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9-20-99

WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

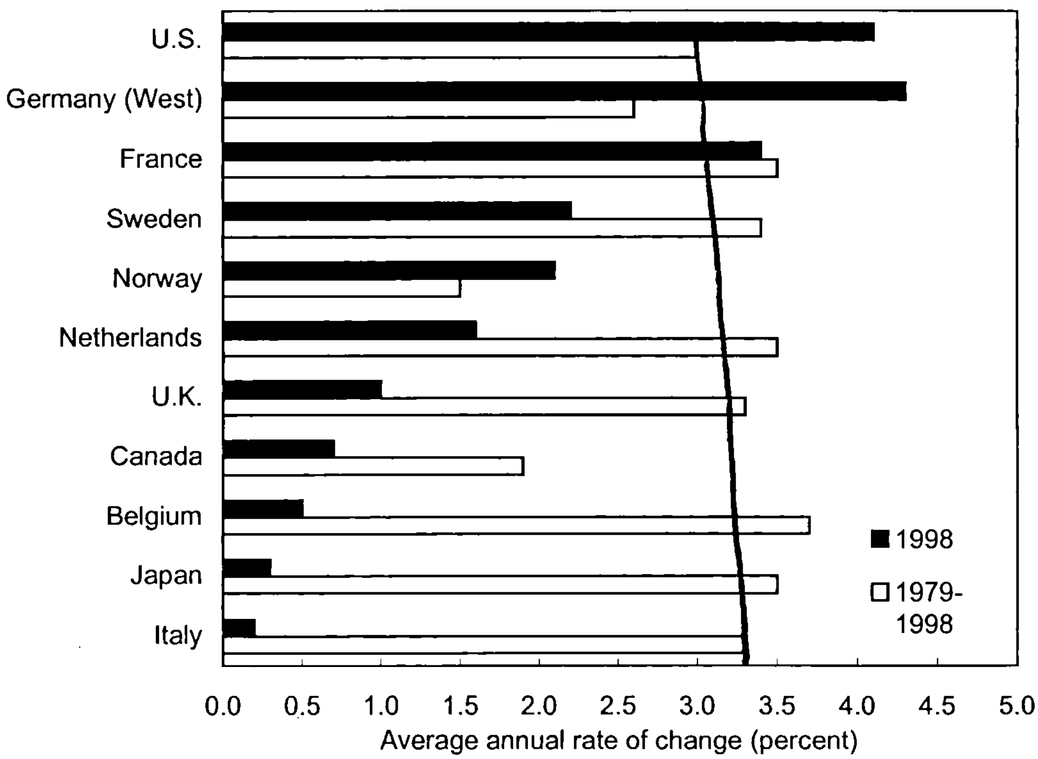
Prepared by the Council of Economic Advisers
with the assistance of the Office of the Vice President

September 17, 1999

Copied
Baily
Podesta

CHART OF THE WEEK

Manufacturing Productivity Growth in Selected Countries



The latest international comparisons of manufacturing productivity from the Bureau of Labor Statistics show that labor productivity in U.S. manufacturing increased 4.1 percent in 1998, second only to Germany's 4.3 percent. The United States and Germany (together with Norway) were also the only countries to achieve faster growth in 1998 than their long-term trend growth rate. (The U.S. output series used for international comparisons is different from the one used in the standard quarterly series on productivity and costs.)

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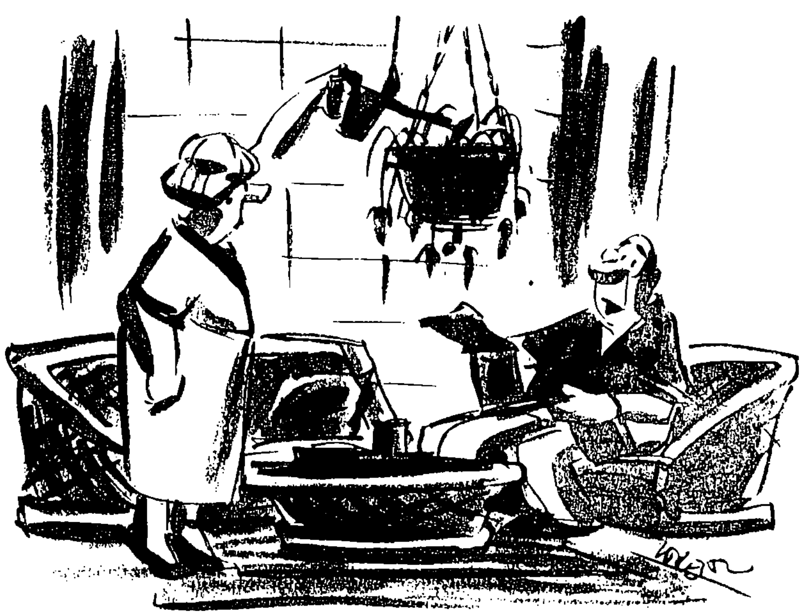


"Is this the year, Pumpkin? Goodbye, love boat, hello, elder hostel?"

