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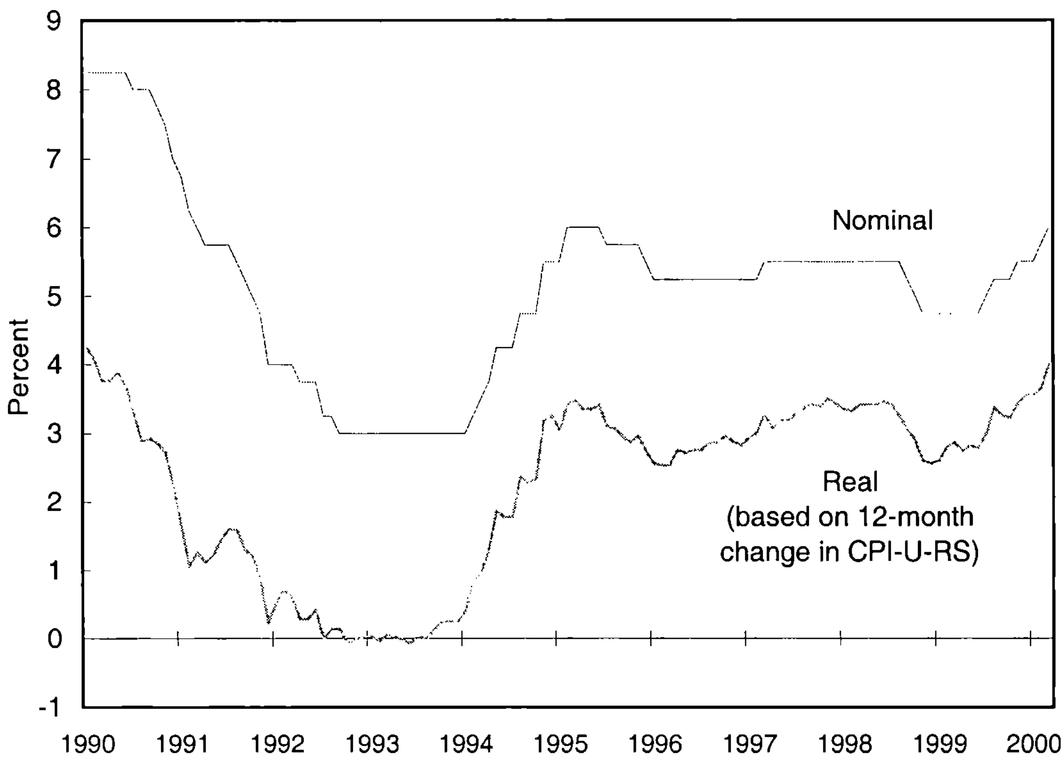
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

March 24, 2000

CHART OF THE WEEK

The Federal Reserve's Target Federal Funds Rate



This week the Federal Reserve raised its target for the federal funds rate for the fifth time since June. The current rate of 6 percent was last seen in June 1995. Trends in the real rate are sensitive to how inflationary expectations are measured, but according to one plausible measure, the real federal funds target is slightly higher now than it has been at any time since 1990.

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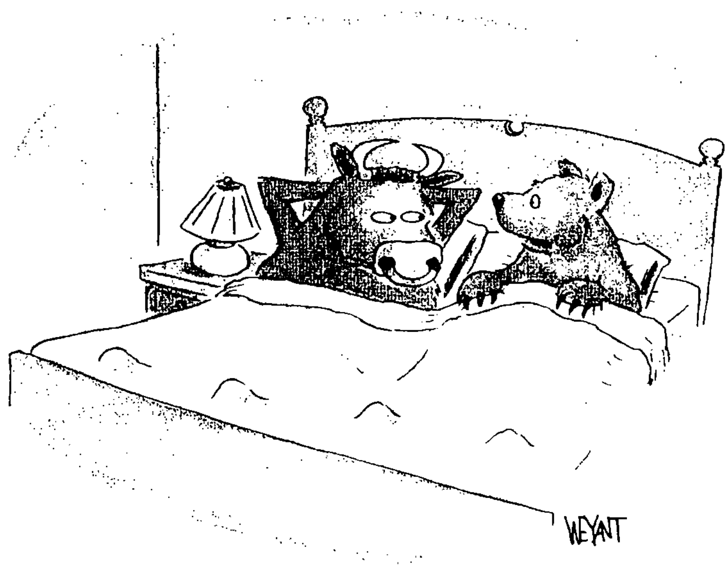


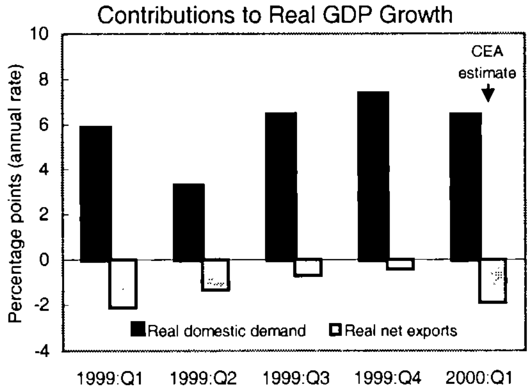
"Sure, it may be great for us, but it's hell on the markets."

MACROECONOMIC UPDATE

The Boom Goes On

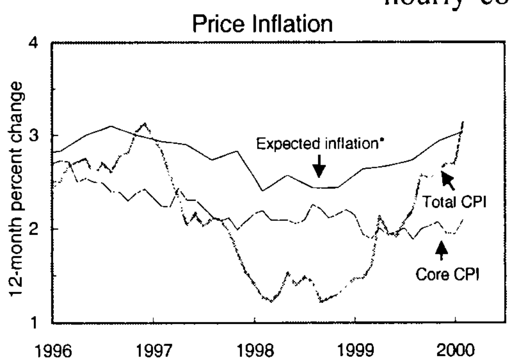
The economy continues to grow, with domestic demand remaining very strong. The consensus forecast for real GDP growth over the four quarters of 2000 has moved up to 3.4 percent, 0.7 percentage points above last November's consensus.

Domestic demand. Despite past concerns about a post-Y2K slump, real consumption appears to be growing at about a 6½ percent annual pace in the first quarter and is consistent with record levels of consumer confidence. Investment in computer-related equipment is also set for a solid gain after slowing in the fourth quarter. With domestic demand growing faster than domestic supply, imports are rising faster than exports so that net exports are reducing real GDP growth—at least based on January data (see upper chart).



Jobs. Job growth was anemic in February (possibly because of unusual weather), but initial claims for unemployment insurance for the 4-week period through mid-March have fallen to the lowest level of this expansion. Despite the tight labor market, nominal increases in the ECI measure of hourly compensation have been stable for the past 3 years.

Inflation. Over the past 3 years, the recipe for low and stable inflation has included stable growth in hourly compensation offset by strong productivity growth and falling nonoil import prices. Thus far, the recent inflation pickup has been confined to petroleum products. The longer-term worry is that the boost to CPI inflation from petroleum prices will elevate wage demands and upset the balance between wages and productivity. Surveys of inflation expectations have started to move upward—but only modestly so far (see lower chart).



* Quarterly average of median year-ahead expected inflation rate from the Michigan Survey of Consumers.

SPECIAL ANALYSIS

Where the Jobs Will Be in 2008

The latest Bureau of Labor Statistics projections of U.S. labor force, industrial, and occupational trends through 2008 show that the highest employment growth rates will be in job categories requiring higher levels of education. Nevertheless, most jobs will continue to require only a high school education.

Overall labor force growth. The labor force is projected to grow at 1.2 percent per year over the 1998-2008 period. Total growth in jobs is projected to be about 20 million. This labor force growth rate is roughly the same as that achieved over the 1988-98 period, but the demographic composition of the workforce will change.

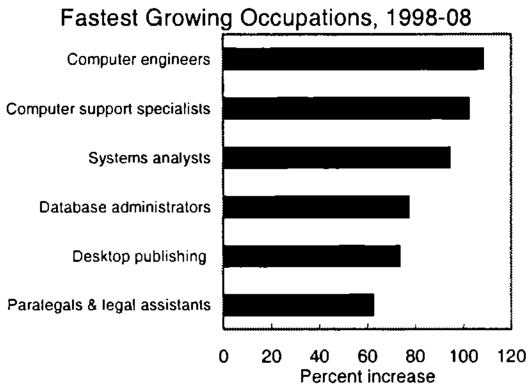
- More women. Women's labor force participation rates will continue to rise while those for men remain steady in most age groups, boosting the share of women in the labor force from 46 percent in 1998 to an estimated 48 percent by 2008. Women will account for an estimated 58 percent of the growth in the labor force during the period.

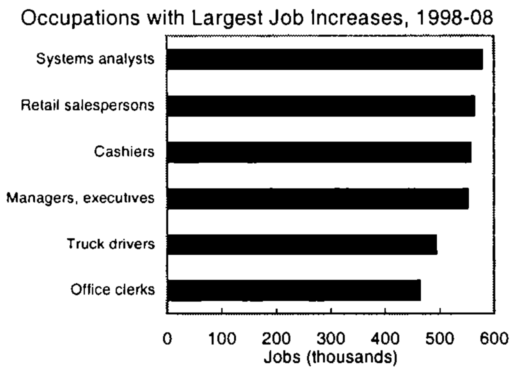
- More foreign born. Immigration will continue to play a major role in the growth of the labor force. The Hispanic labor force will expand nearly four times faster than the rest of the labor force, so that Hispanics will be 13 percent of the labor force by 2008, compared with 10 percent in 1998. Hispanics will account for an estimated 31 percent of the growth in the labor force during the period.

- An older workforce. The fastest growth in the labor force will be among those age 45 and older, reflecting the aging of the baby-boom cohort. This is expected to push the median age of the labor force to almost 41 years by 2008, a level not seen in several decades.

Growth by industry. As in the recent past, almost all of the increase in jobs will occur in the service-producing sectors. The computer and data processing services industry is expected to lead all others in the rate of employment growth, expanding by nearly 2 million jobs though 2008 (twice the gain of the 1988-98 period). The health services industries are also projected to experience substantial increases, adding nearly 3 million jobs. Rapid employment gains are also expected across a broad range of business and professional services. Employment in manufacturing, however, is expected to remain at current levels, as growth in output (especially in computers and other technology-intensive areas) is driven primarily by strong growth in productivity.

Growth by occupation. Of the top 30 occupations with the fastest projected employment growth rates from 1998-2008, two-thirds are computer or health-related occupations. The top five are all expected to be computer-related (see





upper chart). At the same time, however, other occupations, because of their large size, will experience large numbers of net new jobs even though they are expected to grow at average or below-average rates. Among the six occupations with the largest projected job increases, systems analysts will add the largest number over the period with a gain of nearly 600,000 (see lower chart). More broadly, the top 30 occupations with the largest job increases are concentrated in four industry sectors: retail trade (including salespersons, cashiers, and food service workers), business services, health services, and public and private education.

Education requirements. Many of the fastest growing occupations and those with the largest projected increases require post-secondary education. In fact, occupations requiring at least an associate degree, which accounted for one-fourth of all jobs in 1998, are projected to account for about 40 percent of total job growth from 1998 to 2008. However, the economy will continue generating jobs for workers of all levels of education and training: 57 percent of new jobs are projected to require no post-secondary education or training other than short-term on-the-job training, even though many of these occupations are projected to have below-average job growth rates.

Implications. These BLS projections suggest that less-skilled workers will continue to have employment opportunities even as the proportion of jobs requiring more skills increases. Nevertheless, the substantial rewards to acquiring better skills and education are likely to continue.

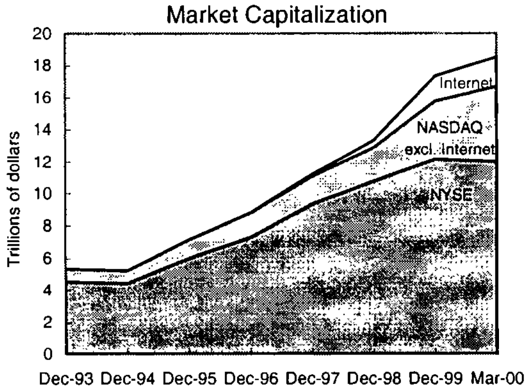
ARTICLE

The Changing Stock Market and the Economy

Over the past 2 years, increases in stock market wealth have come disproportionately from technology and Internet stocks. It remains an open question, however, whether this has made the market more or less vulnerable to shocks or corrections and how the market will respond if interest rates keep rising.

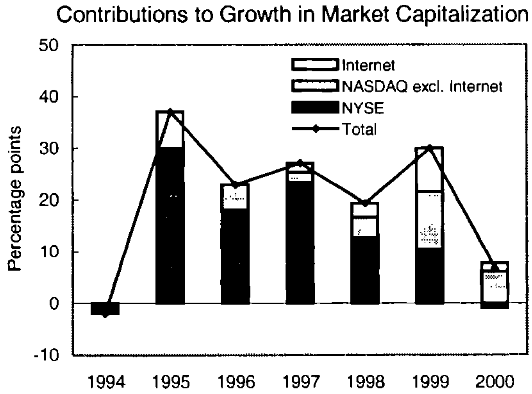
Market capitalization. Stocks listed on either the New York Stock Exchange (NYSE) or the NASDAQ account for almost all of the market capitalization of U.S.-listed stocks. At the end of 1994, NYSE stocks had a market capitalization of about $4.4 trillion, with NASDAQ stocks adding another $0.8 trillion (see upper chart). In 1995-97, the market capitalization of each approximately doubled. Since 1998, however, the market capitalization of NASDAQ stocks generally and Internet stocks in particular have grown much faster than that of NYSE stocks. (Internet stocks are treated in the chart as a subset of NASDAQ stocks, because AOL is the only significant non-NASDAQ Internet stock). With a market capitalization of about $1.9 trillion (up from less than $0.2 trillion in December 1997), Internet stocks now represent about 10 percent of the combined NASDAQ and NYSE market capitalization of roughly $19 trillion. The share of NYSE stocks has fallen from 85 percent in December 1994 to 65 percent today.

Market Capitalization



Patterns of growth. With their larger initial market capitalization and roughly balanced growth across the two exchanges, NYSE stocks accounted for the bulk of the increase in stock market wealth in 1995-97 (see lower chart). By 1999, however, the bulk of the increase came from NASDAQ stocks. Looking at technology stocks more generally, almost half of the growth in the market capitalization of the Standard and Poor's 500 stocks (from about $4.6 trillion in 1995 to $11.5 trillion today) came from technology stocks, which now account for roughly a third of the S&P 500's market capitalization.

Contributions to Growth in Market Capitalization



Is there froth? Although the stock market is at very high levels based on historical values of measures such as price-earnings ratios, no one can be certain that it is fundamentally overvalued. But suppose Internet stocks were to lose half their value. This would reduce stock market wealth by about $1 trillion. Based on the "wealth effect" rule of thumb that each dollar change in stock market wealth translates into a permanent change in consumption of about 3½ cents, this would cut consumption by about $35 billion, and knock perhaps a third to a half percentage point off GDP once investment and other effects were taken into account. Any assessment of how the overall market would react to such a sharp decline in Internet stocks is highly speculative. At times this year, investors have acted as though they regard technology and blue chip stocks as substitutes—when the NASDAQ falls the Dow goes up and vice versa. This would imply that a correction focusing on Internet stocks would not have a negative effect on the rest of the market and might even be offset by rallies elsewhere. But at other times, stocks have tended to move together suggesting that a decline could spread.

Interest rates and stock prices. Economic theory suggests that the value of a stock varies directly with the company's earnings prospects but inversely with interest rates (because the present value of future profits goes down when interest rates rise). This would suggest that higher interest rates would cause the prices of Internet stocks to go down since most of their expected profits are in the future. Nevertheless, fluctuations in the price of Internet stocks (and technology stocks generally) may be more sensitive to changing expectations about future profits than about changes in interest rates in the short run. Higher interest rates (particularly in the context of tighter monetary policy and slower growth) might, however, have a depressing effect on "old economy" stocks to the extent that real near-term profits are expected to go down.

What is the Fed up to? These considerations suggest that tightening monetary policy might affect spending through a stock market effect. However, any concern that the Federal Reserve is conducting monetary policy with an eye to cooling off the stock market appears to be misplaced. Rather, the Fed seems to be conducting monetary policy the old-fashioned way. Recent tightening seems motivated by a general concern that demand is growing faster than potential supply, threatening a buildup of inflationary pressures. Higher interest rates might or might not affect stock prices, but they would likely have the usual effects of slowing housing and other interest-sensitive spending. As these sectors slowed, the impact would then spread more widely.

Conclusion. Increases in stock market wealth, which recently have come disproportionately from technology and Internet stocks, are one factor that has fostered the ongoing strong growth in spending that the Fed is now trying to slow. But the Fed does not appear to be targeting the stock market per se, and it certainly is not trying to discourage the acceleration in productivity and future growth in potential supply that is probably an important factor contributing to the rise in stock prices.

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

"Living Wage" Has Mixed Effects. A growing number of cities have recently implemented "living wage" ordinances mandating that companies with city contracts or receiving city assistance pay their workers a wage sufficiently high to support a family. These wages are typically much higher than Federal and state minimum wages, including the proposed higher Federal minimum wage. A recent study found that living wage ordinances do indeed boost the wages of low-wage workers. However, they also appear to raise the costs to employers of hiring such workers enough that employment rates of low-wage workers and the number of hours worked fall. These countervailing forces suggest there are winners and losers following a large legislated increase in wages. Those who remain employed earn a higher wage, but others are no longer employed or work fewer hours as a result. On balance, the study finds modest reductions in poverty rates associated with living wage ordinances. Thus, these findings suggest that living wage ordinances may help to achieve the goal of reducing urban poverty in the aggregate, but at the cost of lost employment and hours of work for some low-wage workers.

Railroad Mergers Stuck in the Station. Unlike most mergers, which are reviewed by the Federal Trade Commission or the Department of Justice (DOJ), railroad mergers fall under the jurisdiction of the Surface Transportation Board (STB), an independent agency in the Department of Transportation. Historically, critics have accused the STB of being too lax, for instance in approving mergers over the objections of the DOJ. Last week, however, the STB suspended all merger activity in the railroad industry for 15 months while it develops new guidelines. The move was prompted by advance notice of the proposed merger between the Burlington Northern and Santa Fe Railway Company (BNSF) and the Canadian National Railway Company (CN). The Board noted that the last round of railway mergers was accompanied by a number of serious service problems and that railroad stocks have been falling since. It also expressed concern that the merger between BNSF and CN will prompt another round of mergers that could leave the industry with only two major railroads serving North America.

How Wide is the Earnings Gap between Black and White Men? Following a substantial narrowing between the 1940s and the 1980s, the earnings gap between African American and white male workers remained stuck at 31 to 33 percent between 1982 and 1996, according to a recent study. In fact, the gap between comparable workers might be even wider. The study notes that African American men are more likely than whites not to be working or to be incarcerated. To the extent that those who are incarcerated or not in the labor force are relatively low wage workers, their absence from the labor force raises the average earnings of those who are working. The study estimates that if employment-to-population rates were the same for African American and white male workers, the earnings gap between them would be nearly 40 percent. It is worth noting that the study ends with 1996 data, and thus misses any improvement in the past few years when labor markets have been especially strong.

INTERNATIONAL ROUNDUP

High Oil Prices and Developing Countries. Oil consumption in developing countries has risen 5 percent per year over the last three decades, compared with 1 percent per year in OECD countries. Developing economies also rely more on energy-intensive manufacturing sectors to spur economic growth than do OECD economies, and they use on average more than twice as much oil to produce each unit of economic output. Thus, high oil prices may impose a particular burden on some developing countries. Indeed, the International Energy Agency (IEA) reports that the oil import bills of several developing countries, including India, the Philippines, and Thailand, have risen by more than 160 percent with the increase in oil prices of some 80 percent since April 1999. Higher oil import bills reduce trade surpluses, increase inflationary pressure, and may lessen the benefits of international development assistance. In the case of Thailand, the Philippines, and China, the extra oil bills are twice or more as large as foreign aid received. Higher oil prices may also weaken government budgets in countries that subsidize oil prices for domestic users. The IEA reports, for example, that the Indian Oil Pool Account, which manages the balance between domestic and international oil prices, has been drained by the high cost of oil imports.

FDI on the Rise in Mexico. Foreign direct investment into Mexico is expected to reach $12.4 billion in 2000, a 24 percent increase over last year, according to a survey of over 350 major foreign companies released by the Mexican Investment Board this week. About 200 new foreign plants will be built this year—a 36 percent increase. The industries with the largest projected investments are telecommunications (26 percent), automotive (18 percent), electronics (10 percent), and energy (10 percent). The release of this survey follows a recent upgrading of Mexico's foreign debt by Moody's Investor Service to investment grade. These positive developments in investor confidence are being hailed as a reflection of Mexico's global free trade alliances such as the free trade agreement with the European Union that Mexico will formally sign this week.

Addressing Inadequate Nutrition. Nearly a quarter of all newborns (30 million babies) in developing countries are low birthweight, and more than 150 million preschool children worldwide are underweight, according to a new report by the United Nations. As the report highlights, however, several countries have had considerable success in reducing the incidence of malnutrition. In Thailand, for example, the prevalence of underweight preschool children fell from over 50 percent in 1982 to 10 percent in 1996, and maternal death rates fell by over 90 percent. This was achieved through an approach that included weighing all pre-school children every 3 months; a program of nutrition education that encouraged breastfeeding and the timely introduction of foods and proper hygiene; the establishment of 5,000 school lunch programs; and the training of volunteers who monitored mothers and children in their communities. The UN report also suggests dietary changes, including increased vegetable and fruit consumption to prevent childhood blindness and other poor health outcomes and a major increase in fish and lean meat consumption in some communities, particularly South Asia.

RELEASES THIS WEEK

Advance Durable Orders

****Embargoed until 8:30 a.m., Friday, March 24, 2000****

Advance estimates show that new orders for durable goods decreased 2.3 percent in February, following a decrease of 2.2 percent in January.

U.S. International Trade in Goods and Services

The goods and services trade deficit increased to $28.0 billion in January from $24.6 billion in December.

