving today, imagine what will happen when the baby boomers retire. It is hard to think meaningfully about national saving after the baby boomers retire, because there will not be much of it. To put things in perspective, in recent years pension funds have accounted for most of the accumulation of personal wealth in this country. In fact, the National Balance Sheets produced by the Federal Reserve Board show that between 1980 and 1990 the real change in assets held by pension funds was roughly equal to the real change in national wealth. By that measure, pension funds accounted for essentially all of national wealth accumulation.

As Go Pensions, So Goes Saving: We have already seen ample evidence of this truth. In 1987, the government attempted to raise additional revenue by limiting the circumstances under which corporations could make deductible contributions to defined benefit pension plans. As a result, contributions to defined benefit

II. Today's Bromides from Washington

What is the Social Security Administration response? What do they say in particular about the Medicare liabilities, of which they are most certainly aware? Basically, they say two things.

Mirage of Medical Cost Containment: The first thing they say is, "Don't worry too much because medical cost containment is on its way. That's a priority of the Administration -- we're overhauling the health care delivery system." Once again this observation is not reassuring. The effects of cost containment are still largely speculative; they have not been proven, certainly not on a national scale. We are not certain we can control medical cost inflation in this country. But even if we could, it is important to realize that the projected increased program costs for Medicare are driven largely by demographics, independent of any health care cost inflation.

Even with no real increases in the prices of medical services, there will still be a huge increase in Medicare program costs during the next century, due to the fact that the baby boomers are aging. As the baby boomers -- this very large generation of Americans -- move into retirement and become elderly, they will also become more intense consumers of medical care. So short of a Logan's Run solution in which we terminate everyone over 30, the increase in medical care program costs is, to a large extent, out of our hands.

This is particularly frightening because the baby boomers may live significantly longer than the Social Security Administration expects. There are a number of demographers who believe that we have significantly underestimated likely increases in life expectancy for the next century. By some forecasts, the Social Security Administration has understated the number of octogenarians in the next century by a factor of four. Obviously, octogenarians are rather intensive users of medical care.

Mirage of Better-Future Growth: The Social Security Administration's second response is, "We make these long-run fiscal projections because we're required to make them. We don't think they are very precise. We're talking about a very long time horizon. Our forecasts depend on a large number of parameters, and there is a tremendous amount of uncertainty. So one shouldn't worry too much. After all, we may witness a return to a period of relatively high real wage growth. Real wages have been stagnant for the last 20 years, but that may turn around. If it does, the forecasts change dramatically, and the future looks much more rosy. So perhaps, instead of panicking, we should wait and see."

Yet again this is not overly reassuring. For one thing, if we delay action, and if nothing unusually fortuitous happens, the crisis will only become more severe. In addition, the prospects for a return to sustained long-run real wage growth are slim. I will explain my reasons for this pessimism shortly. We may be able to

government's obligations also include Social Security, Medicare, welfare, unemployment benefits, education, and so forth. The basic conclusion of this study is that this country is on an unsustainable fiscal path.

Future Tax Rates - The Shocking Truth: During the next century, the government is scheduled to spend trillions of dollars more than it expects to bring in as revenues. The actions that are required to restore balance are quite drastic. For example, we could attempt to restore fiscal balance by increasing taxes. To do so would require a permanent 32% increase in all income taxes effective immediately. And the situation becomes much worse if we wait. If we delay 15 years before taking action, it will take a 63% permanent increase in all income taxes to achieve fiscal balance.

We can also address the problem by adjusting OASDI benefits. If we took immediate action, this would require a 70% permanent reduction in benefits. And once again, if we wait, the problem becomes much worse. If we delay 15 years before doing anything, it will be impossible to achieve fiscal balance for this country by adjusting OASDI, even through the complete elimination of benefits. We can, of course, go after health benefits as well as OASDI. That possibility seems remote, given the objectives of the current Administration.

However, even if we were willing to reduce health benefits in addition to OASDI, it would require a 29% permanent decrease in all of these benefits to restore fiscal balance. Once again, the situation is much worse if we wait. A 15-year delay would essentially require us to cut all of these benefits in half.

And finally, if we fail to take any action, the requirement of fiscal balance would necessitate tax rates in excess of 80% for future generations of Americans.

This 80% is not a forecast. Long before we reach average tax rates in excess of 80%, there would presumably be some kind of revolution. Properly interpreted, these calculations are simply telling us that we are on an unsustainable path, and that something must give. Tax rates won't necessarily rise above 80%; OASDI may not be eliminated; but something has to give, and that something has to be big.

Public Policy Myopia: The fiscal crisis is barely on the political horizon. We do not run into real difficulty with paying for Social Security until well into the next century. That means that the problem is not going to be addressed right away. And the nature of this problem is that, the longer we wait without doing anything, the more drastic the response has to be when we get around to doing something. In particular, if we wait until closer to the retirement of the baby boom generation, a one-and-a-half percentage point increase in the payroll tax isn't going to do it. It's going to require more like a four or a five percentage point increase in the payroll tax to put OASDI back on track.

Inclusion of Medicare Shortfall: Now we still may not be panicked by this alone. After all, cumulative increases in taxation have, in the past, totaled more than 4 percentage points. Again, perhaps the American system is not going to collapse. But wait: that's just OASDI. What about the other unfunded promises and obligations of the federal government? The most significant of those obligations is of course Medicare. The Social Security Administration is conspicuously silent, for the most part, on the topic of Medicare. Back in 1983 when the Social Security task force set about formulating the 1983 Amendments, they were specifically instructed by the Administration to focus exclusively on OASDI and to ignore health insurance entirely. This was despite the fact that, even at that point in time, it was evident from the forecasts that the potential unfunded liabilities of Medicare were roughly three times the liabilities of OASDI.

Greenspan Commission's Omission: Why was the 1982 Greenspan Commission Social Security task force instructed to ignore this problem? I suppose we will never know the true answer to that question. The cynical answer has to do with timing. At that point in time, Health Insurance was forecasted to be in pretty good shape through the end of the century, and certainly well beyond the horizon of the then-current Administration. Consequently, when the 1983 amendments were formulated, the much bigger and more serious health insurance problem was left as a problem for the future. When victory was proclaimed and the financial security of the Social Security system announced, the larger problem was never mentioned.

What is the current magnitude of the fiscal problem associated with Medicare and the other government liabilities not included in OASDI? Recently, Professor Alan Auerbach of the University of Pennsylvania and Laurence Kotlikoff of Boston University released a major study concerning the long-run fiscal outlook for this country.¹ This study paints a comprehensive picture of the unfunded obligations of the federal government. Those obligations of course include the federal debt, which is the obligation that seems to get the most attention in the popular press. But the debt isn't the most important item in quantitative terms. The

¹ Alan J. Auerbach and Laurence J. Kotlikoff, "The United States' Fiscal and Saving Crises and their Implications for the Baby Boom Generation", Special Report to Merrill Lynch & Co., Inc., February 1994.

Plummeting Dependency Ratio: Today we have 3.2 workers for each Social Security beneficiary – this is known as the "dependency ratio". In the year 2029 that figure probably will have declined by almost a third, to 2.1 workers for each Social Security beneficiary. And these figures only become worse with the progressive graying of America as the baby boom generation moves further and further into retirement. It is probably not news when I say that the potential economic implications of this transition are dire, and deserve our serious consideration.

I. Fiscal Implications

In order to have the full picture before us, let us begin by elaborating on some of the major economic implications of the demographic transition. First I will discuss the fiscal implications of this transition. It has been known for some time that the impending retirement of the baby boom generation poses, to put it mildly, a challenge for financing the Social Security system. During the early 1980s this problem was obvious and the government set out to do something about it.

In particular, the Reagan administration ordered a thorough review of the finances of the Social Security system, and this culminated in the Social Security Amendments of 1983. Through a combination of measures, most notably a delayed, phased-in increase of the ordinary retirement age from age 65 to age 67, fiscal balance was *purportedly* restored to the Old Age Survivor and Disability, or OASDI, portion of the Social Security system. Victory was proclaimed, and the American public was told, "Don't worry, once again you can have full confidence in this system because in the long run it's in quite good shape."

Smoke and Mirrors: Perhaps it is the fourth corollary of Murphy's Law which states that things always turn out to be worse than expected. Eleven years after the 1983 Amendments, it appears that the government achieved fiscal balance largely through smoke and mirrors. Currently the Social Security Administration is projecting a huge shortfall in the OASDI system. They are also downplaying this shortfall, which is somewhat disturbing. We are told that the shortfall only amounts to a 1.5 percentage point increase in the payroll tax. If we wanted to cover this shortfall, we could simply increase payroll taxes by 1.5% right away.

The Social Security Administration puts that in perspective by saying that we have just gone through a successful deficit reduction effort, and while it was very difficult to achieve a political consensus, we accomplished a tax increase of roughly this order of magnitude. Therefore, a 1.5 percentage point increase in the payroll tax is presumably not going to be the end of the American system. However, this reasoning is not particularly reassuring .

THE COMING ENTITLEMENTS CRISIS

– A Case for Divine Intervention –

Editor's Note: In my own view, the coming entitlements crisis poses by far the most important economic and political challenge we have confronted since the Great Depression, if not the Civil War. Most investors think of this as just another problem which will be "dealt with" in due course. And so it will. But what exactly does this mean? What are the options?

In preparation for S.E.D.'s Client Conference in New York this past May, I asked Doug Bernheim at Princeton to prepare a candid and far-reaching appraisal of these issues. [He has recently moved from Princeton to Stanford, his new base.] Along with John Shoven at Stanford, Doug is the most interesting and knowledgeable pension-and-entitlements thinker I know.

Conference attendees particularly enjoyed his talk, so he has kindly edited it for purposes of publication. The result is important if disturbing food for thought, especially for investors charged with longer-run strategic planning for their institutions *and* their families.

While Doug focuses on the situation in the US, his remarks apply to other G-7 countries all of whom confront the common problem of a collapsing "dependency ratio". At the end of the paper, I have appended a couple of personal comments extending Doug's reasoning via game theoretical arguments.

– H. W. Brock

I was recently involved in designing and implementing a survey of baby boomers that was sponsored by Merrill Lynch. One of the topics that we looked at in this survey was the sources of information and advice on financial matters that are used by members of the baby boom generation. We listed a number of choices, including financial professionals, relatives, employers, the government, and so forth.

One of the most striking and surprising findings of this study, in my view, was that more of the baby boomers rely for financial information and advice on *prayer* than on the government and employers combined! We did not offer "prayer" as an option in the survey. This was a write-in campaign for prayer. If we had actually listed it as an option, it might have shown up as the number one source.

Anyone who has gazed into the next century and looked carefully at the economic trends should understand why so many of the baby boomers are seeking divine intervention: their prospects are not particularly good. This country stands at the threshold of an unprecedented demographic transition. Today the elderly make up about 12% of the U.S. population. By the year 2029, which is the year in which the oldest baby boomers reach age 65, that figure will have risen to about 20%.

FROM WADY BROCK

FOR PRESIDENT CLINTON

THE PRESIDENT HAS SEEN

11/23

THE COMING ENTITLEMENTS CRISIS
- A Case for Divine Intervention -

by Professor B. Douglas Bernheim
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innovate. Firms must now organize productive factors from around the world, and find new ways to produce the goods and services demanded by international markets. And *competition* is the engine that drives innovation.

One way to increase competition is to *phase out or reform federal programs or activities that insulate particular industries from healthy market pressures*. There are four principal ways that government today artificially supports various industries' rates of return, reducing their incentives to innovate and become more efficient:

- 1) Special **spending subsidies**, such as those for farm companies and inland-waterway operators;
- 2) Special **tax subsidies**, such as those for energy producers and building construction;
- 3) Special **trade protections**, such as those for textile producers and machine-tool manufacturers;
- 4) Special **economic regulations**, such as those for some segments of the telecommunications industry and the financial sector.

In a global economy, these domestic subsidies, protections, and regulations cost the nation jobs and growth. Not only do they reduce normal competitive pressures to innovate for *foreign* competition, but they also place industries not receiving favored treatment at a *domestic* disadvantage by effectively raising their capital and labor costs relative to the subsidized or protected sectors.

The result: Industries receiving subsidies become less competitive, while those denied them have incentives to take advantage of globalization and move some of their operations to countries where labor costs are lower or special subsidies are available.

This new growth policy for a global economy does *not* dictate that government should end *every* instance of special-sector spending, tax treatment, or regulation. In some cases there are overriding social purposes, such as health-care spending for the poor and tax incentives for middle-class home ownership. Furthermore, some subsidies and regulations are intended to offset *genuine market failures*. The demands of global competition require that we phase out those provisions that artificially raise the rate of return *for particular industries with political clout, but for no overriding social or economic purpose*.

Congress and the president should establish a Commission on National Competitiveness and Industry Subsidies, modeled on the Base Closing Commission. This body would identify spending programs and tax provisions that provide anti-competitive transfers to particular industries and recommend to the president an annual package of appropriate reforms. The president would submit the package to Congress, which would have to vote on the package without amendment. ***Cut-and-Invest to Compete and Win*** identifies more than \$114 billion in spending subsidies and \$111 billion in special tax provisions that should be evaluated by such a commission -- and this is only a beginning.

The savings from eliminating or reforming these programs could finance substantial new public investments in education and training, basic research, and economic infrastructure, as well as initiatives in welfare reform, community policing, and National Service. In addition, sufficient resources would remain to support a measure of middle-class tax relief and additional deficit reduction.

Cut-and-Invest to Compete and Win

A Budget Strategy for American Growth

Policy Report No. 18

by Robert J. Shapiro

The 1994 debate over the federal budget will challenge President Clinton and Congress's ability to use the budget to promote U.S. growth and global competitiveness.

Meeting this challenge won't be easy, because Washington debates over the budget are usually disengaged from the economics of growth. Both political parties have been consumed with the distributional questions of who will pay more taxes and who less, and who should gain new benefits and who should shoulder any program cuts. Traditional liberals tend to focus on increasing spending and, when necessary, taxes as well, while conservatives concentrate on *cutting* both spending and taxes.

For the United States to succeed in the international economy, these variations of tax-and-spend macroeconomics must give way to a new strategy of **cut-and-invest**. This strategy proposes that the government use the budget both to promote higher levels of private and public investment and to actively encourage vigorous market competition to drive private-sector innovation and productivity.

> **First**, we must ensure that U.S. workers and firms have the means to compete more effectively in world markets. As President Clinton pledged, *the government should expand public investments in worker education and skill training, basic research for new technologies, and the primary infrastructure networks that link firms and customers to markets*. These investments in human, technological, and physical capital will help us compete, especially with the advanced countries that produce comparable goods and services to our own.

Public investment is different from other government spending. Its only purpose is to expand the private economy's capacity to create wealth, and it is called for only in those areas where markets invariably fail to generate appropriate levels of private investment. A budget that aims to enhance national growth in the global economy must promote greater private *and* public investments in training, research, and world-class communications and transportation systems.

To advance this process, the budget should be divided into two separate accounts: one for public investments; the other for all other expenditures. Deficit spending should be limited to the net investment account, and total expenditures should grow no faster than the economy.

> **Second**, we have to enhance domestic competition, because only increased competitive pressures can drive firms and workers to make the most of public and private investment. This imperative takes on special importance in the global economy, where successful firms must not only produce their goods and services efficiently, but they must also

attack subsidies as a whole. President Clinton should press Congress to create a national commission on industry subsidies modeled on the successful base-closing effort. This commission would prepare a package of proposed subsidy reforms and cuts, and Congress would have to approve or reject the package without amendment. This effort will not be easy, but success would make the President and Congress real champions of the general welfare and a genuine scourge of the special interests.

3. Promptly implement the GATT agreement. America's leadership in the global economy, already fostered by last year's approval of NAFTA, should be advanced further by implementing the GATT agreement *this year*. By early 1996, our current expansion, like other protracted business cycles, will need to tap rising foreign demand. Therefore, prompt American action on GATT is required -- including finding \$14 billion to finance it under our budget laws -- if President Clinton hopes to take advantage of next year's expected economic recoveries in Europe and Japan and expand U.S. exports.

The President and Congress should make no mistake about GATT's importance. Even a year's delay could mean its defeat, as opposition among environmentalists and ultra-conservatives matures by the day. If GATT fails, American exports will decline, which in turn will exert downward pressures in 1995 and 1996.

4. Deregulate small business. Another factor in both an enduring expansion and long-term growth is well-timed bursts of business creation and job expansion. Here, President Clinton can act directly and decisively by relaxing the federal regulation of small and new businesses, except in truly vital areas of health and safety. Most economists (and virtually all business people) now agree that federal regulation of small businesses, especially new ones, exerts a substantial drag on investment and jobs. As it happens, the Regulatory Flexibility Act of 1980 already directs federal agencies to consider ways of reducing the regulatory burdens on small entities, but most agencies have ignored this mandate. The President can make this law an aggressive instrument of new entrepreneurial activity by issuing executive orders directing agencies to follow through -- in specific areas and specific ways, now.

These four course corrections are an insurance policy for sustaining the current expansion. In many respects, the specifics are no more than President Clinton pledged in 1992, and fulfilling these pledges would leave few Americans in doubt about his present commitment to their economic interests. Whatever the political outcome, a program of long-term fiscal discipline, renewed public investment, open trade and business deregulation will leave a splendid legacy of a stronger American economy for years to come.

Dr. Robert J. Shapiro is Vice President of the Progressive Policy Institute

ultimately support serious reforms. The President also can draw on a growing consensus that serious Social Security reforms are needed in any event, just to ensure the system's long-term solvency. Pulling off entitlement reform will make President Clinton and Congress genuine heroes for finally taming the permanent deficit, and thus helping to create the conditions for long-term national prosperity.

2. Cut-and-invest. As we ask middle-class people to accept less in future entitlement benefits, we should also offer economic reforms that will strengthen their future prospects: namely, greater public investment in their training and education, basic research and transportation systems. These investments should be financed by asking specific industries to give up their special subsidies. As public investment can strengthen national productivity and efficiency, these subsidies reduce the economy's potential, by insulating favored sectors from healthy market pressures to upgrade themselves, and by raising the cost of capital and labor for those without subsidies.

The cornerstone of President Clinton's strategy for reviving U.S. growth and productivity in a global economy is investment -- not only private investment by companies, but also public investment through the government in the training, education, basic research and infrastructure that can make every worker and firm more productive. This approach is fundamentally sound; but congressional resistance to cutting programs that don't work and subsidies for special interests has denied this strategy the resources it needs to succeed. As a result, funding for these economy-wide public investments is rising by just two-or-three percent a year -- not nearly enough to affect national productivity and growth.

To finance meaningful public investment, the Progressive Policy Institute recently compiled a list of 68 tax and spending subsidies totalling \$225 billion over five years, each one currently protected by its favored industry.¹ For example, on the spending side the list includes subsidies to defray airlines' costs to expand and upgrade terminals, payments to farmers whose commodities sell at below government-set prices, and cut-rate power from federal hydroelectric plants for private utilities in selected states. On the tax side, the list includes special credits for firms producing ethanol or natural gas from certain geological formations, a tax holiday for profits earned by firms on their operations in Puerto Rico and other U.S. possessions, a special one-year deferral for agribusiness on taxes for much of the income from crops, and many other singular provisions.

Phasing out these subsidies could clearly provide the resources for aggressive public investment, as well as a measure of tax relief for middle-class families with children. Yet the prospects of cutting subsidies for such powerful interests are slim, especially if we try to cut them one at a time. One way to break this gridlock is to

¹ Robert J. Shapiro, *Cut-and-Invest to Compete and Win, A Budget Strategy for American Growth*, Progressive Policy Institute, Policy Report No. 18, January 1994.

What should President Clinton and Congress do? First, they should understand why the great expansions of the 1960s (which lasted 34 quarters) and 1980s (which lasted 30 quarters) survived so long. The 1960s cycle, after nearly expiring when the Fed hiked interest rates sharply in 1966, drew new strength from persistent productivity gains, Vietnam War spending and rising trade surpluses. Several factors contributed to the long life of the 1980s expansion. The deep recession of 1981-82 left the economy with unusually high levels of unused factory capacity and unemployed labor, so the cycle could draw on large amounts of idle equipment and workers before hitting the wall. Inflation also was checked for a while by competition from cheap imports. In addition, from 1986 to 1989, exports grew as the dollar weakened, and financial deregulation and falling interest rates supported massive credit expansion that offset declining budget deficits.

In both cases, fiscal and monetary policies moderated each other, so that one could expand as the other contracted, rising foreign demand offset weakening domestic demand, and the economy benefitted from bursts of new business activity.

These lessons can be adapted to change the conditions of this business cycle. The President should advance four policy adjustments that could both address structural problems in the economy *and* raise the odds of sustaining growth for several more years.

1. Entitlement reform. The most powerful tool at President Clinton's disposal is the ability to alter the mix of fiscal and monetary policies. Fiscal stimulus won't help, because it would drive up long-term interest rates. Nor is short-term fiscal tightening an answer, because it cannot be reliably timed to precisely offset inflationary pressures.

Instead, the President should build a solution around new measures for long-term deficit reduction that could relieve pressures on long-term interest rates and expand private investment. His next budget should include proposals for permanent entitlement reform which, once passed, would deflate long-run inflationary pressures and so promote declining long-term interest rates in mid- to late-1995. Enacting these reforms in 1995 to phase-in for 1997 and beyond, moreover, would protect the economy from a short-term contraction without reducing its anti-inflationary punch.

To achieve this, the President could propose to (a) accelerate the currently scheduled increase in the retirement age for full benefits under Social Security and other retirement programs; and (b) reduce the spending and tax benefits for retirement and health care for people with incomes of \$100,000 a year or more.

Next year may offer a rare political opening for these reforms. The Kerrey-Danforth entitlement commission could absorb and answer the initial opposition and help mobilize support, if its leading members believe that the White House would

How long will this cycle last? No one can be certain when the current expansion will naturally end, but it probably has at least four more quarters to go. Over the last year, growth accelerated as long-term interest rates fell and a recapitalized banking system responded to rising demand for credit at the lower rates. Through the rest of this year and into 1995, strong corporate earnings should support healthy business investment, and higher cash flows for the many households benefiting from mortgage refinancing and rising stock prices in 1993 and early 1994 should drive consumption spending.

The Federal Reserve's recent interest-rate hikes may help lengthen the cycle by moderating the recent spurt of strong growth, but the Fed alone cannot sustain the expansion much beyond its natural course. Consider the problem from the point of view of factory capacity and employment. Expansions normally expire when the economy's capacity to expand production and employment is exhausted. Factories and offices run at full capacity and additional workers are hard to find at prevailing wages, but demand continues to grow. This gives rise to inflationary pressures so the Fed steps down hard on demand with higher interest rates, and the economy snaps back and down.

Today, 83 percent of the economy's factory capacity is in use, less than two percentage points lower than the peak for the 1980s expansion, which ended quickly after the "capacity utilization rate" hit 84.8 percent. There should be a bit more room this time since strong business investment and corporate downsizing have increased the economy's productive capacity. As a result, peak capacity utilization is now probably about 86 percent. Similarly, the current unemployment rate is 6.4 percent, or just about one percentage point from the lowest (adjusted) point in the 1980s expansion.

At the rate at which business has brought on line its unused capacity and hired new workers over the last two years, the current expansion should have about one year to go before reaching its peak.

We cannot depend on Fed fine-tuning to forestall the downturn. There are those who say that the Fed can continue to fine-tune the cycle, using incremental interest rate changes that modulate demand and so ensure that the expansion never hits the ceiling. The Fed has *never* been able to pull this off in the past; and its ability to do so now is *less* than it used to be, because financial deregulation and global capital have weakened its control over the total supply and price of credit. Besides, will a Republican Fed chairman, who tried hard to promote a strong economy for a GOP president in 1992 -- *and failed* -- do better this time?

The bottom line: Under current policies, the expansion could stall by mid- to late-1995, without addressing the economy's nagging structural problems.

meaningful income gains for most working Americans. In the 1980s only highly educated and skilled workers -- professionals, managers, investors -- gained significant economic ground, while the middle class saw their incomes inch up by less than 5 percent over the decade. If the CEA is correct, the 1990s will be the *fourth* consecutive decade of declining rates of growth and income gains.

The economy's problems are evident in the current expansion, which has been weak and could soon end. It began *more than three years ago* in April 1991, and so already has lasted longer than all but three of the eight business cycles since World War II. Its first year (April 1991 to March 1992) was the slowest first year of any postwar cycle, with economic demand growing by 1.8 percent, versus the average 6.5 percent. The cycle accelerated in 1992 as the campaign ended and the President's program was implemented, and demand in the second and third years of the expansion grew one-third faster than the average. This year, however, will be weaker than the fourth year of other postwar expansions lasting this long.

Annual Growth Rate of Domestic Final Sales, Postwar Expansions

	Previous Postwar Expansions	Current Expansion
First Year	6.5%	1.8%
Second Year	3.9%	4.5%
Third Year	3.8%	5.9%
Fourth Year	5.4%	3.5% (est.)

Moreover, on a quarterly basis this cycle is emerging as *the weakest of the postwar era*. At this rate, the expansion will not produce significant income gains for most people. Its success, therefore, will have to depend on its duration, and thus on the President's ability to put in place policies to gather new, sustained strength.

Length and Strength of Postwar Expansions

Start	Duration in Quarters	Real GDP/Quarter
1954/3	12	1.00%
1958/3	7	1.57%
1961/2	34	1.35%
1970/1	11	1.27%
1975/2	19	1.10%
1980/3	4	1.00%
1982/4	30	1.03%
1991/2	12 (to date)	0.75%

THE PRESIDENT HAS SEEN 11/27

May 31, 1994

CLINTONOMICS: THE CASE FOR A MID-COURSE CORRECTION

Robert J. Shapiro

The economy is growing, the deficit is shrinking, trade is expanding. Yet President Clinton's economists forecast slower growth through the 1990s than in the 1980s, tacitly acknowledging that the U.S. economy's structural problems persist. In addition, interest-rate increases and other economic evidence signal that the current expansion could well end by early 1996. The President has ample time, however, to combine good policy and good politics by adjusting his program to target these problems and promote strong sustained growth.

The basic challenge for the rest of 1994 and into 1995 is to adopt policies that can, at once, permanently increase the economy's long-term productivity and help extend the current expansion. In the main, this course closely tracks the economic strategy proposed by Governor Bill Clinton in 1992. First, next year's budget should include fundamental entitlement reforms to both break the structural budget deficit once and for all, and deliver another timely dose of low long-term interest rates. Second, the President's next budget also should provide for substantial public investment in education, training, research and infrastructure, financed by deep cuts in unproductive business subsidies. Third, Congress can promote growing demand for U.S. products next year and into the future by implementing the GATT agreement this year. Fourth, the President can boost business and job formation by deregulating small and new businesses.

These steps build on the Administration's considerable achievements. Last year's budget reforms have reduced federal spending's claim on the economy over the next five years to an annual average of 21.5 percent of GDP, as compared to 23 percent under Presidents Reagan and Bush. And approval of NAFTA and conclusion of the GATT should extend the global economic reach of American workers and firms.

Yet these reforms have *not* significantly altered the U.S. economy's long-term prospects. The President's Council of Economic Advisers (CEA) forecasts that real growth for the rest of this decade will average only 2.6 percent a year -- significantly less than the 2.8 percent average of the 1980s. That will be too slow to generate

raising taxes — as the Republicans propose to do — will require devastating reductions over the next seven years in the discretionary side of the budget. These reductions will dwarf the largest cuts Ronald Reagan ever proposed. Allowing discretionary cuts to pay for tax cuts will likely lead to still-larger tax cuts and still-deeper discretionary cuts in the years ahead and make this problem more severe.

It is understandable that the White House would feel a strong temptation to follow this route. It makes it easier to pay for a larger middle-class tax cut. But the long-term consequences for children's programs and other discretionary programs are serious.

III. Investments

The Republican Congress is likely to reject many of the Clinton investments. I would recommend having a shorter list of investments than in last year's budget, choosing the investments carefully, and picking several of the investments proposed in the budget to fight for visibly.

* Among the investments I would keep in the President's budget are Head Start and WIC. I understand that the "passback" to HHS and USDA shortly before Thanksgiving included an increase of \$400 million for Head Start and \$350 million for WIC. I think those are very reasonable numbers. I hope they have not been reduced since late November.

I don't know enough about what the budget contains for other investments or children's programs to offer comments on them.

IV. Larger Strategy Questions

One final concern. I hope the White House is considering which elements of the Contract it most wants to beat and what allies it needs to do so. The question then arises of whether any of the cuts proposed in the budget would undermine such alliances. In other words, are there any budget cuts under consideration that would jeopardize larger, more important Administration goals and priorities? I don't know whether the White House is pursuing these questions in fashioning its budget cuts.

