FOIA Number: 2018-0275-F

FOIA MARKER

This is not a textual record. This is used as an administrative marker by the William J. Clinton Presidential Library Staff.

Collection/Record Group: Clinton Presidential Records

Subgroup/Office of Origin: Records Management - SUBJECT FILE

Series/Staff Member: Subject Files

Subseries:

OA/ID Number: 17032

Scan ID: 050857SS

Document Number:

Folder Title:
BE

Stack:	Row:	Section:	Shelf:	Position:
S	83	4	3	1

CS

0508573SS

THE PRESIDENT HAS SEEN
1-21-94 BE

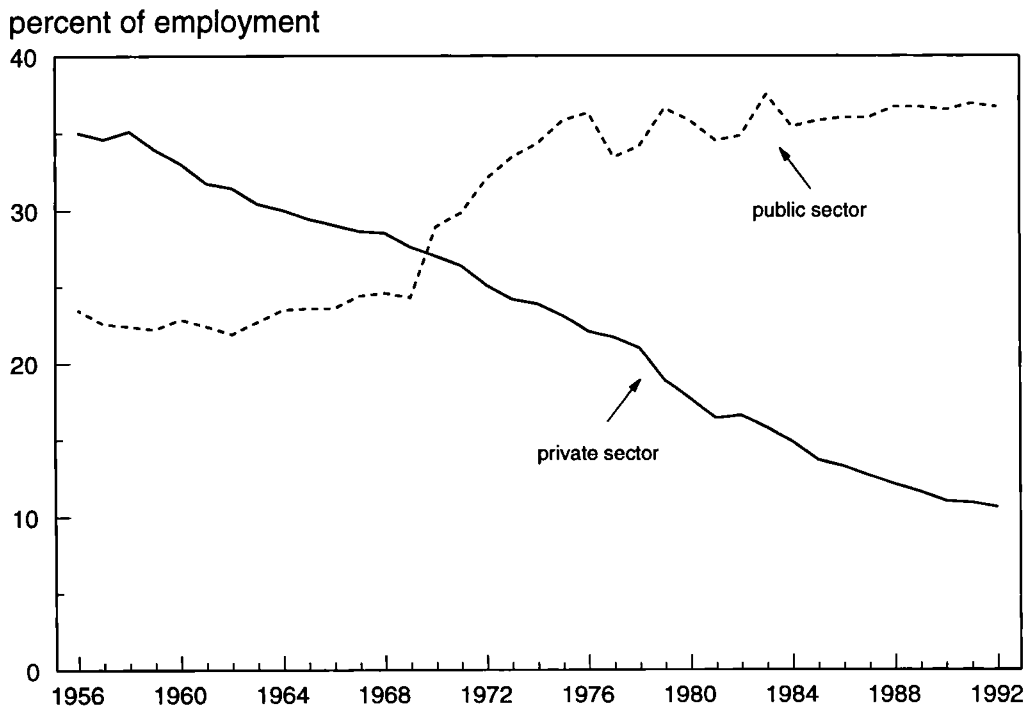
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

Prepared by the Council of Economic Advisers
with the assistance of the Office of the Vice President

January 21, 1994

CHART OF THE WEEK

Public and Private Unionization Rates



The fraction of union members in the total workforce has fallen from 33 percent in the 1950s to 15 percent in 1992. Private sector unionization fell faster than the overall rate, but public-sector unionization increased.

050857

CONTENTS

"Daddy's not mad at you dear— Daddy's mad at the Fed."

CURRENT DEVELOPMENT

Los Angeles Earthquake: Economic Assessment

The earthquake will have a large effect on Southern California. The effect on the national economy will be much smaller, but possibly big enough to change GDP growth this year. A rough chronology is as follows:

First 2 Months: Lost Production and Reduced Income. Closed plants and offices mean lost workdays and lost paychecks. Destroyed housing reduces rental income. Insurance company payouts transfer income from their stockholders to stricken homeowners and businesses.

Months 3 to 12 and Beyond: Rebuilding Destroyed Property. Replacing and repairing buildings, furnishings, cars, and highways will boost economic activity. Most of the benefit will go to local contractors, but factories in other states will also get increased orders. The private-sector rebuilding is likely to take place mainly in the first year. But rebuilding the public infrastructure will take much longer.

Long Run: Rebuilding Lost Wealth. Many households will need to dip into savings to replace uninsured property. Over a period of many years, they will then rebuild their financial assets by spending less. Taxes may also increase in the future to finance repairs to highways and public buildings.