MAJOR RELEASES NEXT WEEK

Consumer Confidence—The Conference Board (Tuesday)
Gross Domestic Product (Thursday)

U.S. ECONOMIC STATISTICS

	1970-1993	1999	1999:2	1999:3	1999:4
Percent growth (annual rate)					
Real GDP (chain-type)	3.0	4.5	1.9	5.7	6.9
GDP chain-type price index	5.2	1.6	1.3	1.1	2.0
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.6	0.6	5.0	6.4
Real compensation per hour:					
Using CPI	1.0	1.7	1.4	2.1	0.8
Using NFB deflator	1.5	3.0	2.9	4.0	2.1
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.6	12.7	12.5
Residential investment	4.5	4.4	4.5	4.4	4.4
Exports	8.2	10.8	10.7	10.8	10.9
Imports	9.2	13.5	13.4	13.8	14.0
Personal saving	6.6	1.7	1.8	1.5	1.3
Federal surplus	-2.8	N.A.	1.3	1.4	N.A.

	1970-1993	1999	December 1999	January 2000	February 2000
Unemployment Rate (percent)	6.7**	4.2**	4.1	4.0	4.1
Payroll employment (thousands)					
increase per month			309	384	43
increase since Jan. 1993					20823
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.2	0.5
PPI-Finished goods	5.0	3.0	0.1	0.0	1.0

**Figures beginning 1994 are not comparable with earlier data.

FINANCIAL STATISTICS

	1998	1999	January 2000	February 2000	March 23, 2000
Dow-Jones Industrial Average	8626	10465	11281	10542	11120
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.32	5.55	5.73
10-year T-bond	5.26	5.65	6.66	6.52	6.08
Mortgage rate, 30-year fixed	6.94	7.43	8.21	8.33	8.23
Prime rate	8.35	8.00	8.50	8.73	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level March 23, 2000**	**Percent Change from**	
		Week ago	**Year ago**
Euro (in U.S. dollars)	0.969	-0.2	-11.2
Yen (per U.S. dollar)	107.5	1.7	-9.0
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	95.95	0.4	1.6

International Comparisons [1]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	4.5 (Q4)	4.1 (Feb)	3.2 (Feb)
Canada	4.7 (Q4)	6.8 (Jan)	2.3 (Jan)
Japan	0.0 (Q4)	4.7 (Dec)	-0.9 (Jan)
France	3.2 (Q4)	10.4 (Dec)	1.6 (Jan)
Germany	2.3 (Q4)	8.7 (Jan)	1.7 (Jan)
Italy	2.1 (Q4)	11.1 (Oct) [2]	2.2 (Jan)
United Kingdom	2.9 (Q4)	5.9 (Nov)	1.9 (Jan)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.
2/ Data from OECD standardized unemployment rates.

EYES ONLY

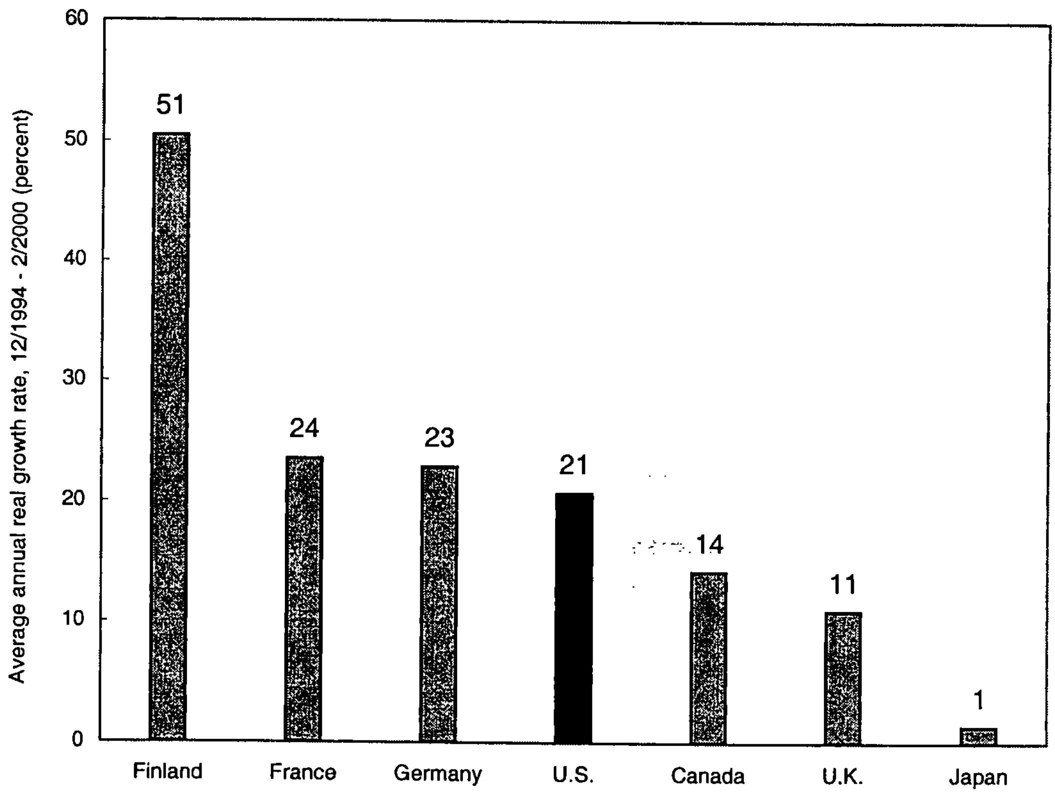
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

March 31, 2000

CHART OF THE WEEK

U.S. Not Alone in Stock Market Boom



Stock markets have boomed in many developed countries over the last 5 years. In fact, real stock gains in Finland, France, and Germany exceeded those in the United States over that time. Finland's amazing stock market boom is primarily driven by the impressive performance of one technology firm, Nokia. In contrast, Japan's weak economy has contributed to a stagnant market.

EYES ONLY

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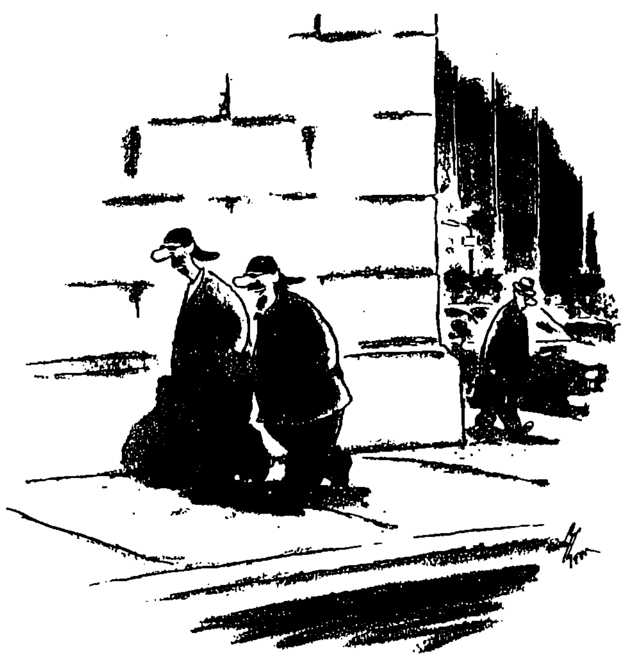


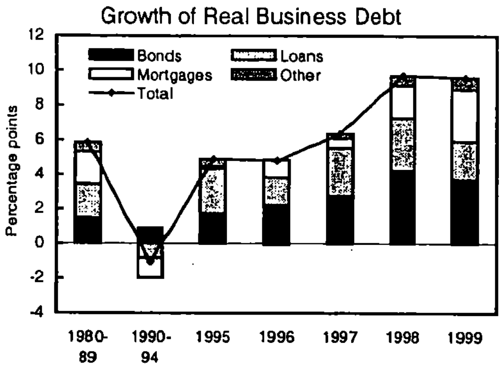
"Have you ever wanted something so bad that you'd actually save up the money to buy it?"

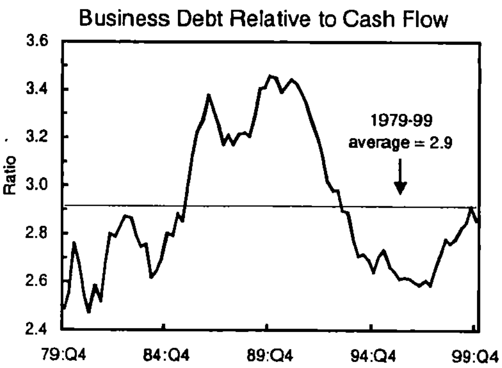
EYES ONLY

CURRENT DEVELOPMENT

The Financial Condition of Businesses

Business borrowing was robust in 1999 for the second straight year. But strong cash flow has kept the debt burden manageable. Other indicators suggest businesses generally enjoy good financial health.





Business debt is on the rise ... Real debt in the non-financial business sector climbed 9.6 percent in 1999, nearly the same rate as in 1998 (see upper chart). Commercial mortgage borrowing was especially strong last year, accounting for about a third of the total increase in business debt. Corporate bond issuance continued to soar, with bond financing accounting for about 40 percent of debt growth. Banks, however, tightened terms on business loans in 1999, according to Federal Reserve surveys, and bank loans accounted for a relatively low 23 percent of debt growth.

... but, the debt burden remains under control. Real cash flow increased 6.5 percent in 1999, marking the third consecutive year that cash flow growth lagged behind borrowing. As a result, the debt-to-cash flow ratio is up about 10 percent from its low mid-1990s level, and is now close to its long-run average (see lower chart). Low interest rates, however, have helped to keep the debt service burden from escalating. The ratio of interest payments to cash flow over the last few years has remained low and stable. Both ratios are well below their peaks reached in the 1980s.

Other indicators of business sector health. Delinquency rates and business failures remained at very low levels, although both picked up somewhat in 1999. However, the default rate on high-yield "junk" bonds reached levels not seen since the 1990-91 recession and more non-financial debt was downgraded than was upgraded in 1999, indicating some financing difficulties for some firms.

Businesses mirror households. Robust cash flow gains and low interest rates have allowed business debt to surge without a dangerous rise in debt burden. This pattern mirrors that of household finances reported in an earlier *Weekly Economic Briefing*. An economic downturn, coupled with higher interest rates, could push up the debt burden appreciably, but most likely not to the levels of the 1980s.

EYES ONLY

SPECIAL ANALYSIS

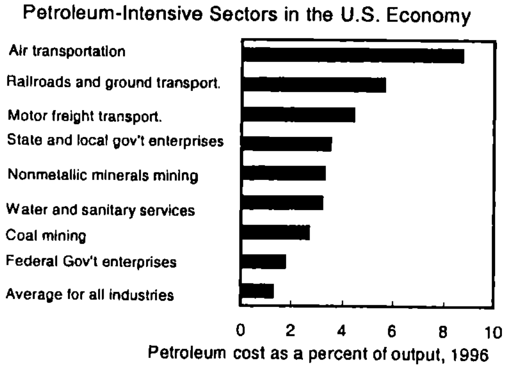
Who Feels the Pain of Higher Oil Prices?

With significant improvements in energy efficiency and structural change, the economy is much less dependent on oil today than it was a quarter century ago. Since 1974, U.S. petroleum consumption has increased 17 percent while the economy has grown nearly 120 percent. Nonetheless, the rise in oil prices over the past year has increased the costs to users of petroleum products.

Impacts of gasoline prices on the typical household. The national average price for gasoline appears to have plateaued this month just above $1.50 per gallon. The average gasoline price this year will likely be about 30 cents per gallon higher than last year ($1.14 per gallon in 1999). The typical household will pay over $300 more to fill up its vehicles in 2000 than in 1999, representing more than a 25 percent increase. Nevertheless, gasoline cost as a share of a household's income has fallen significantly over the past 20 years. In 1980, the typical household spent 5 percent of its income to fuel its vehicles, while in 2000, fueling costs will require about 1.6 percent of the typical household's income.

Impacts of gasoline prices on motor vehicle purchases. In 1999, more than 16.8 million cars and light trucks (including SUVs) were sold in the United States. So far this year, the pace of new vehicle purchases is even higher; light weight vehicle sales in February exceeded an annual rate of 19 million units. In recent years, the average fuel economy of all new motor vehicles purchased has fallen as consumers have shifted away from more fuel-efficient automobiles to less fuel-efficient light trucks. The costs to fuel vehicles vary significantly. For example, assuming an average of 11,300 miles traveled per year, it will cost the typical driver this year more than $1800 to fuel a Ferrari 550, about $1000 for a Jeep Grand Cherokee, about $850 for a Dodge Caravan, more than $600 for a Toyota Camry, and less than $400 for a Volkswagen New Beetle. Still, the recent high gasoline prices do not appear to have influenced America's love affair with SUVs despite their high fuel costs.

Petroleum-Intensive Sectors in the U.S. Economy



Impacts of oil prices on airlines. The air transportation industry spends 7 times as much for petroleum products per unit of economic output than the average industry (see chart). However, between 1987 and 1996, the air transportation sector reduced the petroleum intensity of its output by 22 percent. This reflects in part the significant improvement in fuel economy of airplanes manufactured by Boeing. High oil prices would not appear to provide a competitive advantage to either Boeing or Airbus, the two largest airplane manufacturers in the world, because of the similar fuel economies of their comparable models. While fuel costs are an important component of operating costs for airlines, they do not always serve as a good predictor of changes in airfares.

Impacts of diesel prices on motor freight. Expenditures on petroleum products represent less than 4½ percent of economic output for the motor freight transportation and warehousing industry. However, fuel costs of small carriers may make up more than three times as much of their operating costs as large carriers. With the average price for diesel estimated to be nearly 30 cents per gallon higher this year than last, tractor-trailer operators will likely have to pay over $3,000 more to fuel their trucks this year compared to last year.

Impacts of oil prices on state and local governments. Petroleum products represent nearly 7 percent of all input costs for state and local governments. Higher oil prices can increase the costs of operating various government vehicle fleets, such as police cars, fire trucks, and school buses. For example, with the increase in diesel prices, the costs of operating a school bus will increase on average by more than $250 this year over last year.

Conclusion. While the recent increase in oil prices appears to have less effect on the economy than previous hikes in oil prices, those who rely on petroleum products have experienced a significant increase in costs. Improvements in energy efficiency and higher incomes have helped many consumers adapt to higher fuel prices.

EYES ONLY

<u>ARTICLE</u>

The Experience of Foreign Investors in China

China's WTO accession will give foreign firms the right to distribute products in China directly. A recent study draws on extensive interviews with managers and professionals in foreign (disproportionately American) firms in China and sheds light on the potential benefits of these rights. Foreign investors find the murky legal environment a challenge; nevertheless, the study highlights the steady trend towards increased transparency and reliance on the rule of law. WTO accession will further this trend.

The murky legal environment. The study notes that China had no legal system in the Western sense in 1977. Shortly after its founding, the People's Republic of China had declared all previous laws invalid—but never replaced them with a new code of law. Instead, China relied on often secret decrees, bureaucratic regulations, and personal orders of various officials. In the late 1970s, China began promulgating new laws and codes. Although numerous gaps still remain, China has by now published and circulated the major laws affecting foreign enterprises.

Even with this progress, the legal system is clearly in transition. Existing laws are often ambiguous, so that the distinction between what is permissible and what is not often depends less on clearly stated codes, and more on personal relationships with influential officials. Businesses find these legal ambiguities to be a source of risk, since official interpretations might change. On the other hand, they see a need to move aggressively to avoid being boxed out by competitors.

Legal hurdles to selling in China. Many of the firms in the study invested in China to gain access to the Chinese market. However, they continue to face significant obstacles in selling their products there. Foreign firms face severe legal limitations on their ability to provide distribution and other services (such as after-sales maintenance). Because these services are so crucial to selling their products in China, foreign firms have become more deeply involved in distribution than the law might suggest is possible. For example, they work hard to exploit subtle loopholes in ambiguous laws; they may also let a Chinese firm technically provide the needed services—with the foreign firm in fact providing all the actual management and marketing.

Conclusions. WTO accession will alleviate the need for creative efforts to circumvent restrictions on distribution and services, and reduces uncertainty about whether current legal interpretations will change. Clear rules benefit Chinese firms as well as foreigners. Nevertheless, complete reliance on a rule of law will take time, since the necessary institutions, skills, and culture are not yet developed. As the study notes, China is in a transition that will take decades to complete."

EYES ONLY

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Job Corps Does Good. Participation in the Job Corps raises initial education and earnings outcomes and reduces arrests and incarcerations, especially for those aged 16 and 17, according to a recent study. A sample of youths eligible for Job Corps were randomly assigned to either a program group or a control group in the mid-1990s and then followed for 30 months. Job Corps led to more education and training, higher GED attainment, and large increases in vocational certification relative to the control group, even though many control group members participated in other education and training activities. Arrests, convictions, and incarcerations were about 20 percent lower and average earnings were significantly higher for Job Corps participants. Self-reported alcohol and illegal drug use and family formation were unaffected by program participation. A full cost-benefit analysis of this more-than-$1-billion-per-year program awaits completion of a 48-month follow-up study.

Asian Crisis Hit States' Manufacturing Exports. A recent study finds that most states' exports to East Asia declined during the East Asian crisis, but the severity of the decline varied across states. East Asian markets accounted for 30 percent of U.S. merchandise exports prior to the crisis. Six states had manufacturing exports to East Asia of more than $1,000 per capita prior to the crisis, and 19 states exported more than $500 per capita. In general, western states—especially Alaska, Arizona, and California—were more dependent on East Asian markets, and were hit hardest by the trade shock. Overall, forty states experienced declines in exports to East Asia from 1997 to 1998, with seven states and the District of Columbia seeing exports to East Asia fall by more than 30 percent.

Another Look at Adolescent Fertility. As reported in a previous *Weekly Economic Briefing*, the birth, pregnancy, and abortion rates for teens aged 15-19 have declined in recent years. A study released by the National Center for Health Statistics examines these and related trends in greater depth. One of the interesting findings is related to changes in the rates of teens having their second child. The teen birth rate for a first child declined 10 percent between 1991 and 1997 (with most of the decline occurring in the final 2 years). The rate of second births to teenagers has fallen even more sharply, 21 percent since 1991. This decline was especially evident for African-American teenagers, for whom the second birth rate dropped 28 percent. The study also finds that among the factors accounting for the overall falling teenage pregnancy rates are decreased sexual activity, increased condom use, and the adoption of injectable and implant contraceptives. The switch from the pill to Depo-Provera and Norplant among African-American teenage mothers may be an important factor in the recent sharp decline in their second birth rates during the 1990s.

INTERNATIONAL ROUNDUP

EU Sets Strategic Economic Goals. European Union leaders agreed to a broad set of economic and social initiatives that are intended to strengthen employment, promote innovation, and prepare for the transition to a knowledge-based economy. One goal is to raise the employment rate from 61 percent today (compared to 74 percent in the United States) to 70 percent by 2010, while increasing the employment rate of women from 51 percent (67 percent in the United States) to 60 percent. Proposed policies include a Europe-wide database on jobs and learning opportunities, promotion of training for the service sector, and improved childcare provision. The Council advocated the completion of a single EU market, by eliminating barriers to trade in services and liberalizing public utilities. In the area of information technology, the Council called for adopting pending legislation on the legal framework for electronic commerce and introducing greater competition in local access networks before the end of 2000 to substantially reduce the costs of Internet access. The latter proposal would be similar in many respects to the U.S. Telecommunications Act of 1996. The Council also urged the Member States to ensure that all schools have access to the Internet by the end of 2001.

Combating TB. Last week, 20 countries heavily burdened by Tuberculosis (TB) participated in a Ministerial Conference on TB and Sustainable Development, hosted by the World Bank and the World Health Organization. Around 8 million people annually become sick with TB, and about 2 million die each year from the disease, 98 percent of which are in developing countries. Moreover, inadequate supplies of drugs, ineffective treatment, and poor management increase the risk of an outbreak of drug-resistant TB, which is extremely costly to treat. A proven cost-effective strategy of fighting TB called DOTS (Directly Observed Treatment, Short-course), which stresses close observation of dosages, has been available for many years. The DOTS program costs between $10 to $20 per patient, and has a cure rate of about 80 percent (compared with 45 percent for non-DOTS areas). As of 1998, 119 countries have adopted DOTS, and 43 percent of the global population had access to this program; still, only 21 percent of estimated global TB cases received DOTS. The Conference set a goal of providing DOTS to 70 percent of TB cases by 2005.

Japan to Cut Retirement Benefits. Japan's parliament voted this week to reduce retirees' pensions and raise the retirement age to stabilize the long-term funding of the public pension system. This reform will cut public pension benefits for new retirees by 5 percent on April 1 and will gradually raise the age at which retirees start to receive benefits from 60 to 65 by 2025. Japan's public pension account is expected to run a deficit this year. An aging society and low birth rate will only exacerbate this problem. While there were 4.2 working age people for every person age 65 or over in 1998, this ratio is expected to drop to 2.2 in 2025 and to 1.7 in 2050. Some economists have argued that the new reforms do far too little, as the current pay-as-you-go pension system is unsustainable and needs a drastic overhaul.

EYES ONLY

RELEASES THIS WEEK

Gross Domestic Product

According to revised estimates, real gross domestic product grew at an annual rate of 7.3 percent in the fourth quarter of 1999.

Consumer Confidence

Consumer confidence, as measured by The Conference Board, declined 4.1 index points in March, to 136.7 (1985=100).