December 13, 1994

For both political and policy reasons, the Administration shouldn't propose a tax cut that benefits upper-middle income families more than families right in the middle of the income spectrum or hard-working families in the lower-middle class.

- If the tax cut is provided in the form of a tax credit, the credit should be at least partially "refundable." A refundable tax credit is one, like the earned income credit, that provides a payment to families that qualify for it but have incomes too low to owe income tax. A *non-refundable* credit does not provide a payment to those owing no tax. A substantial fraction of families with children owe no income tax and would not benefit from a middle-class tax cut provided as a non-refundable credit. (They also would not benefit from an increase in the personal exemption or expanded IRAs.) On the other hand, many of these families are benefitting from the expansion of the earned income credit.

Making a tax credit fully refundable probably increases its cost too much, but there are lower-cost options that involve partial refundability. The children's tax credit in the Contract with America is refundable to a very limited degree. If it proposes a tax credit, the White House might consider including at least as much refundability as the Contract's tax proposal does.

Paying for the Tax Cut

Under current law, a tax cut must be paid for through offsetting cuts in entitlements or increases in taxes. I understand that one option now under consideration calls for changing the budget laws so that the savings from lowering the cap on discretionary (i.e., non-entitlement) programs can be used to pay for tax cuts.

I believe this would be a dangerous route to follow. Once the Administration proposes changing the budget law to allow cuts in discretionary programs to be used to pay for tax cuts, the Republicans will seize upon it. They are likely to cut discretionary programs substantially deeper than the Administration proposes to do — and to use the additional savings to help fund larger tax cuts. This is a pattern that could be repeated in subsequent years.

Since the current budget structure was enacted in 1990, the requirement that a tax cut be paid for by an entitlement cut or a tax increase has worked extremely well in restraining tax-cutting. To abandon this procedure just when the Republicans are searching for ways to finance their rather massive tax cuts would, in my view, be folly. To balance the budget in seven years without touching defense or Social Security or

view that he lacks core beliefs and is essentially a pol who doesn't stand for basic principles.

- It would anger the groups that supported the White House on health care reform. It would antagonize governors as well. It's hard to figure out who would like the proposal.

II. Middle-Class Tax Cut

I understand the political need to propose a middle-class tax cut. The question is how to design it and how to pay for it. Here are some thoughts.

- Keep the tax cut as modest as possible consistent with achieving its political goals. The Administration's tax cut will be a starting point, from which the size of the tax cut will grow on Capitol Hill. And with the balanced budget constitutional amendment likely to pass — and Social Security and defense off-limits — a large tax cut will make the reductions in other parts of the budget even more excruciating as we approach 2002. (2002 is the year the budget has to be balanced under the proposed constitutional amendment.)
- Draw a firm line so high-income people don't get the tax cut. I gather the White House plans to do this.
- Provide the tax cut in the form of a tax credit rather than in the form of an increase in the personal exemption or an expansion of eligibility for Individual Retirement Accounts (IRAs). A tax credit provides the same amount of tax relief to a family at \$20,000 as to a family at \$75,000. By contrast, an increase in the personal exemption is worth nearly twice as much to upper-middle income families in the 28% tax bracket as to lower-middle and middle-income families in the 15% bracket. Expanding IRAs is the least desirable of these approaches. IRA tax breaks are already available to families with incomes up to \$50,000 (about 70% of families). A proposal to expand the IRA tax break would principally benefit those at higher income levels. Moreover, average middle-income families can't afford to put much into IRA accounts, while more affluent families can. The data showing that the expanded IRA tax bracket would be of little value to typical middle-income families are strong. (There may also be other middle-class tax cut options under consideration. I'm not aware of the specific tax cut proposals being considered.)

Of particular concern is the fact that the most important advance in health care coverage for children over the past decade — the federally mandated extension of Medicaid to cover virtually all low-income pregnant women and young children and (by 2002) virtually all poor children through age 18 — would be in serious jeopardy. The federal requirement would disappear under the proposed block grant, and this would be a likely place for states to cut back.

- Also in jeopardy would be the federal requirement that states provide Early Periodic Screening, Diagnosis, and Treatment (EPSDT) exams for children in Medicaid and provide Medicaid coverage for medical problems uncovered by the EPSDT exams. This requirement, also, would be dropped under a block grant.
- Another group likely to be adversely affected would be elderly poor people who are not on SSI. Federal law requires that Medicaid help pay the ever-mounting Medicare premiums, deductibles, and co-payments that these low-income elderly face. Under the proposed block grant, many states could be expected to pare back or drop this coverage.
- Yet another problem is that Medicaid coverage would have to be cut back sharply during recessions. Under the current entitlement structure, increased federal Medicaid matching funds automatically become available when state Medicaid caseloads and costs rise during recessions. Under a block grant, a state's federal Medicaid funding for a year would be fixed; no additional funds would be provided if a recession hit. If the economy turned down, many states would be forced to put new Medicaid applicants (such as poor children in newly unemployed families) on waiting lists for Medicaid.
- Also, if a formula were developed to allocate block grant funds among states, still another problem could arise. Some states would be big "losers," while other would be "winners."

Political Problems

- This proposal would be seen as an Administration flip-flop. One year, the President proposes universal coverage. The next year, he proposes changes that would swell the ranks of the uninsured.
- As a result, this would likely be seen as crass political repositioning on the part of the President. That would intensify the already too-widespread

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12-14-94

ISSUES RELATING TO THE BUDGET

This memo covers the following areas: turning Medicaid into a block grant; the middle-class tax cut; investments; and thinking strategically about budget cuts. I have limited knowledge of what's under consideration now and thus can't comment on other issues.

I. Medicaid Block Grant

An option has been developed to turn Medicaid into a block grant and cap it so it grows at 7% to 8% per year (rather than at the higher rates at which it is currently projected to grow). This is a very unwise idea for both substantive and political reasons.

Substantive Problems

- Absent strong action to reduce the rate of growth in costs throughout the U. S. health care system, this proposal would compel states to make large cuts in Medicaid eligibility and/or services. *The strong likelihood is that the number of uninsured would rise significantly as a result.*
- The proposal's proponents apparently argue that the rate of growth in Medicaid costs — projected at about 12% — is too high, and states should be able to bring it down to 7% or 8%. This argument misses several points. First, the 12 percent rate of growth in Medicaid costs is due not only to the rise in health care costs throughout the U. S. health care system but also to growth in the Medicaid beneficiary population. The number of beneficiaries is growing at a rate of about four percent per year, for three reasons: 1) federal requirements that states cover more poor children each year; 2) the steady growth in the number of disabled people; and 3) the steady increase in the number of low-income people who apply for Medicaid when they lose employer-based coverage. Many states are already moving aggressively to control the costs of health services reimbursed under Medicaid by shifting to managed care. To slow overall growth further so it is 7% or 8%, the first step that many states would likely take — if freed from federal Medical requirements — would be to reduce, or slow the increase in, the number of beneficiaries. That would most certainly mean more uninsured people — and in particular, more uninsured children.

Brad Brown

\$144 Million Advice Network

A vast advice network has developed over the years within the federal government. When someone counted a couple of years ago, it consisted of 1,088 official advisory committees composed of 28,317 members whose operations cost \$143,911,021, or about a seventh of a billion dollars. The advice covers subjects as diverse as the space program and policy toward flue-cured tobacco. The network even has its own statute, the Federal Advisory Committee Act of 1972 (FACA).

As part of his "reinventing government" program, President Clinton eliminated a number of advisory committees through an executive order. A recent article in *The Post* indicated that 31 more committees currently required by statute are earmarked for elimination through omnibus legislation proposed by the Office of Management and Budget.

Great, but the president's effort, though well intentioned, is not a permanent resolution to the overall problem. Eliminating the Board of Tea Experts is not enough. The real problem stems, in large part, from FACA. Until this legislation is reexamined and amended, the proliferation of the federal government's advice network will continue.

An advisory committee is a formal group "which is established by statute or established or utilized by the president or any agency official for the purpose of obtaining advice or recommendations on issues or

Unless checked, it will proliferate.

policies within the scope of his or her responsibilities." Over the years, many of these groups have made valuable contributions in developing common-sense solutions to complex policy issues. On the other hand, some, quite frankly, have not, and they have wasted taxpayers' money.

The problem with advisory committees began with the administrative expansion promoted by the New Deal. These groups, then unchecked, started to grow in number, and as their power increased they collectively became known as a "fifth arm of government." They also began to worry the executive branch and Congress.

Critics pointed out that allowing industry leaders to meet with government officials created a potential antitrust problem. The concern was that a closed-door meeting of an advisory committee to discuss a proposed government action might give the committee members a competitive advantage over nonparticipants.

After years of discussion, FACA was

passed. It was an effort to reduce the potential for abuse and to improve the efficiency and effectiveness of these committees.

Under the act, open-door meetings were to be the standard and closed meetings the exception. New advisory committees were to be established only when it was "essential," and their number kept to a minimum.

FACA was put in place for good reason. But in the 22 years since it was passed, this streamlining measure has proven ineffective, and its intended purpose has not been fulfilled. The act's implementing regulations and guidelines are so vague, confusing and full of loopholes that closed-door meetings continue to abound, and the number of advisory committees has grown to a figure well beyond anyone's notion of "essential."

A report issued annually by the General Services Administration, which monitors committee activity throughout the government, indicated that in fiscal 1993 (as in FY 1992) there were more closed and partially closed meetings (2,225) than there were open meetings (2,162). In addition, once again the total number of committees was more than 1,000, a ridiculously high number relative to the clearly stated purpose of the act. The Department of Health and Human Services alone had 315 advisory committees costing \$59 million to operate.

If federal advisory committees are indeed the "fifth arm of government," the question we should perhaps ask ourselves today is, does it need 1,000 arms? With 28,000 committee members giving advice to the president and the executive branch, it's little wonder that decision-making is so difficult.

Today we are interested in the potential for strategic alliances, joint initiatives and government-private sector "partnerships." Such relationships, like those in "virtual corporations," have to be based on trust and the type of fluid communications that FACA prevents. The president cannot encourage business and government to communicate better and work together without calling for FACA to be amended.

In many respects this well-intentioned piece of legislation now impedes progress. It is outdated and is not equipped to allow the private sector to work with the federal government in a common-sense fashion relative to our evolving technological environment.

Proposing periodic legislation to cut 31 or 310 advisory committees will not resolve a thing because, like dandelions, more new committees will crop up next year to replace them. Historically, asking Congress and federal agencies for "restraint" (as this president has) in creating new advisory committees proved ineffective. That should change with the new Congress. But if the president truly wants to "create a government that works better and costs less" relative to advisory committees then he should ask the GSA to tighten pertinent implementing regulations and guidelines. Most important, however, he should call for a complete reassessment of the legislation that has provided us with all these advisory committees in the first place.

The writer was chief counsel for technology at the Commerce Department in the Bush administration.

The Stagnant Wages Theory: Don't Bet the Farm on It

What are the Democrats to do? With the media stricken with Newtomania, with everyone reading from the Republican "contract," the Democrats could be forgiven for lapsing into a strategy of mere sniping. They could simply hang back, wait for the inevitable slip—Newt's book deal, Newt's mom, Newt's House historian—and pounce.

Instead, remarkably, they have come up with an idea around which to rebuild a liberal agenda. Even more remarkably, both congressional Democrats and the White House are using the same song sheet. Rep. Richard Gephardt previewed the idea in a speech last month. President Clinton took up the theme at an address this week to a community college in Galesburg, Ill. The New Republic's Mickey Kaus has elaborated the idea and dubbed it the Stagnant Wages thesis.

It goes like this: While official statistics declare all kinds of good economic news, the electorate is angry because the news on wages is not good. They are stagnant. Median household income is about the same today as it was 20 years ago. The Democrats lost because as the champion of the working man and woman, they controlled the government for two years and did nothing about it. True, unemployment is down. But that is not enough. Democrats must raise wages—Clinton in Galesburg: "I want to spend two years working on lifting incomes and prospects"—or they will suffer

more of the bitterness that the electorate turned on them in 1994.

There are several problems, however, with the stagnant wages theory and with pinning one's political renaissance upon curing it. First, the effect is exaggerated. It is true that median household income has remained stagnant for 20 years. But during the same 20 years, per capita income is up 25 percent.

Even if retraining is the solution, the payoff is a long way off.

How can individuals be earning more and households not?

Part of the answer is this: The households have gotten smaller, 15 percent smaller today than in 1973. There are fewer people in each household because of divorce, single parenthood, later marriage and longer life expectancy (the elderly tending to live more alone). And smaller households mean more households, dividing up the income pie into smaller pieces per household.

Consider a married couple each earning \$20,000 a year. They constitute one household earning above the national median. Divorce

them, and you've got two households each now below the national median. The economy is unchanged, their wages are unchanged, yet household income falls by 50 percent. What changed is that they did not stay together in a family where resources are pooled.

About half the stagnant income effect is thus an artifact of smaller families. The rest, however, is economically "real" and related to a variety of factors including competition from low-wage Third World countries and the long-term slowdown in American productivity growth (from 2.5 percent in the '50s and '60s to one percent over the past 20 years).

Here is where Gephardt and Clinton see their opening. The centerpiece of their new Democratic program is government-supported retraining and reeducation to help American workers move up from low-skill, low-wage jobs to high-skill, high-wage jobs. Unfortunately, retraining huge numbers of workers to increase wages and productivity is perhaps the hardest of all social engineering tasks. In a market economy, government is a very clumsy instrument for guiding such fundamental changes. If we knew how to boost wages and productivity, we would long ago have done it.

Moreover, while the Democrats propose to socially engineer a fatter paycheck, the Republicans propose a simpler, quicker way to get there: cut taxes. Government has no clear idea how to raise wages, but it does have a clear way to increase take-home pay: cut the government's take.

Gephardt and Clinton cottoned on to this idea right after the election. They tried to match the Republican offer of a middle-class tax cut with one of their own. But their one-shot tax cut will have little effect on the stagnant wages syndrome.

And in the long run, Democrats can never match the Republicans in a tax cut competition. Republicans are committed in principle—i.e., for non-economic reasons—to cutting government, which would allow larger and larger tax cuts that would raise take-home pay. The liberal idea of government as the engine of social change, indeed the instrument of retraining and heightened productivity, would never allow Democrats to match them. And finally, even if retraining is the solution to the stagnant wage problem, the payoff is a long way off, years beyond even a second Clinton administration. Tax cuts can be felt tomorrow.

Clinton's seizing on the Stagnant Wages theory as the vehicle for rebuilding his domestic agenda shows energy and fight. It shows that while wounded, this administration, unlike the Bush administration in its terminal stages, is far from brain dead. It is, nonetheless, testimony to the depths of the Democrats' current political quandary that the Republicans, if they take Clinton's strategy seriously, are well placed to beat him even at his own game.

William Raspberry

Rejecting Our Own Extremists

Robert Theobald, the futurist, has a surprising candidate for the title "most dangerous phrase."

It is: "I understand . . ."

As in "I understand" why some inner-city teenagers are so violent, or why some animal rights advocates attack fur-wearing women, or why some right-to-lifers kill abortionists.

Understanding unacceptable behavior encourages unacceptable behavior, he says, and the result is the destruction of community, of civility and even of conversation that could lead to the solution of mutual problems.

"Oh, we're quite capable of censuring the attitudes of those on the other side," he explains. "I mean we keep saying, 'Isn't it outrageous that they do this sort of thing?' My point is that we've got to learn to reject our own extremists."

Theobald—who was born in India 65 years ago, grew up in Great Britain and now lives in New Orleans—says the importance of each side reining in its own extremists occurred to him while he was thinking about the violence in Northern Ireland.

"There just aren't that many hard-core IRA people," he said. "Certainly not enough to sustain the level of terrorism and violence we've seen. But there is a significant number of people who say, 'I wouldn't do that, but I understand why they do.' And that understanding gives them the political and moral cover they need."

The principle applies domestically as well, and to all sorts of issues.

"Suppose you are an environmentalist, and you're dismayed by the fact that your movement isn't having the effect you'd hoped. It's easy to find yourself 'understanding'—though, of course, not condoning—the people who go out and spike trees to protect them from loggers." (Loggers' chain saws hit the hidden spikes and fly apart, with deadly force.)

Those who make their living in the timber industry are, of course, outraged at such tactics.

Theobald's point is that committed environmentalists must also be outraged—and in unmistakable terms. "I understand" is a green light.

But it isn't just outrageous behavior that must be circumscribed, says Theobald. So must the outrageous rhetoric that precipitates the behavior. Tree-spiking seems less unreasonable when it happens in the context of a rhetoric that equates the harvesting of forests with the destruction of life on the planet. Shooting abortionists—the latest example of extremism in furtherance of a moral claim—becomes very nearly logical if you accept the rhetoric that abortion is murder of innocent children. Would you consider it wrong to shoot a madman who was poised to lob a grenade into a kindergarten?

It is Theobald's notion that there would be far less terrorism, tree-spiking and potshooting at abortion clinics if the partisans of the extremists learned to say: We won't tolerate certain behavior from our own allies. Nor, he insists, is it merely a matter of paralyzing squeamishness. Rejecting one's own extremists can have the pragmatic effect of creating the conditions for dialogue and negotiation—and change.

Which raises an interesting point. It is my belief (not necessarily Theobald's) that extremism, whether of rhetoric or behavior, is most likely to be the work of those pessimists who have given up on the possibility that their view will prevail.

If you believe in the reasonableness of your position, you're likely to spend your time trying to persuade your opponents: hearing and accommodating their objections, considering their perspective, meeting them halfway.

Activists who are convinced of both the rightness and the futility of their campaigns are freed of the necessity of acting responsibly. They can indulge in outrageous rhetoric and outrageous behavior, not caring at all what their opponents think or that they are rendering the problem more intractable. It's true of skinheads whose paranoia tells them that black people are the reason life is passing them by. It's true of the antisemites who manage to find a Jewish conspiracy behind their every difficulty and disappointment. It's true of shooters and looters, of lawless teenagers and brutal cops. It doesn't matter that most of the people who are experiencing the problem reject the extremist solution; all the extremists need is for their fellow sufferers to "understand" how they came to take such desperate measures.

It is the optimists—the people who believe that the cause is right and who can, through reason and negotiation, be made to prevail—who have to pass up the temptation to provide the extremists on their side the comfort and encouragement of Bob Theobald's "most dangerous phrase": I understand . . .

FRIDAY, JANUARY 13, 1995 THE WASHINGTON POST

The Shift to Early-Outs

By Mike Causey
Washington Post Staff Writer

For the Record

From an interview Wednesday with Walter Mondale, U.S. ambassador to Japan, on the "MacNeil/Lehrer NewsHour":

Jim Lehrer: I read a story that indicated that some of the people in the Japanese government thought Newt Gingrich was pretty much running the United States government now. Have you picked up that kind of thing since the Nov. 8 election?

Amb. Mondale: Well, they were baffled at first. They didn't know what had happened.

Q: What did you tell them had happened?

A: I said, "Look, you've lived most of your years with a divided government. Most of American history, you've had a president one party and the Congress another. And, you know, you went through—usually it's the other way around—a Republican president and a Democratic Congress. So, you're used to that."

I said, "Secondly, if you look at the underlying issues that affect U.S.-Japanese relations, there's pretty much unanimous opinion about the importance. . . ." And I said, "I don't think you'll find much change. . . ." But they did want to go up the Hill.

Q: Sure.

A: They were trying to figure out what's happening.

Q: In your absence—I don't know if you know this, but a lot of people blamed what happened on Nov. 8 on the Democrats just having blown the whole deal. You Democrats brought it on yourselves by not running the government properly. . . . What do you think about that?

A: Really, they said that?

Q: Yes, they really said that. I'm sorry.

A: I can't believe it.

Many federal employees who fail to get buyout offers in the next two months still will get the chance to retire early.

Most agencies will expand early-out offers to allow more employees to leave on immediate pensions if they are at least age 50 with 20 years of federal service, or any age with 25 years of service. Pensions are reduced 2 percent for each year the retiree is younger than 55. Some private companies cut pensions 5 percent for each year the retiree is younger than 65.

Early-outs will be the downsizing tool of choice when buyouts (worth as much as \$25,000) end March 31 in non-Defense agencies. Those agencies will still be under heavy pressure to meet the White House ordered 272,900-job cut, and the Republican Congress is expected to call for even deeper cuts.

Budget cutters want to avoid expensive and disruptive layoffs. Using buyouts, the Clinton administration has managed, so far, to avoid massive layoffs. Thousands of federal employees—mostly retirement-age white men—took buyouts which saved the jobs of younger, low-seniority workers who are first on the layoff list. Early-outs will be critical to downsizing unless Congress extends the buyouts for non-Defense agencies. That is possible, but there is no such plan in the works.

The Office of Personnel Management says 50 agencies are offering early-outs. The early-out window closes March 31 for staff members at OPM, Justice and the Office of Government Ethics and National Endowment for the Humanities.

Early-outs run through Sept. 30 at the National Credit Union Administration, TVA, National Labor Relations Board, Merit Systems Protection Board, National Endowment for the Arts, Board for International Broadcasting, Federal Deposit Insurance Corp., International Joint Commission, Overseas Private Investment Corp., Nuclear Regulatory Commission,

National Gallery of Art, National Archives, Department of Education, Export-Import Bank, Consumer Product Safety Commission, Smithsonian, Veterans Affairs and Housing and Urban Development.

Early-outs will end Nov. 30 at the CIA, July 31 for the Equal Employment Opportunity Commission and May 31 at the Federal Trade Commission.

Let George Do It!

George Nesterchuk, a top Reagan administration appointee, will be the staff director of the new House Government Reform and Oversight Committee's key civil service subcommittee. Rep. **William F. Clinger Jr.** (R-Pa.) is chairman of the full committee, and Rep. **John L. Mica** (R-Fla.) heads the civil service unit.

Nesterchuk was an aide to **Donald Devine** when he was director of the Office of Personnel Management. Devine ran the program to downsize the non-Defense side of government. He ran unsuccessfully against Rep. **Steny H. Hoyer** (D-Md.) last November.

Nesterchuk's appointment will cause added heartburn for federal unions that in the last decade have burned most of their bridges with House and Senate Republicans.

Virginia Tax Deadline

To be on the safe side, federal-military retirees need to send their Form FR 5 (saying whether they accept or reject the state's proposed pension tax refund settlement) by certified mail, return receipt requested. The Virginia Department of Taxation has sent reminders to many retirees—who say they already have filed the form—that they have no record of receiving it. Retirees need proof they met the Feb. 1 deadline.

Benefits Update

At 9 a.m. tomorrow on WUST radio, **Joe Richardson**, of Government Retirement Benefits, is scheduled to talk about retirement, investment and other benefits available to feds, retirees and their survivors. At 10 a.m., Rep. **Thomas M. Davis III** (R-Va.) will talk about what the Republican-controlled Congress may do to, and for, feds and retirees.

FRIDAY, JANUARY 13, 1995 THE WASHINGTON POST

The Republicans' Tax Mirage

The Republicans' capture of Congress, and particularly their emphasis on tax reform, might seem to be developments that economic conservatives should welcome. Republicans as a group are undoubtedly less friendly than Democrats to intrusive, steeply graduated taxation of income—a mode of taxation that is, in my view, inimical to saving, investment and long-run economic growth. The early post-election noises from Republicans on tax policy, however, leave me with a sense of unease, even dread, at what could prove to be a major missed opportunity.

For some time, the beginning and end of Republican tax policy has been to sing the one-note, supply-side litany of a capital gains tax cut. This policy, measured by its likely long-term effect on saving and investment, is a mirage. Perhaps the proponents of cutting the capital gains tax view that measure as a proxy for a cut in the tax on income from capital generally. If so, they have apprehended an important problem but not the solution. The problem is that the U.S. income tax system imposes a heavier burden on saving and investment than on immediate consumption. Although income from capital (which is the typical form of return from saving) and income from labor are ostensibly taxed at roughly the same rates, the tax on income from capital (on saving, that is) is actually a *second* layer of tax, because such income can ultimately be generated only by the investment of after-tax income derived from labor. Income from saving is thus in effect taxed twice compared with income from labor that is immediately consumed.

Income taxation therefore biases individual behavior toward consumption and

capital gain and its taxation is indefinite. If you own a capital asset that has increased in value mightily (shares of Microsoft, for example), a simple way to postpone capital gains tax is not to sell. If you hold a capital asset until death, the capital gains tax is permanently forgiven (through the mechanism of a fair market value basis at death). Taking into account the possible indefinite deferral of the payment of tax, the real tax cost of capital appreciation is fairly low.

It would make relatively little difference in the real tax cost of capital gains under the current income tax whether the nominal rate of tax on capital gains was the same as that on other income, lower, higher or even zero.

Where high capital gains taxes may make a difference is not so much in the tax cost of capital as in the *mobility* of capital. Because an obvious way to postpone capital gains taxes is to hold on to appreciated capital assets, high capital gains taxes do tend to lock in investments, and this "lock-in effect" may prevent investment from flowing freely to its most productive uses. Martin Feldstein recently pitched his support for capital gains tax cuts in the *Wall Street Journal* largely on this ground.

I think, though, that the proponents of capital gains tax cuts exaggerate the lock-in problem and overstate the need for capital gains tax cuts as a palliative. Capital can be unlocked by borrowing against unrealized capital gains, without tax cost, even when capital gains taxes are nominally high. Businesses and individuals (including me) routinely finance investments and consumption with mortgages, home equity loans and margin debt, all sources of liquidity that do not trigger formal realization of capital gains.

Meanwhile, a broader shift in the base of taxation from income to consumption would also promote the mobility of capital and have far more powerful effects on the consumption/saving boundary.

The idea that reduction or elimination of capital gains taxes would sharply reduce the tax cost of capital and induce large increases in investment is mythic. Thoughtful analysts of tax policy, such as Martin Feldstein, do not advance this ground of support for capital gains cuts, but others do, including much of the Republican top brass.

To promote capital formation effectively, it would be necessary to reduce the taxation of *all* income from capital, including interest, business profits, rents, royalties and dividends, which are—far more than capital gains—its predominant forms and which would be unaffected by a capital gains tax cut. The base of taxation, in short, should be shifted from income to consumption across the board. Capital gains tax cuts are a quarter-measure at best, and they reach mostly the wrong quarter.

What is ultimately most distressing about the recurrent focus on capital gains cuts as the end-all of tax reform is the lack of courage that it betokens. No politician that I know of was ever unseated for proposing capital gains tax cuts. History does pin a few political demises (Al Ullman's comes to mind) on the espousal of consumption taxes. Be that as it may, serious tax reform simply must shift some part of the tax burden away from savers and onto consumers.

Such a shift is more important than the nominal level of what we call "taxes." In order to be truthful with the public and with themselves, politicians must come to understand what taxes are and are not. Tax cuts, middle-class or otherwise, are not real unless they are accompanied by spending cuts. The true level of taxation is the size of

government. You can either pay for that government now, through current taxation, or later, through deferred taxation or inflation. A tax cut without a spending cut is an illusion. A spending cut, even without a nominal tax cut, is the only true tax cut. By this measure, the Reagan and Bush administrations, for all their supply-side rhetoric, did not cut taxes at all. Even the Clinton administration has performed better on this score, although perhaps despite itself.

The only way a legislator can cut taxes for real is to cut spending. But few if any of those clamoring for capital gains tax cuts are prepared to face the voters with a

Republicans know that people want higher real incomes, but they show little stomach for asking people to scale down and defer their consumption.

direct, unqualified assurance of lower spending. I will take the Republicans in Congress seriously when they tell people approaching retirement to expect lower Social Security and Medicare benefits, when they tell farmers that federal agricultural subsidies will be reduced, when they tell large defense contractors that the country does not need another strategic bomber designed to counter the threat posed by the Soviet Union of 1952, and when, if they can't or won't cut spending, they tell voters to expect to be taxed more heavily on their consumption. As a substitute for these sober messages, the promise of capital gains tax cuts and a \$500-per-child income tax credit is simply pathetic.

My surmise is that Republicans have not ventured much beyond supply-side bromides out of fear—fear, that is, of their constituents. We are told often enough that middle-class folk are upset, despite fairly high current levels of employment, because their real wages have increased little if at all in the past 20 years. That may well be why people are sore, but that is exactly what to expect from fiscal policies that favor consumption over saving. As capital becomes thin compared with labor, the marginal wage from work declines.

The U.S. economy has been a reasonably abundant generator of jobs in the past two decades—and that's fine—but as you keep adding jobs to a slow-growing base of capital investment, the real incomes of workers do not, and ultimately cannot, grow. Republicans know perfectly well that people want higher real incomes—who doesn't?—but they show little more stomach than Democrats to ask people to pay the price of gaining higher incomes, which is to scale down and defer their consumption.