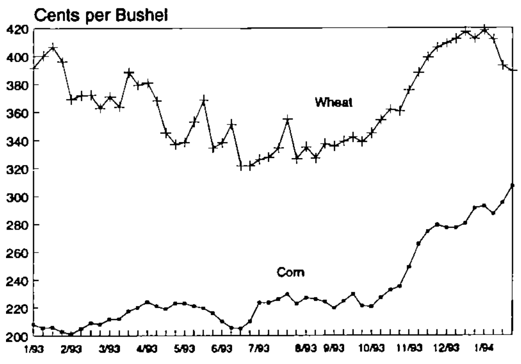
Effects on GDP Growth

The impact on GDP depends on the amount of destruction, which is not yet known. Newspaper reports have suggested property losses of $7 billion dollars. If this is close to correct, we estimate tentatively the following effects on GDP growth: In the first quarter of 1994, the annual rate of real GDP growth will be reduced by 0.1 or 0.2 percentage point. In the second and third quarters, it will be 0.2 or 0.3 percentage point higher. Thereafter, the effects will be negligible.

CURRENT DEVELOPMENT

Rising Grain Prices

Spot Prices of Corn and Wheat



The producer price index for foodstuffs and feedstuffs increased sharply in the last quarter of 1993, heralding rising food price inflation. Rapidly rising corn and wheat prices were important contributors to this increase.

Weather was a major factor in both cases. Heavy rainfall and flooding in the Midwest coupled with drought in the Southeast produced a 1993 corn crop 18 percent below average. Wet weather damaged the quality of the wheat crop more than the size of the harvest. Consequently, the supply of high quality milling wheat is tight.

Demand for milling wheat has also been higher than expected, as aggressive use of export subsidies has partially offset reduced purchases by the former Soviet states and China. Demand for low quality wheat has been buoyed by high prices of alternative feed grains and by last week's heavily subsidized sale of feed wheat to China.

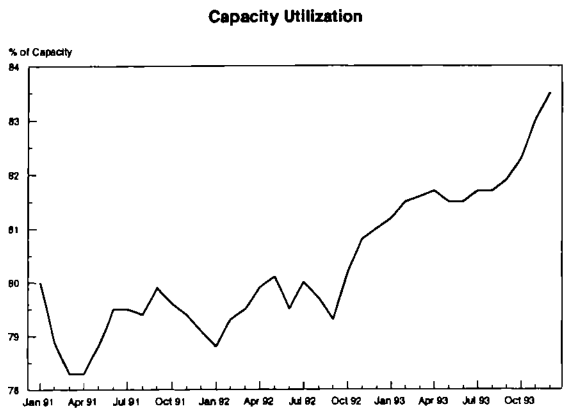
Corn stocks in 1994 are expected to be lower than in any year since 1975. Supply will be tight and prices high throughout the year.

Domestic Impacts of Export Subsidies

U.S export subsidies for wheat have large effects on domestic and international markets because subsidized U.S exports account for close to a quarter of world wheat trade. Our export subsidies create a gap between a high domestic price and low world price that, ironically, attracts imports. Durum wheat, used to make pasta, is an example. In 1992/93 crop year, the average U.S. price of durum was 45 percent higher than the average Canadian price, up from 20 percent higher a year before. Predictably, imports of durum from Canada jumped by 42 percent and now account for 33 percent of U.S. consumption.

CURRENT DEVELOPMENT

Capacity Utilization High, But Does Not Signal Inflation



Capacity utilization in the nation's factories, mines, and utilities reached 83.5 percent in December, the highest level since 1989. Utilization has increased sharply over the last few months, raising concerns among some analysts about an increase in inflationary pressures.

Analysis. The unemployment rate is coming down faster than expected. Therefore, there is reason to be vigilant about an increase in inflation. But the relatively high level of capacity utilization by itself does not convey an independent signal about inflation.

- The term "capacity" is somewhat misleading. The index measures normal output, not maximum output. Firms can increase their production beyond normal by, for example, adding overtime, increasing the number of shifts, and speeding up assembly lines. Thus, high measured capacity utilization does not necessarily indicate the presence of bottlenecks.

- Statistical evidence suggests that the unemployment rate is a better measure of overall inflationary pressure than is capacity utilization.

- Many of the goods produced by industries with high capacity utilization can be imported. So limits on domestic capacity need not lead necessarily to price increases.