MAJOR RELEASES NEXT WEEK

NAPM Report on Business (Monday)
Leading Indicators (Tuesday)
Employment (Friday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	1999	1999:2	1999:3	1999:4
Percent growth (annual rate)					
Real GDP (chain-type)	N.A.	**4.6**	1.9	5.7	**7.3**
GDP chain-type price index	N.A.	1.6	1.3	1.1	2.0
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.6	0.6	5.0	6.4
Real compensation per hour:					
Using CPI	1.0	1.7	1.4	2.1	0.8
Using NFB deflator	1.5	3.0	2.9	4.0	2.1
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.6	12.7	12.5
Residential investment	4.5	4.4	4.5	4.4	4.4
Exports	8.2	10.8	10.7	10.8	10.9
Imports	9.2	13.5	13.4	13.8	14.0
Personal saving	6.6	1.7	1.8	1.5	1.3
Federal surplus	-2.8	**1.2**	1.3	1.4	**1.2**

	1970-1993	1999	December 1999	January 2000	February 2000
Unemployment Rate (percent)	6.7**	4.2**	4.1	4.0	4.1
Payroll employment (thousands)					
increase per month			309	384	43
increase since Jan. 1993					20823
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.2	0.5
PPI-Finished goods	5.0	3.0	0.1	0.0	1.0

**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.

EYES ONLY

FINANCIAL STATISTICS

	1998	1999	January 2000	February 2000	March 30, 2000
Dow-Jones Industrial Average	8626	10465	11281	10542	10980
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.32	5.55	5.71
10-year T-bond	5.26	5.65	6.66	6.52	6.06
Mortgage rate, 30-year fixed	6.94	7.43	8.21	8.33	8.23
Prime rate	8.35	8.00	8.50	8.73	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level March 30, 2000**	**Percent Change from Week ago**	**Percent Change from Year ago**
Euro (in U.S. dollars)	0.959	-1.0	-10.6
Yen (per U.S. dollar)	105.5	-1.8	-12.1
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	95.44	-0.5	-0.3

International Comparisons [1]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	4.6 (Q4)	4.1 (Feb)	3.2 (Feb)
Canada	4.7 (Q4)	6.8 (Jan)	2.7 (Feb)
Japan	0.0 (Q4)	4.7 (Dec)	-0.9 (Jan)
France	3.2 (Q4)	10.4 (Dec)	1.4 (Feb)
Germany	2.3 (Q4)	8.7 (Jan)	1.8 (Feb)
Italy	2.1 (Q4)	11.1 (Oct) [2]	2.4 (Feb)
United Kingdom	3.0 (Q4)	5.9 (Nov)	2.3 (Feb)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.
2/ Data from OECD standardized unemployment rates.

EYES ONLY

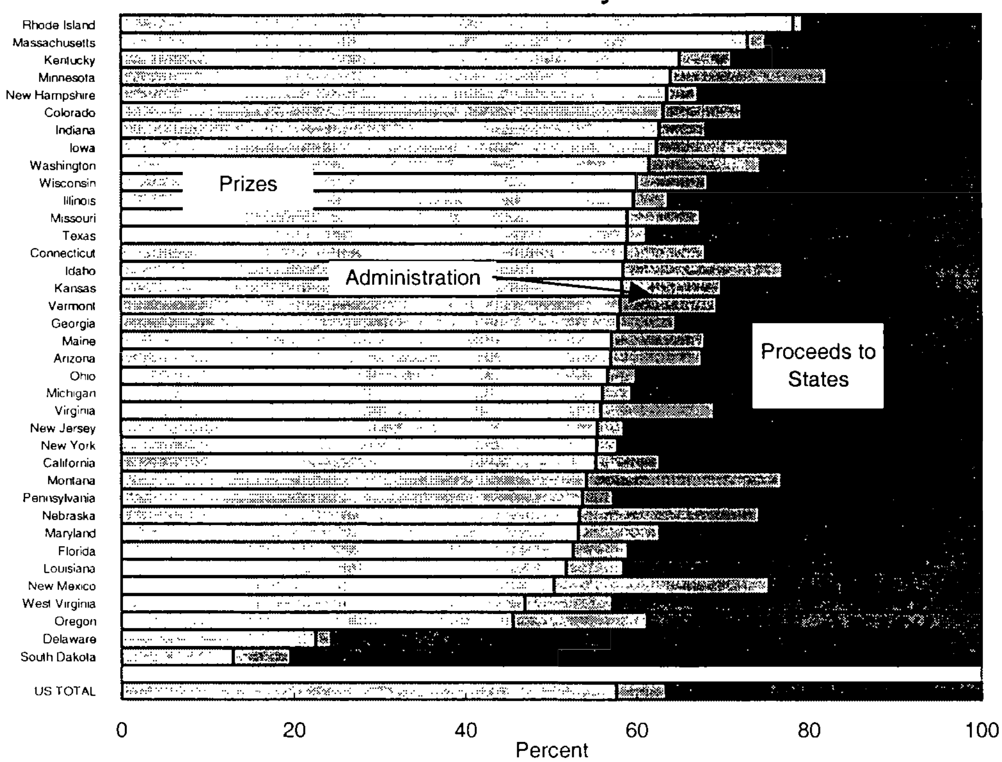
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

May 12, 2000

CHART OF THE WEEK

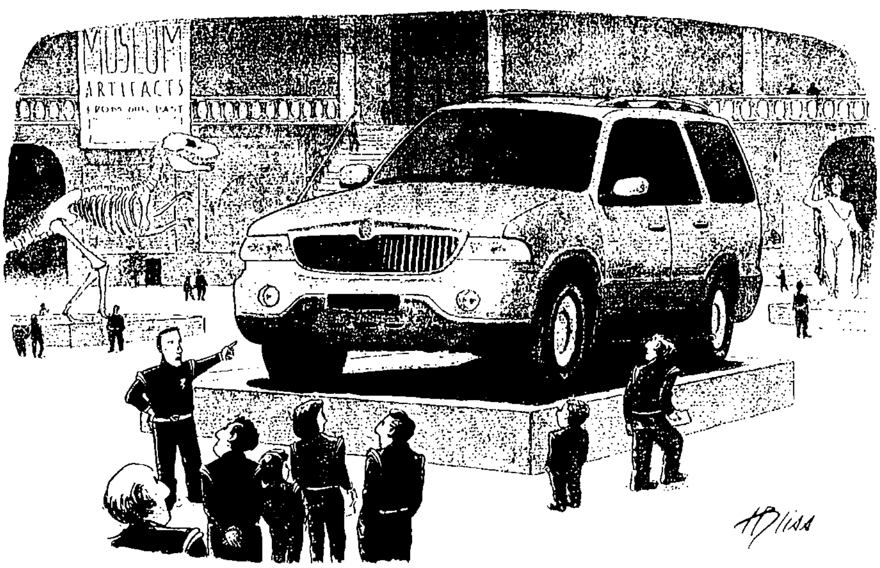
Allocation of State Lottery Collections



Thirty-seven U.S. states have lotteries. In 1998, aggregate ticket sales were $33.3 billion: 57.7 percent of this total was paid out in prizes, 5.8 percent went for administration, and 36.5 percent represented proceeds to the states. Rhode Island and Massachusetts paid out the largest percentage of ticket sales in prizes; South Dakota and Delaware paid out the least.

EYES ONLY

CONTENTS



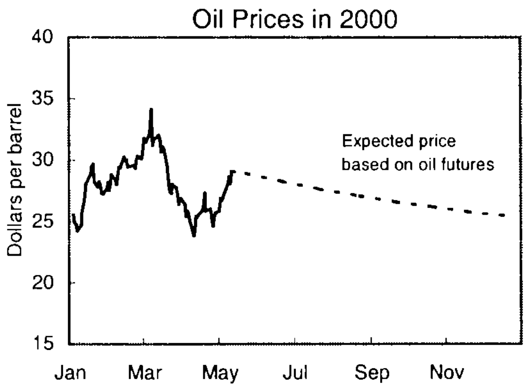
"We're not certain why they disappeared, but archeologists speculate that it may have had something to do with their size."

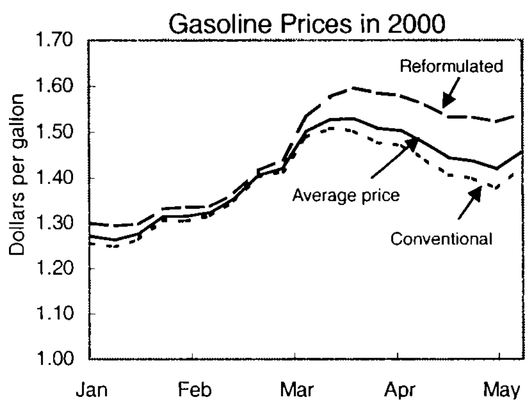
EYES ONLY

CURRENT DEVELOPMENT

Over the Hill on Oil and Gasoline Prices?

After falling nearly $10 per barrel from its early March peak, the price of crude oil has moved up some. Gasoline prices also rose last week after declining for 6 straight weeks. Nevertheless, further large increases are not expected this year.





Oil. West Texas Intermediate crude closed Thursday at $29.13 per barrel, 15 percent below its 2000 peak on March 7, but 22 percent above its 2000 trough on April 11 (see upper chart). The market expects prices to fall slightly over the next few months, but low stocks in the United States and other OECD countries, and increased demand from refiners after the spring maintenance season may support or pull prices up. Some OPEC ministers' comments suggest that the cartel may not increase production at its June meeting.

Gasoline. After falling 11 cents per gallon between March 20 and May 1, the average cost of gasoline rose 3½ cents last week to $1.46 per gallon (see lower chart). The Energy Information Agency's forecast projects gasoline prices to stay between $1.40 and $1.45 through the summer. Gasoline inventories remain lean, however, as we approach the zenith of the summer driving season—a combination that could support higher prices.

Regulatory impacts. Average gasoline prices mask the difference between conventional and reformulated gasoline (RFG). The latter, which has been required since 1995 in areas with severe smog problems, has averaged 2.5 cents more per gallon than conventional gasoline. More stringent RFG standards effective this year were expected to increase this spread to 4 cents per gallon. However, this gap had widened to as much as 14 cents before narrowing to 11 cents in the past week. Transient refinery problems could have caused the spread, but analysts also may have underestimated refining costs, especially since royalties might be required on an RFG patent that was recently upheld in court.

Conclusion. Oil and gasoline prices are expected to remain stable through the summer, but OPEC decisions, lean stocks, and strong demand in the upcoming driving season are risk factors for higher prices.

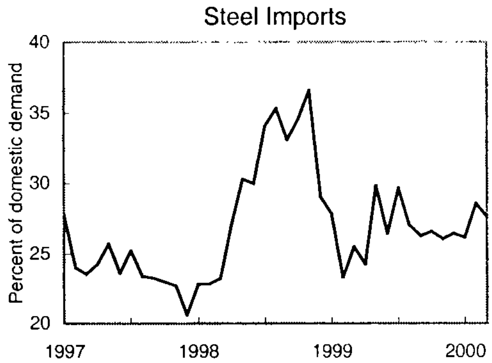
EYES ONLY

SPECIAL ANALYSIS

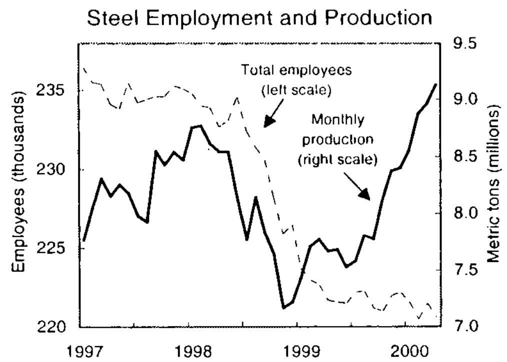
Is Steel Still in Trouble?

November 1998 marked a nadir for the U.S. steel industry; imports accounted for 37 percent of the domestic market while nearly a quarter of domestic production capacity lay idle. Fortunately, the industry has recovered substantially since then.

Fewer imports. Imports now meet just over a quarter of domestic steel demand, up slightly from the 1997 average of 24 percent (see upper chart). Imports in recent months have been led by semi-finished products, which are then processed further by domestic firms. In part, the scaling back of imports reflects the anti-dumping and countervailing measures imposed in 1999, and also the recovery of demand in other steel consuming countries. Declines in imports from Japan and Russia were particularly sizable.

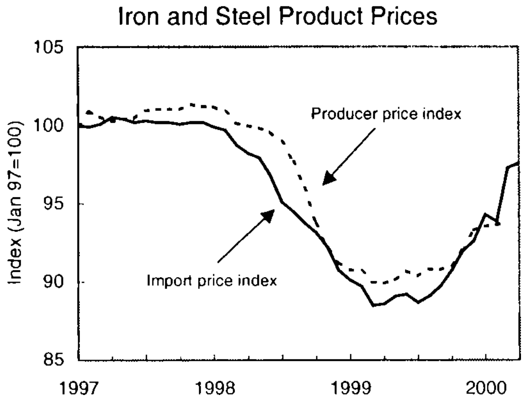


More domestic production. While production and employment dropped sharply in tandem during the 1998 crisis, the booming U.S. economy has facilitated a swift recovery in production since then (see lower chart). Domestic raw steel production in April approached a high annual rate of 110 million metric tons, with demand growth especially strong in the construction sector and in the oil and gas drilling and transportation sector. U.S. steel producers are now operating at over 90 percent of capacity, and the inventory buildup during the crisis has been reversed as new orders and shipments have picked back up.



Employment and productivity. The increase in production has not been accompanied by an increase in employment. The number of employees in the blast furnaces and basic steel products sector remains around 220,000, with increased productivity accounting for the increased output. This pattern is consistent with longer-term trends: steel industry employment has declined steadily since the 1980s to less than half its level then, while greater production efficiency has allowed output to grow.

Prices, profits, and prospects. Prices have also begun to climb back to earlier levels (see chart on next page). Available (but incomplete) earnings results confirm that a recovery is underway. They also show that mini-mills have



weathered the crisis far better than integrated mills. The OECD Steel Committee predicts that in 2000, imports to the United States should fall by 8 percent, as demand continues to recover in other steel consuming countries. Increased production, along with higher prices, should lead to improved performance in 2000 for the main steel enterprises after a difficult period in 1998-99.

Conclusion. The steel industry appears to have bounced back from its 1998 crisis. Nevertheless, longer-term trends of declining employment and the importance of mini-mills are likely to continue.

EYES ONLY

ARTICLE

Is Japan Becoming More Open?

Japan has long appeared relatively closed to foreign goods and investment. Although official barriers to goods, such as tariffs, are low, observers have pointed to a wide range of potential "invisible" barriers. Foreign investors have also faced numerous hurdles. Recent reforms are helping to ease these barriers, and quantitative indicators show some signs of increasing openness. Nevertheless, Japan remains much more closed than other industrial countries.

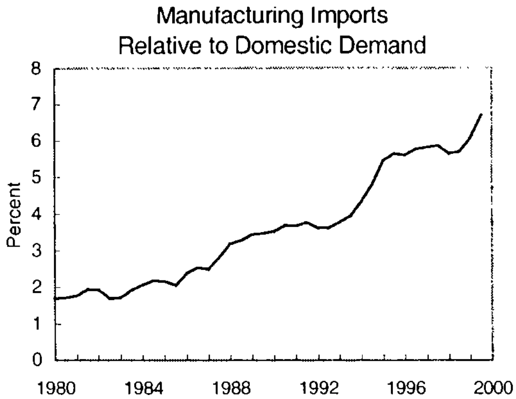
Structural reforms should ease barriers to foreign access. In the 1990s, Japan began a program of structural reforms to create a more efficient and competitive domestic economy. Financial liberalization is creating a more competitive and open financial environment. New accounting standards are improving corporate governance and transparency by making it easier to evaluate the performance of Japanese companies. These standards could also make foreign firms more willing to merge or acquire Japanese companies because they can better evaluate what they are buying. Japan has made some (albeit incomplete) progress at reducing regulation in areas such as telecommunications, energy, distribution, and auto repair. Japan itself is the major beneficiary of these reforms, but foreign providers of goods and capital are also likely to benefit.

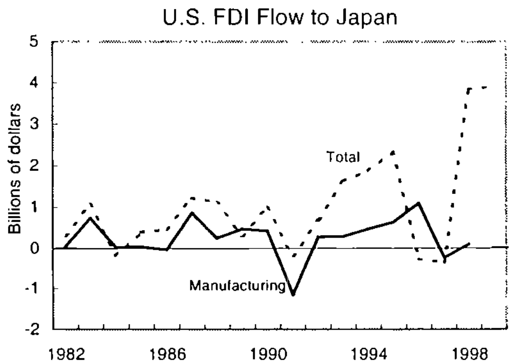
Challenges to the *keiretsu*. One indicator of structural change in Japan is that the *keiretsu* system of affiliated firms (often centered around a lead bank that provides financial support to the group) is now under attack. Cross-shareholding appears to be falling; mergers of weak Japanese lead banks may also attenuate the sometimes cozy ties between banks and companies. A breakdown of the *keiretsu* system should benefit foreign firms. In the past, members of a *keiretsu* may have preferred to purchase inputs from affiliated suppliers, even if foreign suppliers were cheaper; *keiretsu* members may even have colluded to keep potential competitors (including foreign firms) out of the market.

Auto alliances. A second indicator of structural change is that foreign auto companies have now taken major ownership stakes in Japanese auto companies. Renault, for example, is allied with Nissan; Ford is allied with Mazda; General Motors has alliances with Isuzu, Subaru, and Suzuki; Daimler-Chrysler has announced an alliance with Mitsubishi. The president of Nissan was born in Brazil and educated in France, and the president of Mazda is American. These alliances may help further the breakdown in the traditional *keiretsu* system.

Trade and FDI flows. In addition to these qualitative indicators, quantitative evidence suggests some progress. Manufacturing imports showed particularly sharp gains relative to domestic demand in the early 1990s (see upper chart on next page). Nevertheless, the Japanese figure remains about half that of the United States and about a quarter that of the EU.

EYES ONLY





Inflows of foreign direct investment have also risen, driven in part by surging mergers and acquisitions (M&A) related to restructuring. U.S. direct investment in Japan, for example, reached record levels of about $4 billion per year in 1998 and 1999, after essentially no investment in 1997 (see lower chart). Cross-border M&A in Japan rose from $4 billion in 1998 to $16 billion in 1999. While these changes are dramatic, for both FDI inflows and cross-border M&A activity, Japan accounted for only about 2 percent of developed-country totals in 1999, up from less than 1 percent in 1998. By contrast, the roughly similar U.S. and EU shares together accounted for around 90 percent of direct investment inflows and cross-border M&A activity to developed countries in 1998 and 1999.

Progress may be slow. Even after Japan fully implements reforms, it will take time for the full quantitative effects to be apparent. In addition, Japan's prolonged recession and the relative strength of the dollar tend to restrain Japan's imports of U.S. goods. For example, despite some steps taken under the 1995 U.S.-Japan Agreement on Autos and Auto Parts that opened up the Japanese distribution system and auto-repair regime—and despite the ownership stakes of U.S. auto companies in Japanese firms—sales of U.S. autos and auto parts have plummeted in recent years, largely reflecting the adverse macroeconomic environment.

Conclusion. Despite nascent signs of increasing openness, import penetration and inflows of foreign direct investment relative to GDP in Japan remain well below the rates in other industrial countries, which have also been making substantial changes to open their economies. To the extent that structural reforms continue, Japan is likely to open further in the future. Nevertheless, reforms still have a long way to go, and they face domestic political opposition, so that continued progress is not assured.

EYES ONLY

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

The Power of Suggestion in Saving Behavior. How a company presents its savings plan to employees affects their enrollment decision. A recent study examined data from a large U.S. corporation that changed its 401(k) plan from one requiring employees to affirmatively opt into the plan to one automatically enrolling employees unless they made a negative election to opt out of the plan. Although none of the economic features of the plan changed, this switch to automatic enrollment dramatically changed the saving behavior of employees. When they were automatically enrolled, 401(k) participation was significantly higher. Additionally, the default contribution rate and investment allocation chosen by the company under automatic enrollment had a strong influence on the saving behavior of 401(k) participants. This "default" behavior appears to result both from participant inertia and from many employees interpreting the default as investment advice from the company. Automatic enrollment in 401(k) plans also appears to even out differences that previously existed between men and women and between racial and ethnic groups.

Deterrence or Vengeance? The economic approach to optimal punishment suggests that differences in sentence length should be related to their effect on incapacitating criminals and deterring crime. A new paper analyzing sentences for murders finds some support for this hypothesis: sentences are higher when the expected apprehension rate for murderers is lower, for types of murder that respond less to deterrence, and for murderers with higher expected recidivism rates. Victim characteristics also play a role. Consistent with other studies, murderers were found to receive shorter sentences if the victim was black or male. This pattern was observed even in the case of vehicular homicides, where the victim was most likely random and different sentences would be unlikely to have deterrence effects: drivers who killed women got 56 percent longer sentences, while those who killed blacks got 53 percent shorter sentences. These striking effects lead the authors to conclude that sentence lengths may also be driven, in part, by a taste for vengeance.

Just the Facts, Mom. The nation has 35 million mothers aged 15 to 44 to honor this Mother's Day. About a third of these mothers have one child, 40 percent have two, and 9 percent have four or more. Alabama, Alaska, Idaho, Mississippi, and Wyoming have the highest percent of women who are mothers (about 64 percent of women aged 15-44). In contrast, only 38 percent of women in the District of Columbia have ever given birth. In June 1998, nearly 120,000 (3 percent) of women who had given birth during the previous year were in their 40s, compared with fewer than 60,000 (2 percent) in 1980. Mothers are working more and returning to work sooner after giving birth. In 1998, the majority (59 percent) of women aged 15-44 who had given birth in the previous year had returned to the labor force, a 50 percent increase since 1980. As more mothers enter the workforce to help support their families, we are also paying them greater tribute: in 1997, the nation's greeting card publishers shipped $212 million worth of Mother's Day cards, up from $148 million in 1992.

EYES ONLY

INTERNATIONAL ROUNDUP

Internet Prices Falling in the OECD. The cost of accessing the Internet is falling in OECD countries, and a trend toward "unmetered" access bodes well for electronic commerce, according to a new OECD study. The average cost of 20 hours per month of Internet access fell by 15 percent between October 1999 and March 2000. The United States, Australia, Canada, New Zealand, and Mexico have unmetered plans in which the Internet access charge does not vary with connection time. For peak-time, the monthly access charge averages $44 in these five unmetered countries, compared with an average of $256 for 150 hours in metered countries. Since countries with unmetered access have six times as many servers designed for e-commerce, unmetered access appears to facilitate e-commerce. The study also reports that the Internet Service Provider fee has fallen as a share of Internet access costs from 63 percent in 1995 to 23 percent in March 2000 (while the share of telephone service costs has increased).