Growth in investment depends on restraint on government largess and thoroughgoing tax reform. Judging by the marginal—even pusillanimous proposals that Republicans have thus far made the centerpieces of their program for smaller government, it is hardly too soon to declare their turn in power a failure.

The writer is a professor of law at the University of Chicago.

The beginning and end of GOP tax policy has been the one-note supply-side samba of a capital gains tax cut.

against saving. Over time, this means less investment and ultimately less growth than would occur without this tax-induced effect.

To eliminate the bias against saving, the base of taxation should be shifted from income to consumption, which can be accomplished by replacing income taxation with a sales tax, a value-added tax, a tax on consumed income or a payroll tax. Although these various taxes differ somewhat in their timing and in the degree of graduation that can conveniently be grafted onto them, they are essentially similar in macroeconomic effect and more neutral than a pure income tax in their effect on long-term capital formation. What all have in common is that unlike our current income tax, they do not reach income from capital (i.e., savings) until it is expended on consumption.

Cutting capital gains taxes would have a minor effect at best on capital formation. Capital gains are, to be sure, a type of income from capital, but one that is neither especially important nor even particularly highly taxed under the current regime. In fact, the real rate of tax on capital gains under current law is fairly low, despite a nominal rate approaching that imposed on other income.

The key is that capital gains are realized largely at the choosing of their owner. The time between the actual accretion of a

BY WILLIAM BOOTH—THE WASHINGTON POST

Kindergartners enjoy lunch at Jefferson County Elementary School in Fayette, Miss., where most eat for free.

School Worries That 'Johnny Can't Eat'

By William Booth
Washington Post Staff Writer

A1

FAYETTE, Miss.—When the first yellow buses of the morning arrive at Jefferson County Elementary School caked in red clay from their dawn runs through the back roads of rural Mississippi, the children do not walk to the cafeteria. They run.

"I got a little boy come in here every morning and eats everybody's food. Just licks the plate. And you know he's not the only one," said Jeanette Reeves, eagle-eyed and dressed in starched white, a cafeteria manager who doesn't have to tell the children twice to eat all their lima beans. "Many of these children get their only meals right here at school. Lord, it'll be cruel to change that."

As Congress considers ending the federal school breakfast and lunch programs and giving the states block grants and the responsibility of feeding their own children, the subtleties of a debate over the new federalism are lost on many here.

They define the issue a little differently. For them it is about full bellies and fear.

For better or worse, many people here have come to rely on the federal program, and they worry that the educational issue of the late 1990s will no longer be "Johnny can't read," but "Johnny can't eat."

See LUNCHES, A6, Col. 1

LUNCHES, From A1

Six of 10 children in Mississippi receive a free or subsidized school lunch. And Jefferson County—poor, rural, 85 percent black—is just the kind of place that policymakers in Washington were thinking of when they began the nationwide feeding program almost five decades ago.

It is not hyperbole to say the federal government feeds the children of Jefferson County. School officials say 97 percent of the children here eat free lunches. About 80 percent get a subsidized or free breakfast. At least a dozen other Mississippi counties have participation rates almost as high.

Without a federal mandate, parents and school officials here worry that the state will fail to match current spending and support—a concern shared by Democratic lawmakers in Washington who have called the repeal of the National School Lunch Act "unconscionable . . . a swindle . . . and a fraud."

House Majority Leader Dick Armey (R-Tex.) insisted that funding for the program was not being cut but increased by 4.5 percent a year and argued that the states, being closer to the schools, are better administrators for the programs than the federal government. He accused Democrats of "scare tactics" and of having "nothing to offer but fear itself."

But William Billups, the black principal of all-black Jefferson Elementary, is not so sure. A Republican himself, Billups likes much of what he sees these days in House Speaker Newt Gingrich's Washington. But ending the federal school lunch program is too much for him. Billups does not trust the state of Mississippi.

"It's a crap shoot what they'll do with the money," he said, interrupting himself to reach up to ring the school bell. "I'm not saying, if it comes to it, that Mississippi would let its children go hungry. But come on. They'll take a little here and take a little there. It'll be political and I don't think we should be political about food."

Billups points a finger toward the state capitol in Jackson, where one of the most divisive ongoing debates in Mississippi's legislature is the fight between Democrats and

Republicans. Conservative Republican Gov. Kirk Fordice contends Mississippi already spends too much on its schools, that administrative costs are too high, that teachers need to teach better before they are paid more. In this political climate, the prospect of turning the feeding programs over to the state scares Billups and his school's parents.

A spokeswoman for Fordice said the governor was an enthusiastic supporter of block grants but had not decided what he would do about the breakfast and lunch programs. "Kirk Fordice will take care of his fellow Mississippians, and anyone in the state will tell you that," spokeswoman Johnna Van said. "It's an arrogant insinuation for anyone to suggest that Mississippi can't or won't take care of its own."

Many in Mississippi are old enough to remember it was the federal government that ended state-sanctioned segregation and imposed civil rights here 30 years ago. When they hear Mississippi is going to take over the school lunch program, they hope for the best, but they do not count on it.

"The closer you get to the ground, the more politics you get, and when there is competition for scarce resources—in Mississippi or anyplace else—the powerful will prevail," said Jane Boykin, president of the Mississippi Forum on Children and Families, an opponent of transferring the feeding programs to the states.

If there was ever a place that could use a free lunch, it is Jefferson County. The community is completely dependent on monthly welfare checks and food stamps. Four of 10 residents live below the poverty line, including more than half the children. The number of unwed teenage mothers has doubled in the past decade. The county's largest employer is the school system, followed by the county government. Were it not for the monthly government checks, Jefferson County would not have an economic reason to exist.

Two of the county's three small manufacturing plants have closed in the last three years—the jobs gone to Mexico. Many of the graduates of the high school who don't get pregnant leave the county for jobs in Houston or Atlanta. It is a county of mothers and children and old people.

Out in the countryside, most families live in old trailers surrounded by howling dogs and in battered houses at the ends of long drives with names like Hard Times Road. School buses often arrive before 6 in the morning. Children come to school neat and clean, but mothers say it is hard to get their sons and daughters ready so early and also give them breakfast or a sack lunch.

Most of the mothers are single parents and most receive federal assistance. They say food stamps alone do not get them through the month and that cash welfare payments are not enough to cover the costs of a 50-cent breakfast or a 75-cent lunch—especially when multiplied by several children.

"You can't afford to fix a lunch 20 times a month for two or three children," said Loretta Starks, a substitute teacher and mother of one who is working to get her teaching certificate. She lists the costs of juice, bologna and bread to the penny to prove her point.

The schools offer a free lunch to children from families with incomes below \$8,000 a year. The lunches are subsidized—going for half price—to families with incomes below \$15,000. Children from families earning more than about \$15,000—only 3 percent of the school children—pay full price. Almost all the families on welfare get free lunches because a mother with two children gets a maximum of \$120 in cash welfare and \$304 in food stamps each month.

Principal Billups says the breakfast and lunch programs are as necessary as desks and books. "You can see, when they don't

have breakfast, the little ones are all droopy and lethargic," he said. "They can't keep their minds of their work when their stomachs are growling."

He agrees a few children might be getting a free or subsidized lunch when they do not really need one. "But if you're trying to get the few who are getting a free ride and cut back on those who don't, it's not fair," he said.

"The children here can make it," Starks said. "They just need some help."

Starks and many other mothers ask: If the federal government can send food to Africa, why not Mississippi?

"They're pumping millions of dollars into Somalia and Africa and maybe now they're thinking about taking away the little bit of money they give to my children?" Billups asked. "The Republicans say they're not racists. And I guess I believe them. But look at all the programs they're attacking."

This week, under Jeanette Reeves's watchful eyes, children were eating fried chicken, lima beans, peaches, mashed potatoes and corn bread at Jefferson Elementary School.

"Some of these children, I think they only eat at the school, really," she said. "You can't tell looking at them. They might get some snacks or something at home, but they eat their real meals in the cafeteria. It's sad that some mamas are like that, from drugs or whatever. But that's the way it is. It doesn't seem right to blame the children. All those growling little stomachs. I just hope it all works out."

Dollar Keeps Falling Against Yen and Mark

*Analysts Call Decline
A Long-Term Trend*

By John M. Berry
Washington Post Staff Writer

A

The dollar continued to fall on international currency markets yesterday, hitting a new low against the Japanese yen for the third day in a row and weakening further against the German mark.

Many foreign exchange experts said the dollar's weakness is not just a temporary problem, but rather part of a long-term downward trend against the mark and yen, although the dollar is likely to rally from time to time.

There was broad agreement among experts that there is little President Clinton, the Treasury Department or the Federal Reserve can do to give the dollar a boost. Coordinated purchases of dollars on Friday by the Fed and other central banks around the world had almost no impact on the currency's value.

In late New York trading yesterday, it took just 92.80 yen to buy a dollar, down from 94.05 on Friday. Against the mark, it took 1.4048 marks to buy a dollar, the lowest level in more than two years, down from 1.4250 on Friday.

The reasons for the dollar's downward trend, the analysts said, are complex and varied. Some are real, some are psychological; some are as new as the financial crisis in Mexico and some are as old as the tendency of Americans not to save money.

First and foremost is the fact that the United States is running a deficit with the rest of the world of more than \$150 billion a year in trade, tourism and similar transactions,

See DOLLAR, A11, Col. 1

Analysts See Dollar Continuing To Weaken in Currency Markets

DOLLAR, From A1

said economist L. Douglas Lee of NatWest Washington Analysis.

That means that each year foreigners end up with \$150 billion that they may not wish to hold and so exchange for another currency, driving down the dollar's value. In the view of Lee and many other analysts, as long as the United States keeps pushing that many dollars into foreign hands every year, the currency has little chance of strengthening in a fundamental way.

A second key reason for the recent weakness of the dollar that many analysts cited is an abrupt shift in expectations about the level of U.S. interest rates compared with those in other countries, especially Germany.

"The dollar's decline this year has coincided with the evaporation of earlier expectations of future sharp increases in U.S. short-term rates," said John Lipsky, chief economist at Salomon Brothers Inc. in New York.

The level of interest rates is important for a currency because higher rates can encourage investors to move their money from one country to another. Until a few weeks ago, many analysts and investors had expected that the Fed would continue to raise interest rates as it did all last year to cool off the U.S. economy and prevent a surge of inflation. However, recent statistics suggest that U.S. economic growth is slowing and many analysts are no longer looking for higher rates.

A third major reason the dollar is being hammered is that its value has been declining for many years compared with German and Japanese currencies, and some foreign central banks are switching their foreign exchange reserves out of dollars.

"The track record of the dollar in recent years has been poor, and that's what these investors look at, the record," said Scott E. Pardee, special adviser at Yamaichi International (America) in New York. "The U.S. economy is doing fine, but dol-

lars that have been in other hands for many years are being converted into marks and yen."

A fourth key development hurting the dollar, the analysts said, is the political and financial crisis in Mexico, which led the Clinton administration to forge a huge international rescue package, with the United States putting up \$20 billion in loans and loan guarantees.

There is a widespread perception that the United States will suffer in a variety of ways because of its close links to Mexico, including a likely large decline in U.S. exports that will make the U.S. trade deficit worse.

Yet another reason mentioned by the analysts is the currency turmoil within Europe that led to a devaluation yesterday of the Spanish peseta and Portuguese escudo relative to the mark, which is seen by investors and speculators as a "safe haven."

Meanwhile, many Japanese firms are selling the dollars they are earning from exports to the United States in exchange for yen. They are using that yen to cover losses or operating expenses at a time Japanese banks are reluctant to make new loans.

Analysts such as Lee noted that so long as Americans save such a small portion of total national income that they cannot finance the nation's investment costs—plus the combined deficits of federal, state and local governments—foreign investors must make up the difference. In an accounting sense, the gap between saving and investment is equal to the U.S. deficit in trade, tourism and other transactions.

"The way to address the problem is to do something to bring savings and investment closer together—such as reduce the federal [budget] deficit," Lee said. And that pointed to yet another reason for the dollar's weakness—last week's Senate defeat of a constitutional amendment to require a balanced budget, which "was read as a negative by the currency market," Lee said.

Charles Krauthammer

Social Security 'Trust Fund' Whopper

Last week, Sens. Kent Conrad and Byron Dorgan managed to (1) kill the balanced budget amendment, (2) deal Republicans their first big defeat since November and (3) make Democrats the heroes of Social Security. A hat trick. How did they do it? By demanding that any balanced budget amendment "take Social Security off the table"—i.e., not count the current Social Security surplus in calculating the deficit—and thus stop "looting" the Social Security trust fund.

In my 17 years in Washington, this is the single most fraudulent argument I have heard. I don't mean politically fraudulent, which is routine in Washington and a judgment call anyway. I mean logically, demonstrably, mathematically fraudulent, a condition rare even in Washington and not a judgment call at all. Consider:

In 1994 Smith runs up a credit card bill of \$100,000. Worried about his retirement, however, he puts his \$25,000 salary into a retirement account.

Come Dec. 31, Smith has two choices: (a) He can borrow \$75,000 from the bank and "loot" his retirement account to pay off the rest—which Conrad-Dorgan say is unconscionable. Or (b) he can borrow the full \$100,000 to pay off his credit card bill and keep the \$25,000 retirement account sacrosanct—which Conrad-Dorgan say is just swell and maintains a sacred trust and staves off the wolves and would have let them vote for the balanced budget amendment if only those senior-bashing Republicans had just done it their way.

But a child can see that courses (a) and (b) are identical. Either way, Smith is net \$75,000 in debt. The trust money in (b) is a fiction: It consists of 25,000 additionally borrowed dollars. His retirement is exactly as insecure one way or the other. Either way, if he wants to pay himself a pension when he retires, he is going to have to borrow the money.

According to Conrad-Dorgan, however, unless he declares his debt to be \$100,000 rather than \$75,000, he has looted his retirement account. But it matters not a whit what Smith declares his debt to be. It is not his declaration that is looting his retirement. It is his borrowing (and overspending).

Similarly for the federal government. In fiscal 1994, President Clinton crowed that he had reduced the federal deficit to \$200 billion. In fact, what Conrad calls the "operating budget" was about \$250 billion in deficit, but the Treasury counted the year's roughly \$50 billion Social Security surplus to make its books read \$200 billion. According to Conrad-Dorgan logic, President Clinton "looted" the Social Security trust fund to the tune of \$50 billion.

Did he? Of course not. If Clinton had declared the deficit to be \$250 billion and not "borrowed" \$50 billion Social Security surplus—which is nothing more than the federal government moving money from its left pocket to its right—would that have made an iota of difference to the status of our debt or of Social Security?

Whether or not you figure Social Security in calculating the federal deficit is merely an accounting device. Government cannot stash the Social Security surplus in a sock. As long as the federal deficit exceeds the Social Security surplus—that is, for the foreseeable future—we are increasing our net debt and making it harder to pay out Social Security (and everything else government does) in the future.

Why? Because the Social Security trust fund—like Smith's retirement account—is a fiction. The Social Security system is pay-as-you-go. The benefits going to old folks today do not come out of a huge vault stuffed with dollar bills on some South Pacific island. Current retirees get paid from the payroll taxes of current workers.

With so many boomers working today, pay-as-you-go produces a cash surplus. That cash does not go into a Pacific island vault either. In a government that runs a deficit, it cannot be saved at all—any more than Smith can really "save" his \$25,000 when he is running a \$100,000 deficit. The surplus necessarily is used to help pay for current government operations.

And pay-as-you-go will be true around the year 2015, when we boomers begin to retire. The chances of our Social Security benefits being paid out then will depend on the productivity of the economy at the time, which in turn will depend heavily on the drag on the economy exerted by the net debt that we will have accumulated by then.

The best guarantee, in other words, that there will be Social Security benefits available then is to reduce the deficit now. Yet by killing the balanced budget amendment, Conrad-Dorgan destroyed the very mechanism that would force that to happen. The one real effect, therefore, that Conrad-Dorgan will have on Social Security is to jeopardize the government's capacity to keep paying it.

Having done that, Conrad-Dorgan are now posing as the saviors of Social Security from Republicans looters. A neat trick. A complete fraud.

WELL, WE'VE BEEN SAYING WE THOUGHT OF HIM AS A SORT OF PEACEMAKER™



For the Record

From remarks by House Speaker Newt Gingrich at a press conference in Washington on March 7:

Mr. Gingrich: No Congress that I know of ever has worked as hard as this Congress is starting off. We still have another 37 days to finish getting this done. It is very hard work. But I also think that people around the country have the sense that we're seriously trying to bring about real change and that we're keeping our words. I think it's worth getting through this—I can assure all of you, for your own personal planning, that when we get back after the April break, May will not be like this. . . .

Q: It seems, though, the response to the Republican initiatives now has coalesced into a general accusation that you're engaged in class warfare. . . .

A: Surprise, surprise! The liberals have found the same charge they used against Reagan and against Bush, and I suspect used against Eisenhower, although that was earlier enough they may not. But go ahead.

Q: A lot of your programs initially do tighten up government help to the poor and expand opportunities for those with resources.

A: Well, first of all, 90 percent of the money in the \$500-per-child tax credit goes to people with under \$100,000 in income. So I don't regard giving—allowing people to keep \$500 for their own child, if you're a family of \$25,000 or \$30,000 or \$40,000 income, as helping the rich. I mean, I'm not sure, you know—it is true that we send more money back to the states, that we decentralize dramatically. It is true that we reject the welfare state model and that we insist on a work ethic. But I think those are legitimate differences about how you would philosophically solve the problem.

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LETTERS TO THE EDITOR

Still a Need for Affirmative Action

Lally Weymouth's Feb. 15 op-ed column, "J. C. Watts: No Excuses," shows Mr. Watts's lack of understanding and appreciation for affirmative action. Because he is a primary beneficiary of affirmative action, it is surprising that he opposes it so strongly.

J. C. Watts received an athletic scholarship to educate himself, which he did, and was the star quarterback on a national champion NCAA football team at the University of Oklahoma. The athletic scholarship was an investment by the government of the state of Oklahoma in his future and the future of the state. The existence of the oil-rich state of Oklahoma was the result of the federal government's Homestead Act, and the existence of the University of Oklahoma was the result of the federal government's Land Grant Act.

Prentiss Gault was the first African American to play football at Oklahoma University, but it was government action (or the threat thereof), including affirmative action, that finally broke down the institutional barriers for other black athletes, students, administrators

and professors to become a part of the university. They were not trailblazers like the exceptional individual Prentiss Gault. The government played a major role in breaking down barriers on behalf of the masses of average students.

Ms. Weymouth shares Mr. Watts's comments—"quotas, they haven't worked"—but not the context of his comments. She neither challenges his equation of affirmative action and quotas nor shares information which shows that affirmative action has worked or is still needed. For example, according to the U. S. Department of Labor, women represent 51.2 percent of the adult population, blacks 12.4 percent and Hispanics 9.5 percent. Today there are 22.3 percent female, 4.2 percent black and 5.2 percent Hispanic doctors in the country. These statistics suggest that affirmative action is working but that it needs to be continued to constantly narrow and eventually eliminate the gap.

Mr. Watts suggests that affirmative action only helped the "upper-income minorities." That, too, is untrue. Police,

fire, construction and entry-level jobs have all been gained, in the main, because of affirmative action. While affirmative action is not the whole answer and is a conservative remedy, it is probably most responsible for the creation of the emerging middle class in minority communities and for the fuller development and contribution of women in the workplace and in universities.

While Mr. Watts and his parents are to be commended for being responsible hard workers, so are most African Americans and Americans in general. He is an exceptional young man, but he could not have achieved had he not been afforded the opportunity. All Americans deserve the opportunity to achieve. Affirmative action is just one solution for those who have been denied that opportunity. It is a solution that is working, and Mr. Watts should join its other beneficiaries in supporting its continued success.

JESSE L. JACKSON
President and Founder
National Rainbow Coalition
Washington

D.C.: A Life ...

I was amused in reading the Jan. 24 article by Blaine Harden, "Old Remedy Gets New Leech on Life," when I turned to page A12 for the continuation of the article. On the same page was continuation of an article by David A. Vise and Howard Schneider about the

fiscal rescue of the District with a highlighted quote by Del. Eleanor Holmes Norton: "We can't let the District bleed to death." Does the D.C. government have too many leeches?

JIM NAGY
Piney Point, Md.

Bigger Than Poland

In a report from Warsaw [Feb. 9], John Pomfret referred to Poland as "Eastern Europe's largest nation." In fact, the largest East European nation, in terms of both population and geographic area, is Ukraine.

Interestingly, both Ukraine and Poland face similar problems as they seek integration within Europe's political, economic and security structures. It would be nice to see The Post cover in more detail Ukraine's relations with countries such as Poland, Germany, Hungary, Great Britain and France.

ADRIAN KARMAZYN
Silver Spring

Rich

THE MIDDLE CLASS AGENDA:

4. The Republican's Contract goes too far-- It bypasses the middle class to reach the rich

- The Republican "Job Creation and Wage Enhancement Act" is a simple reprise of supply-side economics. It centers on a capital-gains tax cut. This would heavily favor passive income from investments--including gains on the sale of assets investors already own--over income earned by middle-class working people. Those families earning more than \$100,000 a year own 60 percent of the bonds and over a third of other income-producing assets, and are poised to collect the bulk of the benefits from any capital-gains tax break. Fully half the benefits of a capital-gains tax cut would go to the richest one percent. A Clinton Administration Lifelong Learning Tax Cut would concentrate its benefits on the broad middle class, and favor a form of investment that directly, demonstrably expands the middle class.
- The Republican "American Dream Restoration Act" would leave most Americans still locked out of the dream while bloating the budget. It grants richer taxpayers access to tax-advantaged savings which many middle-class people already have; it includes a \$500-per-child tax credit for families with incomes up to \$200,000 per year. The richest one-fifth of families would collect 95 percent of the benefits of the expanded IRA. A Clinton Administration Lifelong Learning Tax Cut, by contrast, would be tightly targeted on the middle class. Instead of expanding the deficit and burdening future middle-class taxpayers, our middle-class tax cut would be paid for.
- The "Senior Citizens' Equity Act" grants advantages to better-off retirees. The Clinton approach is to bolster the retirement income system without threatening middle-class retirees who no longer work and who lack investment income.
- In the 1980's we tested the theory that tax cuts for the rich can spur the economy without busting the budget. Interest on the debt left over from that binge is what prevents a balanced budget today. That interest claims 28 cents of every dollar individuals pay in taxes.
- Even if tax cuts for the rich could ignite a business boom, without skills and education the middle class won't benefit from that boom. Productivity and profits are soaring today, and much of the middle class is still being left behind.
- Any tax cuts we can afford should be focussed on the middle class, and should favor the kind of skill investments that do promote middle-class prosperity and let them share in the recover.
- [○ A balanced budget amendment would dictate as much as \$700 billion in tax hikes or spending cuts--none of which the Contract specifies, making this a stealth attack on middle-income families' budgets.]

WHAT'S WRONG WITH THE "CONTRACT" TAX CUTS

ISSUE	CONTRACT WITH AMERICA TAX RELIEF ACT
Five-Year Cost	\$178 billion
Ten-Year Cost	\$630 billion
Percent of Tax Cuts to Those Earning Over \$100,000	51.5%
Percent of Tax Cuts to Those Earning Over \$200,000	28.1%
Percent of Tax Cuts to Those in Top 1% (\$350,000+)	20.0%
Average Tax Cut for Those in Top 1%	\$20,362
How Much Bigger Is Average Tax Cut for Top 1% Than for Those Earning \$30,000-\$50,000	36 times
Percent of Capital Gains Tax Cut for Those Earning Over \$100,000	76.3%
Percent of Capital Gains Tax Cut for Top 1%	45.9%
Average Capital Gains Tax Cut for 700,000 Families in Top 1%	\$12,931

Source: Department of Treasury, Office of Tax Analysis

MAJOR CUTS FOR CHILDREN AMOUNT TO TINY FRACTION OF TAX CUTS FOR WEALTHIEST

Average 1 Year Cost of Contract's Capital Gains Tax Cut	\$9.2 billion
Savings from Rescissions of AmeriCorps, Summer Jobs, WIC, Goals 2000, and Safe and Drug Free Schools	\$2.8 billion
Savings from Rescissions Above as a Percentage of 1 Year Cost of Contract's Capital Gains Tax Cut	30%

Sources: Department of Treasury, Office of Tax Analysis; H.R. 1158 as amended

PRESIDENT'S TAX BREAKS TARGET THE MIDDLE CLASS, NOT THE WEALTHIEST

ISSUE	PRESIDENT'S MIDDLE CLASS BILL OF RIGHTS	CONTRACT WITH AMERICA
Ten-Year Cost	\$172 billion	\$630 billion
Percent of Tax Cuts for Those Earning Less Than \$100,000	84.6%	48.5%
Percent of Tax Cuts for Top 1%	(*)	20.0% (\$20,362 per family)

(*) Less than one-half of one percent. Source: Department of Treasury, Office of Tax Analysis

2. ESTABLISH PRINCIPLES FOR YOUR WILLINGNESS TO NEGOTIATE: Many of your advisors believe that you should establish clear affirmative principles that are your pre-conditions for coming to the table to work on a compromise budget with the Congress. *By establishing such principles, you can shift the debate from when or whether we are willing to do more on the deficit, to whether the Republicans are willing to meet our conditions for a compromise. These conditions might include:*

Tax Fairness for the Middle Class to Invest in Education -- Not Huge Tax Cuts for the Wealthy

Commitment to Education

Commitment to Health Care Savings Only In the Context of Serious Health Care Reform.

You could identify these three conditions as the core of your economic contract with the American people, and state that you will not negotiate or sign a budget that does not honor them. (If the Congress decides to fold welfare reform into reconciliation, you could add conditions about the kind of welfare reform you are willing to accept to these three conditions.)

ENDGAME STRATEGY

Your advisers are currently evaluating several alternative endgame strategies, including at one extreme the strategy of sticking with our current budget proposal through Stage Three and risking the likelihood of gridlock and temporary shutdown of government activities; and at the other extreme the strategy of offering a budget compromise that embodies meaningful health care reform but nonetheless contains significant cuts in Medicare and additional discretionary cuts to balance the budget over ten years rather than seven. Some of your advisers are also interested in a cut-and-invest strategy of the sort proposed by Rob Shapiro.

Although there are differences among your advisers about both the economic and the political wisdom of additional deficit reduction beyond that embodied in our current budget proposal, there is broad agreement that the ingredients of a successful outcome for us include: a meaningful health care reform that encompasses choice, coverage expansion, quality and cost containment; a welfare reform that meets our basic principles; a tax cut that is both moderate and targeted at the middle class; and adequate funding for our priority investments in children, education and other areas.

4. THERE MAY BE CONTINUED DOWN PRESSURE ON THE DOLLAR: The longer we refuse to engage in budget negotiations, the longer the dollar may be under pressure in global financial markets because of uncertainty about the budgetary outlook for the United States.

RECOMMENDATIONS: *After taking all of these considerations into account, most of your advisers believe that we should refuse to engage in budget deliberations with the Congress until after a budget resolution has been passed. There is, however, some disagreement among your advisers about how long we should adhere to a non-engagement strategy, especially if Stage One lasts a long time--for example, if it takes the Republicans through August to pass a budget resolution. At least one of your advisers believes that we have only a little time left before the cons of the non-engagement strategy begin to outweigh the pros, while several others believe strongly that we should stick with this strategy until the Congress actually passes a budget resolution, regardless of how long that takes.*

Your advisers also differ about the advisability of negotiating with the Congress on particular issues before a budget resolution is passed. There is widespread agreement that we should try to detach welfare reform from the overall budget talks. At least one of your advisers also believes that it may be possible to negotiate on health care reform before a budget resolution is passed, but several others strongly disagree.

In deciding whether we should pursue a non-engagement strategy and for how long, it is important to keep in mind that the public -- when informed of what serious deficit reduction really means -- may not support it. If we enter negotiations too early, we are likely to get identified with the pain of the huge cuts required to balance the budget over seven years, without much of the credit. And we run the risk of seeing a painful compromise deal on the budget collapse as happened in 1990.