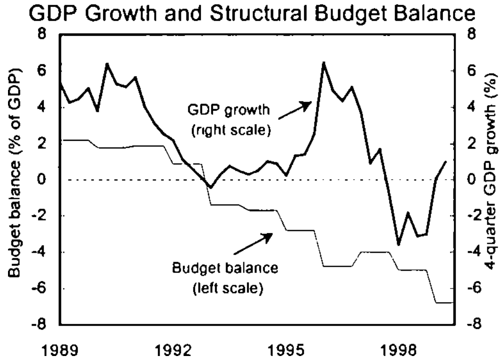
CURRENT DEVELOPMENT

Has Japan Turned the Corner?

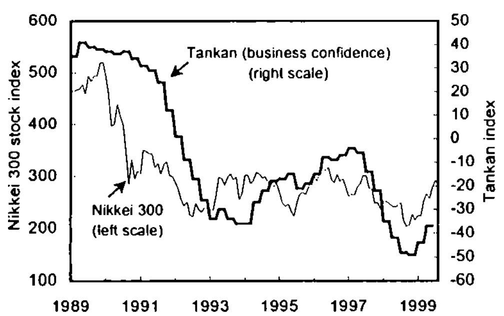
Japanese real GDP growth has recovered strongly in 1999 (see upper chart), following the longest downturn since the war. Despite hopeful signs, however, macroeconomic and structural concerns suggest a need for continued caution.

Slowdown, decline, and rebound. Despite a brief upward blip in 1996, Japan has suffered lackluster economic performance throughout the 1990s. Faced with rising budget deficits, Japan implemented a sharp fiscal consolidation in 1997. But this coincided with the onset of the Asian financial crisis and the collapse of several major financial institutions. The country plunged into recession.

GDP Growth and Structural Budget Balance



Stock Market and Business Confidence Indexes



Despite the large budget deficit, Japan implemented a major fiscal stimulus package in late 1998. Monetary policy became more aggressive in early 1999, as already low short-term interest rates were cut to virtually zero. Structural reforms may also have helped the recovery. For example, Japan has put in place a comprehensive framework to deal with banking weaknesses, and announced a package of tax and regulatory measures to promote corporate restructuring. These steps may have contributed to a recent surge in stock prices and an improvement in (the still low levels of) business confidence in 1999 (see lower chart).

Risks remain. Japan is not necessarily out of the woods. For example, public investment boosted demand in late 1998 and early 1999, but declined in the second quarter and would be a drag on growth if it returns to normal levels as proejcted. Residential investment surged in the second quarter, reflecting tax breaks, but its rapid pace is not sustainable. In addition, non-residential investment remains weak, and yen strength could curtail net exports.

Observers also point to the need to further strengthen the financial system, encourage corporate restructuring, increase labor mobility, and accelerate deregulation. Without continuing structural reforms, combined with appropriate fiscal and monetary policy, Japan runs the risk that rising growth will turn out to be transitory. After all, Japan has already had a previous, sharp recovery of growth—which, unfortunately, ended abruptly with the recession of 1997 and 1998.

ARTICLE

9-20-99

Asset Transfers and Medicaid Receipt

About 35 percent of 65 year-olds will use a nursing home at some point during the remainder of their lifetimes, according to one estimate. Medicaid is the main source of government support for such care. However, it is a needs-based program and is unavailable to individuals who have not first exhausted their own resources.

Policymakers have been concerned individuals have an incentive to transfer their assets to other family members in order to qualify for support. Past research had found little evidence of such asset shifting, but a recent study, using improved data, finds that those who believe they are more likely to enter nursing homes do indeed transfer assets with greater frequency and in larger amounts than others.

The high cost of care. An average nursing home stay now costs more than $40,000 per year, and many people mistakenly believe that Medicare will cover the costs of their long-term care. In fact, however, nearly 50 percent of the costs of long-term care are paid out-of-pocket ~~by nursing home patients~~ and their families, and most of the remaining costs are borne by *Medicaid*. Because costs are so high, spend-down (the process by which individuals first exhaust their own assets before qualifying for Medicaid) typically occurs very rapidly. Using a sample of Massachusetts residents over age 66, one study estimated that 63 percent of those living alone would become Medicaid-eligible within 13 weeks after entering a nursing home.