East Asian Nations Coordinate to Defend Currencies. The governments of East Asian nations have decided to move forward with a proposal to establish a regional financing arrangement to supplement the existing international facilities. This "Chiang Mai Initiative" was launched last weekend by the finance ministers of Japan, China, and the Republic of Korea, along with the ten finance ministers of the Association of South East Asian Nations. The proposal is meant to strengthen the economic defenses of these nations against the sort of speculation that instigated the 1997 Asian economic crisis. Specifically, the proposal involves a network of bilateral currency swaps and repurchasing agreements. The Ministers expressed general agreement over the course of the meetings on the importance of further cooperation among Asian nations in response to the region's growing interdependence.

Growth Does Not Worsen Inequality. Using data for 80 countries covering four decades, a new study by World Bank researchers finds evidence that when a country grows, the income of the poor grows as well. Analyzing growth in per capita GDP and in the average income of the poorest 20 percent of the population the study found that the two tended to grow approximately one-for-one, suggesting that the poor share proportionally in overall growth. The study also investigated whether different sources of economic growth might have differential impacts on the poor. For instance, it found that openness to trade had no effect on the incomes of the poor after controlling for the effect of growth in overall per capita GDP, suggesting that trade does not have negative effects on the poor. The results do indicate that inflation has a disproportionately higher negative effect on the income of the poor, suggesting that measures to control inflation are in fact "super pro-poor" policies. Additionally, the study found that public spending on health and education did not have systematic effects on the incomes of the poor, which might suggest that such spending has been poorly targeted.

EYES ONLY

RELEASES THIS WEEK

Producer Price Index

****Embargoed until 8:30 a.m., Friday, May 12, 2000****

The producer price index for finished goods fell 0.3 percent in April. Excluding food and energy, producer prices rose 0.1 percent.

Retail Sales

Advance estimates show that retail sales decreased 0.2 percent in April following an increase of 0.5 percent in March. Excluding sales in the automotive group, retail sales were unchanged, following an increase of 1.2 percent.

MAJOR RELEASES NEXT WEEK

Consumer Prices (Tuesday)
Housing Starts (Tuesday)
Industrial Production and Capacity Utilization (Tuesday)
U.S. International Trade in Goods and Services (Friday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	1999	1999:3	1999:4	2000:1
Percent growth (annual rate)					
Real GDP (chain-type)	2.9	4.6	5.7	7.3	5.4
GDP chain-type price index	5.2	1.6	1.1	2.0	2.7
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.7	5.0	6.9	2.4
Real compensation per hour:					
Using CPI	1.0	1.7	2.0	0.9	0.3
Using NFB deflator	1.5	2.9	4.0	1.8	1.8
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.7	12.5	12.9
Residential investment	4.5	4.4	4.4	4.4	4.4
Exports	8.2	10.8	10.8	10.9	10.8
Imports	9.2	13.5	13.8	14.0	14.2
Personal saving	6.6	1.7	1.5	1.3	0.5
Federal surplus	-2.8	1.2	1.4	1.2	N.A.

	1970-1993	1999	February 2000	March 2000	April 2000
Unemployment Rate (percent)	6.7**	4.2**	4.1	4.1	3.9
Payroll employment (thousands)					
increase per month			27	458	340
increase since Jan. 1993					21615
Inflation (percent per period)					
CPI	5.8	2.7	0.5	0.7	N.A.
PPI-Finished goods	5.0	**2.9**	1.0	1.0	**-0.3**

**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.
PPI data **embargoed until 8:30 a.m., Friday, May 12, 2000**.

EYES ONLY

FINANCIAL STATISTICS

	1998	1999	March 2000	April 2000	May 11, 2000
Dow-Jones Industrial Average	8626	10465	10483	10944	10546
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.69	5.66	5.96
10-year T-bond	5.26	5.65	6.26	5.99	6.43
Mortgage rate, 30-year fixed	6.94	7.43	8.24	8.15	8.52
Prime rate	8.35	8.00	8.83	9.00	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level May 11, 2000**	**Percent Change from**	
		Week ago	**Year ago**
Euro (in U.S. dollars)	0.902	1.3	-15.8
Yen (per U.S. dollar)	108.5	0.3	-10.3
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	99.42	-0.2	5.1

International Comparisons [1/]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	5.0 (Q1)	3.9 (Apr)	3.7 (Mar)
Canada	4.7 (Q4)	6.8 (Mar)	3.0 (Mar)
Japan	0.0 (Q4)	5.0 (Mar)	-0.5 (Mar)
France	3.1 (Q4)	9.8 (Mar)	1.5 (Mar)
Germany	2.3 (Q4)	8.4 (Mar)	1.9 (Mar)
Italy	2.1 (Q4)	11.3 (Jan)	2.5 (Mar)
United Kingdom	3.0 (Q4)	5.9 (Dec)	2.6 (Mar)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics.

EYES ONLY

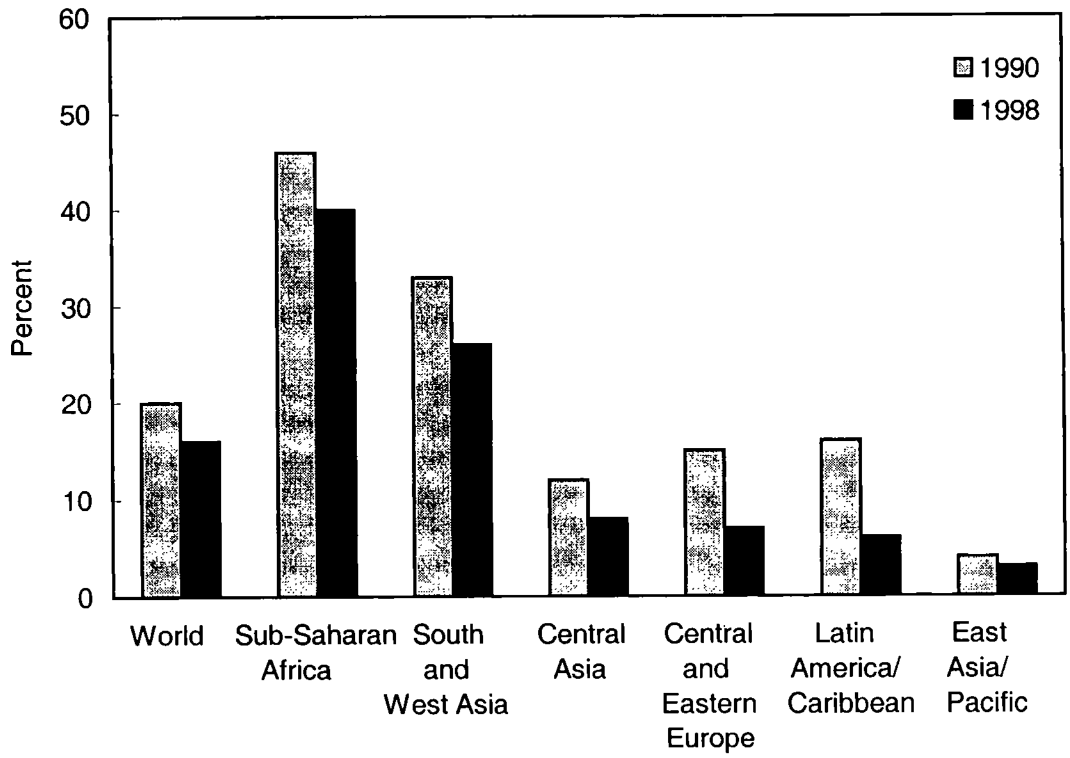
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

May 5, 2000

CHART OF THE WEEK

Primary-School-Aged Children Not Enrolled in School



The proportion of primary-school-aged children not enrolled in school has fallen worldwide and in all less developed regions since 1990. In 1998, 97 percent of the 113 million out-of-school children lived in less developed regions, and nearly 60 percent of them were girls.

EYES ONLY

CONTENTS

"What was it this time, old economy or new economy?"

EYES ONLY

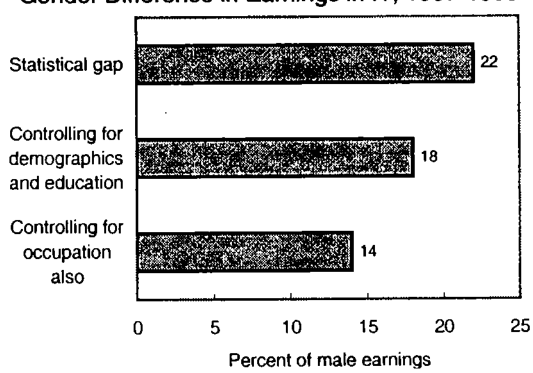
SPECIAL ANALYSIS

Gender Pay Differences in the IT Labor Market

In the U.S. labor market, women earn only about three-quarters as much as men. Gender pay differences in the rapidly expanding field of information technology (IT) provide one perspective on the sources of this pay differential.

Employment and earnings in IT. The IT field is characterized by both high-paying jobs and high employment growth. (IT is defined here to comprise the following five occupations: electrical and electronic engineering, computer systems analysts and scientists, operations and systems researchers and analysts, computer programmers, and computer operators). A CEA analysis finds that the median IT worker earns 74 percent more than the median worker in other occupations ($947 per week versus $544 per week). Employment in IT has grown by almost 23 percent over the past 10 years, to approximately 3.4 million workers, and projections by the Bureau of Labor Statistics suggest that this rapid growth will continue.

Gender Difference in Earnings in IT, 1997-1999



The IT gender pay gap. Women working full time in IT earn about 22 percent less than men—about the same difference as in the labor market generally. Part of this gap reflects gender differences in demographic characteristics such as age and race and in educational attainment. After controlling for these factors, women were found to earn 18 percent less than men (see chart). Differences in the number of hours worked appear to have little effect.

The importance of occupation. Controlling for occupation within the IT sector explains another large part of the pay gap. Only about a fifth of workers in the two most highly paid IT occupations (electrical engineering and computer systems analysts and scientists) are women. By contrast, women account for two-fifths of workers in the other three occupations. In the CEA's statistical model, the gender earnings gap in IT fell to about 14 percent once differences in occupational composition were taken into account.

How much is discrimination? It is tempting to conclude that the impact of gender discrimination is captured by the 14 percent gap that remains after controlling for occupation, education, and demographic characteristics. Some might even argue that the statistical gap is an "upper bound" that would be reduced still further if data were available that would allow an even finer division of occupations. Even with such data, however, it would be difficult to resolve more fundamental concerns about the underlying reasons for the substantial gender differences in occupation composition. First, some women may choose to pursue career paths that provide increased flexibility for devoting time to their families but that also pay less. Second, systematic gender discrimination may exist in hiring and promotion. For example, women may be less likely than men to be hired as systems analysts or may have lower mobility from programming positions to systems analyst positions. Third, women may respond rationally to perceived discriminatory practices by reducing the investments they make in their own careers and thus achieve less.

Conclusion. A statistical analysis of the gender pay gap in IT finds that the raw gap of 22 percent falls to 14 percent once differences in occupation, age, race, and education are taken into account. To the extent that women choose to sacrifice pay for flexibility or other advantages, the gap might be even smaller than this. However, to the extent that discrimination pushes women into lower paying occupations, this statistical analysis—which focuses on the average of gender wage differences observed within occupations—understates the true gap.

EYES ONLY

SPECIAL ANALYSIS

Instant Messaging Disconnect

With network goods, where the value to each user rises as the number of connections increases, the firm with the largest network has an advantage. The instant messaging (IM) market provides an interesting test case of how a dominant firm reacts to competition, and whether consumers' ability to switch services—even at a relatively low cost—is sufficient to preserve competition.

What is IM? Instant messaging services provide a way to send short messages among individuals in pre-established groups using the Internet. Users of the service are notified when other users in their group are online and able to exchange messages with them. America Online has become a leading supplier of this technology, and it claims that it has 90 million registered users. AOL's software can be downloaded at no charge from the Internet, enabling anyone with an Internet connection to send instant messages to other users of AOL's software.

Interconnection and competition. IM is one element of the bundle of services Internet access providers use to compete for customers and advertising revenue. For a dominant firm like AOL (which some claim has a 90 percent market share), there is very little incentive to give away that advantage to rivals by allowing interconnection. Microsoft, which provides its own instant messaging service for users of its network, wanted to interconnect its customers to those using AOL's services. Rather than reaching an agreement with AOL, however, Microsoft devised software that would create the linkage. AOL, in turn, blocked Microsoft's repeated attempts to interconnect to AOL customers.

Creating a standard. One possible solution that could help create more network connections is to establish a standard for IM services. The Internet Engineering Task Force has solicited proposals for a protocol that would allow interconnection among IM services. Creating a standard, however, is different from implementing a standard. In particular, AOL might see little advantage to making its system compatible with any other standard that emerges.

Competition and standards. AOL's smaller rivals are likely to implement the standard because the alternative of remaining a small, isolated network is not a viable long-term strategy. Once all of AOL's rivals are interconnected, the standard will create a larger pool of users that its own customers would want to be able to access. Although AOL could still just say no to standardization, customers who desire such connections could download a rival firm's software anyway, thereby becoming users of both networks.

Implications. In the particular case of instant messaging, where the costs of switching between networks appear to be low, AOL may find that inconveniencing its customers only leads them to defect to rival suppliers. If, however, AOL is able to maintain its position without connecting to other networks that adopt a common standard, that would suggest that first mover advantages are strong. Such an outcome would raise questions about whether competitive forces could erode a dominant position in other markets where network effects are present and switching costs are high.

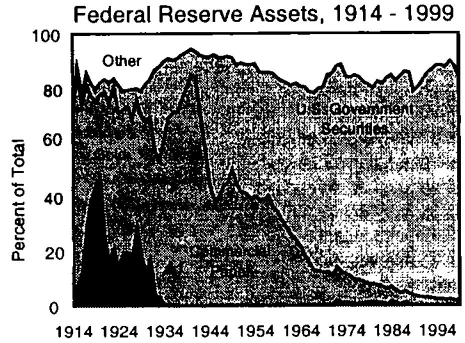
ARTICLE

What Is the Fed to Do when the T-Bills Run Out?

The prospective elimination of all publicly held debt by 2013 poses a practical problem for the Federal Reserve System, which conducts monetary policy primarily through transactions in Treasury securities. In the distant past, the Fed conducted monetary policy using commercial paper, and it could return to this practice. A better alternative, however, would be to find a replacement that has the key characteristics of Treasury securities: liquid and transparent markets and very low credit risk.

What the Fed owns. Except in unusual circumstances, the Fed can own only the following types of financial assets: gold, certain types of short-term private commercial paper, U.S. Treasury and agency securities, foreign sovereign debt, and some securities issued by state and local governments. It has no express authority to purchase corporate equities or bonds, mortgages, or land (other than Federal reserve premises). During its early history, the Federal Reserve's main assets were gold and commercial paper (see chart). Beginning in the 1930s, however, it greatly increased its holdings of Treasury securities, which now make up about 80 percent of Fed assets. The Fed currently holds—either directly or in repurchase agreements—about one-seventh of all Federal debt held by the public.

Federal Reserve Assets, 1914 - 1999



The conduct of monetary policy today... The Fed affects short-term interest rates by manipulating the supply of reserves held by member banks. Banks hold reserves to fulfill reserve requirements on certain types of deposits and to cover claims on their accounts made during the day. When the Fed increases reserves, their price—the federal funds rate—falls. The current practice is to raise or lower reserves principally through the purchase or sale of government securities to member banks in exchange for reserves. In several important ways, Treasury securities represent an ideal instrument for monetary policy. First, Treasury markets are generally very liquid, so that the Fed can easily purchase and sell securities at market prices. Second, price information is widely available, making these markets highly transparent. Third, Treasury securities are backed by the full faith and credit of the U.S. government; hence, the Fed takes on no credit risk in owning them.

...and in the future. With all publicly held Federal debt (which includes Federal Reserve holdings) projected to be retired by 2013, the Fed will need to change its asset portfolio and its conduct of monetary policy. The best option would be to find financial instruments that closely approximate the desirable characteristics of

Treasury securities. Unfortunately, some of the kinds of securities that the Fed is currently allowed to own fail this test. For example, use of foreign government securities would expose the Fed to exchange rate risk. Moreover, the regular use of foreign bonds to adjust reserves could impinge on the Treasury Department's responsibility for foreign exchange policy. Similarly, large-scale direct ownership and discounting of short-term commercial paper—a standard Fed practice in the 1920s—would imply a much more active role for the Fed in pricing risk and potentially interfering with the normal functioning of financial markets with respect to the allocation of credit and risk. One solution might be the creation of new securities by the private sector (see box)—though it might be necessary to broaden the Federal Reserve's power to own private securities to take advantage of such new securities.

A Triple-A Plus Solution

Private institutions could provide a solution to the Fed's problem of replacing Treasury securities in the conduct of monetary policy by creating new, very low-risk securities constructed from a pool of private debt securities. Such securities would be similar to mortgage-based securities currently issued by government-sponsored enterprises like Freddie Mac and Fannie Mae. For example, a financial institution, perhaps called the Triple-A Plus Fund, would buy a set of high-quality corporate bonds. It would then offer to sell a coupon bond called the Triple-A Plus bond that pays a fixed annual interest rate of, say 7 percent, for the life of the bond. The Triple-A Fund would put up its equity capital and take on the default risk of the underlying corporate bonds. Although not completely risk-free, bonds like the Triple-A Plus bond would entail very little credit risk and would be close substitutes for Treasury securities. Liquid and transparent markets should develop, given markets' and the Fed's appetite for such a low-risk security.

Conclusion. Under current projections for the elimination of publicly held Federal debt, the Fed's reliance on Treasury securities for its conduct of monetary policy will have to end. Although not discussed here, a related issue is how the Treasury Department should invest future Federal surpluses once the publicly held debt is paid off. Alternatives exist and the staffs at the Federal Reserve and the Treasury Department are actively evaluating the various options.

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Beige Book Shows Expansion Continuing. The latest reports from the 12 Federal Reserve districts indicated that the economy continued to expand during March and the first 3 weeks of April. The majority of districts reported moderate to strong economic growth, with only Richmond and Chicago noting some signs of slight slowing. Consumer spending was strong. Commercial construction activity generally remained robust, while several districts noted softening residential demand. Factories were running near capacity in some areas, as overall manufacturing activity was strong. Dry soil conditions were reported in many areas, but spring planting proceeded at a rapid pace. Oil drilling activity was up from a year ago. There were more frequent reports of intensifying wage pressures as shortages of workers persisted in all districts. Increasing input prices were noted in nearly every region. Many districts cited wider use of fuel surcharges by shipping firms and other transportation companies. Manufacturers in several areas also reported higher prices for petroleum-related inputs. However, there were only a few reports that increases in input costs were resulting in higher prices at the retail level.

Explaining the Decline in Unionization. While some observers argue that the lack of legal and political support for organizing new workers is an important reason for the decades-long slide in union membership rates in the private sector, a recent study concludes that changes in the economy are far more important. In particular, the study found that between 1973 and 1998, employment in non-unionized establishments and new establishments that were not organized (the non-union sector) grew by an average of 2.8 percent per year. By contrast, employment in unionized establishments (including organization of previously non-unionized workers) shrank by 2.9 percent annually. The authors argue that this divergence in growth rates is related to the structural shift in the U.S. economy away from sectors in which unions were strongest such as manufacturing, transportation, and communications (and within manufacturing to a shift in new capacity to regions that have historically not been favorable to unions). The study suggests that a very large increase in union organizing activity would be required to have a significant influence on the union membership rate in the private sector.

INTERNATIONAL ROUNDUP

ECB Raises Rates but Euro Keeps Falling. Amid concerns that the euro's low value may be contributing to inflationary pressures in the euro area, the European Central Bank announced last week that it would raise its benchmark interest rate by 0.25 percentage points, the fourth increase since November. Nevertheless, the euro continued to slide this week, reaching a record low of 89.0 cents. The value of the euro has fallen 24 percent against the dollar and 27 percent against the yen since its introduction in January 1999. The strength of the U.S. economy relative to Europe's and the prospect of further interest rate increases by the Federal Reserve are seen as reasons for the euro's weakness against the dollar. Some commentators have also suggested that capital markets are skeptical of the pace of labor market and tax reforms by European governments.

Education for All. Representatives from 181 countries at the World Education Forum (WEF) in Dakar last week renewed pledges made in 1990 to pursue education for all, particularly girls. Significant progress has been made in the past decade, with 84 percent of primary-school-aged children enrolled worldwide in 1998, up from 80 percent in 1990. The illiteracy rate among young adults aged 15-24 declined from 26 percent in 1970 to 14 percent in 1998, with evidence that countries are giving higher funding priorities to primary education. Nevertheless, more than 113 million children still have no access to primary education, 880 million adults remain illiterate, and gender discrimination continues. In Africa, the Arab States, and South and West Asia, primary school enrollment rates for school-age girls are about 10 percentage points lower than those of boys. WEF participant countries pledged that by 2015, all children, especially girls and minorities, would have free and compulsory primary education of good quality. In addition, donor countries and institutions promised that lack of resources will not stand in the way of achieving this goal.

New Pan-European Stock Exchange to be Created. The London Stock Exchange and Germany's Deutsche Boerse announced plans to merge this week, combining Europe's two largest stock markets into a new exchange called iX. The two exchanges currently provide the primary listing for 45 percent of Europe's top 300 companies and account for 53 percent of trade volume. In addition, iX said that it has signed a memorandum of understanding with NASDAQ to create a pan-European high-growth market. This new joint venture would represent Europe's biggest high-growth market, accounting for about 80 percent of volume in these stocks. Companies listed will include several hundred from Germany's Neuer Markt, London's techMARK, the NASDAQ 100, and other major U.S. and non-European securities and index funds. NASDAQ's stated goal is eventually to link this venture to other NASDAQ-branded markets around the world, creating a global, 24-hour trading platform. The boards of Deutsche Boerse and the London Stock exchange likewise believe that the merger will provide the basis for developing a global securities market, and talks for including the Milan and Madrid exchanges have already begun.