To minimize the risks and maximize the advantages of pursuing a non-engagement strategy in Stage One, your advisers recommend two approaches:

1. SIGNAL TO THE SENATE DEMOCRATS THAT YOU WANT TO COOPERATE WITH THEM : Most of your advisers believe that they, like us, will gain both message and real advantages from the non-engagement strategy, and we need to try to convince them that this is the case. This will not be easy; and it will probably require that we signal that we are willing to work with them on a budget alternative that would achieve significant additional deficit reduction--perhaps even balance over a ten-year period using the OMB baseline. Whether we are willing to send such a signal depends of course on our ultimate endgame goals. Are we willing to negotiate a budget that involves significant additional deficit reduction? Is additional deficit reduction the best economic strategy, especially if it involves cuts in education and training and other investments? Do we run the risk that we will be defined as supporting their agenda of balancing the budget rather than defending one of our own? *Your advisers are divided on the answers to these and other endgame questions.*

these internal fights. Such fights will weaken their unity and maximize our leverage if and when we do enter the budget negotiations to try to fashion a workable compromise.

CONS AGAINST A NON-ENGAGEMENT STRATEGY IN STAGE ONE

1. THE REPUBLICANS AND THE PRESS WILL CRITICIZE US FOR ABDICATING LEADERSHIP ON THE DEFICIT: As long as we resist engaging in budget negotiations, the Republican leadership will orchestrate a strong and concerted attack on our alleged lack of leadership on the deficit. Because it is to their advantage to have us involved in the negotiations before they have detailed a budget, they will mount an extensive attack--with likely support from the elite media--on our fiscal irresponsibility. Indeed, the first salvos of this attack have already been launched--a call by Gingrich for the President to come first with a balanced budget plan; a sudden Republican concern about the solvency of the Medicare Trust Fund; and hearings and other tactics to force us to make proposals for Medicare cuts they need to pay for their agenda. Many of your advisers anticipate that there will be explicit calls for a budget summit by the Republican leadership before the Congress has passed a budget resolution.

2. CONGRESSIONAL DEMOCRATS MAY WANT TO DEAL IN STAGE ONE: *We will also be under intense pressure to negotiate during Stage One from many moderate Senate Democrats, especially those who voted for the balanced budget amendment, and those, like Conrad and Dorgan, who voted against it but want to support a budget resolution that reaches balance.*

If we fail to negotiate during this Stage, it is possible, although not very likely, that the moderate Senate Democrats will fashion a compromise with the Republican leadership that will render us irrelevant and that will make it impossible for us to fashion a Democratic alternative that we prefer. The danger of such a compromise would be greatly intensified if the Senate Republican leadership decides to adopt only modest tax cuts or decides to eschew them altogether. In such an eventuality, the pressure on us to enter the negotiations from Senate Democrats would become even greater.

3. WE MAY GAIN A REPUTATION AS DEFENDERS OF THE STATUS QUO: *The longer we refuse to cooperate, the greater the danger that we appear as defenders of the status quo and that our criticism of Republican proposals rules out middle ground that might otherwise be a basis of consensus later in the year.*

As long as we refuse to negotiate, we will be engaged in a heated public campaign to criticize the Republican proposals. For example, we may rightly wish to criticize them for huge and painful cuts in Medicare to pay for tax breaks for the wealthy. But the more detailed and effective such an assault, the more difficulty we will have fashioning a meaningful health care reform that yields credible amounts of additional deficit reduction over the next five years.

with the Senate in the development of its proposed budget resolution, there would be little reason to engage with the House, so our next point of entry into the budget deliberations in Stage One would be the budget conference, by which time the initial positions of both the House and the Senate would be known.

The Republican leaders have already indicated that they perceive it in their interest to have us engage in the budget negotiations as early as possible. Their motivation is transparent: they do not want to bear sole responsibility for the tough--and politically unpopular--choices that are required to meet their promises of a balanced budget by 2002 and huge tax cuts.

Therefore, the key tactical question facing us in Stage One is whether we should wait for the Congress to pass a budget resolution before we begin to work with them to achieve a budget compromise we can live with.

Your advisers have identified several considerations that bear on this key decision.

PROS OF A NON-ENGAGEMENT STRATEGY UNTIL THE REPUBLICANS PASS THEIR BUDGET RESOLUTION

1. ACHIEVING CLARITY OF OUR GOALS AND MESSAGE

Our budget identifies our priorities and principles. Education and training are increased. Tax cuts are targeted to the middle class and are not paid for by Medicare cuts or education. Medicare cuts outside of the context of health care reform are declared unacceptable. If we enter into negotiations on a new compromise budget with the Republicans before they have identified their own priorities, we will not be able to distinguish our priorities from theirs, and we will lose our ability to define ourselves with the voters in the 1996 election.

2. REALIZING LEVERAGE FOR POLICY MOVEMENT: The ability to define ourselves is more than a message issue. The greater our ability to define our priorities and principles, the greater the likelihood that we will ultimately be able to realize a compromise that reflects them.

3. ALLOWING TIME FOR THE DEVELOPMENT OF INTRA-REPUBLICAN CONFLICTS: There are large potential fissures within the Republican Party on budgetary priorities. Domenici wants a seven year plan to balance the budget with everything else, including generous tax cuts, treated as secondary. Gramm and more recently Dole are insisting on significant tax cuts. The House Republican leadership and Gramm clearly want the full Contract package. Thurmond is calling for an additional \$130 billion in military spending. As the Republicans try to resolve these differences and deliver on their campaign promises, they will have to engage in bitter and destructive internal fights, including fights on agriculture, defense, and Medicare. Our goal during Stage One should be to define our priorities rather than to help them reach a compromise that will save them from the bruises of

THE WHITE HOUSE
WASHINGTON

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April 20, 1995

MEMORANDUM TO THE PRESIDENT

FROM: LAURA TYSON *Laura D. Tyson*
RE: BUDGET STRATEGY

At several points over the coming weeks and months, we will have to make choices about whether, when, and how to engage in budget deliberations with the Congress. We need to plan our strategy now to maximize our chances for realizing our ultimate budgetary objectives. And we need to decide firmly what these objectives are. A group of your NEC, legislative, and political advisers has begun to meet twice a week to develop recommendations for you concerning these critical choices. We hope to meet with you every other week to discuss our recommendations and our ongoing budget strategy.

To guide your decisions, your advisers believe that it is useful to distinguish three separate stages in the budgetary process:

Stage 1--The Present to the Passage of a Budget Resolution
(May/June-August)

Stage 2--Passage of a Budget Resolution to Reconciliation
(August/September)

Stage 3--Reconciliation to a Compromise Deal or to the Debt Limit and Gridlock
(September/October)

STAGE ONE STRATEGY AND GOALS

When Congress returns from recess, debate will quickly turn to the budget resolution, with the Senate likely to move first, aiming to complete action by Memorial Day. Current indications are that Senator Domenici will push hard for a resolution that reaches a balanced budget by 2002. Whether this resolution will provide for a tax cut is less clear, but recent statements by Senator Dole suggest pressure to keep the tax cuts. If we choose not to engage

THE WHITE HOUSE

WASHINGTON

April 20, 1995

MR. PRESIDENT:

Attached is a discussion memo on budget strategy from Laura Tyson prepared for your meeting tomorrow morning at 8:45 am.

The focus of the memo is on whether we should pursue a strategy of non-engagement with Republicans until they come up with their own Budget Resolution.

We have provided copies of this memo only to Leon and the Vice President.

John Podesta
Todd Stern

James K. Glassman

Yes, Cut Taxes

Critics of the Republican budget in the press, Congress and the White House may be drastically underestimating the power—both political and economic—of those tax cuts the House passed in April. I know I did.

First, a little history. The Republicans won the November congressional elections, using a contract that pledged a balanced budget and a tax cut.

President Clinton figured they couldn't do it, so his strategy was to sit back and let them take the heat for overreaching. His February budget opted for the status quo, which means annual deficits of \$200 billion-plus forever.

Now, the Republicans are offering their official budget plans, and—whaddaya know?—they show they can indeed balance the budget by their target year, the palindromic 2002. And they can do it by *increasing* spending in each year by an average of \$45 billion.

But skeptics see two problems. The first is Medicare. Republicans want to increase spending on the program by about 6 percent annually instead of 10 percent. In Washington parlance, this is a "cut" of \$280 billion, so it's not expected to be easy to sell.

The second problem is tax cuts. Sen. Pete Domenici (R-N.M.), who heads the Senate Budget Committee, said Sunday, "We don't have a tax cut until we balance the budget." But his House counterpart, Rep. John Kasich (R-Ohio), thinks the country can have both at the same time.

The trouble with tax cuts is that they're hard to justify at the same time you're ordering painful limits—and some outright reductions—in spending. Also, it's likely that a total restructuring of the tax system (a flat tax or a national sales tax) will be a big issue in next year's presidential election. So why piecemeal changes now?

In the past, I made these same arguments in urging Congress to shelve the tax cuts. But that was before I did something that most journalists (and even politicians) still haven't done: I took a close look at the tax bill.

Now I'm changing my mind. The tax changes are a political plus—and likely an economic plus as well. Once Americans understand them (and few do now) they're apt to become very, very enthusiastic. Reluctant politicians risk being trampled.

The two main provisions of the tax bill, H.R. 1215, are these:

(1) Nearly every family with children can reduce its final tax bill by \$500 per kid.

For example, the average household headed by a married couple has an income of about \$50,000 a year. If that family has three children, its current federal income tax bill, according to a study by Price Waterhouse, is \$4,643.

But if H.R. 1215 becomes law, the family's tax bill will be reduced by \$1,500—to \$3,143, a cut of a whopping 32 percent. Such a family with two children would save 20 percent, with four children, 47

percent.

These are huge cuts, perhaps unprecedented in U.S. fiscal history. Yet I doubt that most Americans know much about them. The press coverage of H.R. 1215 earlier this year was dominated by a specious controversy over whether tax relief benefited the wealthy. Of course, it does—but only if the rich are willing to invest their money, not spend it. Which brings us to the second element . . .

(2) Taxes on capital gains will be cut dramatically.

This is the part that's meant to encourage investing, and it's a fact that most investing is done by families with higher incomes. But the capital gains cuts in H.R. 1215 aren't a replay of the Reagan tax cuts, which didn't work as advertised.

Those 1986 cuts lowered the tax rates on income (salaries, bonuses, interest on bonds) but actually *raised* the rates on capital gains (profits from the sales of assets like stocks and real estate). As a result, the changes encouraged consumption, but not investment. In fact, the paltry U.S. savings rate actually fell.

The changes in the tax bill the House passed in April are directly targeted at investment—and they're extremely powerful.

The bill does two things: First, it reduces a family's capital gains rate to one-half of its income-tax rate. So, if you're in a 28 percent bracket (taxable income of \$38,000 to \$92,000 for a couple filing jointly), you'll pay just 14 percent on your stock profits.

Second, the bill indexes capital gains, which means that you only pay taxes on real profits, not on inflation. Indexing can produce huge tax savings—but only for long-term investors. And long-term investors are what the U.S. economy desperately needs; they provide the capital that creates good jobs.

Consider a family with taxable income of \$80,000 a year that buys 200 shares of Wal-Mart at \$25 a share, holds the stock for six years, then sells it for \$50 a share—a profit of \$5,000.

Right now, taxes would be \$1,400 (28 percent of \$5,000). But under H.R. 1215, if inflation over those six years averaged about 3 percent, the family would pay tax only on its "real" (non-inflationary) gain—on \$4,000, rather than on \$5,000. And the rate would be just 14 percent. So the tax bill would be \$560 instead of \$1,400, a reduction of 60 percent.

Would capital gains cuts of that magnitude entice Americans to save and invest rather than to consume? It's a good bet.

The tax changes in H.R. 1215 would mean that the Treasury would receive about \$80 billion less revenue in 2002 than it now expects. That's a shortfall of about 4 percent that would have to be met with extra spending restraint. Is the trade-off worth it? It's more and more clear the answer is yes.

E. J. Dionne Jr.

The Democrats' Turn

The Republicans have offered a radical deficit reduction plan. The question is whether the Democrats will be just as radical in pushing the debate over the size and scope of government to essential questions. A budget debate that is merely a series of quibbles over a few programs and numbers would do American voters a disservice, because it would disguise what is really at stake in this fight.

In the first week of the Great Budget War, the Republicans got a lot of credit for putting some big choices on the table. That's fair enough. Now, the Republicans will have to start explaining what their choices mean. What follows is a guide to how this debate might develop if the Democrats and the Republicans dare to debate the fundamentals.

Stage One: Have the Republicans really done what they claim? The engaging House Budget Chairman John Kasich does not want to engage this issue at all. He says his budget proves that you can eliminate the deficit in seven years and cut taxes, too. "The debate about whether you can do both is over," he said on CBS's "Face the Nation" Sunday. "That argument should be laid to rest."

No, it shouldn't. Already some big questions are being raised about how the House budget does what it does. Unlike the Senate budget, the House budget assumes lots of savings by predicting interest rate reductions that Senate Budget Chairman Pete Domenici refuses to take for granted. The House budget, moreover, contains a cumulative deficit that is \$204 billion larger than the Senate's over seven years. The big House cuts kick in toward the end of the seven-year period. Sound familiar? Tax cuts up front, budget cuts later. As David Rogers and Christopher Georges wrote in the Wall Street Journal, "backloading" budget cuts "raises questions as to whether the House plan is credible when it claims to balance the budget by 2002."

Moreover, many of the cuts in both the Senate and House plans are achieved at this point by simply declaring huge reductions in future spending on Medicare and Medicaid. To be credi-

ble—and to permit honest debate over what the real options are—House and Senate Republicans have to offer much more detail on exactly how these cuts would work. And please, no more claims that the Medicare cuts are about some "crisis" in the system and not part of the budget. Without Medicare cuts, these budgets wouldn't even balance on paper.

Stage Two: Who pays? The Republicans claim they've courageously hit all constituencies. But it's plain fact that these cuts do far less damage to Republican constituencies than to Democratic constituencies. The reason is simple: Republican constituencies are, on the whole, wealthier and benefit more from lower taxes than from government programs (except in defense, which the Republicans aren't touching). Democratic constituencies are poorer and depend on government. To his credit, Republican strategist Bill Kristol acknowledged the political tilt of the cutting. Given "the nature of where government monies go, it's going to hurt Democrats more," he said in an interview. The big cuts in Medicaid and welfare will *not* hurt huge numbers of Republicans. The lower-income elderly, who tend to be Democrats, will have a harder time handling the Medicare cuts than the wealthier elderly.

Kasich had a gutsy way of dealing with this problem: He wanted to go after some of the more outrageous tax loopholes that do benefit Republican constituencies. But this effort was largely derailed by Ways and Means Chairman Bill Archer. If the Democrats have any courage, they will put the issue of tax loopholes and subsidies back on the table. Why not offset some of the big cuts in job training, education and health by getting rid of loopholes that John Kasich himself admits are giveaways?

Stage Three: Health care reform, anyone? Because health care costs by their nature slosh around between public and private budgets—most hospitals serve both private and public patients—it makes no sense to cut Medicare and Medicaid without also examining what this would do to the rest of the health system. If the GOP wants to deal with

health costs, good. But let's not pretend that the issue here involves only old people or poor people helped by the government. Like it or not, broader questions of health reform have to be revisited.

Stage Four: What's the real purpose of this exercise? The Republicans are now reasonably candid about their goal: They say the big problem the country faces is big government, so the most important thing is to cut down government's size. Deficit reduction is really only a means to this end for the GOP. Remember: In the 1980s, when they were cutting taxes, a lot of Republicans said the big deficits didn't matter. Now that they have a chance to cut government, they say deficits do matter. The agenda all along, as conservative Irving Kristol was honest enough to admit in 1982, was to "put the welfare state in a moderately tight straitjacket."

Will Democrats be bold enough to question the Republicans' core assumption about government? The issue in this debate should not be whether to reduce the deficit, but how that can be done in ways that will help increase living standards and average wages, which have been dropping for two decades.

If this becomes the core question, it leads to a direct challenge to many of the priorities in both the Kasich and Domenici budgets. If raising living standards is the issue, then government should be doing *more*, not less, to help Americans secure job training and education and to help kids go to college; more to help welfare recipients and their children get jobs and lead productive lives; more to restrain health costs and help all Americans get health insurance. And if paying for such programs requires not only cuts elsewhere but also new revenues—first, closing loopholes and, if necessary, maybe even tax increases—we should talk about them openly.

Will the debate get this far? It can get there only if the Democrats—and especially President Clinton—are willing to challenge the Republicans as forcefully as the Republicans have challenged them.

William Raspberry

Glenarden to the Rescue

Glenarden, Md., the all-black town of 5,000 just outside the District of Columbia, is embarked on a social experiment that *has* to work. I don't mean that its success is a mathematical certainty; I mean that America can't afford for it to fail.

Glenarden is trying to combat crime—particularly the violence that has become the No. 1 cause of death for America's young black men. And it is trying to do so in a way that ought to give it an excellent chance for success: by doing everything at once.

The town, in Prince George's County, is tutoring youngsters, providing recreation and mentors and Bible study for them, teaching them the techniques of nonviolent dispute resolution. Participants include teachers, parents, social workers, police officers and an unbelievable array of volunteers, all determined to make Glenarden safe.

Glenarden, it needs to be said, was never a full-fledged combat zone in the drug wars. Founded in 1939 for a growing black middle class that still wasn't welcome in the white suburbs, the town of split-level homes and green lawns never lost its essential middle-class character. Even at its criminal peak, the numbers looked almost benign by comparison with those in the District: a homicide or two per year, 48 assaults in 1990, perhaps a total of 300 violent crimes a year. But it was enough to alarm a community grown used to quiet evenings and well-behaved children.

"We could see the crime that occurred in our streets every day, and we just decided it was going to take everyone working together to make a difference," the Rev. John Jenkins told a reporter for The Post, explaining why, four years ago, Glenarden launched its all-out campaign to rescue its children.

As it happened, nearby Bowie State University was looking for a community in which to try a violence-prevention program created by one of its faculty. The

match was made in 1991 with a \$500,000 grant from the W. K. Kellogg Foundation, and the cooperation since then has been little short of phenomenal.

Has it worked? Statistically, it's hard to say. Crime is down by a tenth over the past three years—but crime is down in other Prince George's towns as well. Still, violent crime has been falling at a rate far above

It's almost the opposite of the approach lately taken by Congress, where the prevailing prescription is to frighten young people into decent behavior.

the countywide rate. The number of violent crimes fell by about a third last year—from 300 to just over 200. On the other hand, one Glenarden neighborhood has been particularly resistant to the campaign: a low-income apartment complex that is still a center of drug dealing and other crime.

But not all improvement shows up in crime statistics. Take this passage from Post reporter Jon Jeter's recent account of a conflict-resolution class:

"I used to just go crazy when I got into a fight," [15-year-old] Aaron Lee said of his past, which includes fights and run-ins with school administrators. "I would be trying to kill somebody. But they've really helped me a lot here. I know how to control that anger a lot more."

"Two months after Aaron and his father began coming to the weekly meetings, the fights have stopped, and Aaron has raised his grade-point average from 0.57 in the fall term to 2.57 in the winter term."

The conflict-resolution program aside, the most intriguing aspect of the Glenarden effort is its indirectness; it fights crime by rescuing children.

It's almost the exact opposite of the approach lately taken by Congress, where the prevailing prescription is to frighten young people into decent behavior—with tougher law enforcement and longer prison terms.

Glenarden is proceeding on the assumption that if you take care of the children—not just their physical needs but their need to know that they matter—a good deal of crime will take care of itself. And the best evidence to young people that they matter is what the rest of us do on their behalf. That's why the much-maligned midnight basketball programs work—not because there's magic in the game but because of the influence of the men who volunteer as coaches. And that's why the involvement of a broad cross-section of Glenarden's adults bodes so well for success there.

Even the resistant youngsters in the Glenarden Apartments, I am confident, will eventually be tempted to trust—and to modify their behavior as a result. And maybe the rest of us will learn the importance of building trust in those whose behavior we would change.

The Kellogg grant has run out. What survives is community—the newly revived sense that people are in it together and that all of Glenarden's children are worth saving.

Will it work? It *has* to.

David S. Broder

If Clinton Would Stick to His Guns

DENVER—Here in Colorado, the most populous of the four Rocky Mountain states that President Clinton carried in 1992, it is hard to find anyone in either party who thinks he is likely to repeat the feat next year.

Back in Washington, Clinton's problem in the West is ascribed to the fact that he has been pro-environment and anti-gun. Colorado Democrats paint a different, and more complex, picture.

Former senator Gary Hart, now practicing international law and hosting a weekly radio talk show, says that Clinton's success in Colorado last time was almost an accident—the byproduct of factors that are unlikely to recur in 1996.

In 1992 Clinton was the new face, enjoying the advantage of youth in

His retreat from trying to remake Washington has erased the credit he might have gained on other issues.

what Hart has believed ever since his own 1984 presidential bid is a tide of generational change. In 1996 Clinton is clearly not a new face; the Republicans, except for Sen. Bob Dole, may claim that title.

More important, Clinton had Ross Perot on the ballot. It was Perot's getting almost a quarter of the vote that enabled Clinton to best George Bush, 40 percent to 36 percent. If it is a two-way contest in 1996, Colorado Democrats say Clinton would be a distinct underdog to any of the top Republicans, except maybe Sen. Phil Gramm of Texas. Gramm backers, including Republican national committeeman Jim Nicholson, say the Texan would win here, too.

Growing and prospering, Colorado looks increasingly conservative—a trend that Sen. Ben Nighthorse Campbell acknowledged in his recent switch from the Democratic to the Republican Party.

Democratic Gov. Roy Romer is the

great exception to this trend, having won reelection to a third term in 1994. But Mike Beatty, the former top Romer aide who is now the state Democratic chairman, sees little chance for a Clinton comeback unless the White House and the national party change direction.

The change he is talking about does not involve softening environmental policy, backing down on gun control or otherwise kowtowing to the latest incarnation of the "sagebrush rebellion." To the contrary, Beatty—who is himself the former president of a Texas-based energy conglomerate—thinks the administration should stick to its guns on these subjects.

Colorado is now dominated by its metropolitan areas, Beatty said, with four of the six House seats centered in the urban belt from Boulder through Denver to Colorado Springs. The issues that move the metro voters are the very ones that Clinton has emphasized—crime, schools, economic growth and the environment. They are not the ones that stir people trying to repeal the assault weapons ban or kill the Endangered Species Act. That is the same view that another former Colorado Democratic senator, Tim Wirth, now undersecretary of state, has been arguing to White House officials.

The good news for Clinton is that he does not have to try to turn around the folks who denounce his environmental and gun control policies, Beatty and Hart say. The bad news is that he has lost too many of the metro area voters, because he no longer is seen as the force for change they hoped he would be back in 1992.

Much of the problem, Beatty and Hart both say, came from Clinton's decision in 1993 to let the Democratic congressional leadership set the limits on how much reform was permissible—the decision that doomed the line-item veto, for example, and contributed to the stalemate on lobbying and campaign finance reform. His retreat from trying to remake Washington has erased the credit he might have gained on other issues. The Republican takeover of Congress has broken the hammerlock that the congressional Democrats had on Clinton. But that is not enough.

From the Denver perspective, Clinton appears to be playing the budget issue as if he thought he could win with the old Democratic coalition of labor, liberals and senior citizens. In a young and growing state like this one, that is a losing game.

The swing voters are not ones who want to see Clinton and Gore simply denouncing the Republican budget. They are tired of partisanship. The president, Beatty says, should instead tell them, "The goal of balancing the budget is right, but cutting education and other investments is the wrong way to do it. Here's my way."

That's a different take on the Clinton problem in the West, but it's one the people on the scene believe.

Jim Hoagland

Briefing Yeltsin On Iran

Iran is aggressively pursuing a nuclear-weapons acquisition blueprint drawn up at least four years ago with the aid of Pakistani officials, President Clinton told Boris Yeltsin when they met in Moscow last week.

Clear evidence of Iran's Pakistani connection was a central element in the five-page, single-spaced U.S. intelligence report on Iran's drive for the bomb that Clinton presented to Yeltsin on May 9. The report had been translated into Russian the night before so Yeltsin could read it in Clinton's presence.

"We know that Iran has an organized structure whose purpose is the production of nuclear material for nuclear weapons," the report flatly states before detailing that structure, modeled after Pakistan's successful campaign to buy technology and hardware piece by piece from Western and Asian companies over eight years.

At no point did Yeltsin challenge the accuracy of the U.S. report, which relied heavily on "humint" and "sigint"—espionage jargon for human intelligence and communications intercepts. Clinton could not offer Yeltsin satellite photography or other physical evidence, since Iran has not yet begun construction of an identifiable nuclear weapons site.

Instead the United States shared with the leader of the Kremlin sensitive details of Iranian contacts with foreign companies that sold the equipment the Pakistanis used to develop the components of a nuclear weapon. The summit document also reflected U.S. agents' reports from South Asian capitals.

U.S. officials say they believe Prime Minister Benazir Bhutto's government has halted all nuclear cooperation with Iran since it came to power 19 months ago in Pakistan. The cutoff was one factor in the warm welcome that Clinton extended to Bhutto in Washington a month ago.

Details of Clinton's Moscow presentation provided by U.S. officials leave no doubt that Tehran has been seriously trying to build a bomb with outside help, particularly in the past from Pakistan and China. But the compelling detective work done by the United States was overshadowed by the predictable but shortsighted political hubbub over whether the meeting was a "success" or "failure" for Clinton.

The intelligence was needed to convince not only Yeltsin. The president's decision to break off trade with Iran and to push Russia to cancel nuclear sales to Tehran provoked a fierce debate within the administration before the summit, with Secretary of State Warren Christopher leading the charge against other Cabinet members who warned against damaging U.S. business interests and diplomacy.

But Clinton feels he must get a handle on an increasingly dangerous situation in South Asia, where Iran is not the only potential nuclear flash point. India, locked in a bitter dispute with Pakistan over Kashmir, exploded a nuclear device in 1974. Pakistan has been able since 1990 to "make a bomb with a few turns of the screwdriver once it decides to do so," as one U.S. official puts it.

U.S. pressure has deterred Pakistan from completing and testing a nuclear device. But the intelligence summary underlines the potential that Pakistan still has to be a dangerous source of expertise for other Islamic countries interested in the bomb.

Extension of the nuclear Non-Proliferation Treaty last week frees the administration to prod India and Pakistan to provide safeguards against moving to develop and deploy nuclear warheads on the ballistic missiles each now possesses.

An active Pakistani role in helping the Iranians had been suspected for some time. And Iran's nuclear program began 30 years ago, when Shah Mohammed Reza Pahlavi launched a grandiose plan to construct 20 nuclear plants by buying a small U.S.-built research reactor. The shah was overthrown by Islamic fundamentalists in 1979.

But the intelligence reporting contained in the summit document seems to support the thesis of a forthcoming article in *Survival* magazine by Zalmay M. Khalilzad, a senior Defense Department official under George Bush. Khalilzad writes that Iraq's devastating defeat in Operation Desert Storm in early 1991 convinced other countries, including Iran, that only the possession of nuclear weapons could prevent the United States doing the same thing to them. Tehran launched a crash five-year, \$10 billion effort that was aided by Pakistan's then chief of staff, Gen. Mizra Aslam Beg, and by China, which sold Iran a uranium-enriching calutron in mid-1991, according to current U.S. officials.

Clinton used this information and more to persuade Yeltsin to cancel the sale of a gas centrifuge and the training of 10 to 20 Iranian scientists a year in Moscow. Sharing American intelligence with the Kremlin is still an unsettling idea for Americans, and properly so. But in this case it seems to have been worth it.

LETTERS TO THE EDITOR

NPT: A Big Part of the Cure

Permit me to correct a monumentally incorrect claim in Lally Weymouth's column "Riches to Rogues" [op-ed, April 20].

Mrs. Weymouth claimed that the nuclear Nonproliferation Treaty (NPT), which outlaws the spread of nuclear weapons, "is as much a part of the problem as it is an answer" to nonproliferation, because it allows some civilian nuclear programs that "can serve as the foundation of a nuclear weapons program." By this logic, antibiotics—which are effective against many but not all infections—are as much a cause of disease as they are a cure.

Without the NPT, civilian nuclear programs still would happen, but there would be no international protection against diversion to weapons. Without the NPT—the long-term future of which is being decided today at the United Nations—seals could be broken, cameras could be turned off and inspectors would be turned away at some 900 sites around the world now subject to international safeguards.

The NPT isn't perfect—in real life, hardly anything is. But America and the world are far better off with the treaty as it now stands than without it.

When the NPT was written in the late 1960s, experts predicted scores of functioning nuclear weapons owners within two decades. Arguably, these would have included Iran, Iraq, Libya and the World Trade Center bombers. The NPT and its supporting export control regimes have thwarted nuclear weapons ambitions in many unsavory places.