Evidence of asset transfers. Previous efforts to examine the extent to which people transfer assets to others as a means of qualifying for Medicaid used data on individuals who were already in nursing homes or were very likely to enter them, and hence whose transfer behavior might already have occurred. (Current rules prohibit the transfer of assets within 3 years of entering a nursing home, the so-called "look back" period.) The new study makes use of a nationally representative survey of individuals above age 70 that contains, among other key information, individuals' assessments of the likelihood that they will enter a nursing home within 5 years and the amount of money already transferred to others. It finds that a household with average net worth and a self-assessed 60 percent probability of entering a nursing home within 5 years will make transfers that are 21 percent higher than a household with average net worth and the average self-assessed probability of entering a nursing home (19 percent). In addition, among those who made transfers of more than $1,000 the average amount transferred was over $6,000.

Costs to Medicaid. The recent research suggests that the cost savings to the Medicaid program could be larger than previously thought. It is estimated that close to 12 million households might transfer assets for the purpose of qualifying for Medicaid. If everyone transferred assets at the same rate as the study

THE PRESIDENT HAS SEEN
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population, these 12 million households would make $3.5 billion in transfers, representing 15 percent of Federal Medicaid spending on nursing homes in 1993. Of course, not all of these transfers represent a loss to the Medicaid system since some of the individuals who transfer money to qualify for Medicaid do not actually need nursing home care, and the study suggests that the actual loss to the Medicaid system from these transfers is likely to be less than half of this amount.

Implications. Although the new evidence suggests that asset transfers are large enough to raise Medicaid costs, efforts to control costs by tightening rules regarding transfer behavior have been unpopular. Alternative approaches might examine ways to control rising long-term care costs, increase the availability of long-term care insurance, and create positive incentives for individuals who can afford it to share responsibility for payment.

Yes

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Long-Term Temps Are a Rare Breed. Although popular perceptions may be otherwise, employment in the temporary help services industry is relatively small (about 1 to 2 percent of the labor force). Moreover, only a small fraction of temps represent long-term jobholders, according to a recent analysis of Bureau of Labor Statistics data by a private foundation. In fact, 54 percent of all temps leave their jobs within 6 months. And while 38 percent of new temps cite inability to find a permanent job as their reason for temping, this percentage drops to below 6 percent for those with more than 48 months of tenure. Those with longer tenure are also considerably more likely to prefer their current arrangement. This study emphasizes the positive side of temporary work for some, while previous analyses in the *Weekly Economic Briefing* (November 14, 1997 and September 11, 1998) have also recognized that lower wages and changeable work settings may create problems for other temporary workers.

How Do Layoffs Affect Stock Prices? Layoffs may be getting more attention in the press than they used to, but a recent study finds that the total number of layoff announcements follows the business cycle quite closely. What has changed, according to the study, is the stock market's reaction to layoff announcements: on average, a layoff announcement is more likely to be associated with a rise in the price of the company's stock than it used to be. One possible explanation for this change is that reductions in force designed to improve efficiency are becoming more common relative to those designed to deal with reductions in demand for the company's product. The study found that layoffs associated with reorganization have, in fact, increased dramatically and that the fraction associated with plant closings has declined. It also found that layoffs due to plant closings received a negative stock market reaction while those due to reorganization were generally positively received. However, the authors were more confident in documenting that stock market reactions to layoffs have become less negative over time than they were in attributing this change to any particular cause.

Attending Elite Colleges May Have Little Payoff—Except for Minorities. A new study finds that attending a more selective (higher average SAT score) college does not appear to boost future earnings, contrary to previous findings. The study uses 1995 earnings data for about 14,000 students who entered college in 1976. Because factors affecting college admission may also affect future earnings, the study groups together students who were accepted and rejected from a similar set of schools, and then compares, within groups, the outcomes of those who chose to attend a more selective college with those who chose a less selective one. Post-college earnings were found to be similar for those who attended elite colleges and those who could have, but did not—except for students from more disadvantaged backgrounds, whose earnings were raised by attending a more selective college. An implication of the study is that efforts to attract qualified students from more disadvantaged family backgrounds to elite colleges could improve matching of these students' abilities to their future jobs, without adversely affecting that matching for others, on average.