EYES ONLY

RELEASES THIS WEEK

Employment and Unemployment

****Embargoed until 8:30 a.m., Friday, May 5, 2000****

In April, the unemployment rate was 3.9 percent; it was 4.1 percent in March. Nonfarm payroll employment rose by 340,000.

Productivity

According to preliminary estimates, nonfarm business productivity rose 2.4 percent at an annual rate in the first quarter of 2000. Manufacturing productivity rose 6.9 percent.

Leading Indicators

The composite index of leading indicators increased 0.1 percent in March.

NAPM Report on Business

The Purchasing Managers' Index decreased 0.9 percentage point in April to 54.9 percent. (A reading above 50 percent indicates that the manufacturing economy is generally expanding.)

MAJOR RELEASES NEXT WEEK

Retail Sales (Thursday)
Producer Prices (Friday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	1999	1999:3	1999:4	2000:1
Percent growth (annual rate)					
Real GDP (chain-type)	2.9	4.6	5.7	7.3	5.4
GDP chain-type price index	5.2	1.6	1.1	2.0	2.7
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	**3.7**	5.0	**6.9**	**2.4**
Real compensation per hour:					
Using CPI	1.0	1.7	**2.0**	**0.9**	**0.3**
Using NFB deflator	1.5	**2.9**	4.0	**1.8**	**1.8**
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.7	12.5	12.9
Residential investment	4.5	4.4	4.4	4.4	4.4
Exports	8.2	10.8	10.8	10.9	10.8
Imports	9.2	13.5	13.8	14.0	14.2
Personal saving	6.6	1.7	1.5	1.3	0.5
Federal surplus	-2.8	1.2	1.4	1.2	N.A.

	1970-1993	1999	February 2000	March 2000	April 2000
Unemployment Rate (percent)	6.7**	4.2**	4.1	4.1	**3.9**
Payroll employment (thousands)					
increase per month			**27**	**458**	**340**
increase since Jan. 1993					**21615**
Inflation (percent per period)					
CPI	5.8	2.7	0.5	0.7	N.A.
PPI-Finished goods	5.0	3.0	1.0	1.0	N.A.

**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.
Employment and unemployment data **embargoed until 8:30 a.m., Friday, May 5, 2000.**

EYES ONLY

FINANCIAL STATISTICS

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Dow-Jones Industrial Average	8626	10465	10483	10944	10412
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Prime rate	8.35	8.00	8.83	9.00	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level May 4, 2000**	**Percent Change from** Week ago	Year ago
Euro (in U.S. dollars)	0.891	-1.9	-15.9
Yen (per U.S. dollar)	108.2	1.7	-10.6
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	99.62	1.6	4.9

International Comparisons 1/	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
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Italy	2.1 (Q4)	11.2 (Jan) 2/	2.5 (Mar)
United Kingdom	3.0 (Q4)	5.9 (Dec)	2.6 (Mar)

U.S. unemployment data **embargoed until 8:30 a.m., Friday, May 5, 2000.**

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.

2/ Data from OECD standardized unemployment rates.

EYES ONLY

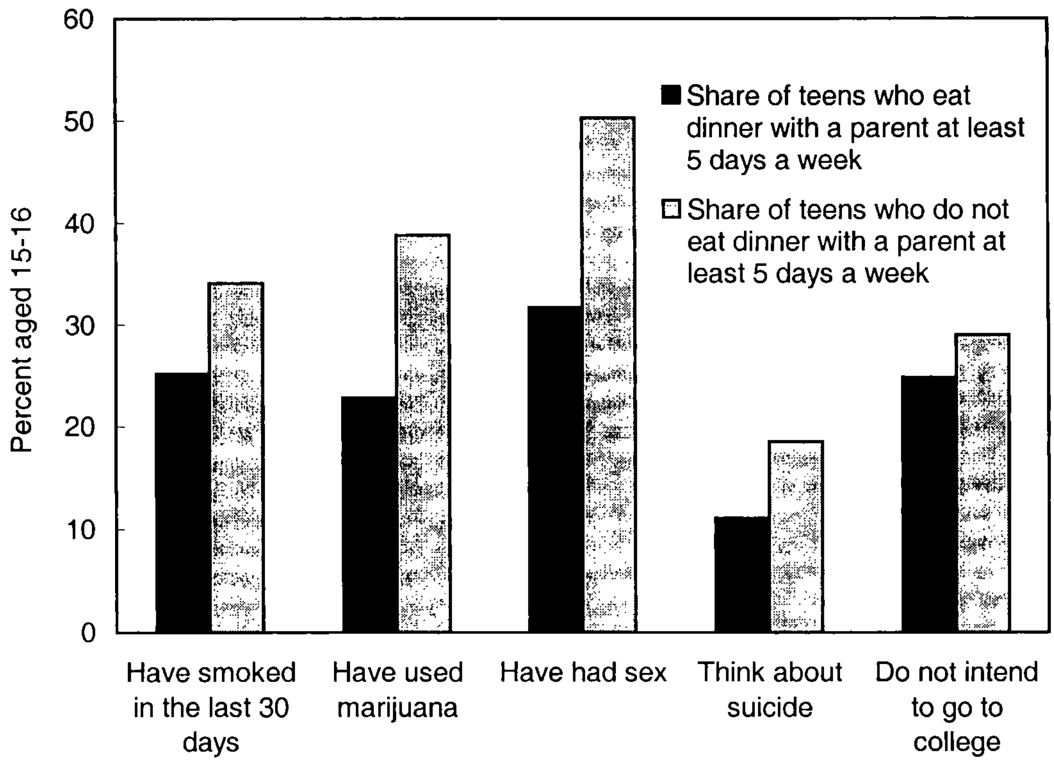
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

April 28, 2000

CHART OF THE WEEK

Parental Involvement and Teen Behavior



Teenagers who eat with a parent at least 5 times a week do better on a wide variety of indicators than those who do not. A CEA White Paper described in this *Weekly Economic Briefing* provides a range of evidence on the importance of parental involvement in influencing teens to make responsible decisions.

CONTENTS

EYES ONLY

"O.K., guys, now let's go and earn that four hundred times our workers' salaries."

EYES ONLY

CURRENT DEVELOPMENT

GDP Scorecard: First Quarter 2000

Real GDP is estimated to have increased at a 5.4 percent annual rate in the first quarter of 2000, with strong growth in consumption, fixed investment, and state and local government spending. Final sales (GDP less the change in private inventories) increased at a 6.9 percent annual rate, the fastest rate in over 15 years. Inflation, as measured by the price index for GDP, increased at a 2.7 percent annual rate in the fourth quarter, but the core GDP price index, which excludes food and energy components, increased at only a 2.1 percent annual rate.

Component	Growth*	Comments
Total consumer expenditures	8.3%	First-quarter consumption surged, with durable goods purchases up nearly 27 percent at an annual rate. The saving rate fell to 0.7 percent.
Equipment and software	23.7%	Growth was the strongest it has been in 2 years, and solid gains were recorded in all major categories. Computer investment rebounded after briefly faltering late last year when businesses "locked down" computer systems purchases in preparation for Y2K.
Nonresidential structures	13.4%	Spending bounced back after declining 3.9 percent during 1999.
Residential investment	6.7%	Good weather contributed to solid growth, despite elevated mortgage rates. Housing indicators suggest some slowing in the second quarter.
Inventories (change, billions of 1996 dollars)	$31.1	Inventory accumulation slowed in the retail trade sector following a sizable buildup in the fourth quarter of 1999. Robust final sales caused the inventory-to-sales ratio to decline further.
Federal purchases	-15.5%	Defense spending fell sharply, more than reversing a surge in the fourth quarter of 1999.
State & local purchases	7.4%	Spending continued to accelerate.
Exports	-0.2%	First-quarter exports were held down by the Boeing strike, which has since been settled. Even after accounting for the effect of the strike, however, growth was relatively weak.
Imports	9.5%	Growth was down somewhat from the pace of the last few years.

*Percent real growth in the first quarter at annual rates (except inventories). This advance estimate is subject to substantial revision–especially for exports, imports, and inventories, where the estimates are based on only 2 months of data.

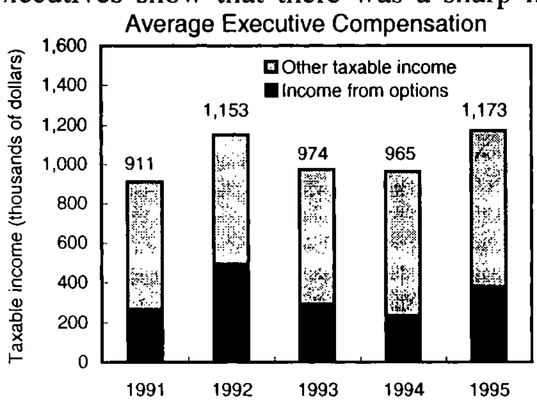
EYES ONLY

SPECIAL ANALYSIS

The Effect of Taxes on Executive Compensation

The last two decades have seen major shifts in income tax policy toward the very wealthy, as marginal income tax rates were first lowered and then raised. Some studies of the Reagan-era tax cuts suggest that the lowering of the top marginal rate caused large increases in taxable income, which may have been caused by upper income taxpayers shifting compensation between taxable and nontaxable forms. Others have argued that these results are overstated, because other confounding changes occurred at that time. The responsiveness of taxable income to tax changes matters because attempts to get the wealthy to pay a greater share of the total tax burden are much more difficult if taxpayers alter their behavior substantially in response to higher marginal rates.

Evidence from the rate increase in 1993. To understand better how taxpayers respond to changes in top marginal rates, one study examined executive compensation data before and after the increase in top marginal tax rates in 1993. Data on salary and other types of compensation for high level company executives show that there was a sharp increase in taxable income reported by these executives in 1992 (see chart). After the tax increase in 1993, total income dropped, which is consistent with the hypothesis that taxable income is sensitive to changes in the top marginal rates. A closer examination of the types of compensation received by executives, however, shows that this large swing in reported taxable income was caused by the stock options exercised in 1992. Since the intent to raise tax rates on high income individuals was announced during the presidential campaign in 1992 before becoming law in 1993, executives apparently anticipated the rate increase and exercised their stock options before the increase became effective, causing a short-term boost in compensation.



Analysis. A statistical analysis confirms that the exercise of options explains between 90 and 95 percent of the changes in taxable income for high-level executives during the years surrounding the tax changes. Moreover, even though there was some increase in nontaxable forms of income, those increases do not explain the drop in taxable income between 1992 and 1993. More generally, other attempts (with other types of data) to examine previous changes in top marginal tax rates over the last 60 years suggest that the results from the mid-1980s tax cuts appear to be atypical, and that, more commonly, the responsiveness of taxable income to changes in the top marginal tax rate is relatively small.

EYES ONLY

ARTICLE

Raising Responsible and Resourceful Youth

In conjunction with the White House Conference on American Teenagers, the Council of Economic Advisers will release a White Paper analyzing trends in teen behavior and the role of parental involvement. The report outlines significant opportunities and challenges for teens in the 21st century and demonstrates that teens are more likely to take advantage of opportunities and avoid risks when their parents are involved in their lives.

Trends in teenage behavior and outcomes. The report analyzes a number of trends affecting teenagers. Many, such as teen pregnancy and birth rates, working while in school, and gun violence among teens, have been discussed in previous *Weekly Economic Briefings*. Additional findings include the following:

- Health and prosperity. Teenagers today live far healthier, more prosperous and promising lives than ever before. Life expectancy for 15-year olds today is 77 years compared with 62 at the beginning of the century. Such killers as typhoid, cholera, polio, and smallpox now pose only minimal threats to American teens' health. Per capita income has increased eight-fold over the course of the century, and girls and minorities now have vastly greater educational and occupational choices than ever before.

- Educational attainment. Today's teens are taking more courses in core academic subjects and more challenging courses than their counterparts in the 1980s. African-Americans and whites now complete high school at virtually the same high rate: almost 90 percent. Most young people enroll in post-secondary school within 20 months of graduating high school. However, while 90 percent of children from the richest 25 percent of families pursue post-secondary education, just 60 percent of students from the poorest 25 percent do. And of those going on to post-secondary studies, nearly three quarters of children from the richest families attend 4-year colleges, while over half of those from the poorest families attend vocational, technical, or 2-year institutions.

- Community service. Evidence suggests positive effects. One study found, for example, that teens who participated in community service programs had a 75 percent lower rate of school dropout, and a 43 percent lower rate of pregnancy.

- Nutrition. According to one recent estimate, only 5.5 percent of American teens are faced with concern over where their next meal will come from. But poor food choices lead to significant nutrition deficiencies and imbalances among today's teens. For example, some 60 percent of teen boys and 80 percent of teen girls are calcium-deficient. Obesity also appears to be a problem.

- Smoking. White teens are more likely to smoke than African-American teens. Suburban teens and those with more highly educated parents are more likely to smoke than teens living in cities or rural areas. Research suggests that the decline in cigarette prices over the early 1990s led to about one-third of the increase in smoking among high-school seniors.

The importance of the parent-teen relationship. The study presents evidence showing that parental involvement is a major influence in helping teens avoid risks such as smoking, drinking, drug use, unwanted pregnancies, violence, and suicide attempts, while increasing educational achievement and expected attainment. Significant differences were noted between teens who eat dinner with their parents at least five times a week (61 percent of teens aged 15 or 16) and those who do not (see the Chart of the Week) and between those who reported feeling "close" to their mother and/or father (81 percent of 15-16 year olds) and those who did not. These results persist after taking account of differences in teens' gender, poverty status, and family structure. The report includes data for other age ranges, but the following results for 15-16 year olds are representative:

- Smoking, drinking, and drug use. Forty-two percent who do not feel close to at least one of their parents smoke, compared with 26 percent who do feel close to at least one parent. Over 34 percent who do not regularly eat dinner with a parent smoke, compared with just 25 percent who do eat dinner regularly with a parent. The prevalence of drinking is nearly twice as high among those who do not feel close to a parent and among those who do not eat regularly with a parent, compared with those who do. Over 50 percent of 15-16 year olds who are not close to their parents have used marijuana, compared with just 24 percent of those who are close to their parents.

- Violence. Less than 30 percent of teens aged 15-16 who eat dinner with their parents have been in a serious fight, compared with more than 40 percent of those who do not regularly eat dinner with their parents.

- Sexual activity. Over 50 percent of those who do not eat dinner with their parents have had sex by age 15-16. By contrast, only 32 percent of teens who do eat dinner with their parents have ever had sex.

- Suicide. Those who do not feel close to their parents are more than three times as likely to think about suicide as those who feel close; those who do not dine with their parents regularly are twice as likely to have attempted suicide.

- Educational achievement. Teens of all ages who eat dinner regularly with their parents and feel close to their parents have higher grade point averages than those who do not. They are more likely to intend to go to college, and they are less likely to have been ever suspended from school.

EYES ONLY

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Internet Traffic May Be a Clue to Internet Stock Valuation. A recent study confirms the common perception that traditional financial information appears to be of little use in explaining the value of Internet stocks. In particular, the study found that, for a sample of e-tailers and portal/content companies (including AOL and Yahoo), bottom-line financial information explained almost none of the variation in the market value of these stocks and that the relationship between net income and market value was actually negative. The study did, however, find that gross profits (which do not subtract marketing and R&D expenses from revenue) were positively related to stock prices, as were measures of Internet usage such as unique visitors to a web site or the number of pages viewed. The study concludes that usage data seem to capture some of the same information as gross profits but retain some independent explanatory power for how investors value Internet stocks. This suggests that information about revenue and customer base is more important than net income, at least in the fledgling stages of these companies.

Keeping Fathers Involved. Poor, urban, unmarried fathers are more likely to be involved in their children's lives if they are employed or have at least a high school education, according to a recent summary of research on fatherhood. Interviews with poor fathers in Philadelphia and Chicago suggest that mothers were often less supportive of a father's contact with his children when he could not support them, and fathers often separated themselves from their families out of shame. For instance, many fathers felt spending quality time with their children required money. Related findings showed that the level of fathers' involvement over time was closely related to the quality of their relationship with their children's mother. These findings suggest that providing job training and employment services to non-custodial fathers, as well as services designed to improve parents' relationships may be good ways to increase both child-support payments and fathers' involvement with their children.

Generational Differences in Medicare. A new study calls attention to differences in rates of return on Medicare for different generations and the impact of possible reforms. The study allocates payroll taxes, premiums, general revenue financing, and Medicare expenditures across cohorts and estimates future payments and expenditures based on the Trustees' assumptions. As with Social Security, rates of return are highest for generations born earliest, but Medicare rates of return are consistently higher than those of Social Security. Whereas the cohort born in 1910 earned a 27.6 percent rate of return (compared with 8.4 percent in Social Security), today's youngest workers can expect to earn a 2.2 percent rate of return (compared with 1.9 percent in Social Security). The study observes that this rate of return is above the steady-state return for a pay-as-you-go system (estimated to be about 1 percent), indicating that the burden on future generations is growing. Cutting benefits to achieve balance rather than raising payroll taxes would have a substantially larger negative effect on current middle-aged cohorts than on future generations, because the former have mostly already paid into the system. Raising payroll taxes would have the opposite effect.

INTERNATIONAL ROUNDUP

OECD Confirms Steel Market Recovery. The OECD Steel Committee recently released a favorable market outlook for the year 2000, confirming the recovery of the global steel market. The latest OECD estimates show an increase in steel consumption of over 2 percent for the OECD area in 2000 and continued demand growth in China, the Asian crisis economies, and the Newly Independent States. Strong economic growth should boost demand in motor vehicles, construction, machinery, and other steel consuming sectors. Steel product prices, which had mostly stopped falling or had begun to recover in the second half of 1999, should continue to rise throughout the year 2000. These favorable trends are expected to reduce commercial conflicts, which peaked towards the end of 1998 and the beginning of 1999. U. S. steel imports are expected to fall by 8 percent in 2000, in part as a result of the anti-dumping and countervailing duty measures imposed in 1999, and as demand recovers in other steel consuming countries. In addition, crude steel production could hit 100 million tons for the first time since 1981. Increased production and higher prices should lead to improved performance in 2000 for the main steel enterprises after a difficult period in 1998-99.

EU to Liberalize "Local Loops." The European Commission this week adopted a Recommendation calling on all member states to enact legal and regulatory measures to open competition in "local loops," the physical circuits that connect homes and companies to telecommunications operators. Such measures would mean that incumbent telephone companies would have to allow new competitors to use the incumbents' local loops. The objective of this proposal is to increase competition and technological innovation, stimulating the provision of services such as broadband multimedia and high-speed Internet. The adoption of this Recommendation marks the first step towards the goal set by the Lisbon European Council in March to bring about a substantial reduction in the cost of Internet access. The liberalization of local loops should take place by December 31, 2000, according to the Commission.

ODA Fell in the 1990s but Became Better Allocated. Net Official Development Assistance (ODA) from the Development Assistance Committee (DAC) countries fell from 0.33 percent of combined GNP in 1990 to 0.24 percent in 1998. Despite the decrease in total aid, however, the 1990s saw a significant shift in the allocation of aid in favor of countries with better economic policies, according to a recent World Bank study. The distribution of aid was much more sensitive to good country policies (measured by an index incorporating 20 indicators of economic policy) in 1997-98 than in 1990. Much of this improved allocation resulted from sharp cuts in aid to countries with poor policies with only modest cuts in aid to countries with good policies. For the one-third of countries with the worst economic policies, net ODA fell sharply from an average of $44 per capita in 1990 to $16 in 1997-98, whereas in the best one-third it fell from $39 to $28. Several countries, including Kenya, Nigeria, Pakistan, Togo, and Zaire (Congo) experienced cuts of at least 50 percent in their aid per capita.

EYES ONLY

RELEASES THIS WEEK

Gross Domestic Product

According to advance estimates, real gross domestic product grew at an annual rate of 5.4 percent in the first quarter of 2000.

Employment Cost Index

The employment cost index for private industry workers increased 4.6 percent for the 12-month period ending in March.

Advance Durable Orders

Advance estimates show that new orders for durable goods increased 2.6 percent in March, following a decrease of 2.0 percent in February.

Consumer Confidence

Consumer confidence, as measured by The Conference Board, declined 0.2 index points in April, to 136.9 (1985=100).

MAJOR RELEASES NEXT WEEK

NAPM Report on Business (Monday)
Leading Indicators (Tuesday)
Productivity (Thursday)
Employment (Friday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	**1999**	**1999:3**	**1999:4**	**2000:1**
Percent growth (annual rate)					
Real GDP (chain-type)	2.9	4.6	5.7	7.3	**5.4**
GDP chain-type price index	5.2	1.6	1.1	2.0	**2.7**
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.6	5.0	6.4	N.A.
Real compensation per hour:					
Using CPI	1.0	1.7	2.1	0.8	N.A.
Using NFB deflator	1.5	3.0	4.0	2.1	N.A.
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.7	12.5	**12.9**
Residential investment	4.5	4.4	4.4	4.4	**4.4**
Exports	8.2	10.8	10.8	10.9	**10.8**
Imports	9.2	13.5	13.8	14.0	**14.2**
Personal saving	6.6	1.7	1.5	1.3	**0.5**
Federal surplus	-2.8	1.2	1.4	1.2	N.A.