Of course, further steps are desirable, including a cap on fissile material that could be used for bomb production. But the NPT is in no sense part of the proliferation problem, and it is a large part of the answer. Anyone inclined to think otherwise might spend a few minutes in front of the still-standing World Trade Center contemplating the fact that a world without the NPT would be even more frightening than a world without antibiotics.

JOHN D. HOLUM

Director
Arms Control and Disarmament Agency
Washington

Good Service on Amtrak

On the subject of public carriers, horror stories abound, particularly when the member of the public carried is irritated by a slipped disk and the railroad is blamed for the shortcomings of the travel agent ["Rough Riding on Amtrak," *Close to Home*, April 30].

My mother and I recently spent six days and nights on Amtrak trains traveling from Washington to San Francisco and back. It was the experience of a lifetime watching the wonders of our vast country glide by our window: the blossoms of the Appalachians, the plains, the desert, the Humboldt Sink, the wild variety of mountains, the highest meadows in the world, the snow of the Sierra Nevada melting in the dazzling sunshine reflected by Donner Lake.

The trains were comfortable and clean, the service attentive and good-humored and the food varied and appe-

No Feeling for the Vietnamese People

Robert McNamara's book is about Vietnam, yet after going twice through its 390 pages, I could not find a single instance in which he expressed any feeling for the Vietnamese people or their suffering. The United States intervened in Vietnam in the name of a containment policy that, at least in part and in theory, was to help the Vietnamese people defend themselves against Communist tyranny. But Mr. McNamara writes as if the Vietnamese people never existed.

He describes the government in South Vietnam as corrupt. It is not up to us, who lost everything and had to suffer humiliation after humiliation in Communist concentration camps or as refugees abroad, to defend South Vietnamese government corruption. We only ask Mr. McNamara to take a look at the monumental corruption that prevails now in Vietnam. We also wonder if his experience at the World Bank in the years since he formed his opinion of the South Vietnamese government has made him a little more aware of corruption in other parts of the world.

Mr. McNamara writes of the lack of determination of the South Vietnamese people to fight for freedom and democracy. More than 300,000 of my countrymen laid down their lives in the war out of a population not even one-tenth that of the United States'. In April and May of 1972, South Vietnamese

troops—supplied only by air—were surrounded by superior enemy forces inside the small district capital of An Loc. They stood their ground through ferocious house-to-house fighting and stopped short the North Vietnamese onslaught on Saigon. No American ground troops were involved.

The defender of An Loc, Gen. Le Van Hung, took his own life immediately after the fall of Saigon. Three other generals—Nguyen Khoa Nam, Tran Van Hai and Le Nguyen Vy—also took their own lives then.

Mr. McNamara wrote: "I believe we could and should have withdrawn from South Vietnam either in late 1963 amid the turmoil following Diem's assassination or in late 1964 or early 1965." How can a man billed as one of America's "best and brightest" be so callous? Directly or indirectly, the United States was behind the coup against President Ngo Dinh Diem in November 1963, but Mr. McNamara advocates a withdrawal right after the coup. By what morality could the United States come and go at will, even after contributing to the mess in Saigon, without any consideration of what would happen to the Vietnamese people?

BUI DIEM
Rockville

The writer was South Vietnamese ambassador to the United States from 1967 to 1972.

Mr. Yeats's 'Rough Beast' (Cont'd)

The April 25 issue of *The Post* yielded a pleasant and encouraging surprise to one longtime resident of this political town—quotations and a photograph of Irish poet William Butler Yeats on facing pages ["Mr. Yeats's 'Rough Beast,'" letters; "Feathered Minds, Marginal Men," op-ed].

Although most of Yeats's poetry was not overtly political—and I would query both Algerian Ambassador H. Osman Bencherif's interpretation of the "rough beast" as fascism [For the Record, April 13] and Michael Sterner's as moral decay [letters, April 25]—the power of Yeats's poems to come to terms with the complexities of modern life is evidenced by their being used so

frequently as referents. Those who search for metaphors for the endless violence humans continue to inflict upon each other find in Yeats unflinching examination of human inconsistency and a refusal to seek poetic closure when life continues to confound.

Yeats's searching rhetorical questions in the passage quoted by George Will in his April 25 op-ed column (the first question refers to the Easter Rising of 1916, not to Ireland's Civil War, which occurred several years later) are self-focused, but they provide a model for what we all should continue to ask, especially those in public office.

CHRISTINA HUNT MAHONY
Washington

Michael Sterner was provocative and right about what Yeats had in mind in his "rough beast" reference—as "right," that is, as any other surmise, including that of the Algerian ambassador.

But the rough beast image in Yeats's "The Second Coming" who "slouches toward Bethlehem to be born" is posed as a question. It is not the answer but the question that stirs the imagination of poetry lovers.

ANDREW KILLGORE
Washington

The Washington Post

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PHILIP L. GRAHAM, 1915-1963

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Letters should be signed and must include the writer's home address and home and business telephone numbers. Because of space limitations, those published are subject to abridgment. Although we are unable to acknowledge those letters we cannot publish, we appreciate the interest and value the views of those who take the time to send us their comments. Letters intended for publication should be addressed to Letters to the Editor.

In conscience, we cannot leave unanswered the criticism of Amtrak employees leveled by Chris Kielich, who—to mix a metaphor—paints with a wide brush on a small canvas. We made a round trip from Washington to Grand Junction, Colo., about a year ago, and our experience was quite the opposite.

Our trip was beset by many mechanical problems (all of which could be remedied with a little money), but every member of the crew and the terminal personnel were most solicitous. They all went out of their way to compensate and gave every evidence of their desire to be helpful. We intend to repeat the trip next year.

ROBERT AND JEAN WATTLES
Arlington

'What Crisis?' (Cont'd)

MAYOR MARION BARRY, who likens himself to the captain of a ship, claims that most of the storm is over and that the District's crisis is no more. When Mr. Barry gets over his jet lag, he may wish to check out the situation with D.C. General Hospital's AIDS center. The center, with a workload of 800 AIDS patients—some desperately ill—is down to one doctor for them. Now, is that a crisis or what?

AIDS patients, especially those in the late stages, need all the medical care they can get. For the poor, that kind of expensive treatment can be hard to come by. That's why the AIDS center at D.C. General Hospital has been a godsend for patients too poor to pay doctor and care bills. For the past few years, this clinic, with its specialized treatment facilities, has been the place that poor AIDS patients with complex cases have turned to. But what did they find when they went to the center this week?

According to one physician at D.C. General Hospital, more than a third of the patients with appointments at the AIDS center were not seen as scheduled. They were sent away with rescheduled appointments for some time in the future. And why? Because the center's director and an AIDS specialist in infectious diseases quit. They were unsettled by the hospital's budget crisis and fearful that they too would eventually lose their jobs as cutbacks occurred. Despite being told

that special grant money ensured them of jobs, they concluded that D.C. General's future was too unstable. Mr. Barry brags that he's "a captain who can give the passengers a sense that we know where we are going." Don't look now, Mr. Mayor, but two of your crew have jumped ship.

D.C. General Hospital's Linda Ivey is aggressively recruiting replacement doctors for the AIDS center and volunteers to work in office and patient settings throughout the hospital. But for now, the clinic is making do with one badly outnumbered physician and the hospital's emergency room. For patients struggling against a fatal disease that is taking a turn for the worse, the breakdown in city services couldn't come at a more crucial time. The Whitman Walker AIDS Clinic, also in a financial bind caused in part by the city's maddening administrative machinery, can't absorb many new patients.

Mayor Barry also claimed in his State of the District Address that "there's a steady hand on the wheel." The doctors' bailout suggests a different take on his stewardship. Their departure caught the hospital and the patients by surprise. That is truly unfortunate for both. But it's no secret that a number of D.C. General staff are looking around for other work, given the uncertainty caused by the way the city's budget has been handled by the city's leaders. And the real losers, again, are those in the city who can least afford further loss.

The Pennsylvania Avenue Proposal

THE CHOICE between closing off and keeping open that stretch of Pennsylvania Avenue in front of the White House for vehicular traffic is a tough call. That is as it should be. Two compelling and difficult-to-reconcile objectives are at stake. First there is the matter of the president's security and the need to protect the first family and the White House from modern-day risks and dangers. Those are critical concerns. But they are not the only ones.

Presidential safety also must be weighed against a legitimate desire to prevent the chief executive from becoming enveloped in an ever-expanding protective cocoon that intensifies his isolation and remoteness. The task is to reach a decision that addresses the legitimate concerns inherent in each national interest without doing serious violence to either.

The federal independent advisory committee recommendation to close the avenue presents serious problems. But it is not the product of a snap judgment. It grows out of a review of White House security and Secret Service performance that predates the bombing in Oklahoma City. That horrible blast, however, was a reminder of the damage that a truck bomb parked outside a federal building or the White House gates could do. But would closing off Pennsylvania Avenue to vehicular traffic actually achieve a great deal more in security? It's worth noting that the three incidents that prompted the White House and the

Treasury secretary to order a security review were unrelated to bombings.

A plane crash on the White House South Lawn, a gunman firing a semiautomatic rifle from the north sidewalk, a knife-wielding homeless man, again on the sidewalk—each was a serious and disturbing episode. But closing off the avenue to cars would not prevent a recurrence of those incidents. And that, of course, is the point that people who are hesitant to embrace the street-closing idea are making. Without wanting to second-guess the Secret Service, some are asking, with justification, whether shutting down a vital Washington thoroughfare (with all the disruption that would bring) would add much to White House or presidential security—especially if pedestrians are free to roam just outside the see-through iron gates.

From the Hill to the White House, the capital has undergone extraordinary—and unpleasant—physical rearrangements recently to protect Congress the president, his family and staff from acts of madness and violence. Each protective impulse—and barricade—can be justified, and each comes at a cost in relative ease of access and even, in a way, in dignity to the individuals and institutions being protected. Now there are rumblings about fencing in the Capitol and glassing in the visitors' galleries. Those steps, including closing Pennsylvania Avenue, should not be taken without much more explanation—and justification—than has been produced to date.

Squeezes on the Area's Schools

WHETHER THERE'S a school board with authority over how its money is spent—but not how much it gets—the financial pressures on local governments are not sparing the education budgets. Throughout the region, local leaders find themselves pitted against school boards, with the bucks stopping well short of requests. It's not just shortages of money but also shortages of slack given the schools boards by newly elected, newly pressured officials. When they ran for office, the government heads pledged a better financial shake for the schools; but when they won and met up with financial reality, these new leaders gave schools lower marks on their budgets.

In Prince George's County, for example, Wayne Curry promised more money for the schools. Now, however, he's being sued by the school board and is under fire as well from some teachers, parents and others who charge that his school budget is anti-children. The school board's suit charges that the budget proposal doesn't meet state requirements for local "maintenance of effort." However this is resolved, Mr. Curry's broader budget objective is to steel the county against (1) an existing deficit and (2) uncertain but surely negative impacts of national and state assistance cuts still to come. It is the kind of necessary

political dirty work that elected officials had best do early in their terms.

Montgomery County Executive Doug Duncan is taking a similar responsible course and meeting similar resistance. He, too, still considers the schools a top priority, but he, too, has upset school board members with an operating budget that they say fails to address educational needs and could mean eliminating 400 jobs next year, including hundreds of teachers and aides. In Fairfax, the supervisors just approved a higher budget for the schools but school board members have said that it's not enough, that more money is necessary to balance the school budget without having to expand class sizes.

The concerns of school board members are genuine, even if their projections of damage may be slightly overstated. But do they or others believe for a minute that the county executives, supervisors or council members anywhere enjoy cutting school budget requests? Per-student spending is not in itself a measure of educational quality. Sound financial policies—budget calls that go beyond schools alone to the total mix of services that governments must provide—demand strong leaders with the ability to strike highly delicate and generally unpopular balances.

The Washington Post

AN INDEPENDENT NEWSPAPER

A Bad Idea, Well-Hidden

TUCKED AWAY in the middle of Senate Budget Chairman Pete Domenici's 97-page budget blueprint are two lines describing a proposal with a minuscule impact on federal spending but enormous meaning for the nation's political process. Mr. Domenici, following a suggestion by Sen. Mitch McConnell (R-Ky.), proposes the elimination of public financing for presidential campaigns after the 1996 election.

This is not only a terrible idea; it also has no place in the budget debate. A change this large in the electoral system should be debated on its own, independent of the great confrontation that is about to occur on the deficit. The amount of money involved is trivial in a budgetary sense—roughly \$45 million a year in a \$1.5 trillion budget—but hugely important to efforts aimed at limiting the impact of campaign fund-raising on the presidency.

Public financing of presidential campaigns has actually worked. It was instituted after the Watergate scandal revealed all sorts of unsavory fund-raising shenanigans in the 1972 campaign. The idea is simple: The presidency ought not be put up for bid, the major party candidates ought to compete on a level playing field, and the party in power should not enjoy a prohibitive financial advantage. Existing law provides for a Presidential Election Campaign Fund that is financed through a voluntary \$1 checkoff on income tax returns. For the general election, each major-party

candidate draws the same amount from the fund—George Bush and Bill Clinton got \$55.2 million each in 1992. The law also includes provisions for future public financing for any third party that makes a substantial electoral showing (as did the independent movements of John Anderson in 1980 and Ross Perot in 1992). And it provides for a system of matching funds in the primaries, whereby candidates who raise a certain amount in private contributions qualify for a share of the federal funds. The formula puts a premium on smaller contributions, so candidates who are serious but without huge interest group backing have a chance to make their case.

There are problems with the system that need to be addressed. The campaign fund has been running low, and the checkoff amount needs to be increased. But at a time when Congress's emphasis should be on finding ways to *reduce* the impact of money on politics, this proposal moves in entirely the wrong direction. It is also interesting that the budget proposal would leave the current system in place long enough to allow Republican presidential candidates (such as Sens. Dole, Gramm, Specter and Lugar) to take advantage of it at while the GOP is out of the White House, and only abolish it after the next election.

If Mr. McConnell wants an open debate on the merits of the public financing system, he can encourage one. But a change this large should not happen covertly as part of the budget process.



For the Record

From a Fox "Morning News" interview yesterday with Sen. Sam Nunn (D-Ga.):

Q: President Clinton is proposing tougher legislation for dealing with terrorism in the United States. Among other things, the president's Omnibus Counterterrorism Act would grant the military the power to help investigate crimes involving high-explosive chemical or biological weapons. . . . This is kind of a gray area, legally—getting the military involved in domestic investigations.

Sen. Nunn: Well, it is. It goes way back in our history. We had a statute passed back in the late 1860s . . . that was called posse comitatus. It was brought about because of the Reconstruction resentment in the southern part of the United States, with the military . . . being used for basic law enforcement. And also a resentment in the North because of the military being used to suppress labor unrest. . . .

But there are modern reasons also for being very cautious in this area One is that the military is not trained for law enforcement. They are trained to search and destroy using massive military force, not detect and investigate and arrest in accordance with due process and civil procedures. . . . Another is, we don't want to have our military so involved in law enforcement that they cannot carry out their primary mission, which is to defend the nation. . . .

Q: But clearly, the military does have expertise in things like nuclear weapons, biological weapons, chemical weapons. And that's what is hoped can be tapped into here. . . .

A: I think that's the legitimate part of the president's proposal. . . . We already have an exception to the posse comitatus statute, which permits the military, in nuclear areas, to utilize their expertise to assist law enforcement.

POSTAL NOTES

First class postage 32¢ — mules, boats and bush pilots included free.



The 32¢ first class stamp you stick on an envelope imposes an obligation on the U.S. Postal Service to get your letter from wherever you are to wherever it's going, whatever it takes. To fulfill this mission "to provide uniform service throughout the nation," occasionally it takes quite a lot.

Mules carry mail to the bottom of the Grand Canyon. Bush pilots deliver mail above the Arctic Circle or in the Alaskan wilderness. We use mailboats to deliver to ships on America's rivers, and along the bayous of Louisiana. And we do it six days a week, 580 million pieces of mail a day.

But, you say, if the USPS could do all that for 29¢ last year, why is it 32¢ this year? Because, unlike many other government services, the USPS is a self-supporting business, not funded by tax dollars. So when the price of gasoline goes up a penny a gallon, for instance, it costs us more than \$1 million extra in operating costs. We don't have exact figures on mule food, but that probably costs more too.

On the other hand, through high-tech equipment and automation, the USPS continues to have the lowest-cost rates for first-class mail of any industrialized nation in the world.

And with the USPS you can count on getting the same service everywhere, from our biggest office (the one in Manhattan) to our smallest, the 61 square foot office at Ochopee, Florida.



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ERAL PAGE

Print to Balance the Budget

million in savings over seven
ould go to a tax cut), compared
proposed by the Senate GOP a

day earlier. Here are the proposed savings and costs over seven
years compared with the Senate plan and with projected
federal spending without changes in current law.

- Cut National Park Service operations by 10 percent
- Reduce national forest system
- Reduce management of lands and resources
- Impose 5-year moratorium on land acquisition for U.S. Fish and Wildlife Service, National Park Service, Bureau of Land Management
- 5-year reduction in new construction for same agencies
- Apply a cost-benefit test to Superfund projects

House savings: \$19.6 billion

Senate savings: \$23.7 billion



COMMUNITY AND REGIONAL DEVELOPMENT

*Funds community and regional
development and disaster relief,
including programs administered by*

*HUD, Appalachian Regional Commission, Tennessee
Valley Authority, Economic Development Administration,
Bureau of Indian Affairs, Federal Emergency
Management Agency and the Department of
Agriculture.*

- Eliminate the Economic Development Administration
- Eliminate Appalachian Regional Commission
- Reduce Community Development Block Grants
- Reduce Bureau of Indian Affairs and construction

House savings: \$12.6 billion

Senate savings: \$20.1 billion



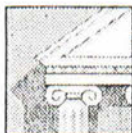
LAW ENFORCEMENT, JUSTICE

*House Republicans want block grants to
fight crime, including resources
President Clinton wanted specifically
designated for community policing as
called for in the Omnibus Crime Bill of 1994. Unlike
the Senate, the House Republicans would reduce the
Violent Crime Trust Fund, accounting for savings not
reflected in the Senate budget proposal.*

- Reduce block grant funding for Justice Assistance Program
- Eliminate funding for death penalty resource centers
- Phase out federal funding for the Legal Services Corp.
- Reduce the Violent Crime Trust Fund
- Terminate the State Justice Institute
- Terminate the U.S. Parole Commission

House savings: \$ 11.1 billion

Senate spending: Would increase spending by \$27.4
billion over seven years due primarily to enactment of
the Violent Crime Trust Fund, which funds prison
construction and community police.



GENERAL GOVERNMENT

*Limits are placed on federal building and
construction by the General Services
Administration; smaller executive branch
agencies, including those that provide
assistance to U.S. territories, are cut.*

- Impose 5-year moratorium on construction
- Impose 7-year moratorium on acquisition of new federal buildings
- Eliminate all territorial assistance
- End government's monopoly on printing
- Eliminate the Office of Technology Assessment
- Reduce General Accounting Office funding by 15 percent
- Reform the Office of Personnel Management; transfer certain OPM responsibilities to other agencies

House savings: \$9.5 billion

Senate savings: \$6.8 billion



VETERANS

*House budget cutters mainly focus on
cost of living allowances and health
benefits for veterans and limiting
hospital construction in the VA's vast
medical system.*

- Limit Veterans Affairs major construction
- Reduce cost of living allowances
- Withhold compensation benefits for certain incompetent veterans with large estates
- Collect per diems and copayments from certain veterans
- Verify income of veterans receiving medical care

House savings: \$8.3 billion

Senate savings: \$15.1 billion

MISCELLANEOUS

*Includes various budgetary functions and undistributed
offsetting receipts.*

- Reduce federal agency overhead
- Reduce the number of political appointees
- Replace dollar bills with dollar coins
- Increase civilian employee contributions to retirement trust fund by 2.5 percent of salary

**House savings: \$40.2 billion from allowances and
additional undistributed offsetting receipts**

Senate savings: \$73.6 billion

SOURCES: House Budget Committee Republican staff, Senate Budget
Committee Republican staff, Washington Post research

- Increase user fees on products regulated by the FDA
- Reform the Consumer Product Safety Commission
- Cut substance abuse and mental health services
- Reduce ineffective funding for the National Health Services Corps
- Terminate federal funding for physical fitness and sports
- Encourage prioritization of NIH-supported research funding by 5 percent
- Transfer Mine Safety and Health Administration to OSHA, cut 20 percent

House savings: \$282.3 billion for Medicare; \$198.5 billion for Medicaid and other health areas

Senate savings: \$256 billion for Medicare; \$202.3 billion for Medicaid and other health areas



WELFARE, FEDERAL RETIREMENT

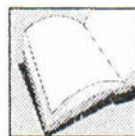
House Republicans propose a budget in line with legislation they approved in March that would replace dozens of federal programs and regulations with six

lump-sum payments to the states, allowing them to design their own welfare programs, including nutrition programs. They also propose cuts in food stamps. Not in the welfare legislation but also affected by yesterday's budget proposal are several housing programs.

- Renew Section 8 housing grants
- Deregulate public housing authorities, enabling them to more efficiently use operating funds
- End construction of new public housing units
- Reduce homeless assistance grants
- Reduce grants to emergency shelters
- Reduce funds for elderly housing
- Reduce HOPE grants
- Eliminate Indian Housing Loan Guarantees
- Transfer lead based paint abatement responsibilities to EPA
- Eliminate extended unemployment benefits
- Create child care block grant
- Create family nutrition block grant
- Create school nutrition block grant
- Cut food stamps program
- Cut child nutrition program

House savings: \$116.7 billion

Senate savings: \$82.9 billion



EDUCATION, TRAINING, EMPLOYMENT, SOCIAL SERVICES

House Republicans target educational, cultural and job training programs for drastic cuts. They call for the elimination of the Education Department and a wide variety of its programs including some of the leading Clinton administration initiatives.

- Eliminate funding for Goals 2000
- Eliminate duplicative school improvement programs
- Eliminate duplicative higher education grants
- Phase out all special interest scholarships
- Terminate bilingual and immigrant education
- Eliminate federal funding for Howard University, redirect half of the savings to historically black colleges fund
- Eliminate federal funding for libraries
- Fund Head Start at FY 1994 level
- Privatize the Corporation for Public Broadcasting
- Eliminate the Corporation for National and Community Service
- Cut vocational and adult education (homeless adults)
- Eliminate the Woodrow Wilson International Center
- Cut training and employment services

House savings: \$22.4 billion

Senate savings: \$51.3 billion



AGRICULTURE

Republicans call for streamlining and reductions in the massive Agriculture Department and its extensive research and services.

- Reform Foreign Agricultural Service
- Reform Farmers Home Administration
- Reduce funds for the National Agriculture Statistics Service
- Streamline USDA bureaucracy
- Cut the Agricultural Research Service
- Cut the USDA Extension Service
- Cut USDA's Cooperative State Research Service
- Reduce agricultural production programs

House savings: \$20 billion

Senate savings: \$14 billion



GENERAL SCIENCE, SPACE AND TECHNOLOGY

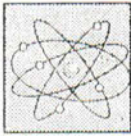
House Republicans scale back NASA expenditures and Energy Department research and call for reprioritizing

general science research activities, including those at the National Science Foundation. In keeping with President Clinton's budget proposal, they would cut the space shuttle budget by about a third and trim science, aeronautics and technology development.

- Reduce academic research infrastructure
- Reduce salaries and expenses
- Reduce expenditures on major research equipment
- Cut funds for human space flight
- Cut funds for space mission support

House savings: \$10.3 billion

Senate savings: \$6.7 billion



ENERGY

Republicans call for the elimination of the Energy Department, which includes solar, renewable and fossil energy programs; conservation research and

development; civilian nuclear waste disposal; and state energy conservation grants.

- Reduce energy supply research and development
- Reduce fossil energy research and development
- Reduce energy conservation research
- Sell the Naval Petroleum Reserve
- Privatize four power administrations

House savings: \$8.7 billion

Senate savings: \$11.5 billion



NATURAL RESOURCES

Funding for water resources, conservation and land management, recreational resources and pollution control are targeted, with big reductions in the

national forest system, the National Park Service and the U.S. Geological Survey.

- Reduce NOAA operations, research and facilities
- Reduce funding for wastewater treatment, according to Appropriations Committee recommendations
- Reform Bureau of Reclamation

THE FEDERATION

House Republicans' Blueprint

House Republicans yesterday released their proposal to balance the budget by the year 2002. The plan calls for the elimination of three departments, 13 agencies and 284

programs for a total of \$1.4 trillion years (of which \$360 billion would be with \$960 billion in savings pro-



DEFENSE

House Republicans would substantially increase defense spending over the next seven years with funds going to reviving weapons spending as well as increasing the pay of the military and improving their housing. Additionally the Budget Committee stipulates some savings would be squeezed from projected defense spending by reducing the number of Defense Department civilians involved in acquisition work.

House additional cost: \$46 billion over Clinton's five-year budget; \$92 billion more (over seven years) than current law.

Senate additional cost: No increase over Clinton's budget; \$26 billion more than current law.



INTERNATIONAL AFFAIRS

The House Budget Committee would radically reduce the amounts of funds for most U.S. non-military activities abroad, with actual spending declining from the current \$18.9 billion to \$10.7 billion a year in 2002. Funds go to the State Department, Agency for International Development, U.S. Information Agency and the Arms Control and Disarmament Agency, trade promotion, U.S. participation in multilateral development banks and the United Nations.

- Terminate Voice of America and Radio Marti broadcasts to Cuba
- Terminate Board of International Broadcasting
- Eliminate the International Development Association
- Privatize Overseas Private Investment Corp.
- Charge risk-related fees for Export-Import Bank
- Reduce aid to former Soviet Union
- Eliminate USIA and educational and cultural exchanges
- Cut funds for Peace Corps
- Eliminate U.S. Institute of Peace
- Eliminate Asia Foundation
- Reduce funds for Agency for International Development

House savings: \$28.8 billion over current law

Senate savings: \$18.1 billion over current law



HEALTH, MEDICARE, MEDICAID

The House Budget Committee proposal radically curbs the growth of Medicare and Medicaid programs, affects discretionary spending for health services, the National Institutes of Health, the Centers for Disease Control and Prevention, the Indian Health Service and consumer and occupational health and safety programs.

- Create Medicaid block grant

- Terminate funding for the National Endowment for the Arts and National Endowment for the Humanities
- Cut subsidy program for student loans
- Cut funds for foster care

House savings: \$73.2 billion

Senate savings: \$59.4 billion



COMMERCE AND HOUSING CREDIT

Discretionary housing programs, such as subsidies for single and multifamily housing; mortgage insurance provided by the Federal Housing Administration;

Postal Service spending; and the Commerce Department were hard hit by GOP budget cutters.

- Eliminate the Commerce Department
- Eliminate the U.S. Travel and Tourism Administration
- Make Patent and Trademark Office self-funding and independent
- Eliminate the SBA's tree planting program
- Terminate industrial technology services
- Make SBA loan guarantee program self-financing
- Eliminate Minority Business Development Administration within the Commerce Department
- Increase patent and trademark user fees
- Increase FCC user fees

House savings: \$3.4 billion

Senate savings: \$12.5 billion



TRANSPORTATION

Republicans cut spending for the federal aid highway program, mass transit operations and capital assistance, rail transportation, Amtrak, the Interstate Commerce Commission, the FAA, aviation facilities, water transportation through the Coast Guard and the Maritime Administration.

- Rescind funds for NASA wind tunnel
- Eliminate DOT's minority business program
- Eliminate the Tennessee Valley Authority
- Eliminate highway demonstration projects
- Eliminate funding for intelligent vehicle development
- Eliminate Federal Maritime Commission
- Streamline the Coast Guard
- Eliminate the Maritime Administration
- Eliminate the Interstate Commerce Commission
- Phase out mass transit operating subsidies
- Phase out Amtrak operating and capital subsidies between 1999 and 2002
- Eliminate funding for high-speed rail development
- Cut the Pennsylvania Avenue Development Corp.
- Eliminate flood insurance subsidy on structures built before 1975

THE WASHINGTON POST

...R THURSDAY, MAY 11, 1995 A21

THE FEDERAL PAGE

House Republicans' Blueprint to Balance the Budget

House Republicans yesterday released their proposal to balance the budget by the year 2002. The plan calls for the elimination of three departments, 13 agencies and 284

programs for a total of \$1.4 trillion in savings over seven years (of which \$360 billion would go to a tax cut), compared with \$960 billion in savings proposed by the Senate GOP a

day earlier. Here are the proposed savings and costs over seven years compared with the Senate plan and with projected federal spending without changes in current law.