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INTERNATIONAL ROUNDUP

Asian Recovery Exceeds Forecasts. After strong first-quarter regional growth of 4.8 percent (relative to year earlier levels), reinforced by continued strong growth in the second quarter, the Asian Development Bank raised its forecasts for most countries in the 14 "Developing Asia" economies. The faster-than-expected recovery in 1999, from 1 percent growth in the last quarter of 1998, has been fueled by domestic demand stimulated by expansionary policies and increased global demand for semi-conductors and electronic products. The implementation of corporate and financial sector reforms has helped raise industrial production and exports in most of the crisis-affected economies and, in many cases, reverse capital outflows. However, the recovery has not been evenly spread, with South Korea, Taiwan, Singapore, the Philippines, and Thailand leading the way, while Hong Kong, Malaysia, and Indonesia are lagging behind. Despite an overall positive forecast, the Asian Development Bank notes several factors that could moderate the effectiveness of the reforms in the region, including debt and structural problems of Korean Chaebols, the slow pace of bank restructuring and consolidation, and the problems associated with China's banking and state-owned enterprise sectors.

Israel Moves Toward ILO Core Labor Standards. Although Israel has made progress in ratifying International Labor Organization core labor standards, progress still needs to be made in order to protect some groups of workers from abuses, according to a WTO-commissioned report by the International Confederation of Free Trade Unions (ICFTU). The report found that, while most Israeli workers are able to exercise their basic trade union rights, the government has at times forced striking workers to return to work in arbitrarily defined "essential" public services. The report also found that significant discrimination against women and Israeli Arabs remains despite legislative improvements in recent years, due in part to lack of resources for enforcement. Also, while child labor is a relatively minor phenomenon, it is reported to be a problem for some groups of the population. The ICFTU recommends that Israel amend its law on the definition of "essential" public services, remove the penalty of forced labor for those engaging in an illegal strike, extend full freedom of association and collective bargaining rights to all workers including those from the West Bank and Gaza, and provide adequate resources for implementing its laws regarding discrimination against women and Israeli Arabs.

UK sees record lows in unemployment, inflation. Unemployment as measured in the United Kingdom fell by 22,300 in August to a 19-year low of 4.2 percent of the workforce. (The unemployment rate approximating U.S. concepts is nearly 2 percentage points higher.) The number of people employed in the UK rose to a record high in the May-July period, increasing by almost 300,000 from the same period last year. Average earnings also increased in July by 4.6 percent, up from 4.4 percent in June. At the same time, inflation fell to its lowest level since the mid-1960s, standing at just over 1 percent.

RELEASES THIS WEEK

Housing Starts

****Embargoed until 8:30 a.m., Friday, September 17, 1999****

Housing starts were about unchanged in August at 1.676 million units at an annual rate. For the first 8 months of 1999, housing starts are 5 percent above the same period a year ago.

Industrial Production and Capacity Utilization

The Federal Reserve's index of industrial production rose 0.3 percent in August following an increase of 0.7 percent in July. Capacity utilization rose 0.1 percentage point to 80.8 percent.

Consumer Price Index

The consumer price index increased 0.3 percent in August. Excluding food and energy, consumer prices rose 0.1 percent.

Retail Sales

Advance estimates show that retail sales rose 1.2 percent in August following an increase of 1.0 percent in July. Excluding sales in the automotive group, retail sales rose 0.7 percent following an increase of 0.4 percent.

MAJOR RELEASES NEXT WEEK

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

U.S. ECONOMIC STATISTICS

	1970-1993	1998	1998:4	1999:1	1999:2
Percent growth (annual rate)					
Real GDP (chain-type)	2.7	4.3	6.0	4.3	1.8
GDP chain-type price index	5.4	0.9	0.8	1.6	1.5
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.5	2.6	4.1	3.6	0.6
Real compensation per hour:					
Using CPI	0.6	2.5	2.0	2.9	1.5
Using NFB deflator	1.3	3.7	3.4	3.0	3.7
Shares of Nominal GDP (percent)					
Business fixed investment	10.9	11.0	11.0	11.0	11.2
Residential investment	4.5	4.3	4.5	4.6	4.7
Exports	8.2	11.3	11.3	10.9	11.0
Imports	9.2	13.0	13.1	13.2	13.7
Personal saving	5.2	0.3	-0.0	-0.5	-0.9
Federal surplus	-2.7	0.9	0.8	1.4	1.6

	1970-1993	1998	June 1999	July 1999	August 1999
Unemployment Rate (percent)	6.7**	4.5**	4.3	4.3	4.2
Payroll employment (thousands)					
increase per month			281	338	124
increase since Jan. 1993					19403
Inflation (percent per period)					
CPI	5.8	1.6	0.0	0.3	**0.3**
PPI-Finished goods	5.0	0.0	-0.1	0.2	0.5

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

New or revised data in **boldface**.