	1970-1993	**1999**	**January 2000**	**February 2000**	**March 2000**
Unemployment Rate (percent)	6.7**	4.2**	4.0	4.1	4.1
Payroll employment (thousands)					
increase per month			394	7	416
increase since Jan. 1993					21213
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.5	0.7
PPI-Finished goods	5.0	3.0	0.0	1.0	1.0

**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.

EYES ONLY

FINANCIAL STATISTICS

	1998	1999	February 2000	March 2000	April 27, 2000
Dow-Jones Industrial Average	8626	10465	10542	10483	10888
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.55	5.69	5.59
10-year T-bond	5.26	5.65	6.52	6.26	6.23
Mortgage rate, 30-year fixed	6.94	7.43	8.33	8.24	8.13
Prime rate	8.35	8.00	8.73	8.83	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level April 27, 2000**	**Percent Change from Week ago**	**Percent Change from Year ago**
Euro (in U.S. dollars)	0.908	-3.1	-14.7
Yen (per U.S. dollar)	106.4	0.9	-11.5
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	98.08	1.5	3.0

International Comparisons [1]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	5.0 (Q1)	4.1 (Mar)	3.7 (Mar)
Canada	4.7 (Q4)	6.8 (Feb)	3.0 (Mar)
Japan	0.0 (Q4)	4.9 (Feb)	-0.6 (Feb)
France	3.1 (Q4)	10.0 (Feb)	1.5 (Mar)
Germany	2.3 (Q4)	8.6 (Feb)	1.9 (Mar)
Italy	2.1 (Q4)	11.2 (Jan) [2]	2.5 (Mar)
United Kingdom	3.0 (Q4)	5.9 (Dec)	2.6 (Mar)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.
2/ Data from OECD standardized unemployment rates.

EYES ONLY

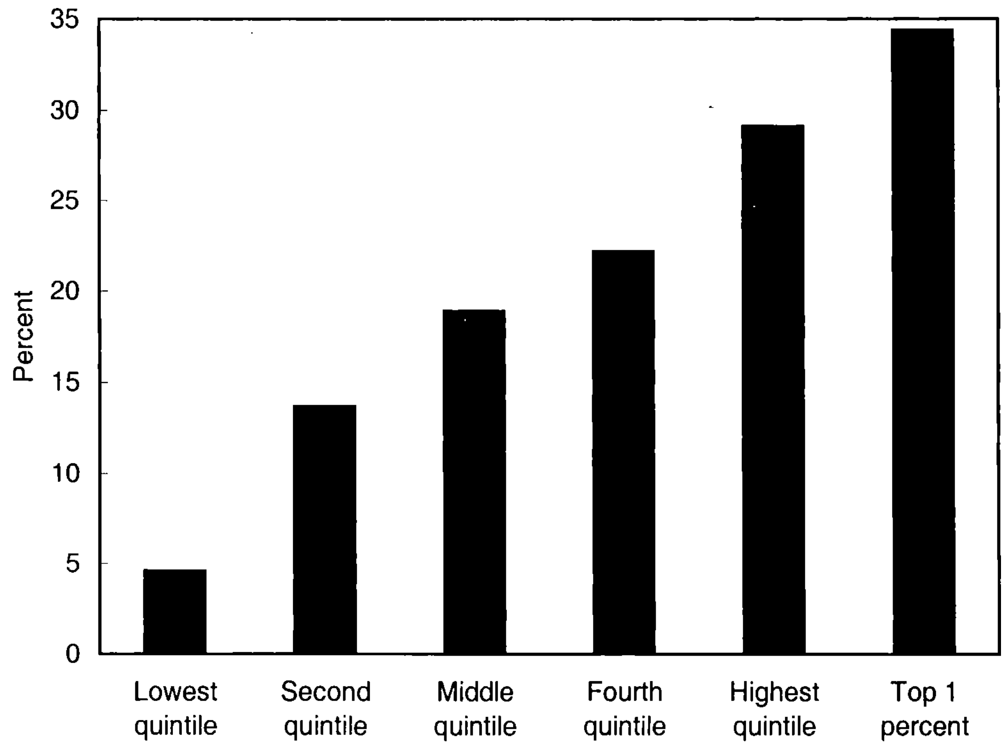
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

April 21, 2000

CHART OF THE WEEK

Effective Federal Tax Rates by Income



Based on CBO projections for 1999, the effective federal tax rate—combined income, excise, and payroll taxes as a percent of adjusted family income (including realized capital gains)—was less than 5 percent for the lowest income quintile and 29 percent for the highest income quintile. Since 1991, the largest changes in tax rates have been in the lowest quintile (down 3.3 percentage points) and the highest quintile (up 2.9 percentage points).

EYES ONLY

CONTENTS

"Uh-oh. The so-called marriage penalty."

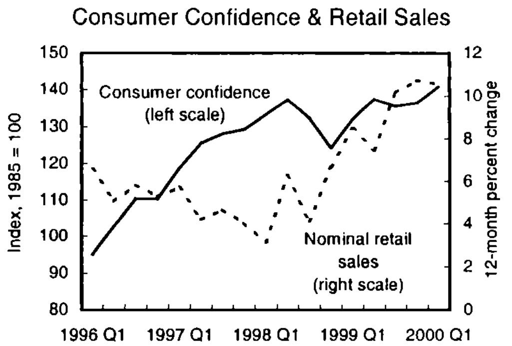
EYES ONLY

MACROECONOMIC UPDATE

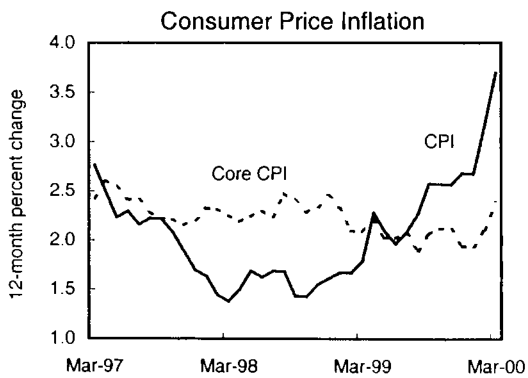
First Quarter Looks Strong

Consumption, housing, and labor market data all point to strong real GDP growth in the first quarter of 2000. Rising oil prices sent overall consumer price inflation up sharply, but a greater concern is the March pickup in core inflation.

Continued strong demand. The strong economy and a stock market up 3.5 percent over the first quarter propelled consumer confidence to an all-time high (see upper chart). Retail sales surged in the first quarter, with motor vehicles selling at a record 18.1 million unit annual pace. Real personal consumption is now projected to increase about 8 percent at an annual rate in the first quarter. Residential investment seems to have been strong, but forward-looking housing indicators point to a decline in the second quarter. It is worth noting that recent stock market declines should have little immediate effect on spending.



Supply side factors. Production worker hours increased about 3 percent at an annual rate in the first quarter. Together with the spending data, the hours data point to first-quarter real GDP growth of about 5½ to 6½ percent at an annual rate. Labor markets remain tight, with the unemployment rate stable at 4.1 percent and 817,000 net (non-farm) jobs created. Capacity utilization inched upward for the first quarter, but remains slightly below its long-run average.



Inflation. With energy prices up sharply, CPI inflation shot up in the first quarter (see lower chart). Core-CPI inflation rose sharply in March and was 2.4 percent over the last 12 months, well above the 1.9 percent rate of 1999. It remains to be seen if the March jump is just a one-time event or if continued higher core inflation is on the horizon.

EYES ONLY

SPECIAL ANALYSIS

Why Isn't Japan a New Economy Too?

The Japanese economy sputtered through most of the 1990s, hobbled by weak consumer and business demand and severe financial sector crises. At the same time, the supply side of the economy has worsened: Structural unemployment has risen and productivity growth has slowed. As a result, estimated potential output growth has fallen from nearly 4 percent per year in the 1980s to about 2 percent in the 1990s. These developments are mirror images of those in the United States.

Rising NAIRU. The OECD estimates that Japan's NAIRU rose 1.2 percentage points to 3.7 percent during the 1990s. In contrast, the OECD estimates that the NAIRU in the United States declined 0.4 percentage point to about 5.4 percent. One explanation for the rise in Japan's NAIRU is increased mismatch between worker skills and job requirements, especially among older workers. Moreover, labor markets in Japan can be more rigid than in the United States, a problem that may have been masked during the high growth decades, but has manifested itself in a weak economy.

Productivity slowdown. Productivity growth in Japan slowed markedly in the 1990s. Average annual growth in GDP per employed person fell by 2.4 percentage points relative to the preceding two decades. Cyclical effects and shorter work hours may explain some of this decline. Reduction in the pace of capital accumulation, however, accounts for more than half (1.3 percentage points) of the decline in productivity growth. Moreover, with business investment weak, Japan's capital stock is getting older and falling behind cutting-edge technologies, further reducing productivity growth.

A report by Japan's Economic Planning Agency cites a number of factors that help explain the slowdown in the rate of capital accumulation. First, the high-flying Japanese economy and stock market of the late 1980s may have lead to overly optimistic business plans and excessive capacity build-up. After the stock market bubble burst in 1990 and the economy cooled, investment slowed as businesses sought to reduce capacity. Second, weak corporate profits, stagnant stock prices, the collapse of major financial institutions, and a reluctance to provide business loans reduced funds for investment in the 1990s. These developments stand in stark contrast to those in the United States, where investment—especially in the technology sectors—was strong during the late 1990s and labor productivity surged.

Prospects and policies for the future. Some of the deterioration in Japan's potential output growth may prove transitory. For example, the pace of capital accumulation should eventually return to normal levels. Although it is difficult to differentiate cyclical developments from longer-run trends, the evidence suggests that potential output growth declined significantly in the 1990s and that fundamental problems remain. A number of economic policies could help

EYES ONLY

improve the outlook for Japan's economy. First, it is important for Japan to use coordinated monetary and fiscal policy to stimulate demand and improve consumer and business confidence. Second, structural reforms including deregulation of product markets and reform of financial markets are needed to add greater flexibility to Japan's economy and increase productivity.

EYES ONLY

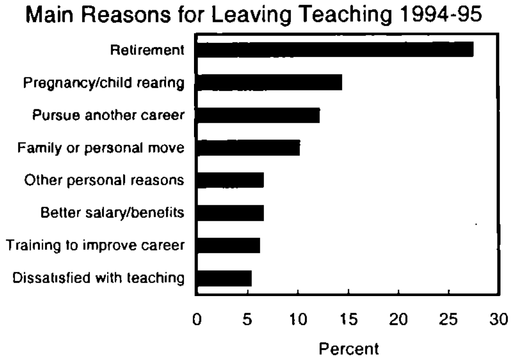
ARTICLE

Encouraging Teachers to Stay

The Department of Education estimates that between 1.7 and 2.7 million new public school teachers will be needed between 1998 and 2008. About 750,000 of these recruits will replace retiring teachers, while about 200,000 will fill new spots in expanding school districts. The remainder of new recruits will replace teachers who leave the profession for reasons other than retirement. How can schools minimize turnover and recruitment costs and boost teacher job satisfaction? Evidence points to good working conditions and competitive wages as key factors.

Reasons for leaving. About 6 percent of public school teachers leave their profession each year. Retirement and family decisions are among the leading reasons why teachers left the profession in 1994-95, according to national survey data (see chart). Other reasons, however, are more likely related to working conditions and compensation, including "to pursue another career," "for better pay or benefits," and "dissatisfaction with teaching as a career."

Main Reasons for Leaving Teaching 1994-95



Satisfaction not guaranteed. For the 20 percent of respondents who cited "dissatisfaction with teaching as a career" as one of their *three* main reasons for leaving the profession, the survey asked respondents to identify their main area of dissatisfaction. Many of the answers relate to working conditions. The most frequently cited areas were a lack of recognition or support from the school administration (29 percent), student discipline problems (18 percent), poor student motivation to learn (18 percent), and poor salary (11 percent). A different study on what matters for job satisfaction among current teachers finds a similar ranking. In addition, it concludes that factors difficult to change, such as school size, minority enrollment, teacher race or gender, or years of teaching experience are only weakly related to job satisfaction. The statistical analysis also suggests that compensation makes only a small contribution to job satisfaction.

Money matters. Although pay does not appear to be the dominant factor in whether teachers like their jobs, it seems to have a more pronounced effect on their decision to stay in the profession. For example, over half of teachers in a 1994 national survey reported that providing higher pay would be the most effective way to encourage teachers to remain in the field. Economic research has also found a significant negative relationship between higher pay and turnover rates.

Conclusion. A sizable portion of teachers leave the profession for reasons related to working conditions and pay. Efforts by school leaders to improve these areas would encourage more teachers to stay in the field and lessen the need for costly recruitment.

Are Teacher Salaries Competitive?

According to a 1998 survey of the nation's 200 largest school districts, more than two-thirds of respondents reported an insufficient supply of teacher applicants. It is difficult to determine the extent to which these reported shortages reflect the effects of low teacher pay or generally tight labor markets.

Comparing the salaries of teachers and other groups provides one indicator of the competitiveness of teacher pay. For new teachers, the average salary ($25,600) was 25 percent less than the average for all recent college graduates ($34,199), according to a 1997 survey. The data suggest, however, that this gap in pay shrinks considerably among older teachers. Additionally, these salary comparisons ignore differences in job characteristics such as summer vacations.

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Go to the Doctor! A large proportion of American men have only limited contact with the health care system, according to a recent study. Many men fail to get routine checkups, preventive care, or health counseling. Moreover, they often ignore symptoms or delay seeking medical attention when sick or in pain. One quarter of American men did not see a physician in the year prior to the survey (three times the rate for women) and a third did not have a regular doctor, compared with a fifth of women. Men's irregular contact with doctors means they often do not receive any preventive care or screening for potentially life-threatening conditions. Lack of health insurance exacerbates the problem; uninsured men are at more than three times the risk for not getting needed health services and basic primary care.

Professors' Salaries Lag Further Behind. Real salaries of full-time college and university teachers increased an average of about one-half percent per year, since 1990, a pace well below that of other highly skilled occupations. Whereas faculty earned about 14 percent less than other highly educated workers in 1985, by 1997 this gap nearly doubled to roughly 24 percent. Academics worry that this growing gap will cause future generations of top students to pass over academic careers in favor of more lucrative ones, to the detriment of higher education in this country. Differences also exist within the profession; in particular, the study notes a gender pay gap. This differential appears to be partly explained by women disproportionately working in lower-status appointments or lower paid disciplines (humanities vs. natural sciences) or spending more time in teaching and university service than research.

Civic Participation, Poverty, and Race. Involvement in civic organizations, such as neighborhood associations, church groups, PTAs, or cultural groups, is not only likely to enhance social trust in society but may establish and reinforce norms in communities that mitigate the negative consequences of living in isolated poor communities. A recent study examined the effect of neighborhood poverty and race on participation in such organizations. Individuals who live in neighborhoods with high poverty rates belong to fewer organizations. Controlling for neighborhood poverty, however, African Americans participate in more organizations than whites. Moreover, civic participation by African Americans is stronger when they live in neighborhoods with other African Americans. This finding supports the theory that heightened ethnic consciousness, resulting from socio-economic disadvantages in society, might lead blacks to participate more than other groups, particularly in organizations designed to improve society.

EYES ONLY

INTERNATIONAL ROUNDUP

Famine Alert for Horn of Africa. The Food and Agriculture Organization issued a dire famine warning for the Horn of Africa this week, stating that the region needs urgent and adequate food assistance to stave off famine and mass starvation threatening about 16 million people, half in Ethiopia. The situation is also very severe in parts of Kenya, Somalia, and Uganda, according to the report. Armed conflicts in the region and the recent drought contributed to the current crisis. Cereal import requirements are expected to reach a record 6 million tons in 1999/2000, almost double the amount imported in the previous year and more than 30 percent higher than in 1984/1985, a major famine and drought year. Food aid requirements for 1999/2000 in the area have risen sharply and are currently estimated at about 2 million tons, more than double last year's volume and the highest level for the past 15 years. 1.4 million metric tons of food aid have been requested in international appeals; the United States plans to supply about half of the total request.

Anti-Dumping Claims Surge in 1999. The number of anti-dumping investigations initiated worldwide rose to a record 328 in 1999, up 41 percent from 1998 and 110 percent from 1995, according to a new study. The European Community was the largest instigator of anti-dumping cases last year, opening 65 cases, followed by India (60) and the United States (45). China continued to be the primary target, with 39 cases brought against it. Chemicals and steel were the most frequent industries for anti-dumping investigations, accounting respectively for 31 percent and 28 percent of total cases in 1999. The recent increase in cases may be partly attributable to weak global economic conditions following the Asian financial crisis. The study reports that the last decade has seen a shift away from traditional initiators of anti-dumping investigations (the EC, United States, Australia, and Canada). Between 1985 and 1989 these four accounted for 90 percent of all cases opened, whereas by 1999 the proportion fell to 46 percent, reflecting the increased use of anti-dumping measures by South Africa, India, Brazil, Mexico, and Argentina.

Threats to World's Ecosystems. A joint report by the U.N. Development Programme, the U.N. Environment Programme, the World Bank, and the World Resources Institute indicates that most of the world's ecosystems are in fair, but declining conditions. The report analyzes ecosystem health in terms of its ability to produce sufficient quantities of basic goods and service such as food and clean water, storage of atmospheric carbon, and maintenance of biodiversity. Soil degradation, which already has affected two-thirds of the world's agricultural land, may impair future food production. It also warns that overfishing and destruction of habitats have reduced the productive capacity of coastal ecosystems, with nearly 70 percent of the world's major marine fish stocks overfished or fished at their biological limit. In addition, forest area has declined almost 10 percent in developing countries since 1980.

EYES ONLY

RELEASES THIS WEEK

U.S. International Trade in Goods and Services

The goods and services trade deficit increased to $29.2 billion in February from $27.4 billion in January.

Housing Starts

Housing starts fell 11 percent in March to 1.604 million units at an annual rate.

MAJOR RELEASES NEXT WEEK

Consumer Confidence—The Conference Board (Tuesday)
Advance Durable Shipments and Orders (Wednesday)
Gross Domestic Product (Thursday)
Employment Cost Index (Thursday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	1999	1999:2	1999:3	1999:4
Percent growth (annual rate)					
Real GDP (chain-type)	2.9	4.6	1.9	5.7	7.3
GDP chain-type price index	5.2	1.6	1.3	1.1	2.0
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.6	0.6	5.0	6.4
Real compensation per hour:					
Using CPI	1.0	1.7	1.4	2.1	0.8
Using NFB deflator	1.5	3.0	2.9	4.0	2.1
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.6	12.7	12.5
Residential investment	4.5	4.4	4.5	4.4	4.4
Exports	8.2	10.8	10.7	10.8	10.9
Imports	9.2	13.5	13.4	13.8	14.0
Personal saving	6.6	1.7	1.8	1.5	1.3
Federal surplus	-2.8	1.2	1.3	1.4	1.2

	1970-1993	1999	January 2000	February 2000	March 2000
Unemployment Rate (percent)	6.7**	4.2**	4.0	4.1	4.1
Payroll employment (thousands)					
increase per month			394	7	416
increase since Jan. 1993					21213
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.5	0.7
PPI-Finished goods	5.0	3.0	0.0	1.0	1.0

**Figures beginning 1994 are not comparable with earlier data.

EYES ONLY

FINANCIAL STATISTICS

	1998	1999	February 2000	March 2000	April 20, 2000
Dow-Jones Industrial Average	8626	10465	10542	10483	10844
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.55	5.69	5.63
10-year T-bond	5.26	5.65	6.52	6.26	5.99
Mortgage rate, 30-year fixed	6.94	7.43	8.33	8.24	8.16
Prime rate	8.35	8.00	8.73	8.83	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level April 20, 2000**	**Percent Change from**	
		Week ago	**Year ago**
Euro (in U.S. dollars)	0.938	-1.6	-11.8
Yen (per U.S. dollar)	105.5	-0.3	-10.8
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	96.62	0.7	1.5

International Comparisons [1]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	4.6 (Q4)	4.1 (Mar)	3.7 (Mar)
Canada	4.7 (Q4)	6.8 (Feb)	2.7 (Feb)
Japan	0.0 (Q4)	4.9 (Feb)	-0.6 (Feb)
France	3.2 (Q4)	10.0 (Feb)	1.4 (Feb)
Germany	2.3 (Q4)	8.6 (Feb)	1.8 (Feb)
Italy	2.1 (Q4)	11.2 (Jan) [2]	2.4 (Feb)
United Kingdom	3.0 (Q4)	5.9 (Dec)	2.3 (Feb)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.
2/ Data from OECD standardized unemployment rates.

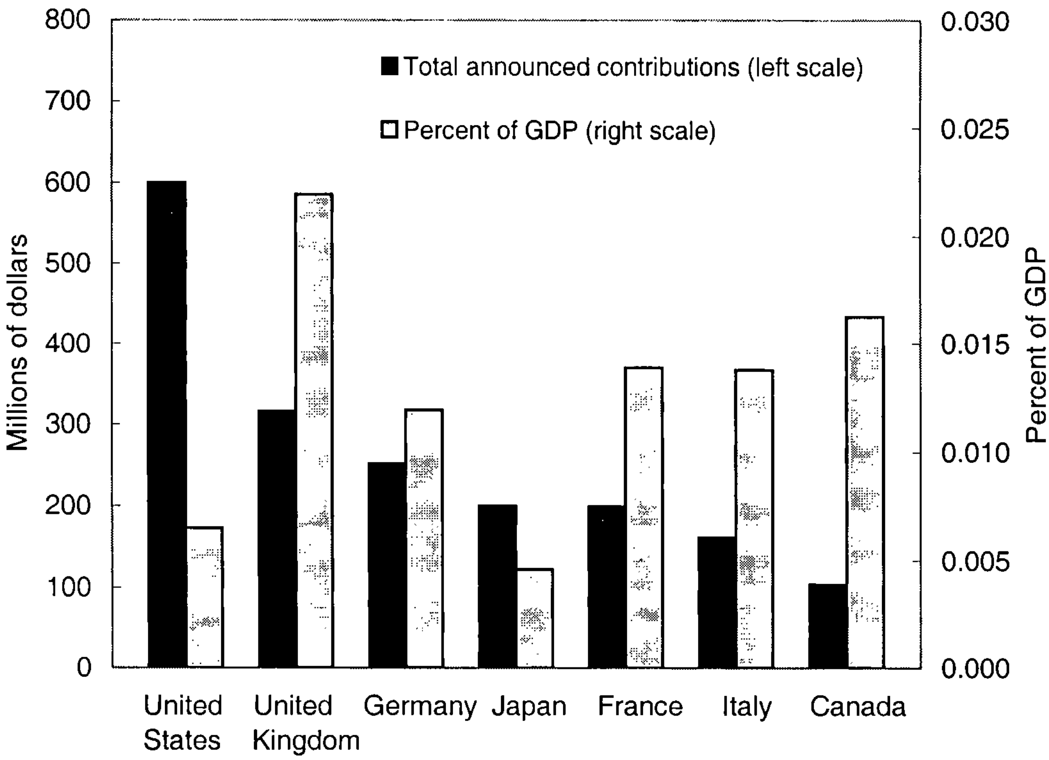
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

April 14, 2000

CHART OF THE WEEK

G-7 Announced Contributions to HIPC Trust Fund



The Heavily Indebted Poor Countries (HIPC) Trust Fund is seeking $3.6 billion of external support for regional multinational development banks that are unable to pay their share of the $28 billion enhanced HIPC Initiative. Thus far $329 million in contributions have been received from 16 countries, and 26 countries have pledged almost $2 billion more. The largest donors to the Trust Fund are the G-7 and the Netherlands. Some countries have conditioned pledges or additional new funding on a U.S. contribution.