DEFENSE

House Republicans would substantially increase defense spending over the next

- Terminate funding for the National Endowment for the Arts and National Endowment for the Humanities
- Cut subsidy program for student loans

- Cut National Park Service operations by 10 percent
- Reduce national forest system
- Reduce management of lands and resources



GENERAL GOVERNMENT

Limits are placed on federal building and

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THE PRESIDENT'S ECONOMIC PLAN:

A BALANCED BUDGET THAT PUTS PEOPLE FIRST

Embargoed

For 9 p.m. EDT
6/13/95

THE PRESIDENT'S ECONOMIC PLAN: A BALANCED BUDGET THAT PUTS PEOPLE FIRST

AN OVERVIEW

The President today proposed a bold plan to balance the budget by 2005, cut taxes for middle-income Americans, and continue investing in education and training -- all to raise average living standards.

The President's plan provides a sharp contrast between his policies and those of the Republicans. The President wants to balance the budget over a reasonable period of time -- 10 years -- so he can protect Medicare, and invest in education and training and other priorities for the American people. Because Republicans balance the budget more quickly, and also provide a huge tax cut for the wealthy, they have to slash Medicare and Medicaid and cut education.

- To help raise living standards of average Americans, the President's plan will:
 - balance the budget, freeing up capital for private investment;
 - invest in education and training to give Americans skills to get high-wage jobs; and
 - take the first, serious steps to reform the health care system, expanding coverage and reducing costs for average Americans.
- By contrast, Republican policies will:
 - increase the "education deficit;"
 - turn Medicare and Medicaid into second-class health care systems; and
 - give huge tax breaks to the wealthy.

The President would balance the budget **the right way**, by eliminating wasteful spending, streamlining programs, and ending unneeded subsidies; taking the first, serious steps toward health care reform; reforming welfare to reward work; cutting non-defense discretionary spending that doesn't include the President's investments by 22 percent in real terms, while leaving room to provide increases for education, the environment, and anti-crime efforts; and targeting tax relief to middle-income Americans.

Republicans would balance the budget **the wrong way**: To reach balance in 7 years and provide a huge tax break for the wealthy, they would slash Medicare and Medicaid and cut deeply in education and other investments that help raise average living standards.

The President's plan builds upon the policies of his first 2-1/2 years that cut the deficit, created nearly 7 million jobs, controlled interest rates and inflation, expanded trade to create more high-wage jobs, and rewarded work by cutting taxes for 15 million families. The President is also building on his efforts to create a new kind of government, one that creates opportunity, not bureaucracy, and provides the tools that average Americans need to build better lives for themselves and their families.

THE PRESIDENT'S ECONOMIC PLAN:

HIGHLIGHTS

- The President, who has cut the deficit from \$290 billion in 1992 to an estimated \$190 billion this year, proposes to balance the budget by 2005.

-- Republicans, none of whom voted for the President's 1993 plan, now want to balance the budget the wrong way -- cutting Medicare, education, and other important priorities deeply to fund a huge tax break for the wealthy and reach balance in 2002.

- The President proposes to take a first, serious step toward health care reform, providing net savings of \$124 billion in Medicare and \$55 billion in Medicaid by 2002 while expanding coverage and initiating insurance reforms.

-- Republicans would simply cut over \$430 billion from Medicare and Medicaid, enough to turn them into second-class health systems.

- The President would save \$64 billion in non-health entitlements by 2002 by reforming welfare, farm, and other programs.

-- Republicans would cut too deeply; for example, by increasing interest costs of student loans.

- The President would cut \$200 billion from discretionary programs by 2002 by eliminating, cutting, or consolidating hundreds of programs and targeting available funds to defense, education, children, and anti-crime efforts.

-- Republicans would cut education and anti-crime programs; for instance, their cuts would throw hundreds of thousands of children off Head Start and nutrition programs, and gut the President's anti-crime efforts.

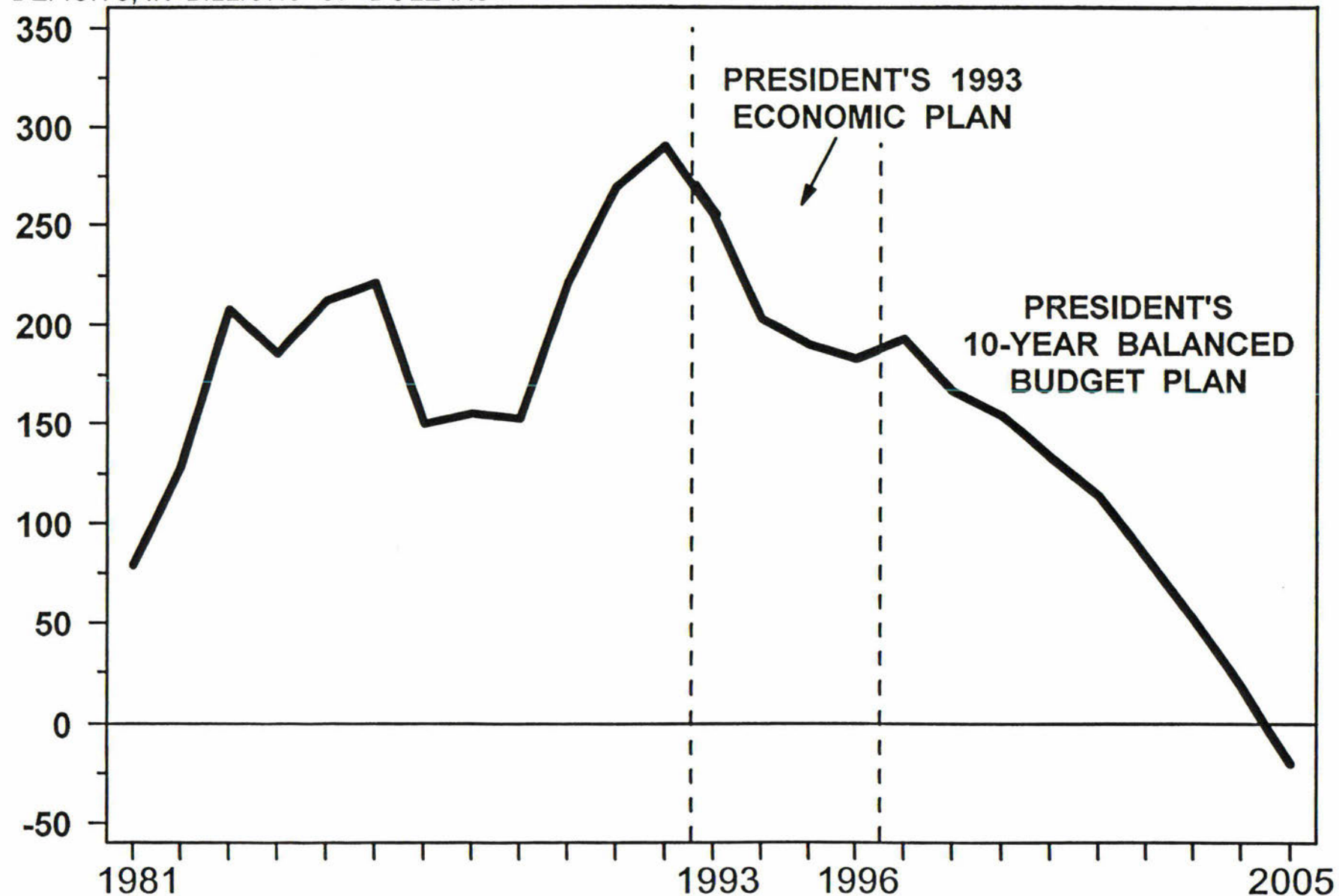
- The President would target tax relief to middle-income Americans, enabling them to more easily raise their children, pay for post-secondary education, and save for the future.

-- Republicans would provide a huge tax break whose benefits would flow disproportionately to the wealthy, and also would raise taxes on millions of working families.

- The President proposes to work with Congress to save \$25 billion by eliminating unneeded corporate subsidies.

BALANCING THE BUDGET: THE PRESIDENT'S ECONOMIC PLAN

DEFICITS, IN BILLIONS OF DOLLARS



THE PRESIDENT'S ECONOMIC PLAN:

REACHING BALANCE IN 2005

- In 1993, the President faced a deficit that was rising out of control -- from \$290 billion in 1992 to more than \$600 billion early in the next century.
- The President's 1993 economic plan has cut the deficit dramatically -- from \$290 billion to a projected \$190 billion this year.
- More importantly, it cut the deficit as a percentage of the economy (GDP) -- from 4.9 percent in 1992 to an estimated 2.7 percent this year and 2.1 percent by the end of the decade.
- If not for interest on the debt accumulated between 1981 and 1993, the budget would be in balance today.
- But, largely due to health care costs, the deficit will begin to rise again -- gradually reaching \$266 billion in 2005.
- Now, the President proposes to finish the job -- to balance the budget by 2005.
- In 2005, the President proposes to save:
 - \$96 billion in entitlements:
 - Medicare, \$67 billion
 - Medicaid, \$19 billion
 - Poverty programs, \$9 billion
 - Other entitlements, \$1 billion
 - \$92 billion in discretionary spending:
 - Defense, \$27 billion
 - Non-defense, \$65 billion
 - \$6 billion in corporate subsidies.
 - \$117 billion in interest savings.
- The President would target tax relief to average Americans, costing \$26 billion in 2005.
- All told, the President's plan would bring the budget at least to balance by 2005.

THE PRESIDENT'S HEALTH REFORM INITIATIVE: A SERIOUS STEP TOWARD HEALTH CARE REFORM

As the President has said, the key to long-term deficit reduction is controlling health care costs through health care reform. Thus, in his plan to balance the budget by 2005, the President presents a serious first step toward reform that:

- strengthens the Medicare Hospital Insurance (HI) Trust Fund, ensuring Medicare solvency until 2005;
- provides health security for 6 months for working families after a job loss;
- reforms Medicare to make quality managed care options more attractive while preserving choice;
- improves Medicare with new benefits that (1) provide Alzheimer's respite care, and (2) waive the copayment for women who need mammograms;
- provides home- and community-based care grants for disabled and elderly Americans;
- maintains Medicaid as a safety net for low-income Americans while reforming it to target funds more efficiently and increase state flexibility;
- reforms the insurance market to ensure that Americans can keep their coverage if they change jobs, that they won't lose coverage if they get sick, and to improve the availability and affordability of coverage for small businesses;
- gives small businesses voluntary pooling options, including access to Federal Employees Health Benefits Program (FEHBP) plans;
- expands the self-employed tax deduction to 50 percent; and
- reduces the deficit by \$271 billion over the next decade.

The President's plan expands coverage, cuts the deficit with less than half the Medicare savings and a third of the Medicaid savings that Republicans propose, and imposes no new cost increases on Medicare beneficiaries.

By contrast, the Republican budget proposals threaten Medicare beneficiaries, reduce Medicaid coverage for millions of children and elderly Americans, and endanger many hospitals, including academic health centers. The Republicans' cuts (assuming a 50/50 beneficiary/provider split) would increase out-of-pocket costs for couples by \$1,700 in 2002 alone (under the House budget resolution). Moreover, the Republicans do not reinvest one penny into health care; instead, the Republicans use Medicare and Medicaid cuts to pay for hundreds of billions of dollars of tax cuts for well-off Americans.

DETAILED EXPLANATION

1. Reforming the Insurance Market

Insurance reforms, based on proposals that both Republicans and Democrats supported in the last Congress, will improve the fairness and efficiency of the insurance marketplace.

- **Portability and Renewability of Coverage** -- Insurers will be barred from denying coverage to Americans with pre-existing medical conditions, and plans will have to renew coverage regardless of health status.
- **Small Group Market Reforms** -- Insurers will be required to offer coverage to small employers and their workers, regardless of health status, and companies will be limited in their ability to vary or increase premiums on the basis of claims' history.
- **Consumer Protections** -- Insurers will be required to give consumers information on benefits and limitations of their health plans, including the identity, location, and availability of participating providers; a summary of procedures used to control utilization of services; and how well the plan meets quality standards. In addition, plans would have to provide prompt notice of claims denials and establish internal grievance and appeals procedures.

2. Helping Working Families Retain Insurance After a Job Loss

Families that lose their health insurance when they lose a job will be eligible for premium subsidies for up to 6 months. The premium subsidies will be adequate to help families purchase health insurance with benefits like the Blue Cross/Blue Shield standard option plan available to Federal employees.

3. Helping Small Businesses Afford Insurance

- **Giving Small Employers Access to Group Purchasing Options:** Small employers that lack access to a group purchasing option through voluntary state pools would get that option through access to the Federal Employees Health Benefits Program (FEHBP) plans. This would increase the purchasing power of smaller businesses and make the small group insurance market more efficient. Small firms would get coverage from plans that also provide coverage to Federal employees through FEHBP, but the coverage would be separately rated in each state, leaving premiums for Federal and state employees unaffected.
- **Expanding the Self-Employed Tax Deduction:** The President's plan provides a fairer system for self-employed Americans who have health insurance. Self-employed people would deduct 50 percent of the cost of their health insurance premiums, rather than 25 percent as under current law.

4. Reforming and Strengthening Medicare

- **Strengthening the Trust Fund:** The President's plan would reduce spending in Medicare's Part A by \$79 billion over 7 years to ensure the solvency of the Medicare

HI Trust Fund to 2005. The plan finds such savings by reducing provider cost growth, not raising beneficiary costs.

- **Eliminating the CoPayment for Mammograms:** Although coverage by Medicare began in 1991, only 14 percent of eligible beneficiaries without supplemental insurance tap this potentially lifesaving benefit. One factor is the required 20 percent copayment. To remove financial barriers to women seeking preventive mammograms, the President's plan waives the Medicare copayment.

- **Expanding Managed Care Choices:** The President's plan expands the managed care options available to beneficiaries to include preferred provider organizations ("PPOs") and point-of-service ("POS") plans. The plan also implements initiatives to improve Medicare reimbursement of managed care plans, including a competitive bidding demonstration proposal. Also included in his plan are important initiatives to streamline regulation.

- **Combatting Fraud and Abuse:** "Operation Restore Trust" is a five-state demonstration project that targets fraud and abuse in home health care, nursing home, and durable medical equipment industries. The President's budget increases funding for these critical fraud and abuse activities.

5. Long-Term Care

- **Expanding Home and Community-Based Care:** The President's plan provides grants to states for home-and community-based services for disabled elderly Americans. Each state, will receive funds for home-and community-based care based on the number of severely disabled people in the state, the size of its low-income population, and the cost of services in the state.

- **Providing for a New Alzheimer's Respite Benefit within Medicare:** The President's plan helps Medicare beneficiaries who suffer from Alzheimer's disease by providing respite services for their families for one week each year.

6. Reforming Medicaid

The President maintains Medicaid, expanding state flexibility, cutting costs, and assuring Medicaid's ability to provide coverage to the vulnerable populations it now serves.

- **Eliminating Unnecessary Federal Strings on States:** To let states manage their Medicaid programs more efficiently, the President's plan substantially reduces Federal requirements.

- States will be allowed to pursue managed care strategies and other service delivery innovations without seeking Federal waivers; and

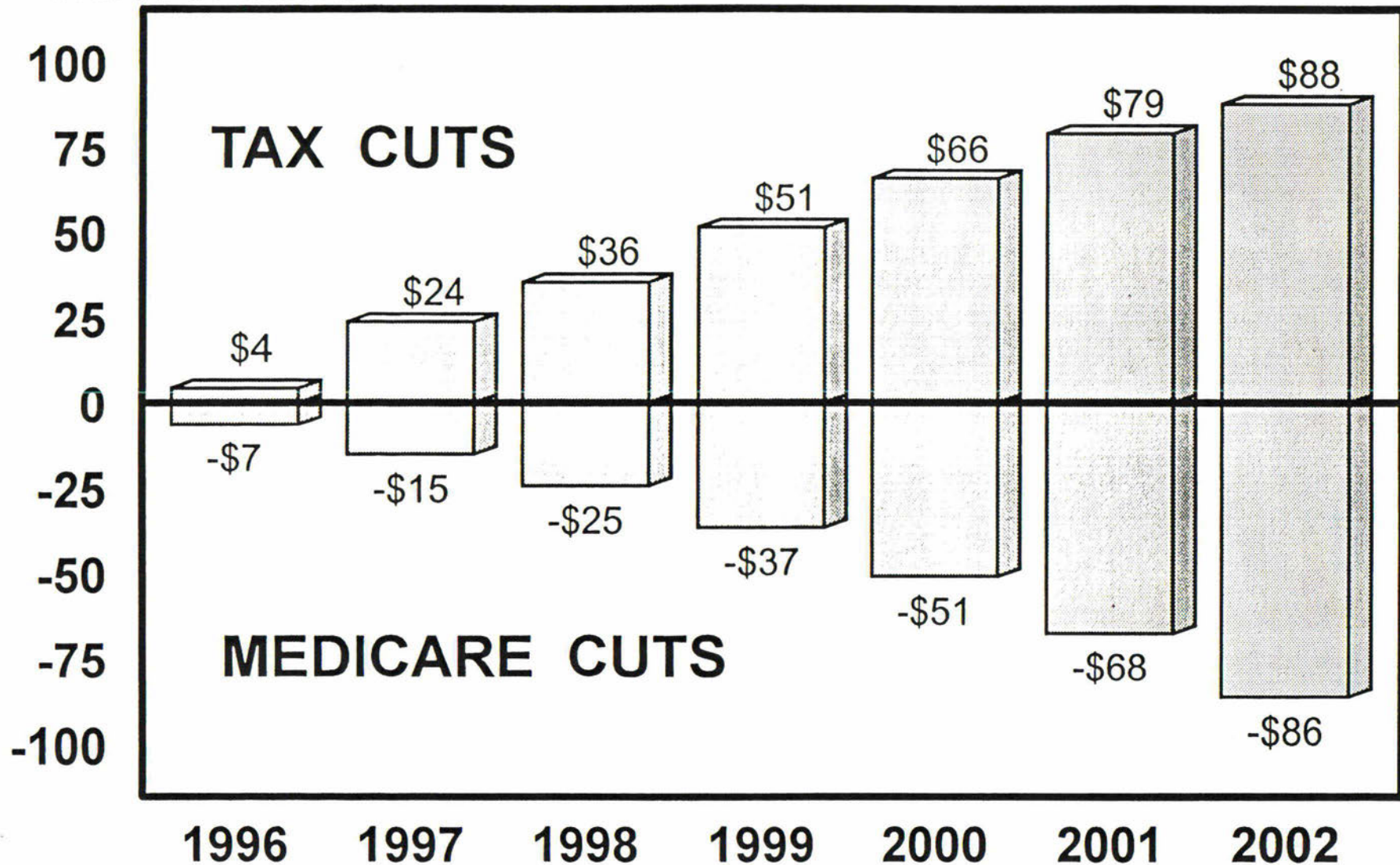
- The "Boren Amendment" and other Federal requirements that set minimum payments to health care providers will be repealed.

- **Reducing Medicaid Costs:** The President proposes a combination of policies to reduce the growth of federal Medicaid spending, including expanding managed care,

reducing and better targeting Federal payments to states for hospitals that serve a high proportion of low-income people, and limiting the growth in federal Medicaid payments to states for each beneficiary. Per-person limits, as opposed to a block grant on total spending, promote efficiency while protecting coverage.

REPUBLICAN TAX CUTS REQUIRE DEEP MEDICARE CUTS

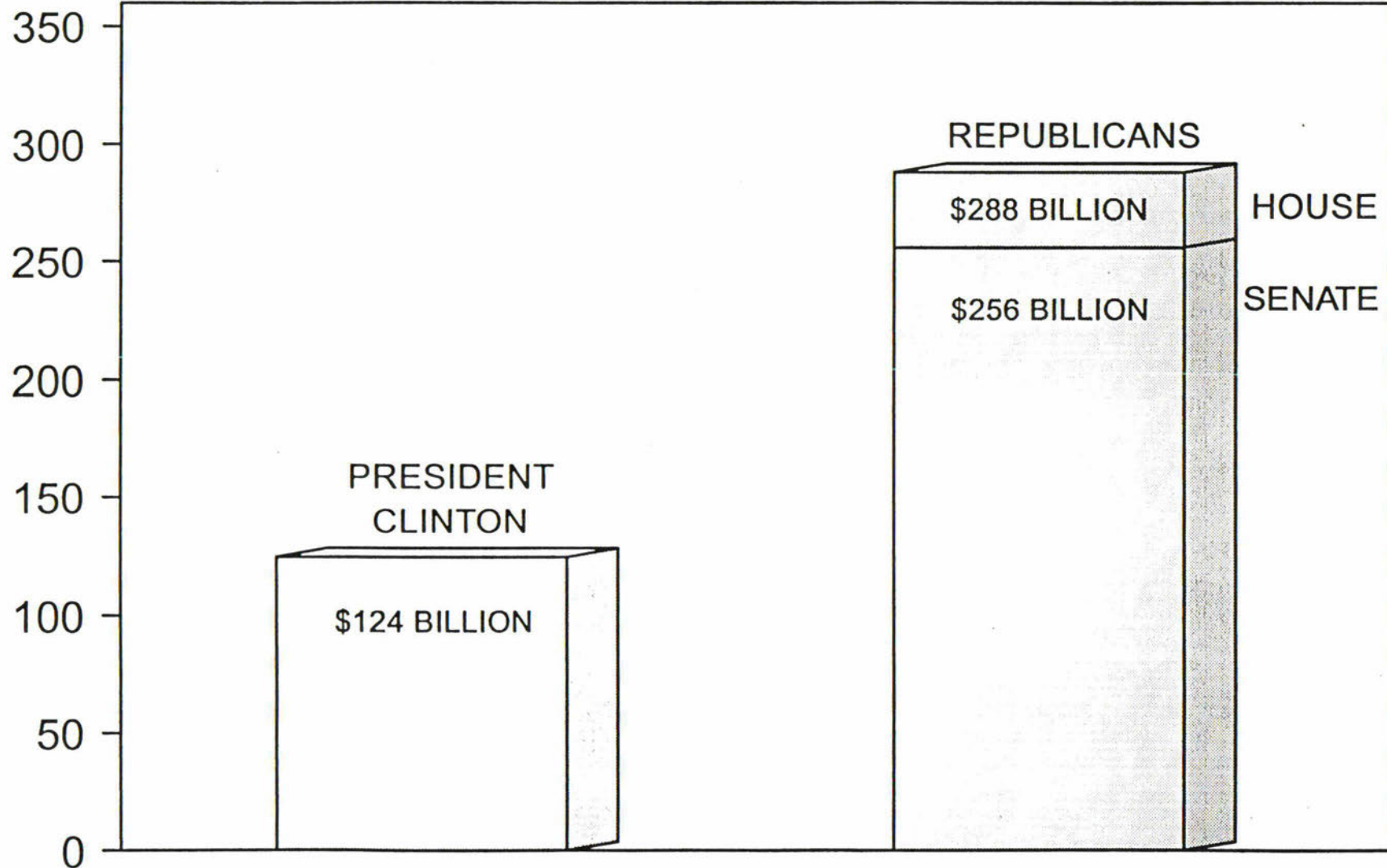
DOLLARS IN BILLIONS



NOTE: House Budget Resolution numbers.

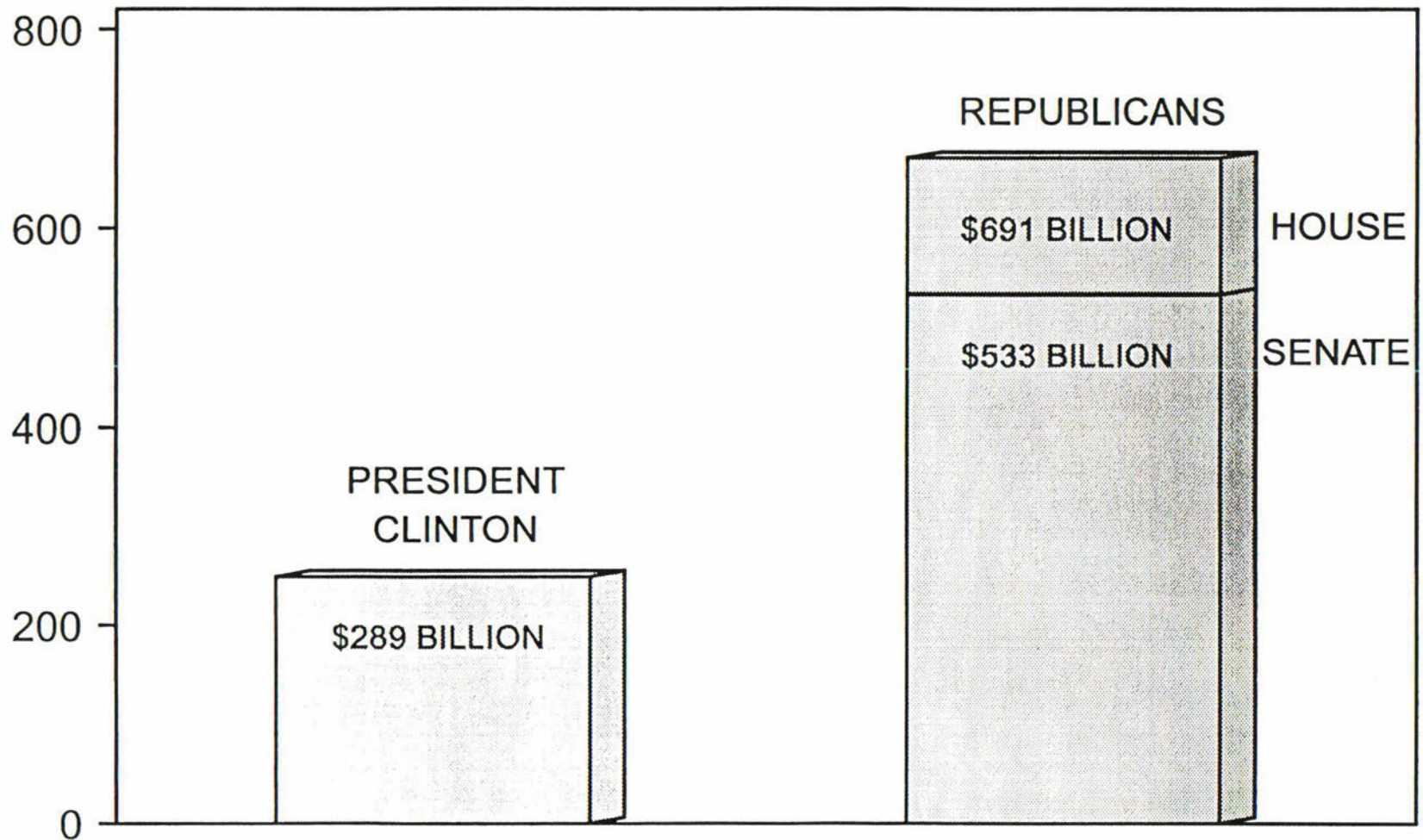
MEDICARE SAVINGS SEVEN YEARS

DOLLARS IN BILLIONS



MEDICARE SAVINGS TEN YEARS

DOLLARS IN BILLIONS



MEDICARE REFORM

IMPACT ON BENEFICIARIES IN 2002

Republican Proposals

▪ \$1,700 CUT PER COUPLE

- Additional Costs
 - Higher Co-Payments
 - Higher Premiums
 - Coercive Plan
 - 2nd Class Health Care System for Seniors

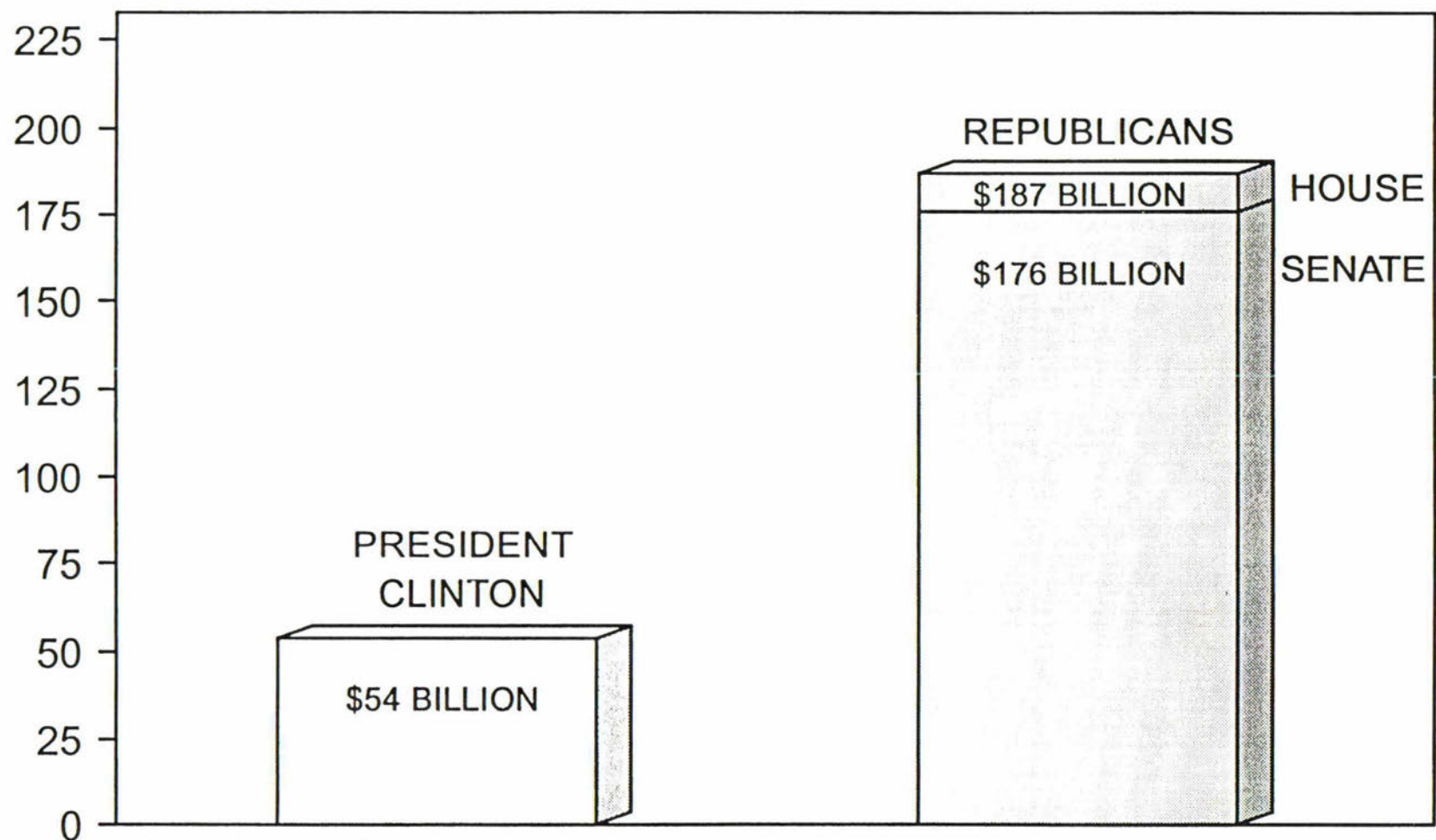
President's Proposal

▪ NO NEW BENEFIT CUTS

- Additional Benefits
 - Home- and Community-Based Care Grants
 - Respite Benefits for Alzheimer's Caretakers
 - Preventive Health Benefits: No Mammography Co-Payment

MEDICAID SAVINGS SEVEN YEARS

DOLLARS IN BILLIONS



THE PRESIDENT'S PLAN: REWARDING WORK AND RESPONSIBILITY

For low-income programs, the President would move people from welfare to work through strict work requirements and investments in training and child care. He would expand efforts to fight fraud and abuse, maintain the national nutrition safety net, target support to the neediest, and protect poor children. These proposals would save \$38 billion over 7 years, after accounting for investments in child care and work and training for welfare recipients. Republican proposals would cut more than \$100 billion over 7 years, tearing apart the social safety net, imposing unattainable work requirements while slashing child care, and putting millions of children at risk.