FINANCIAL STATISTICS

	1997	1998	July 1999	August 1999	Sept. 16, 1999
Dow-Jones Industrial Average	7441	8626	11052	10935	10737
Interest Rates (percent per annum)					
3-month T-bill	5.06	4.78	4.55	4.72	4.57
10-year T-bond	6.35	5.26	5.79	5.94	5.90
Mortgage rate, 30-year fixed	7.60	6.94	7.63	7.94	7.82
Prime rate	8.44	8.35	8.00	8.06	8.25

INTERNATIONAL STATISTICS

Exchange Rates	**Current level September 16, 1999**	**Percent Change from Week ago**	**Year ago**
Euro (in U.S. dollars)	1.042	-1.2	N.A.
Yen (per U.S. dollar)	105.1	-2.7	-22.1
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	93.11	-0.3	-3.6

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	3.9 (Q2)	4.2 (Aug)	2.3 (Aug)
Canada	3.7 (Q2)	7.7 (Jul)	1.8 (Jul)
Japan	1.1 (Q2)	4.9 (Jul)	-0.1 (Jul)
France	2.1 (Q2)	11.3 (Jun)	0.3 (Jun)
Germany	0.6 (Q2)	7.1 (Jul)[2]	0.6 (Jul)
Italy	0.9 (Q1)	12.1 (Apr)	1.7 (Jul)
United Kingdom	1.2 (Q2)	6.1 (May)	1.3 (Jul)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics.
2/ Rate for former West Germany. Using OECD standardized unemployment data, the unemployment rate for unified Germany for July was 9.1 percent.

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SPECIAL ANALYSIS

Privatization of Air Traffic Control in Canada

Recently, U.S. fliers have experienced delays attributable to air traffic control, raising questions about whether the delivery of air navigation services could be improved. Canada's experience with a privatized air traffic control system may provide a useful perspective on this issue.

The decision to privatize. In 1996, Canada transferred the authority to run its air traffic control system to a non-profit private company, Nav Canada. One of the important benefits for Canada from privatization was the ability of the new corporation to raise the funds necessary for long-term capital improvements. Another benefit was separating the role of regulating safety from that of operating the air traffic control system. Responsibility for safety regulation remained with the government, eliminating any possible conflicts of interest.

Getting started. Nav Canada raised more than $2 billion (Canadian) in debt-based financing to fund its start-up and paid the government $1.5 billion for existing assets and operating rights. Nav Canada covers its costs by charging user fees to airlines and other major users of its services. Any excess funds remaining after covering its costs are returned to the users in the form of lower fees. When the user fee system was implemented, the Canadian government eliminated the Air Transport Tax that had been charged to individual consumers.

Building a better air traffic control system. After beginning operations as a private company, Nav Canada made a series of changes designed to improve customer service. It began by setting aside $600 million to fund capital improvements. In addition, the company has tried to improve safety by hiring and training more controllers to overcome chronic shortages inherited from the government-run system. Nav Canada has also implemented a number of cost-control measures, including streamlining its management structure. Because of lower costs, traffic growth, and a broader base of paying customers, Nav Canada has been able to set its fees below the levels originally anticipated, with the result that customers paid approximately 27 percent less than they would have under the Air Transport Tax.

A user-based governance structure. Although Nav Canada is a privatized monopoly, Canada does not impose direct government regulation of its fee level. Instead, responsibility for setting fees is entrusted to Nav Canada's board of directors, which is composed of representatives drawn from the community that uses its services. Five of the 15 board members are drawn from the commercial and general aviation community, with the remainder being representatives of the government, the unions, and the general public. This board composition allows the users most directly affected by the fees to have a say in both the fees charged and in the programs Nav Canada chooses to undertake to improve customer service.