CONTENTS

SPECIAL ANALYSES

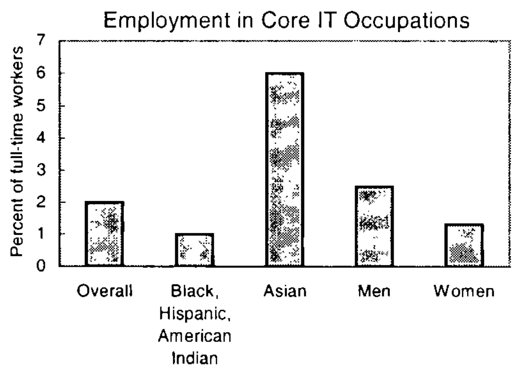
ARTICLE

DEPARTMENTS

SPECIAL ANALYSIS

The Digital Divide in IT Employment

Employment in core information technology (IT) jobs such as computer systems analysts, computer scientists, and computer programmers has doubled over the last decade, reaching 2.2 million workers in 1999. The CEA estimates that median wages are about 80 percent higher than in the non-IT sector. An expanding and well-paid field, IT can offer substantial opportunity for those with appropriate skills. But employment patterns by race/ethnicity and gender reveal another facet of the digital divide.



Minority and female representation. CEA calculations find that employment in core IT occupations represents about 2 percent of the full-time workforce (see chart). For whites, the percentage is slightly higher, while only about 1 percent of African Americans and less than 1 percent of Hispanics hold core IT jobs. Women are only half as likely as men to be employed in these occupations.

Educational attainment. Two-thirds of full-time core IT workers have a bachelor's degree or more, hence differences in educational attainment might help explain these differences in IT employment. For African Americans with a bachelor's degree who work full time, there is no employment gap: the proportion of such workers in core IT occupations is about 4¼ percent, the same as that of comparable non-Hispanic whites. In contrast, even among those with BA/BS degrees, Asians are still about three times as likely to work in IT as non-Hispanic whites. Women with a bachelor's degree are employed at half the rate as men with bachelor's degrees. Evidence for Hispanics is mixed, but having a bachelor's degree does not appear to eliminate the IT employment gap.

What's your major? About two-thirds of core IT workers with a bachelor's degree have a science, mathematics, or engineering background. Thus, the choice of major is a key determinant of subsequent IT employment. Data from a National Science Foundation survey of college graduates indicate that African Americans and Hispanics earn degrees in science and engineering at the same rate as whites. Thus, their low representation in IT employment would seem to reflect lower rates of college attendance, not choice of major once in college. The situation is different for women, who earn more than half of all bachelor's degrees but are much less likely than men to graduate with science or engineering degrees.

Earnings. While much of the under-representation of minorities in core IT jobs appears to be related to educational differences, the variation in earnings in core

IT jobs is substantial even when education is held constant. Although small sample sizes in the available data make it difficult to reach definitive conclusions, African Americans with a bachelor's degree or greater appear to earn substantially less in IT jobs than other racial groups with the same educational attainment. Women, for whom there are more data, earn about 15 percent less than men in core IT occupations after controlling for education. These gender earnings differences exist even though age and hours of work are similar for men and women in core-IT jobs. Race and gender pay gaps may arise because women and African Americans are disproportionately represented in lower-paying sub-occupations.

Conclusion. Employment and earnings differences by race and gender in IT jobs reveal yet another dimension of the digital divide. While educational attainment and choice of major are key factors in explaining these differences, they do not tell the full story.

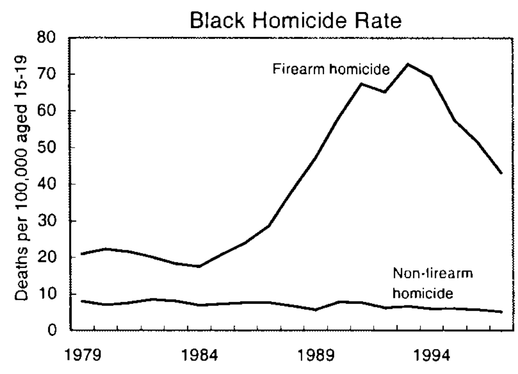
SPECIAL ANALYSIS

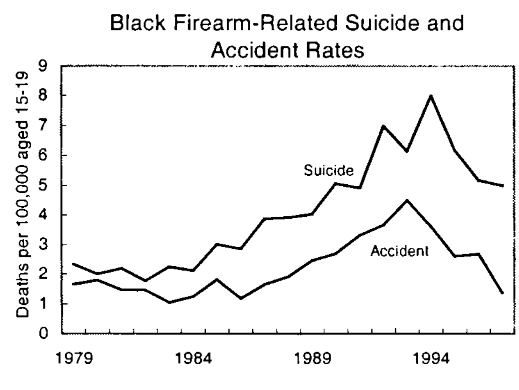
Guns and Teen Violence

Recent trends showing declining teen suicide and homicide victimization are encouraging. Nevertheless, the harmful effects of the proliferation of guns in the mid-1980s remain evident. New evidence focused on African American teenagers is instructive.

The crack connection. Crack cocaine first arrived in large cities like Miami, Los Angeles, and New York around 1983. A large number of youth, especially African American teenagers, were drawn into the crack trade. After remaining fairly constant from 1975 through 1984, drug arrest rates among non-white juveniles more than doubled between 1985 and 1989. Social scientists have hypothesized that a distressing by-product of the rapid growth in crack trade was the dissemination of guns into the hands of many American teenagers, African Americans in particular. The nucleus of the diffusion process was gun possession by teens directly involved in drug markets, but possession became far broader as other teens acquired guns in reaction to this trend—for perceived self-protection or as a status symbol. (One 1993 study conducted in center-city schools found that 22 percent of students possessed guns, with 68 percent citing protection as the main reason.)

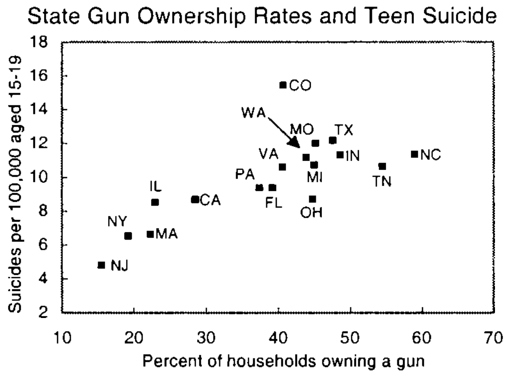
Gun homicide. The apparent increase in teenage gun possession in the mid-1980s has been suggested as a factor in several trends, the most disturbing of which is the rapid rise in deaths among African American teens due to gun homicide (see upper chart). There are two competing explanations for the sharp rise in homicides. First, the rise in gun possession may have directly increased the lethality of confrontations among teens. Second, there may simply have been an increase in teens' inclination toward violence. Indeed both factors may have been at work, but if the latter explanation were the predominant influence, we might expect to observe an increase in both gun and non-gun homicide. In fact, non-gun homicide victimization among African American teens remained roughly constant through the 1980s.





Fatal gun accidents. The underlying premise that more guns were finding their way into the hands of African American teens in the mid-1980s is supported by trends in deaths from gun accidents. The rate of fatal gun accidents was more than four times as high in 1993 as in 1983 (see lower chart on previous page).

Gun suicide. The proliferation of guns also likely played a key role in suicides among African American teens. While the rate of gun suicides increased rapidly in the mid-1980s, the non-gun suicide rate remained fairly constant for this group. The idea that gun access directly leads to increasing suicide is also supported by a cross-state analysis of suicide rates among teens generally. In states where more households have guns, overall teen suicide rates are much higher (see chart, which presents statistics for the 17 large states for which there are data). Importantly, this relationship holds because gun-related teenage suicide is higher in states with high gun ownership; non-gun teen suicides are not correlated with gun ownership. (These results are consistent with an earlier *Weekly Economic Briefing* analysis of overall suicide rates and guns.)



Some good news in the 1990s. The spread of guns among center-city youth in the mid-1980s was likely responsible for the disastrous increases in homicide, suicide and accidental death among African American teens. By the mid-1990s gun-related death rates were declining for this demographic group, perhaps because of a decline in the levels of gun possession by more recent cohorts of teenagers. However, gun homicide and suicide rates remain relatively high, presumably because a large stock of guns remains accessible to youth. Policies that are effective in reducing the gun possession by teens should reinforce the recent downward trend in teen mortality.

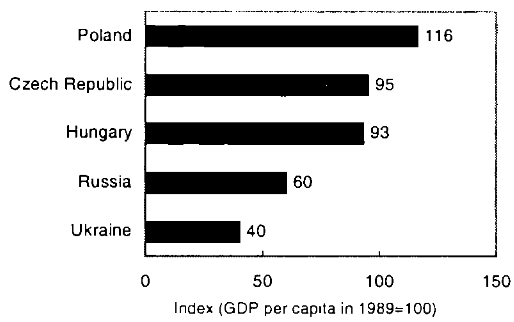
ARTICLE

Poland: Lessons in Transition

Poland has been the most successful of the transition economies in moving from a centrally planned to a market economy. A recent study by a large consulting firm explores the reasons why and points to the economic challenge Poland still faces.

Adjustment and recovery after 1989. Real GDP per capita in Poland dropped by about 18 percent between 1989 and 1991 following the implementation of market reforms. Communist-era products and services found it difficult to pass the market test following liberalization, and government spending fell. Between 1992 and 1998, however, Polish real GDP per capita grew at around 6 percent per year, reaching a level 16 percent higher than in 1989. This success contrasts sharply with other major transition economies, which have not yet regained their 1989 level (see chart).

GDP per Capita in Transition Economies in 1998



Productivity and employment. Poland's turnaround mostly reflects solid productivity growth of 5 percent per year in real GDP per worker between 1992 and 1998. Employment, by contrast, has yet to recover fully from a sharp setback following liberalization. Though down from its peak of 16 percent, the unemployment rate remains above 10 percent.

Growth in productivity resulted from increasing utilization of the industrial assets that continued to operate and from investment in new, more productive facilities. Foreign direct investment accounted for more than half of all private investment in 1998 and was crucial in boosting private investment from 5 percent of GDP in 1995 to 13 percent in 1998. Even this investment level is relatively modest, however, and the overall level of productivity remains low by advanced country standards (29 percent of the U.S. level in 1998).

Sound macroeconomic policies. In contrast to other transition economies, Poland followed sound monetary and fiscal policies. Following a surge after liberalization, inflation has gradually been brought under 10 percent. The public sector budget deficit was kept below 4 percent of GDP, which, along with strong economic growth and debt relief granted by foreign creditors, has cut the public debt-to-GDP ratio to around 50 percent.

Generally successful privatization. Poland established a successful framework for privatization and the process has been virtually completed in much of the economy. In the privatized markets, prices have been freed and competitive conditions apply. Poland has encouraged foreign investment and allowed foreign companies to purchase "key" domestic companies. This has brought in hard currency and both management and technological expertise. The successful, broad-based privatization, together with the sound macroeconomic policies, the study argues, account for Poland's strong performance relative to other transition economies.

In some sectors privatization has been delayed. In mining and steel, the government is trying to reach agreement on, and then put in place, specific restructuring programs, before selling the assets. In banking, telecom, utilities and airlines, privatization is waiting for the appropriate regulatory structures to be established. Other sectors of the economy have been privatized, but with "no layoff" provisions in force for a period of time.

Labor markets. Wage-setting institutions have evolved since 1990. Under the new system, wage bargaining takes place mainly at the firm level, under a nationwide ceiling for increases set by a commission made up of state, employer, and union representatives. Minimum wage rates are negotiated by the same three groups, and the study expressed concern that rising real minimum wages together with large payroll taxes could soon have adverse employment effects in sectors such as retail and apparel, although this has not been a serious problem so far.

Promoting competition. Although the government opened markets in much of the economy, the study identifies areas where more needs to be done. For example, 40 percent of urban dwellings are sheltered from market forces by direct and indirect subsidies. These are not allocated according to need or income and their effect is to discourage new residential housing construction. In addition, the structure of property taxes discourages local governments and private landowners from making land available for either residential or commercial development.

The challenge. Poland illustrates the dilemma faced by transition economies. Rapid liberalization, privatization, and the opening of international trade encourage efficiency, but they also force large structural adjustments. Productivity rises rapidly, but employment falls or rises only slowly, leading to unemployment or rising employment in subsistence activities. In 1997, for example, Poland had between 44 and 50 percent of its workforce (depending on data source) in agriculture and manufacturing, with a high potential for job loss in the unproductive parts of these sectors. Slowing the pace of adjustment can make sense, in order to allow new jobs to grow fast enough to absorb the job losers. But this also slows the creation of a full market economy.

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Working Together: Welfare and Workforce Development. A recent study by the Urban Institute finds that establishing closer links between welfare offices and workforce development systems (including JTPA/WIA agencies, community colleges, one-stop career centers, and private employment and training contractors) can benefit TANF recipients. Coordination and integration among these groups, it finds, allows for referrals to a wider range of services, improved case management, and the convenience of co-location. The study notes that creative approaches to assisting TANF recipients find work, including these partnerships, are being spawned by a greater availability of resources per client, the need to address multiple barriers faced by those still on the rolls, and the rapid expansion of computer technology and computer-based labor market information. In light of the tight labor market, which is increasing employer involvement, the study concludes that the current environment offers unprecedented opportunities for partnerships to help welfare clients move successfully to work.

Teacher Quality and Students' Future Earnings. Longitudinal data on the impact of teacher quality on subsequent earnings of students is relatively limited. But a new study has combined data from a Wisconsin survey of 1957 high school graduates with information about the characteristics of the school districts from which they graduated. In particular, the study found a significant relationship between a set of education and experience characteristics of high school teachers and the future earnings of male graduates 17 years later, when they were in their mid-30s. Using average teacher salary as a proxy for these characteristics and controlling for family education and income, the study found that a 1 percent increase in average teacher salary increased students' future earnings by 0.3 percent. This is over 80 times larger than the estimated effect of a comparable increase in family income.

Why Do Larger Banks Charge Higher ATM Fees? Surveys have shown that large banks charge higher ATM fees than do smaller banks. To some extent at least, these fees reflect the higher costs to the bank and greater convenience to their customers of deploying a larger network of ATMs, according to a recent study. In particular, the study found that differences in the fees that banks charge their own customers for using another bank's ATM are due to differences in cost and convenience. However, larger banks charge non-customers more for using their machines, even after controlling for the greater convenience and higher costs associated with deploying and operating a larger number of machines. This fee structure gives customers an incentive to open accounts at larger institutions with more ATMs, putting competitive pressure on middle-tier banks operating in the same market. Despite the evidence that large banks impose higher fees, the study questions the economic wisdom of bans on ATM charges. Customers can, and for the most part do, avoid paying ATM surcharges by finding machines that do not impose them; bans would limit consumer choice and probably slow the deployment of ATMs; and banks would have to find other, possibly more inefficient ways of financing ATM services.

INTERNATIONAL ROUNDUP

IMF Expects Higher World Economic Growth. World output will grow 4.2 percent in 2000, according to the IMF's latest *World Economic Outlook*. This is 0.8 percentage point higher than in the IMF's October forecast and would mark a significant increase over growth rates of 3.3 percent in 1999 and 2.5 percent in 1998. Despite its optimistic forecast, the IMF points to a number of imbalances that have been building in the world economy, noting that the large U.S. current account deficit combined with persistent surpluses in Japan and the euro area are unlikely to be sustainable. The IMF argues that the large capital inflows into the United States have made the dollar too strong relative to the euro given medium-term fundamentals, which creates the risk of disruptive exchange rate adjustments if market sentiment changes suddenly. The report cautions that world stock markets may be overvalued, due in part to the ample growth in liquidity over the last few years needed to overcome the effects of financial crises in Asia, Russia, and Latin America. In order to secure a transition to a sustainable pattern of global growth, the IMF stresses the need to contain excess demand pressures in the United States while promoting durable expansions in the EU and Japan.

Japan Extends Debt Relief Program. This week, Japan became the latest G-7 country to cancel all non-official development assistance (non-ODA) loans for eligible heavily indebted poor countries (HIPCs). Japan also pledged an additional $190 million to the HIPC Trust Fund (on top of the $10 million it has already contributed) and promised further provision of bilateral grant assistance. As part of the 1999 enhanced HIPC Initiative, the G-7 agreed to forgive 100 percent of ODA debts and 90 percent or more of their non-ODA claims, which include trade insurance and loans made by export-import banks, for eligible HIPC countries. Several G-7 countries have since expressed their intention to waive 100 percent of their non-ODA claims as well. As Japan is one of the largest HIPC donors, with over $10 billion of loans to the 40 HIPC countries, some see Japan's decision to follow suit as critical to the success of the HIPC Initiative.

FDI Promotes Growth in China. A recent OECD study finds that differences in rates of foreign direct investment (FDI) are particularly important in explaining differences in growth rates across Chinese provinces since the mid-1980s. These results help explain why coastal regions of China have grown much faster than central or western regions, since they have attracted the lion's share of foreign investment (88 percent in 1996, for example). The positive effect of FDI on growth is stronger when the average level of schooling of the population is higher, suggesting that FDI and education are complementary. Interestingly, the study finds that differences in export growth have little *direct* impact on differences in output growth rates. Instead, openness to trade contributes to output growth primarily by helping attract FDI. In addition, FDI is higher in provinces with high incomes, high growth rates, and better transportation infrastructure. The study recommends that to achieve more balanced growth, China should encourage FDI in the inland provinces by introducing preferential measures to attract FDI, providing better infrastructure, and improving education.

RELEASES THIS WEEK

Industrial Production and Capacity Utilization
****Embargoed until 9:15 a.m., Friday, April 14, 2000****

The Federal Reserve's index of industrial production increased 0.3 percent in March. Capacity utilization fell 0.1 percentage point to 81.4 percent.

Consumer Price Index
****Embargoed until 8:30 a.m., Friday, April 14, 2000****

The consumer price index rose 0.7 percent in March. Excluding food and energy, consumer prices rose 0.4 percent.

Producer Price Index

The producer price index for finished goods rose 1.0 percent in March. Excluding food and energy, producer prices rose 0.1 percent.

Retail Sales

Advance estimates show that retail sales increased 0.4 percent in March following an increase of 1.8 percent in February. Excluding sales in the automotive group, retail sales rose 1.4 percent following an increase of 1.8 percent.

MAJOR RELEASES NEXT WEEK

Housing Starts (Tuesday)
U.S. International Trade in Goods and Services (Wednesday)

U.S. ECONOMIC STATISTICS

	1970-1993	1999	1999:2	1999:3	1999:4
Percent growth (annual rate)					
Real GDP (chain-type)	2.9	4.6	1.9	5.7	7.3
GDP chain-type price index	5.2	1.6	1.3	1.1	2.0
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.6	0.6	5.0	6.4
Real compensation per hour:					
Using CPI	1.0	1.7	1.4	2.1	0.8
Using NFB deflator	1.5	3.0	2.9	4.0	2.1
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.6	12.7	12.5
Residential investment	4.5	4.4	4.5	4.4	4.4
Exports	8.2	10.8	10.7	10.8	10.9
Imports	9.2	13.5	13.4	13.8	14.0
Personal saving	6.6	1.7	1.8	1.5	1.3
Federal surplus	-2.8	1.2	1.3	1.4	1.2

	1970-1993	1999	January 2000	February 2000	March 2000
Unemployment Rate (percent)	6.7**	4.2**	4.0	4.1	4.1
Payroll employment (thousands)					
increase per month			394	7	416
increase since Jan. 1993					21213
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.5	**0.7**
PPI-Finished goods	5.0	3.0	0.0	1.0	**1.0**

**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.
CPI data **embargoed until 8:30 a.m., Friday, April 14, 2000**.

FINANCIAL STATISTICS

	1998	1999	February 2000	March 2000	April 13, 2000
Dow-Jones Industrial Average	8626	10465	10542	10483	10924
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.55	5.69	5.65
10-year T-bond	5.26	5.65	6.52	6.26	5.94
Mortgage rate, 30-year fixed	6.94	7.43	8.33	8.24	8.12
Prime rate	8.35	8.00	8.73	8.83	9.00

INTERNATIONAL STATISTICS

Exchange Rates	Current level April 13, 2000	Percent Change from Week ago	Year ago
Euro (in U.S. dollars)	0.952	-0.6	-11.7
Yen (per U.S. dollar)	105.8	0.9	-11.9
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	95.99	0.7	1.0

International Comparisons [1]	Real GDP growth (percent change last 4 quarters)	Unemployment rate (percent)	CPI inflation (percent change in index last 12 months)
United States	4.6 (Q4)	4.1 (Mar)	**3.7** (Mar)
Canada	4.7 (Q4)	6.8 (Feb)	2.7 (Feb)
Japan	0.0 (Q4)	4.9 (Feb)	-0.6 (Feb)
France	3.2 (Q4)	10.0 (Feb)	1.4 (Feb)
Germany	2.3 (Q4)	8.6 (Feb)	1.8 (Feb)
Italy	2.1 (Q4)	11.2 (Jan) [2]	2.4 (Feb)
United Kingdom	3.0 (Q4)	5.9 (Dec)	2.3 (Feb)

U.S. CPI data **embargoed until 8:30 a.m., Friday, April 14, 2000.**

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.