- For the Earned Income Tax Credit, the President proposes to continue the expansion of tax relief for the working poor, save \$3 billion over 7 years by improving error and fraud control, and make sure illegal aliens who are not authorized to work in the U.S. do not receive the EITC.

- By cutting the EITC by \$21 billion over 7 years, Senate Republicans would raise taxes on 10 million working families with children and 4 million low-income workers without children.

- For cash assistance and social services programs, the President would save \$10 billion over 7 years by tightening SSI eligibility, tightening rules for AFDC, encouraging recipients to move from welfare to work, curtailing abuses, and investing in child care and work programs.

- Republicans would drastically cut funding for cash assistance (\$29-44 billion over 7 years), remove requirements that States contribute to program funding, place new strings on States, and, in the House plan, ultimately deny cash to millions of children. In addition, the House would eliminate SSI benefits for up to 170,000 disabled children now receiving benefits and for as many as 550,000-850,000 who would otherwise receive them over the next five years.

- For benefits to immigrants, the President would save \$5 billion over 7 years by tightening sponsorship and eligibility rules for non-citizens, thus forcing sponsors of legal immigrants to bear greater responsibility for those whom they encourage to come to the U.S.

- Republicans would slash \$27-\$33 billion over 7 years by denying assistance to low-income immigrants, including over 1 million legal immigrants now in the U.S.

- For food assistance, the President would maintain the national nutrition safety net programs while cutting mandatory spending by \$20 billion over 7 years. He would protect spending on WIC and give 600,000 more women, infants and children access to WIC's important health and nutrition benefits.

- Republicans would eliminate the national nutrition safety net, slashing \$33-\$49 billion over 7 years, by capping Food Stamps and block granting the school lunch and other child nutrition programs. In addition, Republicans would force up to 300,000 women, infants, and children off WIC in 1996.

THE PRESIDENT'S PLAN: REFORMING ENTITLEMENT SPENDING

The President is proposing a series of reforms in entitlements and other mandatory programs that will raise tens of billions of dollars by targeting benefits to those who need them and ensuring that taxpayers get a fair return on public resources. Republicans would cut too deeply into entitlements and threaten services and benefits on which millions of Americans rely.

Veterans:

- The President proposes to protect pensions for poor veterans and compensation for service-connected disabled veterans.
 - Republicans would restrict or eliminate compensation benefits for certain veterans, and redefine and narrow eligibility for service-connected disabilities.

Farm Programs:

- The President proposes to save \$4.2 billion over 7 years by allowing farmers to use more acreage to plant what the market demands, reducing inequitable treatment of farmers by crop and region, and targeting payments to smaller farmers.
 - Republicans would cut farm program spending 3-4 times as much -- the House by \$17 billion over 7 years, the Senate by \$12 billion over 7 years -- without specifying how.

Spectrum Auction:

- The President proposes to raise \$14.3 billion from 1996-2002 by expanding the Federal Communications Commission's spectrum auctions to a variety of new wireless services.
 - The House and Senate also would expand the Government's auction authority.

THE PRESIDENT'S PLAN: INVESTING IN EDUCATION AND TRAINING

The President proposes to invest more in education and training, giving average Americans the skills they need to get high-wage jobs in the new economy. He would increase investment in education and training by \$9.5 billion a year by 2002. The President's plan increases education and training by \$40 billion over the next 7 years; Republicans would cut it by up to \$43 billion over the same period.

- For National Service, the President would expand the Corporation for National and Community Service, enabling nearly 1 million young Americans to serve their communities and earn scholarships for higher education.

- The House would kill all national service programs.

- For the GI Bill for America's Workers (excluding Pell grants), the President consolidates 70 programs and add an additional \$2.3 billion in 2002 for adult skill grants and youth programs.

- Republicans would cut funding 25 percent below the 1995 level.

- For Head Start, the President would increase annual funding by \$1.5 billion by 2002 to reach another 50,000 children -- for a total of 800,000 per year -- and to improve quality.

- House Republicans would cut up to 200,000 children, compared to 1995.

- For Goals 2000, the President would increase funding from \$124 million in 1995 to \$867 million in 2002, helping all States and school systems extend high academic standards, better teaching, and better learning to 44 million children in over 85,000 schools.

- House Republicans would kill support to help States raise education achievement.

- For Pell Grants, the President would increase annual funding by \$3.4 billion by 2002 to reach 960,000 more recipients (for a total of 4.8 million) and increase the maximum award from \$2,340 to \$3,128.

- Republicans would freeze Pell at the 1995 level.

- For Safe and Drug-Free Schools and Communities, the President would maintain funding at \$500 million per year, to help nearly every school district fight drug abuse and reduce violence.

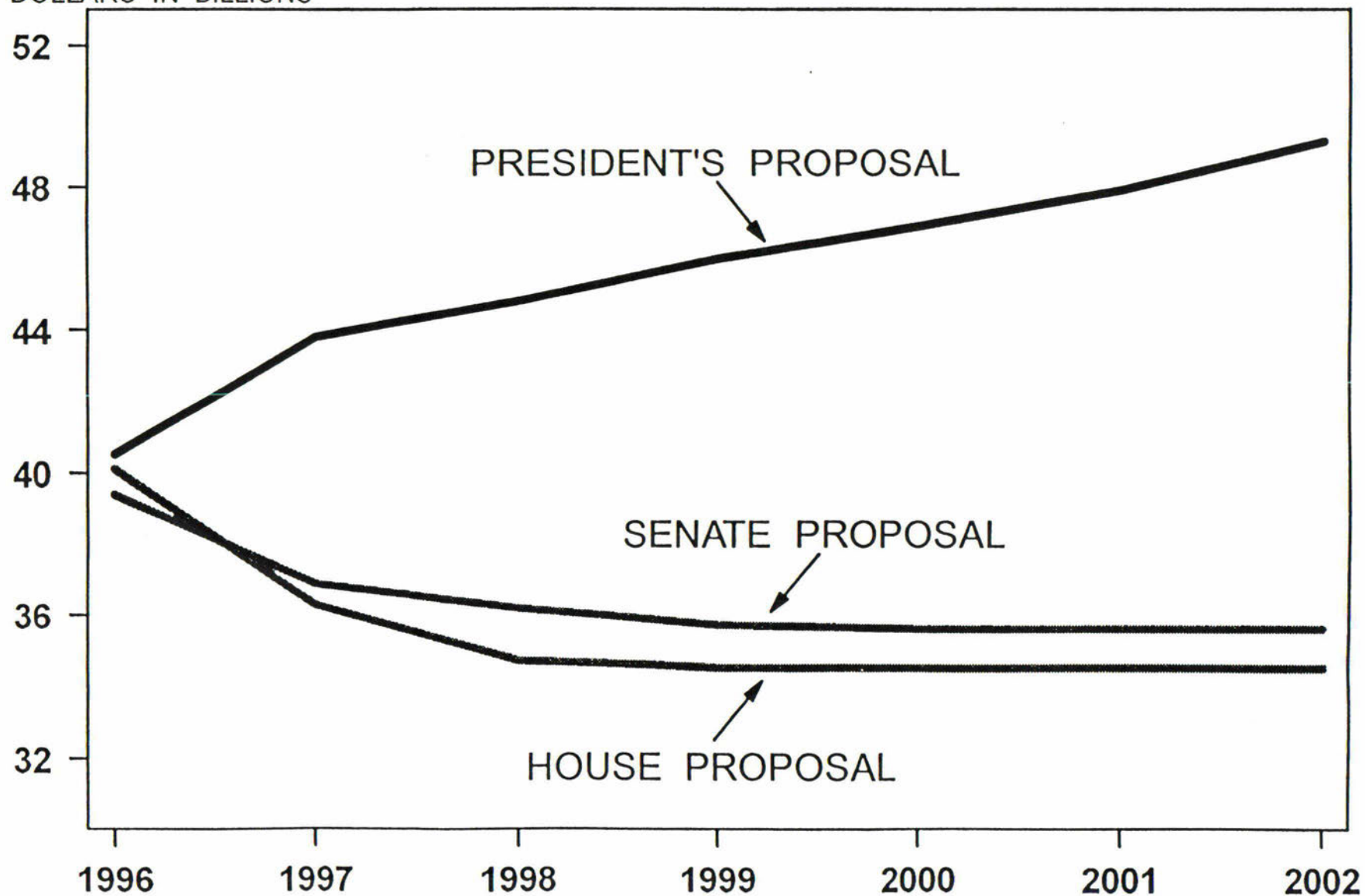
- Republicans would turn the program into a block grant and cut funding 30 percent.

- The President would phase in Federal Direct Student Loans quicker, affecting \$25 billion in loans to 6 million people a year, at lower cost to government, schools, and students.

- House Republicans would eliminate the in-school interest exemption for 4 million financially needy borrowers, requiring a low-income college graduate who borrowed the maximum amount to pay \$3,150 more for loans than under the President's plan.

INVESTMENTS IN EDUCATION AND TRAINING

DOLLARS IN BILLIONS



THE PRESIDENT'S PLAN: PROTECTING THE ENVIRONMENT

The President proposes to protect the environment and our natural resources, but still save money by focusing funds on legitimate Federal functions, cutting or eliminating lower-priority programs, and increasing the use of user fees. Republicans would jeopardize the environment by eliminating funds for constructing municipal wastewater and drinking water facilities, ending the acquisition of land for national parks and forests, and cutting park and forest budgets by 10 percent below 1995.

- The President proposes to consolidate the Clean Water and Safe Drinking Water State Revolving Funds that make loans for municipal wastewater and water treatment construction, giving States more flexibility in meeting local priorities. He would reduce funding over time to \$1.5 billion a year as States gain access, as a permanent source, to the repayments of previous loans.

- The Senate would eliminate these programs by 1998; the House would provide less funding than the President.

- The President proposes to increase funding by \$265 million a year by 2002 for the Environmental Protection Agency's operating program, the backbone of our efforts to protect the environment. This increase comes after \$150 million in savings due to streamlining and decreased EPA oversight of State delegated programs. The operating program increases address global climate change, promote development and export of environmental technology, and protect sensitive ecosystems.

- Republicans would eliminate the program to develop environmental technologies that improve the environment at lower cost while opening new export markets, and terminate funding for programs that protect water quality and preserve habitat for ducks and fish.

- The President proposes increases each year for National Park operations and rehabilitation in order to maintain parks and their facilities.

- Republicans would cut national park construction by half, and park operations by 10 percent, the latter of which would strain the National Park Service's ability to keep parks open and up to standards.

- The President proposes to phase-down spending on Federal land acquisitions to \$100 million a year, focusing on high-priority projects and the expanded use of land exchanges.

- Republicans would terminate Federal land acquisitions.

THE PRESIDENT'S PLAN: CONTROLLING VIOLENT CRIME

The President proposes to expand his vigorous fight against violent crime, providing a \$6.7 billion increase a year by 2002 for grants to States and localities; more resources for Federal investigations, prosecutions, and imprisonment; and more support for the Federal Judiciary to try and convict violent offenders. The President would spend \$7.5 billion more in 2002 than House Republicans and \$200 million more than Senate Republicans.

- The President proposes to fully fund the Violent Crime Reduction Trust Fund (VCRTF), providing the full \$30.2 billion authorized by the VCRTF from 1995-2000. In addition, for 2001-02 the President would add \$8.5 billion, bringing total VCRTF funding to \$38.7 billion for 1995-2002.

- House Republicans would cut programs authorized by the VCRTF from 1995-2000.

- The President's proposal for the VCRTF would finance:

- 100,000 cops for State and local police forces, fulfilling a major promise of the President and adding almost 20 percent to State and local police forces;

- reimbursements to States which have paid to incarcerate criminal illegal aliens; and

- State and local grants to:

- bring new prison cells into service;

- confront the problems of violence against women; and

- finance "drug courts" which provide cost-effective ways to deal with first-time, non-violent drug offenders.

- The President would provide an increase of \$1.7 billion by 2002 for Justice Department crime fighting programs, including heightened border enforcement, increased FBI and DEA funding to address drug abuse, street crime, and terrorism; and increased resources for the Federal Prison System for new prisons and costs tied to a growing population of violent criminals.

- Republicans would not provide specific increases for these programs.

- The President would increase funding by \$500 million a year by 2002 for the Federal court system to adjudicate violent criminal cases.

- Republicans would not provide any increases for the Federal Judiciary.

- The President would terminate several unnecessary or redundant programs, such as the State Justice Institute, the Administrative Conference of the U.S., and the U.S. Parole Commission.

THE PRESIDENT'S PLAN: STRENGTHENING OUR COMMITMENT TO SCIENCE AND TECHNOLOGY

The President proposes to significantly improve the Nation's global economic competitiveness through a balanced mix of basic research, applied research, and technology development, much of it through cooperative projects with private industry. Republicans would significantly reduce investments in basic research, applied research, and technology development.

- The President proposes to add \$2.5 billion a year by 2002 for biomedical and behavioral research at the National Institute for Health.

-- The House would cut biomedical and behavioral research at NIH by \$542 million.

- The President proposes that the National Science Foundation's investments in basic research and education programs keep pace with inflation, adding \$500 million a year by 2002.

-- Republicans would invest significantly less, with the Senate cutting \$100 million and the House adding \$240 million.

- The President would provide \$100 million more a year by 2002 for the science facilities utilization initiative, ensuring more research time for scientists working on "cutting edge" research facilities.

-- Republicans would force many of these valuable facilities to close their doors.

- The President proposes to add at least \$500 million a year by 2002 for NASA's investments in basic research, including Mission to Planet Earth, which will provide the first global study of the impact of man on the Earth's environment.

-- Republicans would cut these important research programs significantly.

- The President is proposing to increase the Advanced Technology Program (ATP) million and the Manufacturing Extension Partnership (MEP) by almost \$500 million a year by 2002. ATP invests in partnerships with industry to accelerate the development of high-risk technologies with significant commercial potential. The MEP is a nationwide, locally managed network of manufacturing centers to help the nation's 381,000 small manufacturers adopt modern manufacturing technologies.

-- Republicans would eliminate both programs.

The President is proposing to increase funding by \$100 million from 1996-2002 for the Defense Department's DOD Technology Reinvestment Project (TRP), which invests in partnerships with industry to accelerate the development of technologies that are critical to national security but can also benefit civilian purposes (i.e., dual use).

-- The House would eliminate it in the draft 1996 authorization bill.

THE PRESIDENT'S PLAN: TARGETING TAX RELIEF TO MIDDLE-INCOME AMERICANS

The President also proposes to raise living standards with a tax cut for middle-income Americans. The President proposes to help average Americans to save, and to meet the cost of raising and educating their children. Republicans would provide a huge tax cut whose benefits flow disproportionately to wealthy people and corporations and whose costs must be offset by deep cuts in Medicare and other priorities.

- To assist families raising children, the President proposes a tax credit of up to \$500 for each child under age 13. The credit starts at \$300 per child through 1998, and increases to \$500 in 1999. It is phased out between incomes of \$65,000 and \$75,000 per year.

- House Republicans also include a \$500 child tax credit, but phase it out between incomes of \$200,000 and \$250,000. Because Republicans propose a tax cut for people of high incomes -- about 6 times that of the typical family -- they must cut deeply into Medicare and other priorities.

- To help families meet the costs of education beyond high school, the President proposes a deduction for post-secondary tuition and fees of up to \$10,000 per year. The deduction begins at \$5,000 in 1996, rising to \$10,000 in 1999. It is phased out at incomes between \$100,000 and \$120,000 per year for married couples (\$70,000 and \$90,000 for other taxpayers).

- Republicans have offered no such incentive for education.

- To help families save, the President proposes to expand Individual Retirement Accounts. Income limits would double; couples with incomes up to \$80,000 (and single persons with incomes of \$50,000) could make fully deductible contributions. The President would allow penalty-free withdrawals for catastrophic medical expenses (including for parents and grandparents), higher education costs, the purchase of a first home, and unemployment. The President proposes a new back-loaded IRA; contributions are not tax deductible, but withdrawals after five years are tax free.

- House Republican have a similar proposal but would allow back-loaded contributions with no income limit -- again, forcing deep cuts in Medicare and other priorities.

* * *

- House Republicans also have proposed enormous tax cuts for wealthy persons and corporations, forcing them to cut deeply into Medicare and other priorities. The tax cuts include: the virtual end of the alternative minimum tax for large corporations, costing \$35 billion over 10 years; a liberalization of tax depreciation laws that would save large corporations over \$150 billion between 1999 and 2005; a cut in estate taxes for persons with at least \$600,000 of accumulated wealth, costing \$20 billion; and a capital gains tax cut, costing \$90 billion and providing 58 percent of its tax benefits to the 2.5 percent of taxpayers with incomes over \$200,000 per year.

July 1, 1994

MEMORANDUM TO WHITE HOUSE STAFF

From: Gene Sperling
Subject: Economic Talking Points

As part of the effort to get out the economic message, we put out the following materials for the House and Senate Democrats. I have also included at the top a very good G-7 one pager that Laura Tyson, Larry Summers, David Sherman did on why the US is leading world growth.

The materials therefore include:

- **One Pager On US Economy at the G-7:**
- **Message Points:** a talking point document that reflects some of the *preliminary* thoughts that people working on the economic message have had.
- **1 Page Summary Sheet:** A One-Pager on Budget/Economic Accomplishments for the basic facts one would need for any speech or talk.
- **New Developments:** This documents lists some facts that have not been in previous talking points that might be of interest. For example, it has a very positive Business Week Poll that shows growing optimism (90%) among business leaders, a Study showing state revenues going up due to growth not taxes, and some proof that good jobs are being created.
- **3 Page Quick Summary of Economic Accomplishments:** This lays out in bullet-form a more expanded list of positive economic news.
- **Facts on Taxes:** This document that gives the facts on why only the top 1.2% pay face higher income tax rates, with these facts being validated by H&R Block and other sources.
- **Key Economic Statistics:** This is has a more in-depth list of economic facts on the main economic indicators that may be useful in defending the Administration's economic record.
- **Validating Quotes.** This documents is has quotes from sources like Alan Greenspan, Lehman Brothers, Business Week, Robert Reischauer that give the Administration credit for the improvement in either the economy or the budget.

THE U.S. ECONOMY ON THE EVE OF THE G-7 SUMMIT: LEADING THE WAY TO RENEWAL

The U.S. economy continues on a path of investment-led growth and low inflation, and is setting the pace for the G-7 as we approach the Summit. We're pleased that, led by our continuing, solid economic expansion, the other G-7 nations are moving into recovery as well.

- **Leading the way in growth.** Since last year's Tokyo summit, real GDP in the U.S. has grown by 4.2 percent. This represents the best performance for the G-7 economies during this period. In fact, it accounted for 75 percent of total G-7 growth for 1993-94. We expect to continue setting the pace for the rest of 1994 and into 1995.
- **Leading the way in job creation.** Our record here is the best in the G-7 as well, and by a wide margin. In fact, we've created 3.1 million private sector jobs since we took office, nearly all of the job creation in the industrialized world.
- **Leading the way in export growth.** U.S. exports in volume terms, are projected to rise by eight percent this year, faster than in any other G-7 country and double the G-7 average.
- **Leading the way in deficit reduction.** We are now on course to have the lowest budget deficit relative to GDP in the G-7 in 1995
- **Leading the way in private investment.** The U.S. has the fastest growth rate for private investment of any G-7 country. Spending on business equipment is at a postwar high.
- **Keeping inflation under control.** The U.S. inflation rate since Tokyo is the lowest in 20 years. Annualized rate for the first five months of 1994 was 2.3 percent.
- **Showing solid productivity gains.** Productivity growth in the U.S. is now more rapid than in Europe, Japan, and Canada.

GENERAL ECONOMIC TALKING POINTS

1. DRIFT IN THE FACE OF ECONOMIC CHANGE WEAKENED OUR ECONOMIC PROSPECTS:

- For over a decade, the past two Administrations chose drift and avoidance in an era of economic change and challenge. To ensure that America's middle class was strengthened during this period, the American people needed leadership that confronted its challenges, a solid foundation for private sector growth, and investment in giving its people the tools they needed to prosper in a new world economy.
- During the 1980s, our Administrations borrowed too much from our people and invested too little in our future. While taxes for the most well-off Americans were lowered, the deficit skyrocketed and at the same time we invested too little in the things that increase the productivity of our nation and the well-being of our people. As a result, too many middle class families found themselves running harder just to stay in place, and there was too little opportunity for others to work their way into a growing middle class.

2. ECONOMIC RENEWAL REQUIRES US TO PUT OUR HOUSE IN ORDER AND GIVE OUR PEOPLE THE TOOLS TO EMBRACE CHANGE AND MAINTAIN GOOD JOBS AND STRONG FAMILIES:

A: PUTTING OUR HOUSE IN ORDER: After skyrocketing deficits for 12 years, this President and the Democrats in Congress had the courage to make the tough choices necessary to bring the deficit down, start fixing the things broken in government, while investing more in our people. Together we took the following steps:

- **Historic Spending Cuts and Deficit Reduction:** As part of the largest deficit reduction package in history, the President and Democrats in Congress cut \$255 billion in spending -- one of the largest spending cut packages in history.
- **Cut 272,000 Positions:** Cut 272,000 positions from the federal bureaucracy over the next five years so that the size of the federal bureaucracy will go to its lowest level since the Kennedy Administration.
- **Improved Tax Fairness Achieved:** While the deficit reduction plan relied on \$255 billion in spending cuts, when taxes were raised, we asked only those in the top 1% to face higher income tax rates -- with every penny going to deficit reduction. At the same time we made over 90% of small businesses eligible for tax cuts and rewarded work by giving 15 million working families a tax cut.

B. POSITIVE RESULTS: Opponents of the 5-year economic plan passed by the President and Democrats in Congress predicted doom and gloom if Congress acted responsibly and passed the President's economic plan. The facts speak for themselves:

- **The Deficit Reduction Plan is Working:** As a result of the passage of the economic plan, the deficit is coming down for three consecutive years for the first time since Harry Truman was in the White House. Because of the passage of the economic plan, our deficit will now be the lowest as a percentage of national income of any of the major industrial countries in the world.

- **Stronger Economy:** After one of the slowest four year periods of job growth since the Great Depression, the economy, under the Clinton Administration, is now enjoying a solid growth with strong private sector jobs creation and low inflation.

- **Jobs:** In the first 16 months of this new Administration, the economy has created over 3 million private sector jobs -- nearly two and a half times more than were created in the economy during the entire Bush Administration.

- **Sound Economic Elements:** Core inflation is the lowest in 21 years; consumer confidence is at a four year high, business investment in equipment is the highest it's been since WWII as a percentage of GDP, and more businesses were incorporated in 1993 since they started keeping records in 1946.

C: EQUIP OUR PEOPLE TO EMBRACE CHANGE, MAINTAIN STRONG JOBS AND STRONG FAMILIES: More needs to be done. While over half the new jobs being created are good, high wage jobs, too many are still temporary, low-paying jobs and too many families feel they are struggling to make ends meet. The only answer is to invest in our people throughout their lives to give them the tools they need to prosper.

- **Education:** That is why we passed a GOALS 2000 legislation to spur education reform, a new school-to-work legislation to provide more avenues for young people who don't get four year college degrees, and a new college loan legislation that will make loans cheaper for millions of young people, while giving students more choice including the option to borrow to invest in your education and then pay back as a small percentage of your income.

- **Change and Jobs:** We must be committed to creating more jobs in this changing economy and ensuring that our people are equipped to prosper. We must pass the new world trade agreement that will create hundreds of thousands of jobs, while also passing a new re-employment and job training program that will help people get the training and the skills they need to gain employment, change jobs, and get ahead in the new economy.

● **Rewarding Work:** Re-employment is only one significant piece of the President and the Democratic Congress' plan to pass a strong pro-work agenda that rewards and honors work. The President has introduced a bold health care reform plan that will guarantee that people have health insurance they can depend on -- that they can never lose, whether they get sick or change jobs. And that is why he insists on welfare reform that ends welfare as we know it, and rewards work instead of idleness.

ONE PAGE SUMMARY ON ECONOMY/BUDGET

SPENDING CUTS:

- The economic plan included \$255 billion in spending cuts, one of the largest spending cut packages in history.
- The economic plan reduces the federal workforce and bureaucracy by 272,000 -- bringing it down to its lowest level since the Kennedy Administration.

DEFICIT REDUCTION:

- The deficit is projected to decline for three years in a row for the first time since Harry Truman was in office.
- The deficit is projected to be cut nearly in half from where it was projected to be by the end of the economic plan.

TAXES:

- H&R Block and CBO confirm that the income tax rate increases will fall on only the top 1.2%, (families with \$180,000 adjusted gross income and over) while 98.8% of American taxpayers paid the same or less taxes.
- Over 15 million families who work and make less than \$27,000 received a tax cut to reward work. The plan made over 90% of small businesses eligible for tax cuts.

INVESTMENTS IN PEOPLE:

- Even with deficit reduction, significant investments were made in the American people. In 1993, funds for training displaced workers were doubled. Head Start was increased by over \$500 million. WIC was put on a full-funding path. GOALS 2000 school reform legislation and a new school-to-work legislation passed. A new college Loan legislation was passed that will make loans cheaper, while giving students more choice including the option to borrow to invest in their education and then pay back as a small percentage of their income. The Earned Income Tax Credit is up \$21 billion, benefiting 15 million working families. To give people real security for change, however, we must pass health care and re-employment.