THE PRESIDENT HAS SEEN
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THE WHITE HOUSE

WASHINGTON

September 12, 1999

MR. PRESIDENT:

Attached are the following weekly reports:

(A) Interest Rates and Stock Prices

(B) Update on Global Markets

(C) Weekly Economic Briefing

(D) OSTP

(E) Cabinet Affairs

Sean Maloney

Tab B - Copied Summers, Podesta

Tab C - Copied Baily, Podesta
Copied pp.3-4 Berger, NSC WW Desk, Ballentine, Podesta
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Copied p.7 HRC, Podesta

Tab D - Copied Lane, Podesta

Tab E - Copied Marshall, Podesta
Copied p.3 HRC, Podesta
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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

September 10, 1999

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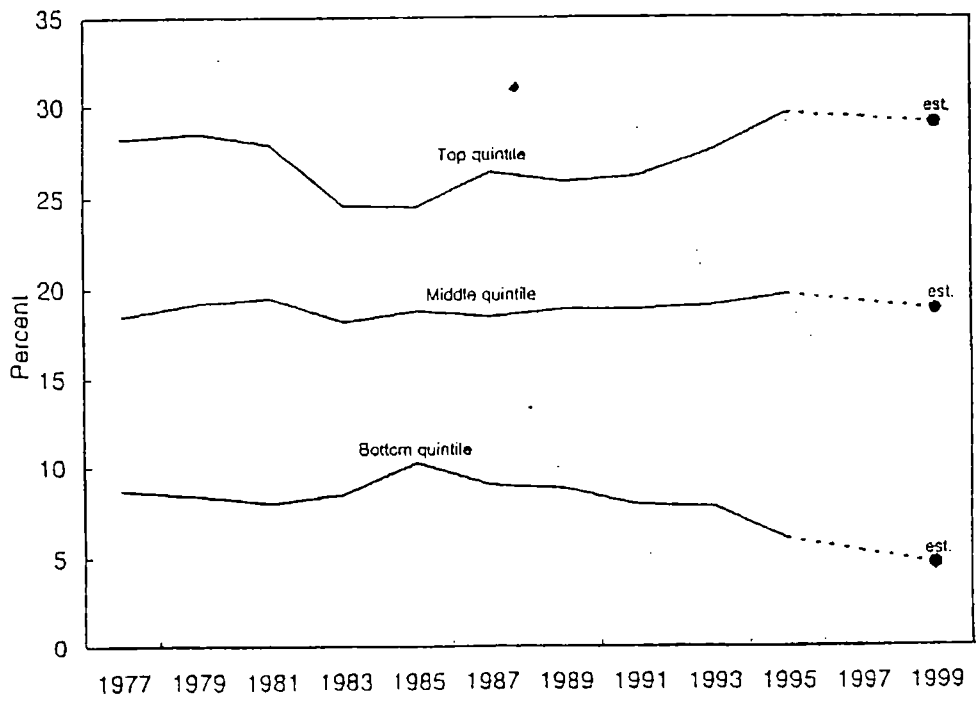
CHART OF THE WEEK

Average Effective Federal Tax Rates



The Congressional Budget Office has just released estimates of average effective Federal tax rates for 1999. Federal taxes as a share of family income for the bottom fifth of families are the lowest they have been since 1977.

CONTENTS

"See, Jimmy? If they give a big tax cut to the wealthy, those guys'll feel good and have us come fix their roof and stuff."

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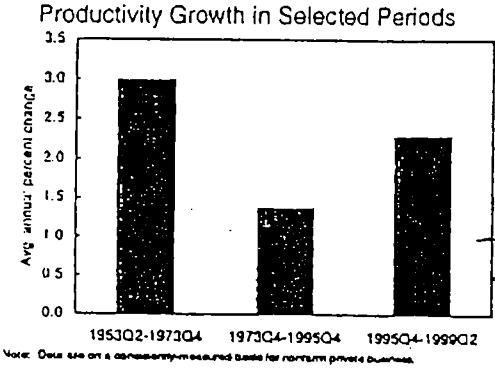
CURRENT DEVELOPMENT

The Role of Computers in Productivity Growth

Productivity growth in the computer and semiconductor industries contributes directly to aggregate productivity growth and, according to one estimate, has been the dominant source of the recent productivity spurt in the U.S. economy. Productivity growth in the manufacture of computers and semiconductors reflects the ability to produce faster processors, greater memory capacity, and larger disk drives without proportional increases in costs. But business investment in computers also adds to the quantity and quality of the capital stock, boosting productivity growth throughout the private sector. In the past, this latter effect on productivity growth was relatively small, but has recently increased.

The importance of computers in aggregate productivity growth. Productivity in the non-farm private business sector grew at a 2.3 percent annual rate over the last 3½ years (see chart). Adjusting for the typical cyclical pattern of productivity, overall "trend" productivity growth is estimated to be about 2.0 percent per year over this period. This marks a 0.6 percentage point pickup in trend productivity growth over the 1.4 percent annual rate estimated for the previous 22 years.