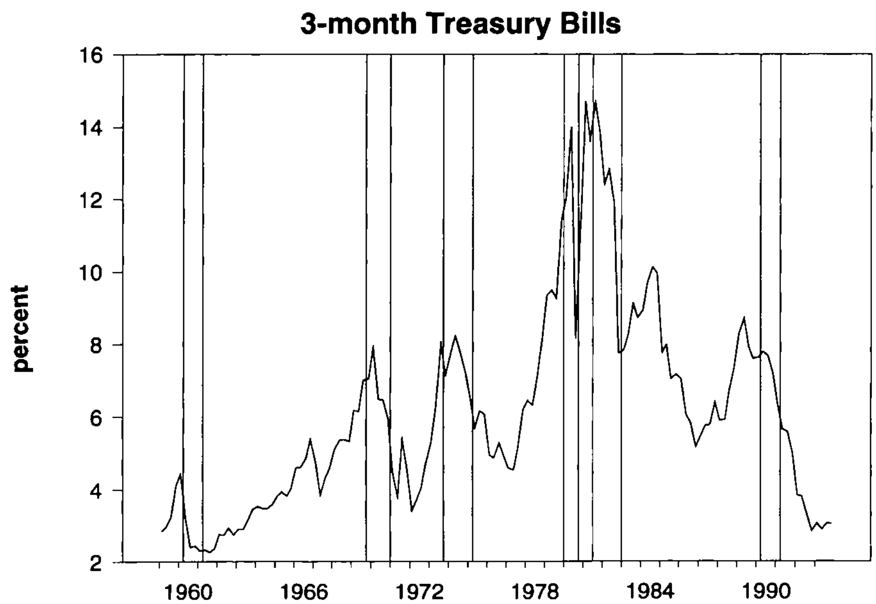
ARTICLE

Short-term Interest Rates: Where Do They Go From Here?

Short-term interest rates have remained roughly constant at about 3 percent for about 18 months. The Administration currently forecasts that short-term interest rates will rise somewhat over the next few years. By the end of 1994, we expect Treasury bills to be yielding 3.6 percent; by the end of 1995, we expect almost a 4 percent yield. We have been forecasting such increases in short rates since you took office. Many private forecasters anticipate even larger increases.

Would an increase in short-term rates of, say, 1 percentage point over 2 years be a cause for concern? The answer is no. A moderate increase in short-term rates is a consequence of continued economic expansion, not a barrier to it.

Interest Rates over the Business Cycle. The graph shows the Treasury bill rate. The shaded areas are recessions, and you can see that interest rates decline sharply in recessions and generally keep falling in the early part of recoveries. As economic expansion continues, however, interest rates begin to rise.



Why Might Short Rates Rise in 1994-1995? Increases in nominal interest rates indicate either higher inflation or higher real rates.

- We forecast only a small increase in inflation during the expansion—under half a percentage point. Therefore, about half of the projected increase in short rates is an increase in inflation. The remainder of the increase is in the real interest rate.

- The real rate rises, in part, from the increase in demand for funds to finance payrolls and inventories as the expansion continues.

- But we expect most of the rise in the real interest rate to come from tighter Fed policy in the near future—though not immediately.

Federal Reserve Policy. The Federal Reserve is likely to increase interest rates to combat what it sees as incipient inflation. The Fed has wide discretion over the timing and magnitude of the interest rate changes. Even if it decides to raise rates, it can do so in ways that minimize the risk to stable growth.

- A modest increase in short-term rates would not harm the expansion, but a significant increase in long-term rates would. If the Fed raises short-term interest rates in a way that makes market participants think more rate hikes are coming, long-term rates could rise substantially. On the other hand, if bond traders believe that the rise in short rates is a one-shot event (at least for a while), long rates would probably increase much less. The point is that the Fed can influence—though not totally control—market expectations by when and how it changes interest rates and what, if anything, it says.

- Some economists worry that a premature tightening by the Fed might take the wind out of the economy's sails, just as the expansion seems to be solidifying. Other economists believe that the Fed should move sooner rather than later on the grounds that, if higher inflation gets entrenched, the Fed would have to apply the monetary brakes much harder—perhaps causing a recession. According to this reasoning, it is better to have slower growth in 1995 than a recession in 1996.

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Southern California Economy Remains Weak. The Federal Reserve survey of regional economic conditions (conducted before the earthquake) reported that overall economic activity continued to expand with signs of acceleration in some sectors. The most significant exception to the strong national trend was in southern California, where economic conditions remained weak. Residential real estate sales and construction were weak in southern California, in contrast to substantial improvements in other districts. Most district banks, including San Francisco, reported that retailers met or exceeded their expectations for holiday season sales.

The survey suggested little upward pressure on wages and prices, but several districts reported increases in the prices of lumber and building materials and scattered shortages of skilled construction workers. In addition, Chicago reported a tightening of the supply of skilled production workers and tradespeople.