2/ Data from OECD standardized unemployment rates.

EYES ONLY

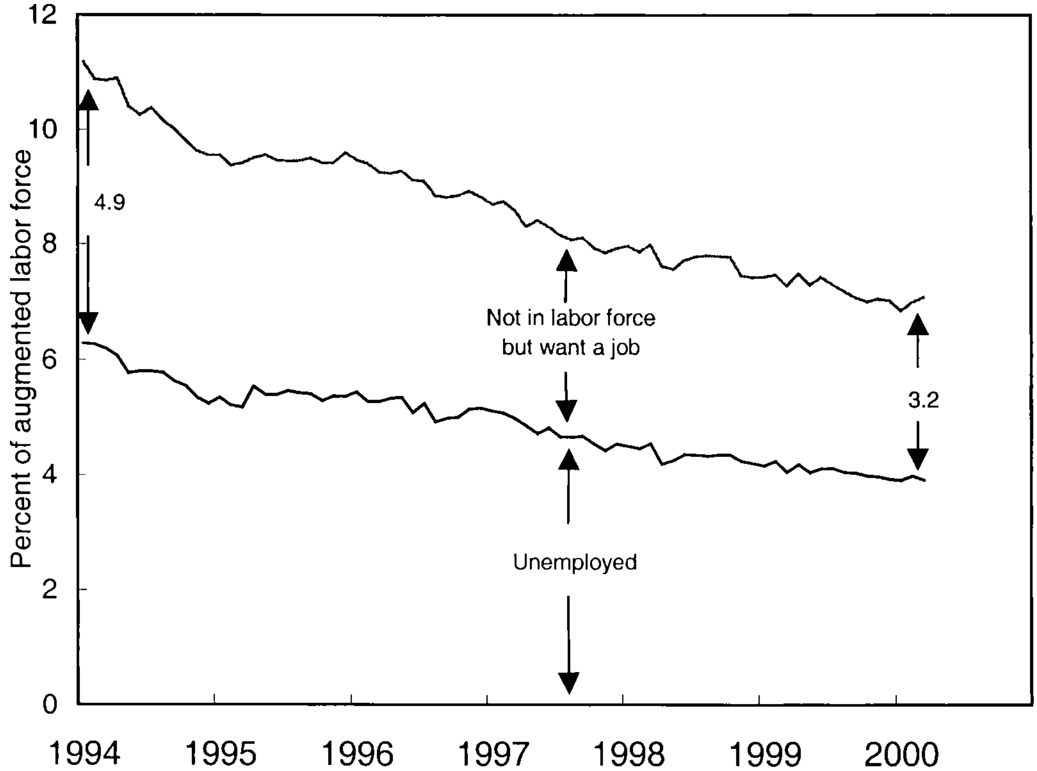
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

April 7, 2000

CHART OF THE WEEK

The Pool of Potential Workers



As Federal Reserve Chairman Greenspan noted again this week in his remarks at the White House conference, overall demand for goods and services has outpaced potential supply over the past 4 years. An increasing share of this extra demand has been met by rising net imports and the rest has been met by drawing down the pool of potential workers, which includes not just the officially unemployed but also those who are not in the labor force (because they did not actively seek work) but say they want a job.

EYES ONLY

CONTENTS

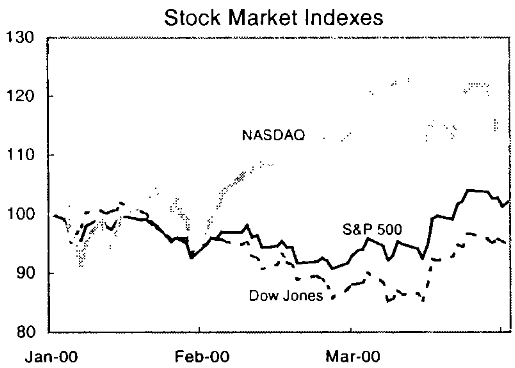
"THIS MUST BE THAT STRANGE CREATURE THEY MENTIONED IN HISTORY CLASS"

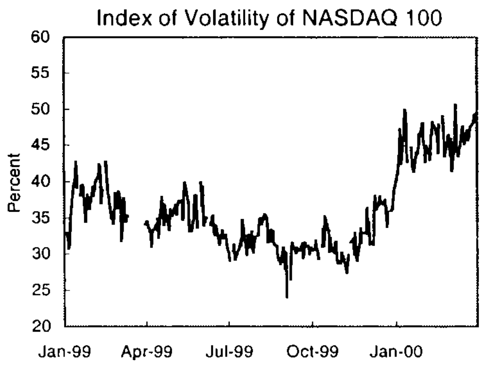
EYES ONLY

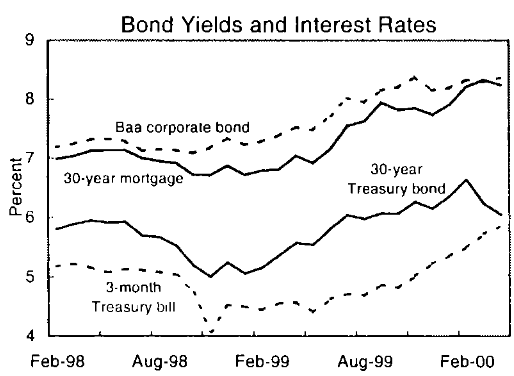
FINANCIAL MARKET UPDATE

First Quarter 2000

Although technology stocks again outperformed the overall market during the first quarter of 2000, a sharp decline at the end of March foreshadowed turmoil this week. Tightening by the Federal Reserve led to generally higher interest rates and borrowing costs, but long-term Treasuries behaved idiosyncratically.







March madness. The NASDAQ Composite Index recorded a solid 12.4 percent gain in the first quarter—though it finished 9 percent below its mid-March peak (see upper chart). The Dow Jones and the S&P 500 showed an opposite pattern, first sinking and then recovering. These gyrations may have prompted a reassessment of the risk associated with investing in the technology sector, with one measure of NASDAQ volatility showing a distinct increase after a year of stability (see middle chart).

Interest rates. The Fed raised its target lending rate 25 basis points in both February and March. At 6 percent, the federal funds target is at its highest level since June 1995. With the Fed continuing to express concern about inflationary pressures, markets expect another 25-basis-point increase in May and a 6.75 percent federal funds rate by year's end. Both mortgage rates and corporate bond yields climbed in the first quarter (see lower chart), raising borrowing costs of businesses and households. Yields on long-term government securities went down—perhaps reflecting supply constraints associated with the fiscal surplus.

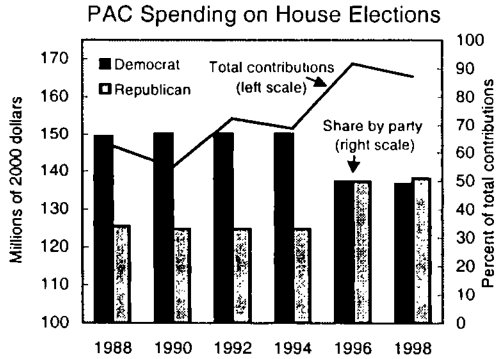
Volatility continues. The role reversal that began to emerge in late March has continued this week with the "old-economy" indexes inching upward and the NASDAQ down about 7 percent. Although the NASDAQ is still up 5 percent for the year, the short-term outlook for technology stocks seems to have become more uncertain.

SPECIAL ANALYSIS

The Political Economy of Campaign Financing

Federal Election Commission data show that direct political action committee (PAC) contributions to House candidates over the last four federal election cycles represented almost one-third of all funds raised by these candidates. As total election spending has increased, the total dollar amount of PAC contributions has risen. For House candidates, total PAC contributions increased by 13 percent in real terms between the 1988 and 1998 election cycles (see chart). Incumbent candidates received the largest share of these contributions, and when the House switched from Democratic to Republican control following the 1994 election, PAC contributions changed as well.

PAC Spending on House Elections



A statistical analysis of PAC contributions. A recent study examined some of the factors that may motivate repeated PAC contributions to candidates across different election cycles. Looking at incumbent members of the House, the study found that after controlling for other factors, the number of PACs that repeatedly gave to candidates over different election cycles declined as the candidates' margin of victory in the last election increased. This effect could be due to either less fund raising by the candidate (because her seat is relatively safe) or fewer contributions by PACs (because they believe they have less influence with candidates in such districts). The study also found that repeated giving by PACs increased significantly as seniority on congressional committees increased, over and above any increase attributable to greater tenure in the House or the effect of being chairman of a committee. As the probability that a Congressman will retire increases, however, the study found that repeat giving by PACs declines sharply.

Reputation effects and PAC contributions. The authors of the study interpret the increase in repeat giving that is associated with greater committee seniority as the outcome of a reputation-building process. Organized interest groups initially may be uncertain about what policies legislators will support when they first arrive on Capitol Hill. As legislators define their positions more clearly over time by working on issues in committees, PACs that favor those issues are more likely to support candidates who represent their interests with repeated contributions. As the probability of retirement increases, however, the repeated interactions required to sustain this outcome become attenuated. PACs may see fewer long-run benefits from contributing to a lawmaker nearing retirement, and lawmakers may decide to support policy positions that some of their contributing constituents may oppose.

Conclusion. This analysis suggests that politicians' reputations affect PAC giving. Implications for campaign finance reform are less clear, though one provocative proposal seeks to separate financial support for positions from possibility that large donors might unduly influence the political process (see box).

Donor Anonymity: an Alternative Approach to Campaign Finance Reform

Concern about the ability of large donors to influence the political process unduly has prompted campaign finance reform proposals that involve limitations on the overall amount that any one donor can contribute to a campaign, as well as requirements that contributions be publicly disclosed. Another approach suggested in a 1998 law review article, however, is to require that all contributions above a certain (low) threshold be made to a blind trust so that the candidate knows how much is available to spend, but not who has given the money. Attendees at a political fundraising dinner, for example, could be asked to pay for the cost of their meal, but would mail checks containing contributions to the trust. With donor anonymity, contributors motivated by a desire to support a particular person because of his views would still be able to do so, but contributors motivated by a belief that their contribution would "buy" future access would be deterred. Such individuals would be indistinguishable from others who simply claimed to make large donations, because the candidate has no knowledge of who has actually contributed to the campaign.

EYES ONLY

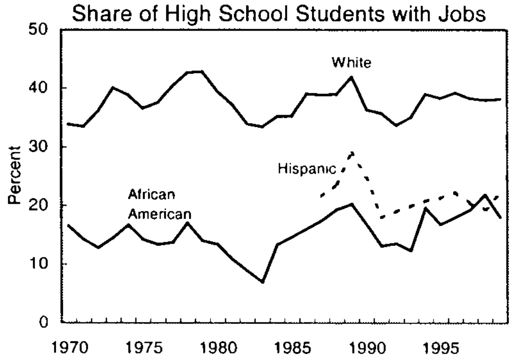
ARTICLE

Working While in School: Are There Net Benefits?

A substantial fraction of today's youth combine school with a job. Working may provide important lessons for young people about responsibility, punctuality, dealing with people, and money management, while increasing self-esteem and independence. In turn, these traits may lead to increased rates of employment and higher wages in the years following high school. However, work may also conflict with schooling by taking away time from other valuable activities, such as studying and sleeping.

Background. Approximately 3.3 million young people (aged 16-24) are both enrolled in high school and employed in the labor market. This figure represents about a third of the 9.9 million high school students in that age group. Of those employed, only about 6 percent report working full-time. While employment rates have been fairly constant over time, there are fairly substantial differences between racial and ethnic groups (see chart). Part of these differences may be explained by the differences in unemployment across the groups. The unemployment rate for white youths who are enrolled in high school is currently 13.4 percent. The rate for African Americans and Hispanics is about 24 percent. When high school students are interviewed directly, about 80 percent report that they have held a job at some point during their junior or senior years of high school. Half of all working 15- to 17-year olds have jobs in the retail sector (restaurants, fast-food outlets, grocery stores, and other retail stores).

Share of High School Students with Jobs



Costs and benefits. Researchers have examined the effect of work on a number of outcomes. The direct effect of high school employment is difficult to identify because the decision to work is correlated with many other observed and unobserved factors. For example, factors such as motivation, work effort, and parental support may be associated with both the decision to work as a teenager and subsequent educational and employment outcomes. Nonetheless, a few conclusions from the literature seem to be emerging.

- Subsequent educational attainment. There is little consensus among researchers about the effect of working while in school on subsequent educational attainment, as measured by school performance (grades), grade completion, and persistence in school. However, a number of studies have found that if harmful effects exist, they result from working many hours per week. One recent study that controls for unobserved factors found that extensive employment during the school year had a negative impact on academic performance, especially that of racial minorities.

- Vocational development and occupational attainment. Researchers have found that students who work in school also tend to have greater future job market success, as measured by better employment prospects or higher wages. However, a recent study that carefully controls for the complicated selection issues found that the future economic returns to working in school (both high school and college) are probably more modest than those found in previous research.

- Health and safety. It has been estimated that each year about 100,000 young people seek treatment in hospital emergency departments for work-related injuries. The rate of injury per hour worked appears almost twice as high for children and adolescents as for adults—about 4.9 injured per 100 full-time equivalent workers among adolescents, compared with 2.8 for all workers. The most common nonfatal injuries observed among working young people are lacerations, sprains and strains, contusions, burns, and fractures.

Moderation is key. While the general evidence is mixed, one clear lesson is that young people who work while in school should do so in moderation. (Evidence suggests that summer employment does not carry the same potential for detrimental impact as does work during the school year.) Health and safety issues are also an important concern.

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

New DOE Forecast Sees Gasoline Price Moderation. This week the Department of Energy released a new energy forecast with gasoline prices through 2000 estimated to be 6 cents per gallon lower than in last month's forecast. Regular unleaded gasoline prices are expected to fall from a peak this month of just over $1.50 per gallon. For the summer driving season, they are expected to average $1.46 per gallon (nearly 30 cents per gallon higher than last summer). Prices are projected to average $1.33 per gallon in the last 3 months of the year. The fall in prices reflects the recent OPEC production agreement. However, low inventories and lower imports may slow the fall in gasoline prices. Gasoline stocks are at the low end of the normal supply range and imports are down in part because some foreign refiners may not be able to meet new environmental standards for gasoline. While imports and stocks usually buffer gasoline prices from refinery outages, a disruption in refinery output this spring or summer could have a larger effect on gasoline prices than in the past.

Economic Factors Can Affect Teen Pregnancy Risk. Teenagers appear to weigh the costs of pregnancy and disease when making decisions about sexual activity and contraception, according to a recent study. For non-economists, teen sexual activity is often considered spontaneous and irrational, and pregnancies are viewed as "mistakes." The study found, however, that "pregnancy risk" (defined as the proportion of teen boys and girls who are sexually active and not using contraceptives) is sensitive to economic factors. According to the study, the increase in teenage employment between 1991 and 1996 decreased pregnancy risk by an estimated 5 percent. (Actual pregnancies fell by 16 percent.) The estimated effect of welfare generosity was that each 10 percent reduction in the maximum state welfare benefit level would lead to a reduced pregnancy risk of 1.2 percent for girls and 0.7 percent for boys. The study also estimated that increased AIDS incidence in a region would increase abstinence. Many effects have contributed to the recent decline in teenage birthrates, but these results indicate that a rational weighing of costs appears to have played a role.

Transportation and the Concentration of the Poor in Cities. A common explanation for why the poor are concentrated in cities in the United States is that wealthier individuals prefer to live in the suburbs where there is more land. A recent study questions this explanation, however, based on low empirical estimates of the sensitivity of the demand for land to income. The authors argue instead that public transportation is a key factor attracting the poor to cities. They report that a detailed examination of different metropolitan areas suggests a three-ring model of urban location: an interior walking ring where rich people live, a middle public transportation ring where poor people live, and an exterior car ring where rich people live. They find as well that the existence of subway systems enlarges the public transportation zone, and that income is low in this enlarged zone. Redistributive factors matter as well: the urban poor are 9.7 percentage points more likely to live in a subsidized public housing unit and 23 percent more likely to receive significant government income transfers than the suburban poor.

EYES ONLY

INTERNATIONAL ROUNDUP

World Health Day 2000 Focuses on Blood Safety. April 7 marks World Health Day 2000, dedicated to the theme of Blood Safety. Availability of blood and avoiding the transmission of infection by blood and blood products are major health safety issues confronting the global community, according to the World Health Organization (WHO). Currently the 83 percent of the world's population living in developing countries has access to only about 40 percent of the blood donated annually in the world. Each year 150,000 pregnancy-related deaths could be avoided with appropriate transfusion therapy. The blood donated in developing countries is not tested for transfusion-transmissible infection in 43 percent of cases, and up to 5 percent of HIV infections worldwide are transmitted through transfusion of contaminated blood and blood products. Through global partnerships, the WHO hopes to encourage member states to implement national blood legislation to ensure the provision of safe blood, and to promote donations from voluntary, unpaid blood donors from low-risk populations.

Bridging the Global Digital Divide. United Nations Secretary-General Annan presented his Millennium Report this week, identifying the pressing challenges faced by the global community and proposing a number of programs to be considered at the Millennium Summit in September. In addition to setting an agenda to reduce poverty and inequality, improve education, combat HIV/AIDS, and protect the environment, he proposed concrete initiatives to "build digital bridges" to help developing countries "leapfrog" the earlier stages of development via information technology. The initiatives include the establishment of 10,000 online sites in hospitals and clinics in developing countries to provide access to up-to-date medical information, and a volunteer corps to train groups in developing countries in the use of the Internet. The report also announced a new disaster response initiative, to be led by the communication company Ericsson, which will provide mobile and satellite telephones as well as microwave links for relief workers in areas affected by natural disasters and emergencies.

Better Governance Could Combat Poverty. Effective governance is often the missing link between anti-poverty efforts and poverty reduction in poor countries, according to a new report by the UN Development Program. The report advocates shifting decisionmaking power closer to poor communities by devolving authority and resources to local governments. However, this decentralization needs to be complemented by strengthening and increasing the accountability of local governments and fostering civic participation by the poor. The report stresses that resources for the poor should be directed toward helping them build their own organizational capacity rather than toward the social safety net. In Ghana, for example, 5 percent of the national budget is now allocated to local districts, which must use 20 percent of their allotment for local poverty-reduction activities. On the international front, the report criticizes the protection of agriculture in industrialized countries, which prevents poor countries from gaining access to export markets at the same time they are being asked to open their domestic markets to imports.

EYES ONLY

RELEASES THIS WEEK

Employment and Unemployment

****Embargoed until 8:30 a.m., Friday, April 7, 2000****

In March, the unemployment rate was unchanged from February at 4.1 percent. Nonfarm payroll employment increased by 416,000.

Leading Indicators

The composite index of leading indicators decreased 0.3 percent in February.

NAPM Report on Business

The Purchasing Managers' Index decreased 1.1 percentage points in March to 55.8 percent. (A reading above 50 percent indicates that the manufacturing economy is generally expanding.)

MAJOR RELEASES NEXT WEEK

Producer Prices (Thursday)
Retail Sales (Thursday)
Industrial Production and Capacity Utilization (Friday)
Consumer Prices (Friday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	**1999**	**1999:2**	**1999:3**	**1999:4**
Percent growth (annual rate)					
Real GDP (chain-type)	**2.9**	4.6	1.9	5.7	7.3
GDP chain-type price index	**5.2**	1.6	1.3	1.1	2.0
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.7	3.6	0.6	5.0	6.4
Real compensation per hour:					
Using CPI	1.0	1.7	1.4	2.1	0.8
Using NFB deflator	1.5	3.0	2.9	4.0	2.1
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.6	12.7	12.5
Residential investment	4.5	4.4	4.5	4.4	4.4
Exports	8.2	10.8	10.7	10.8	10.9
Imports	9.2	13.5	13.4	13.8	14.0
Personal saving	6.6	1.7	1.8	1.5	1.3
Federal surplus	-2.8	1.2	1.3	1.4	1.2

	1970-1993	**1999**	**January 2000**	**February 2000**	**March 2000**
Unemployment Rate (percent)	6.7**	4.2**	4.0	4.1	**4.1**
Payroll employment (thousands)					
increase per month			**394**	**7**	**416**
increase since Jan. 1993					**21213**
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.5	N.A.
PPI-Finished goods	5.0	3.0	0.0	1.0	N.A.

**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.
Employment and unemployment data **embargoed until 8:30 a.m., Friday, April 7, 2000**.

EYES ONLY

FINANCIAL STATISTICS

	1998	1999	February 2000	March 2000	April 6, 2000
Dow-Jones Industrial Average	8626	10465	10542	10483	11114
Interest Rates (percent per annum)					
3-month T-bill	4.78	4.64	5.55	5.69	5.72
10-year T-bond	5.26	5.65	6.52	6.26	5.93
Mortgage rate, 30-year fixed	6.94	7.43	8.33	8.24	8.20
Prime rate	8.35	8.00	8.73	8.83	9.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level April 6, 2000**	**Percent Change from Week ago**	**Percent Change from Year ago**
Euro (in U.S. dollars)	0.958	-0.1	-11.6
Yen (per U.S. dollar)	104.8	-0.7	-13.2
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	95.30	-0.1	-0.1

International Comparisons [1]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	4.6 (Q4)	**4.1** (Mar)	3.2 (Feb)
Canada	4.7 (Q4)	6.8 (Jan)	2.7 (Feb)
Japan	0.0 (Q4)	4.7 (Dec)	-0.6 (Feb)
France	3.2 (Q4)	10.4 (Dec)	1.4 (Feb)
Germany	2.3 (Q4)	8.7 (Jan)	1.8 (Feb)
Italy	2.1 (Q4)	11.2 (Jan) [2]	2.4 (Feb)
United Kingdom	3.0 (Q4)	5.9 (Nov)	2.3 (Feb)

U.S. unemployment data **embargoed until 8:30 a.m., Friday, April 7, 2000.**

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics, except as noted in footnote 2.

2/ Data from OECD standardized unemployment rates.