Productivity Growth in Selected Periods



So far, the pickup in productivity has been mostly limited to the computer industry, which has seen a 40 percent annual growth rate in productivity since the end of 1995—double the rate recorded over the previous two decades. After accounting for cyclical factors and changes in measurement, trend productivity in the private business sector excluding computers shows very little acceleration. Although computers and semiconductors make up only about 5 percent of private output, the awesome acceleration in productivity growth in these industries more than makes up for their relatively small size. This localization of the productivity boom contrasts sharply with the experience of the productivity slowdown of the 1970s, when trend productivity slowed across most sectors of the economy.

The outlook for productivity growth. The outlook for productivity growth depends on the computer and semiconductor industries' ability to continue their recent pace of innovation and improvements in manufacturing efficiency, together with the effects from the use of growing stocks of computers throughout the economy. It is hard to predict whether the unprecedented pace of productivity growth in the computer and semiconductor industries observed over the last few years can be sustained. On the more positive side, the estimated contribution to productivity growth from the use of computers has increased relative to the previous 25 years and will remain at a high level for the near future. During the 1970-95 period, when the share of computers in the capital stock was very small, the contribution to the annual rate of productivity growth from the use of computers is estimated to have been only about 0.2 percentage points. But, the contribution has been growing and is estimated to have been about 0.4 percentage points per year over the last 3½ years, with the largest effects occurring this year.

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SPECIAL ANALYSIS

Benefits for China of Greenhouse Gas Emissions Trading

A recent analysis by the Council of Economic Advisers finds that an international greenhouse gas emissions market would offer substantial economic opportunities for China. By adopting an emissions growth target under the Kyoto Protocol and participating in emissions trading, China could attract significant amounts of capital and technology to reduce its greenhouse gas emissions. By reducing its emissions, China would gain from selling unused emissions allowances to developed countries.

Creating a greenhouse gas market. The Kyoto Protocol calls for the design of an international trading system that will facilitate the transfer of capital and technology to the countries where emissions can be abated at least cost. A country that can abate greenhouse gas emissions at lower cost than others has the opportunity to attract investment for climate-friendly technology. By reducing its emissions, a country can then sell emissions allowances to countries with higher abatement costs. Ideally, an international greenhouse gas emissions market would be similar to the sulfur dioxide trading program in the U.S., which allows trading of permits to emit sulfur dioxide among electric utilities. In the U.S., power plants that can reduce emissions cheaply sell permits to plants for which emissions reduction is more expensive, resulting in estimated cost-savings of 25 to 43 percent. The principle of gains from trade in emissions allowances is basically the same as it is for trade in goods and services.

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In order to engage in trading, the Kyoto Protocol requires a country to have a greenhouse gas emissions target. It is broadly recognized that any such targets must be made compatible with a country's legitimate development needs. One way to do so would be for a developing country to set its target above current emissions levels, but below what emissions are forecast to be without additional abatement policies during the Protocol's first commitment period (2008 to 2012). Such an "emissions growth target" could provide for continued economic development, but with a lower emissions growth rate. To mitigate the risk that a target could end up being too stringent (or too lax), a target could be indexed to a country's economic performance between now and the 2008-2012 commitment period.

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Economic gains for China. While China is making impressive strides towards lowering its greenhouse gas emissions intensity (emissions per unit of output), a variety of economic analyses and modeling efforts indicate that there are still many low-cost emissions abatement opportunities in China. Some analyses suggest that China has lower abatement costs than virtually any other country in the world. These international economic models can simulate an international emissions market by assessing the projected marginal cost of abating carbon dioxide emissions across countries and then estimating the extent of buying and selling until no further economic gains can be achieved through additional trades – i.e., they find the market clearing price for an emissions allowance.

Results from six international economic models indicate that by taking on an emissions target and actively participating in international emissions trading, China would find it economic to reduce emissions 14 to 24 percent below projected 2010 emissions levels and would be able to sell emissions allowances worth from $4 billion to over $14 billion annually.

Environmental gains for China. Efforts to abate carbon dioxide emissions will likely result in significant reductions in emissions of local air pollutants, such as sulfur dioxide and particulate matter, since both kinds of emissions are by-products of fossil fuel combustion. Local air pollution levels are a significant threat both to China's economy and to its citizens. Current pollution levels increase mortality rates, the incidence of chronic illness, and the number of hospital and emergency room visits. China's position as a low-cost producer in a global greenhouse gas emissions market offers a promising avenue for attracting investment in the energy and industrial technologies necessary to significantly address the high levels of local air pollution.