JOBS AND EMPLOYMENT:

- In the first third of the Clinton Administration's first term, over 3 million private sector jobs created -- nearly two and half times more than were created in the entire Bush Administration. When President Clinton came into office, the unemployment rate was 7.7%. Now it has gone down to 6.0%.

STRONG ECONOMIC ELEMENTS:

- Core inflation over the last 12 months is 2.8%, the lowest in 21 years. Consumer confidence is at its highest in four years, business investment in equipment is at its highest level since WWII, and businesses were incorporated in 1993 at a record level.

NEW DEVELOPMENTS

Below are recent or relevant facts or studies that have not appeared in the previous talking points and may be of some interest.

1. GROWTH THROUGH THE EXPANDING THE PRIVATE SECTOR NOT EXPANDING THE PUBLIC SECTOR:

- **Private Sector Growth and Decreases in Government Purchases:** Growth is being generated by the private sector, while there is a decrease in government purchases. While the recent revision of the first quarter GDP numbers for 1994 showed growth increasing by 3.4%, it also showed government spending down by 3.5%. Commenting on this trend a month earlier, the New York Times stated:

"For the first time since the late 1940s, the economy is growing strongly despite a sustained drop in purchasing by Federal, state and local governments. The private sector is the only engine of growth in this recovery, unlike every other recovery in the last four decades, in which government spending accounted for at least part of the expansion."(New York Times, May 17, 1994 p.D1)

- **Private Sector Job Growth:** This same trend holds true for the job growth as well. While 46% of jobs during the Bush Administration were created in the private sector, over 93% of the jobs created in the economy during the Clinton Administration have been in the private sector.

- **Cutting Federal Government Positions:** Those who voted for the 1993 economic plan, voted for cutting over 272,000 federal positions, which will bring the federal workforce to the lowest level since the Kennedy Administration.

2. SUMMARY OF BUSINESS WEEK/HARRIS EXECUTIVE POLL, 7/4/94:

The most recent Business Week/Harris Executive Poll demonstrates broad-based, growing optimism about the future of the economy among business executives around the country.

- 90% of the executives surveyed were optimistic about the outlook of the U.S. economy in the next year, up from 83% in December 1993.

- 44% of the business leaders believe that the rate of growth of the gross domestic product will increase more in the next 12 months than it did in the last 12 months. In comparison, six months ago only 25% of the executives expected higher growth in the next 12 months.

- Only half of the executives polled expect long-term interest rates to increase over the next 12 months, compared with two-thirds of the respondents six months ago.
- 87% of the executives believe that unemployment will either stay the same or fall over the next year. Nearly half the executives plan to increase the number of full-time employees in their company over the next year.
- Dramatically, over 90% of the business leaders expect sales in the next year to be higher than sales in the past year and 69% plan to increase investment in plants and equipment.
- 94% reported making a profit in 1993 and over 80% of those say they expect increased profits in 1994.

3. QUALITY JOBS:

- In 1992 about 50% of all the new jobs created were with temporary help agencies. In contrast, during President Clinton's first year temp jobs accounted for only 13.1% of all the new jobs created. (Business Week, June 20, 1994 p.32))

4. JOB PROSPECTS:

- According to Manpower Inc.'s third-quarter survey of 15,000 companies, 29% of U.S. businesses plan to hire workers this summer, the most bullish forecast since 1989.
- In a recent Business Week poll, nearly half of the senior business executives surveyed reported that they plan to increase the number of full-time employees in the next 12 months, while only 27% foresee a decrease in the number of full-time workers they employ.

5. STATE TAX REVENUES UP THROUGH GROWTH -- NOT NEW TAXES: A new study by the Center of the Study of the States found strong revenue growth for states in 1993 and 1994 due almost entirely to economic growth and not new taxes. This additional revenue takes pressure off local governments to raise taxes. In 1992, by contrast, almost all of the increase in revenues came from legislated tax increases.

	Total	Due to Tax Legislation
1992	7.8	6.8
1993	5.8	0.1
1994	6.7	0.4

Source: Center for the Study of the States

QUICK SUMMARY OF ECONOMIC ACCOMPLISHMENTS

When President Clinton came into office, the deficit had been going up for 12 years, trade agreements were stalled, job growth was at historic lows, consumer confidence was shaky. Since President Clinton came into office, the deficit is down, inflation is down, trade barriers are down, while private sector jobs are up 3 million, growth is strong and steady, consumer confidence is at 4 year highs, and new businesses are being incorporated at record highs.

DEFICIT REDUCTION:

- The deficit is projected to decline for three years in a row for the first time since Harry Truman was in office.
- The deficit is projected to be cut nearly in half from where it was projected to be by the end of the economic plan.
- As a percentage of national income, the United States's deficit is now projected to be the lowest of any major industrial economy.
- By 1998, the deficit will be \$200 billion lower than where it would have been without Clinton deficit reduction plan.
- Because the economic plan relied on conservative numbers instead of rosy scenarios, the Congressional Budget Office has projected the deficit to be even lower than projected by Clinton Administration.

SPENDING CUTS:

- Economic plan included \$255 billion in spending cuts, one of the largest spending cut packages in history.
- The economic plan reduces the federal workforce and bureaucracy by 272,000 positions -- bringing it down to its lowest level since the Kennedy Administration.
- Cut 300 different programs, two years in a row, including every major entitlement program.
- Called for eliminating over 100 domestic programs.

TAXES:

- H&R Block and CBO confirm that the income tax rate increases will fall on only the top 1.2% (families making over \$180,000 in adjusted gross income), while 98.8% of American taxpayers paid the same or less taxes.
- Over 80% of the new taxes were on families making over \$200,000
- Over 15 million families who work and make less than \$27,000 received a tax cut to reward work.
- The plan made over 90% of small businesses eligible for tax cuts.

ECONOMIC GROWTH:

Jobs:

- In the first third of the Clinton Administration's first term, over 3 million private sector jobs were created -- nearly two and half times more than were created in the entire Bush Administration.
- When the Clinton Administration came into office, the economy has created seven more private sector jobs per month than under the Bush Administration.
- One third into President Clinton's term, the economy has created over 3 million jobs, well ahead of the 8 million jobs he promised
- In 1993, over two million jobs were created -- over 60% of them were good, managerial, professional or technical jobs paying 46% (or \$675 per week) above the average job.

Unemployment Rate:

When President Clinton came into office, the unemployment rate was 7.7%. Now it has gone down to 6.0%.

Inflation:

- Core inflation over the last 12 months is 2.8%, the lowest in 21 years. The overall CPI over the last 12 months is 2.3%, the second lowest rate since 1965.

Business Incorporations:

- In 1993, there were more new business corporations than any time since Dunn & Bradstreet started keeping records, nearly 50 years ago at the end of World War II.

Strongest in 20 Years:

- Federal Chairman Alan Greenspan said that the economy was in the strongest shape in two decades, and that the deficit reduction passed in 1993 had contributed to this stronger economy.

Consumer Confidence:

- Consumer confidence went up to 92.0, the largest increase in four years. It is up approximately 50% since the Congress passed the Clinton economic plan.

Investment:

- Business investment in productive equipment is the highest percentage of our national income as since World War II.
- After going down -3.5%, in 1991, and up 6.9% in 1992, business investment in productive equipment was up 16.3% in 1993 and up 16.8% in the first quarter of 1994.

INVESTMENT IN PEOPLE:

- Despite severe deficit reduction constraints, important new economic legislation was passed and significant increases were made in key investments in people.
- In 1993, funds for training displaced workers is doubled, going to over \$1 billion for the first time.
- Head Start was increased by over \$500 million;
- WIC was put on a full-funding path, and increased funding by \$350 million.
- Earned Income Tax Credit is up \$21 billion for 15 million families.
- GOALS 2000 legislation passed to spur education reform, while a new school-to-work legislation passed to provide more avenues for young people who don't get four year college degrees.
- New college Loan legislation was passed that will make loans cheaper, while giving students more choice including the option to borrow to invest in your education and then pay back as a small percentage of ones income.

THE FACTS ON TAXES

The President's economic plan shifted federal priorities while bringing the deficit down in a fair and balanced manner. The plan included over \$250 billion in spending cuts and nearly as much deficit reduction from revenue increases. The plan called for tough choices, including a 4.3 cents per gallon gas tax, requiring the top 12.5% of Social Security recipients to include more of their benefits as taxable income, and a 1% rate increase on less than 1% of major corporations.

Yet, the Administration stated that the tax rates were only raised on the top 1.2% of working households -- while 98.8% saw no tax rate increase, and indeed 15 million households were eligible for an expanded Earned Income Tax credit. While much misinformation was put forth last year, it is important to assess the facts. Attached are some key facts, with some of the source materials attached.

THE PRESIDENT'S PLAN REDUCED THE DEFICIT IN THE MOST FAIR WAY POSSIBLE: BY RAISING RATES ON ONLY THE TOP 1.2% -- HOUSEHOLDS MAKING OVER \$180,000.

- As the Washington Post reported, the Congressional Budget Office has found "only a sliver of tax filers -- 1.2% will face higher income tax bill on April 15 because of the Clinton Administration's economic program, according to the Congressional Budget Office." The "income tax applies only to taxable income in excess of...gross income of roughly \$185,000." ("GOP Tax Issue May Fade Away: Only 1.2% of Filers will face Increase, CBO study Finds," Washington Post 1/13/94 p.A8)
- As Newsweek Columnist Jane Bryant Quinn writes: "What with all that hooting and hollering over President Clinton's income tax law, you might believe that your tax has probably gone up. Relax. The tax increase on 1993 returns hit only 1.2 percent of taxpayers, all of them in the highest brackets. They're influential, so when they holler they get heard. But they can afford the higher rate and their payments will help to slow the rise in the mammoth federal deficit. For everyone else, so little is new that preparing your own taxes should be a breeze." (March 15, 1994)

GAS PRICES ARE LOWER TODAY THAN WHEN THE BUDGET WAS BEING CONSIDERED: The American Automobile Association reported that even after the 4.3 cents a gallon tax increase, gas prices will be down on Memorial Day by 2.7 cents from the year before.

MIDDLE CLASS WORKING FAMILIES ARE HELD HARMLESS: NO INCOME TAX RATE INCREASES: 98.8% OF ALL AMERICANS WILL NOT SEE THEIR TAX RATES INCREASE.

- H&R Block have confirmed that:

- * income tax rates are raised only on the "top 1.2% of all taxpayers"
- * there is "no income tax increase for middle-income taxpayers...income tax rates are unchanged on middle incomes -- 82.2% of all tax payers"
- * there is a tax cut for the other "16.6% of all taxpayers [who] benefit from Earned Income Tax Credit Expansion"

"H&R Block Analysis of the Income Tax Consequences of the Revenue Reconciliation Bill of 1993" pp. 21-24.

- Deloitte & Touche's analysis showed the change for working families in 1993 based on changes in tax rates. The analysis found the following changes:

<u>Income AGI</u>	<u>Taxable Income</u>	<u>Change</u>
\$50,000	\$30,100	\$0
\$100,000	\$73,600	\$0
\$150,000	\$116,346	\$0
\$200,000	\$166,166	\$1,308
\$500,000	\$441,746	\$21,990
\$1,000,000	\$886,746	\$60,260

"Deloitte & Touche Income Tax Rate Analysis, Present and Proposed Law Tax Rate Scenarios, Typical Taxpayers -- New Top 1993 Rates."

15 MILLION FAMILIES -- OVER 15% OF ALL TAXPAYERS WHO WORK -- WILL RECEIVE A TAX CREDIT TO REWARD WORK:

- The President's plan expanded the Earned Income Tax Credit so that 15 million more families and households will get a tax cut to ensure the President's commitment that if you work full-time and have a child at home, you should not have to raise that child in poverty. According to H&R Block, 16% of all taxpayers will get a tax cut due to the Earned Income Tax Credit.
- This expansion helps working families with low-incomes get ahead, and is a first building block in the President's plan to reward work over welfare.

OVER 90% OF SMALL BUSINESSES ARE ELIGIBLE FOR TAX CUTS:

Only about 4% of owners of small businesses make over \$180,000 in adjusted gross income and therefore are affected by the increase in the highest tax rates, while over 90% of small businesses will be eligible for tax reductions through increases in expensing and a new capital gains tax cut targeted to small business. As the Wall Street Journal writes: "only 4% of those taxpayers who report some business income on their tax returns -- and that includes partners in law firms and investment bankers as well as owners of small manufacturing companies -- make sufficient money to be hit by the higher tax rates." "Foes of Clinton's Tax Boost Proposals Mislead Public and Firms on the Small Business Aspects." Wall Street Journal, July 20, 1993

- Small businesses are now allowed to expense 75% more due to the President's economic plan -- going from \$10,000 to \$17,500.
- There is a new capital gains tax cut targeted to expansion and creation of small businesses. Investors who invest for more than 5 years in small businesses can get a 50% cut in their capital gains rate.
- The plan also continued the 25% deduction for health premiums for the self-employed. The President is now proposing a 100% deduction in his health care plan.

TAXES ON THE TOP 1.2% HAVE NOT HAD A NEGATIVE EFFECT ON THE ECONOMY: While all agree that the deficit reduction package has helped strengthen our long-term economic prospects, some had warned that the modest increase on taxes on those in the top 1% of individual and corporate filers could have a negative impact on the economy. Most analysts now reject this view.

● According to the Wall Street Journal: "Just how much will the Clinton tax increase on the most well-off Americans hurt the economic recovery? Although the tax rise will take some zest out of consumer spending, mainstream economists say it poses no serious threat to the economy." ("Higher Taxes Unlikely to Hurt Recovery: Economists See Minor Impact on Consumer Spending," Wall Street Journal, December 22, 1993)

● According to Business Week: Back in August, when President Clinton's five year, \$240 billion tax increase passed, the Senate critics predicted the worst...Well, a funny thing happened on the way to Armageddon. The economy which was growing at an anemic 1.3% annual rate before the tax hike became law, expanded at more than twice that rate during the second half of 1993. What's more, economists figure growth reached 4% or more in the fourth quarter. And in the six months since Clinton signed the measure nearly a million new jobs have been created, while personal consumption has come close to 4%....it suggests that fears about the increase of a modest tax increase were overblown." ("The Tax Hike Won't Derail the Recovery," by Howard Gleckman, Business Week, January 31, 1994)

KEY ECONOMIC STATISTICS

June 29, 1994

1. UNEMPLOYMENT:

- *UNEMPLOYMENT RATE IS DOWN:* The unemployment rate declined from 6.4% in April to 6.0% in May. *It has now declined from 7.7% in January 1993 to 6.0% for May, 1994.*

2. JOB CREATION:

- *THE ECONOMY HAS CREATED ALMOST TWO AND HALF TIMES MORE PRIVATE SECTOR JOBS IN 16 MONTHS THAN WERE CREATED UNDER ALL FOUR YEARS OF THE PREVIOUS ADMINISTRATION:* Under the four year period of the previous Administration only 1.311 million private sector jobs were created (1/89-1/93). In the first 15 months of the Clinton Administration, 3.115 million private sector jobs were created.
 - *While 93% of the jobs created during the Clinton Administration's tenure have been in the private sector, only 54% of the jobs created during the previous four years were in the private sector.*
 - *MORE THAN SEVEN TIMES MORE PRIVATE SECTOR JOBS PER MONTH:* The economy has created 195,000 private sector jobs per month in the first 15 months of the Clinton Administration -- more than seven times the 27,000 private sector jobs per month created in the previous four years.
- *MORE JOBS OVERALL IN 16 MONTHS (3.357 MILLION) THAN IN THE PREVIOUS FOUR YEARS COMBINED (2.444 MILLION):*
- *MORE THAN A MILLION JOBS IN THE FIRST FIVE MONTHS OF 1994: AHEAD OF SCHEDULE FOR 8 MILLION JOBS IN FOUR YEARS:* The economy has now created more than 1,237,000 million total jobs in the first five months of the year, 96% (1,186,000) in the private sector. More than two million jobs were created in 1993. The current pace --247,000 jobs a month -- puts the economy well ahead of schedule to create "2 million more in '94" and ahead of schedule to create 8 million jobs by the end of 1996.
- *MANUFACTURING JOBS ROSE SIX TIMES IN THE PAST EIGHT MONTHS:* After serious declines for several years, manufacturing jobs were up in six of the past eight months. They are now up 56,000 over the last eight months.

- *CONSTRUCTION EMPLOYMENT HAS INCREASED FOR ELEVEN STRAIGHT MONTHS:* Construction employment has increased for eleven straight months. After declining by 664,000 jobs during the Bush Administration, construction jobs are up 386,000 jobs since January 1993.

- *AUTO JOBS ARE UP:* Auto employment has increased 46,000 over the last 12 months from 820,000 to 866,000.

3: HIGH QUALITY JOBS ARE BEING CREATED

- In 1993, over half of the new jobs created were professional, managerial or technical jobs paying 46% above the average wage.

- In 1992 about 50% of all the new jobs created were with temporary help agencies. In contrast, during President Clinton's first year temp jobs accounted for only 13.1% of all the new jobs created.

4. BUSINESS PEOPLE ARE OPTIMISTIC ABOUT FUTURE JOB CREATION:

- In a recent Business Week poll, nearly half of the senior business executives surveyed reported that they plan to increase the number of full-time employees in the next 12 months, while only 27% foresee a decrease in the number of full-time workers they employ. 86% believe that unemployment will either stay the same or decline.

- In addition, the Manpower Inc.'s third-quarter survey of 15,000 companies shows that 29% of U.S. businesses plan to hire workers this summer, the most bullish forecast since 1989.

5. MORE BUSINESSES BEING CREATED & FEWER ARE FAILING: Dunn and Bradstreet stated that "In 1993, the United States posted the greatest number of yearly business incorporations since Dunn & Bradstreet began reporting this data in 1946." In addition, business failures also declined by 11.4% in 1993.

6. INFLATION REMAINS LOW:

- While we are vigilant in watching for inflation, the signs so far remain positive.
- Core CPI (excluding food and energy prices), over the past 12 months rose 2.8% – the lowest annual increase in over 21 years. The overall CPI has been 2.3% over the last 12 months, the second lowest since the 1966.
- Top private forecasters still see moderate/low inflation, and have even decreased their inflation forecasts. The June Blue Chip Forecast projects inflation to be down from 3.0 percent in 1993 to 2.7 percent in 1994 and at 3.3 percent in 1995.
- The American Automobile Association reported that even after the 4.3 cents a gallon tax increase, gas prices will be down on Memorial Day by 2.7 cents from the year before.
- The Producer Price Index was negative (-0.4%) over the last 12 months and the core PPI was just 0.4% -- close to the smallest increase since the government started measuring this series in 1974, when price controls were in place.
- Average prices of finished goods leaving America's factory gates are lower, in absolute terms, than a year ago.

5. BUSINESS CONFIDENCE IN THE ECONOMY:

- Fortune Magazine, finds CEOs of both large and small companies are more optimistic about the future than they have been in nearly a decade. More than 80% of small business and major CEOs report that their own sales are up, and 40% say they plan to hire new employees.
- The most recent Business Week/Harris Executive Poll published in the July 4, 1994 demonstrates broad-based, growing optimism about the future of the economy among business executives around the country. The poll showed that:
 - 90% of the executives surveyed were optimistic about the outlook of the U.S. economy in the next year, up from 83% in December 1993.
 - 44% of the business leaders believe that the rate of growth of the gross domestic product will increase more in the next 12 months than it did in the last 12 months. In comparison, six months ago only 25% of the executives expected higher growth in future 12 months.

- Nearly half the executives plan to increase the number of full-time employees in their company over the next year. In addition, 87% of the executives believe that unemployment will either stay the same or fall over the next year.
- Dramatically, over 90% of the business leaders expect sales in the next year to be higher than sales in the past year and 69% plan to increase investment in plants and equipment.
- 94% reported making a profit in 1993 and over 80% of those say they expect increased profits in 1994.

6. CONSUMER CONFIDENCE:

- Consumer confidence is up to 92.0 on the Conference Board Index for June, the highest in four years. Indeed, consumer confidence is up over 50% since the passage of the economic growth plan in August, 1993.
- People are starting to become more upbeat about job prospects. According to the consumer confidence survey from the University of Michigan, the number of people believing that jobs were hard to get has declined from 41.6% to 29.1%.
- A USA/CNN/Gallup Poll released May 25, 1994 found that more people now believe they are better off economically than at any time since September 1990.

7. BUSINESS INVESTMENT:

- Investment spending for equipment in 1994 is now at the highest level relative to GDP in the postwar period.
- In the first quarter of 1994, investment in equipment was also up a strong 16.1% at an annual rate. Business investment in equipment from the end of 1992 to the end of 1993 was the highest in 20 years.
- Since the beginning of 1993, real business spending on equipment is up 17.8%. Total capital spending reached \$592 billion in 1993 (in inflation-adjusted dollars), a near record 12% of the gross domestic product.
- Capital spending will remain strong in the future. The most recent Business Week/Harris poll of business leaders reports that nearly 70% of the executives plan to increase the amount of investment in plant and equipment over the next year.

- Factory capacity growth so far in 1994 is the fastest since 1985. According to economists at Dean Witter Reynolds Inc., U.S. companies have announced plans for more than 60 new plants and 70 plant expansions already this year.
- A Commerce Department report on June 9, 1994 revealed that US businesses plan to lift real investment on new plant and equipment by 8.9% in 1994.
- Federal Reserve Data reveals that "businesses are increasing their borrowing from banks to help finance expansion plans, adding fuel to the economy" and that business loans at the nation's banks rose \$20 billion between September and March 23, according to the Federal Reserve. ("Firms Increase Bank Financing for Expansion," Wall Street Journal, April 8, 1994)

8. BLUE CHIP FORECAST:

- The Blue Chip Forecast for June showed solid growth with low inflation for the next two years.
- The Blue Chip forecast for June predicts growth of 3.7% in 1994 and 2.8% in 1995.
- The Blue Chip inflation forecast is lower. While inflation was 3.0 in 1993, it is projected to be down to 2.7% in 1994, and up to only 3.3% in 1995.

9. INTEREST RATES:

- Deficit reduction plan helped lower interest rates and which fueled the interest-sensitive parts of the economy and helped jump-start and solidify economic recovery.
- Over 5 million families were able to refinance their homes at average savings of over \$1000 a year, and most are still reaping those savings even as interest rates have moved up, because they refinanced at fixed rates.
- Longterm interest rates today are still far below the 9.9% average of the Bush-Reagan Administrations, while mortgage rates are well below the 11.06% average of the Reagan-Bush era.

10. HOUSING STARTS:

- Housing starts are up 29.0% since January, 1993 after declining -38.5% during the Bush Administration. Housing permits are up 22% over the last year.

11. AUTO SALES:

- **Auto sales up almost 17% in the first quarter:** Sales of new cars and light trucks are "booming" -- up almost 17% for the first quarter of 1994 over the first quarter of 1993, and sales hit a seasonal adjusted rate of 15.9 million units in March. Sales have dropped back in April and May, but are still above year-earlier levels. Earlier in 1994, Chrysler reported its highest monthly vehicle sales in its 69-year history and Ford and General Motors had their highest light truck sales ever.

- Auto jobs have increased by 46,000 over the last 12 months.

12. PRODUCTIVITY:

- Productivity growth in the Clinton recovery has been strong a strong 2.6%, far higher than the 1.6% annual average under the Bush-Reagan Administrations.

COMMENTARY ON ECONOMIC PLAN

Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System, 1/31/94:

"The actions taken last year to reduce the federal budget deficit have been instrumental in creating the basis for declining inflation expectations and easing pressures on long-term interest rates. Although we may not all agree on the specifics of the deficit reduction measures, the financial markets are apparently inferring that, *on balance, the federal government will be competing less vigorously for private saving in the years ahead. Partly because of these structural adjustments, the foundations of the economic expansion are looking increasingly well-entrenched.*"

"The outlook, as a result of subdued inflation and still low long-term interest rates, is the best we've seen in decades." 2/22/94

"The outlook for the U.S. economy is as bright as it has been in decades. Economic activity has strengthened, unemployment is down, and price trends are subdued. In addition, unlike some earlier periods, business spending on new plant and equipment has been an important contributor to growth. This strength in investment will enhance economic efficiency and lay the foundation for the production gains that will bolster the economic welfare of our nation." (Testimony to the House Budget Committee, 6/22/94)

Robert D. Reischauer, Director, Congressional Budget Office, 1/27/94:

"The deficit picture is significantly brighter than it appeared one year ago when the Congressional Budget Office projected that the deficit would soar above \$350 billion by fiscal year 1998. CBO now projects that the federal budget deficit will fall from \$223 billion in the current fiscal year to below \$170 billion in 1996, then creep up to \$200 billion in 1999. *The dramatic improvement since last January is largely the result of the enactment in August of a major package of tax increases and spending-cuts--the Omnibus Budget Reconciliation Act of 1993.*"

Lehman Brothers, 1/10/94:

"To President Clinton's credit, early last year he rejected an either/or construction for U.S. growth versus deficit reduction. Clinton's blueprint for economic revival had as its centerpiece a multi-year program of deficit reduction, but it promised higher growth in the short run. A move to restrain deficit spending, he wagered, would both lower U.S. long-term interest rates and energize U.S. interest sensitive sectors. Lower deficits, lower long-term rates and higher real growth was the overall promise. With the data now rolling in for December 1993, it seems clear that President Clinton delivered on all three counts over the second half of the year."

Stephen Roach, Senior Economist at Morgan Stanley (Wall Street Journal, 6/6/94):

"The forces of moderation are now intact. We could grow at 2.5% to 3.0% for two or three years or longer without a major glitch."

Business Week, 2/7/94:

"Both Clinton and the economy head into 1994 on the momentum from a strong showing at the end of 1993. *Lower long-term interest rates, for which the White House can take partial credit*, helped to rev up spending for cars, homes, and durable goods generally, boosting factory orders and production, while better growth in jobs and incomes kept people happy. The good news for the first quarter is that the fundamentals that lifted the economy at the end of last year remain in place, ready to support job growth this quarter."

Business Week, 7/4/94:

"Indeed a new Business Week/Harris poll shows that top managers are far from fearful of the economic future. Fully 90% of the 401 senior executives surveyed were optimistic about the outlook for the U.S. economy in the next year, up from 83% in a similar query last December. Likewise only half of the executives polled expect long-term interest rates to increase over the next 12 months compares with two-thirds of the respondents six months ago."

U.S. News & World Report, 2/14/94:

"The danger is that Washington's ideological clamor will drown out a quiet economic truth: *Last year's budget package changed fiscal policy significantly, and the economy is already responding.* The yield on a 10-year Treasury note averaged just 5.9 percent in 1993, compared with the 6.7 percent forecast by CBO one year ago and consumer spending moderated to 2.7 percent down from 3 percent that CBO had predicted. Clinton's budget for fiscal 1995 will project a deficit of roughly \$178 billion – a dramatic improvement over the \$230 billion shortfall that economists predicted just one year ago. Clinton will propose freezing or cutting budgets at 10 of 14 cabinet agencies and eliminating perhaps 115 separate federal programs."

David Stockman as Reported by David Broder, 2/8/94:

"The most upbeat analysis of what lies ahead for America, under his (President Clinton's) policies, comes from none other than David Stockman, the architect of the Reagan administration budgets that the Democrats loved to hate. Stockman, now a New York investment banker, showed up in Washington last week with an economic forecast that he acknowledged is brighter and shinier even than those he produced as Reagan's budget director in the early '80s, which Democrats derided as "Rosy Scenario." At a conference here, Stockman drew a picture of: Steady economic growth through the end of the decade, with little or no threat of inflation. A budget deficit sinking to a "comfortable" and infinitesimal

fraction of the nation's annual economic output. Health care costs under control, especially if Congress passes a stripped-down version of the Clinton plan."

Allen Sinai of Lehman Brothers as Reported by the Washington Post, 3/2/94

"This is the healthiest the American economy has been in 30 years."

Washington Post, 2/14/94

"Slowly, but successfully, the American economy seems at last to have worked through the past two decades' accumulated policy errors and resulting disasters. For the first time in years, official Washington's midwinter forecasts speak of strong performance ahead. One reason for it is the decline in the federal deficit, an achievement being loudly celebrated by the Clinton administration....But there more, and the optimism goes well beyond the White House. The most cautious of observers, Federal Reserve Board Chairman Alan Greenspan, concedes that the foundations of economic growth "are looking increasingly well-entrenched. Robert Reischauer of the Congressional Budget Office, whom one senator described as "somewhat of a dark messenger in the pasts, sees years of steady growth ahead. Mr. Greenspan points out that core inflation rate is now lower than at any time since the early 1970s Next year the CBO calculates, the budget deficit will be smaller in proportion to the size of the economy than in any year since 1979. As a result of those two things, interest rates are low, and business investment is rising powerfully."