Bankruptcies Down. In 1993, for the first time in 5 years, fewer publicly-traded companies filed for protection from creditors under Chapter 11 than left bankruptcy. Of the 83 publicly-traded companies that entered bankruptcy last year, only two had assets exceeding $1 billion—in contrast to more than 10 such firms in each of the 4 previous years.

IPOs Backed by Venture Capitalists Rise. A recent survey of companies backed by venture capitalists found that these firms raised a record $6.9 billion in initial public offerings in 1993. Surveyed companies ranged in size from 53 to 1,418 employees. Computer and other technology companies dominated the public offerings. The value of offerings in the health-care industry dropped by half from 1992. The boom in initial public offerings has continued into 1994, with one investment banker reporting plans to underwrite 12 new public offerings in the first quarter in contrast to 24 in all of 1993.

Heat-shield Technology Keeps Pizzas Hot. A defense contractor has taken heat-shield technology developed to protect satellites from laser attacks and applied it to pizza plates. Pizza Hut has licensed the new pizza plate technology, which will keep a pizza hot for 90 minutes. The plates have been tested at hockey games, school cafeterias, and factories, and will soon be tested for home delivery.

RELEASES THIS WEEK

Merchandise Trade

The merchandise trade deficit fell slightly to $10.2 billion in November.

Housing Starts

Housing starts increased 6.2 percent from November to December, to an annual rate of 1.54 million units.

MAJOR RELEASES NEXT WEEK

Durable Goods (Thursday)
GDP (Friday)

U.S. ECONOMIC STATISTICS

	1970–1992	1992	1993:1	1993:2	1993:3
Percent growth (annual rate)					
Real GDP	2.5	3.9	0.8	1.9	2.9
GDP deflator	5.8	2.8	3.6	2.3	1.6
Productivity					
Nonfarm business	1.1	3.6	−1.8	−0.4	4.3
Manufacturing (begins 1977)	2.0	4.9	5.1	5.9	3.1
Real compensation per hour	0.6	2.1	−0.9	−1.0	2.5
Shares of Real GDP (percent)					
Business fixed investment	10.9	10.6	11.1	11.5	11.6
Residential investment	4.8	4.0	4.2	4.0	4.1
Exports	7.9	11.6	11.6	11.6	11.5
Imports	9.0	12.3	12.8	13.1	13.2
Shares of Nominal GDP (percent)					
Personal saving	4.9	4.0	2.8	3.3	2.8
Federal surplus	−2.8	−4.6	−4.2	−3.5	−3.3

	1970–1992	1992	Oct. 1993	Nov. 1993	Dec. 1993
Unemployment Rate	6.7	7.4	6.7	6.5	6.4
Payroll employment (thousands)					
increase per month			162	202	183
increase since Jan. 1993			1,429	1,631	1,814
Inflation (percent per period)					
CPI	6.0	2.9	0.4	0.2	0.2
PPI-Finished goods	5.3	1.6	−0.2	0.0	−0.1

No new data this week.

FINANCIAL STATISTICS

	1992	Oct. 1993	Nov. 1993	Dec. 1993	Jan. 20,* 1994
Dow-Jones Industrial Average	3284	3626	3675	3744	**3892**

Dow-Jones at a **record high.**

Interest Rates	1992	Oct. 1993	Nov. 1993	Dec. 1993	Jan. 20,* 1994
3-month T-bill	3.43	3.02	3.10	3.06	2.97
10-year T-bond	7.01	5.33	5.72	5.77	5.76
Mortgage rate, 30-year fixed	8.40	6.82	7.16	7.17	7.05
Prime rate	6.25	6.00	6.00	6.00	6.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level Jan. 19, 1994**	**Percent Change from Week ago**	**Year ago**
Deutschemark-Dollar	1.745	+0.7	+8.6
Yen-Dollar	111.1	−1.1	−11.4
Multilateral (Mar. 1973=100)	96.50	+0.2	+5.0

International Comparisons	**Real GDP growth (last 4 quarters)**	**Unemployment rate**	**CPI inflation (last 12 months)**
United States	+2.8 (Q3)	6.4 (Dec)	2.7 (Dec)
Canada	+3.0 (Q3)	11.0 (Nov)	1.8 (Nov)
Japan	+0.5 (Q3)	2.7 (Oct)	1.4 (Oct)
France	−0.7 (Q3)	11.5 (Oct)	2.2 (Oct)
Germany	−1.4 (Q3)	6.5 (Nov)	3.7 (Nov)
Italy	−0.6 (Q2)	10.6 (Jul)	4.1 (Nov)
United Kingdom	+2.1 (Q3)	10.1 (Nov)	1.4 (Nov)

*Owing to the closure of the Federal Reserve Board because of the weather, the interest rates are for January 19.