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ARTICLE

Child Poverty Across Industrialized Nations

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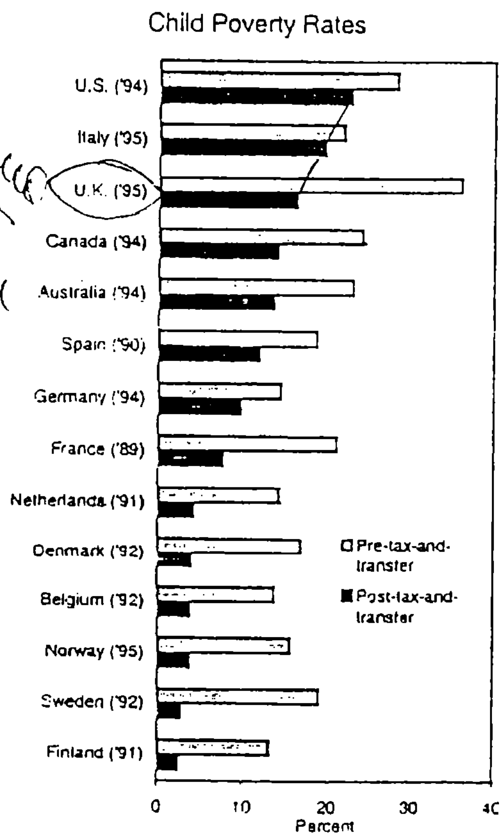
Although the official U.S. child poverty rate declined from 22.7 percent in 1993 to 19.9 percent in 1997, child poverty remains more prevalent in the United States than in many other industrialized countries. A major reason is that government support for low income families is typically more generous in these other countries. However, there is a tradeoff. More generous policies may be associated with adverse labor market effects such as higher unemployment and less job creation.

Child poverty comparisons, relatively speaking. No official international standard exists for measuring poverty, but a common approach in making cross-country comparisons is to use a relative income measure. For example, a forthcoming study examines pre- and post-tax-and-transfer child poverty rates for a number of countries using a poverty threshold based on 50-percent-of-median household income (see chart). This threshold is similar to the official European Commission poverty definition of 50 percent of average household disposable income, but the use of medians rather than averages makes the statistics less sensitive to extremely large or small incomes.



We should look at what they do — the unemployment pretty low

Unlike the money income concept used in the official U.S. poverty measure, the income measure used in the study reflects taxes and tax credits (including the EITC) and near-cash transfers (such as food stamps). Like the official U.S. measure, it excludes non-cash transfers such as public housing and publicly-provided health care. The estimated U.S. pre-tax-and-transfer child poverty rate is higher than that of most of the other countries, and it is reduced only modestly through taxes and transfers. In fact, the U.S. post-tax-and-transfer poverty rate is the highest among the countries shown.

Comparing absolute living standards. One reason for the relatively high U.S. child poverty rate is that half of U.S. median income is a high absolute threshold in comparison to other countries. Other countries would have higher child

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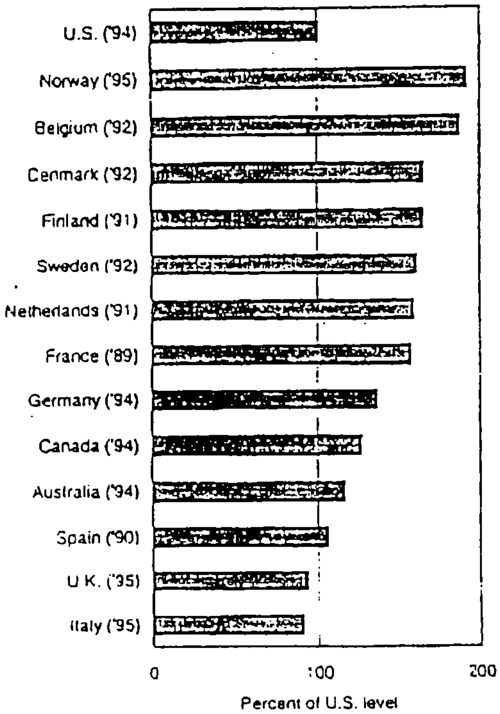
poverty rates based on the U.S. absolute threshold. A consistent measure based on the same absolute threshold does not exist. But, one available measure suggests that many poor children in the United States have limited resources relative to poor children in other countries. In particular, the chart shows that the dollar value of the household income available to the U.S. child at the 10th percentile of the U.S. income distribution is less than that of children at the 10th percentile of many other countries' distributions. Canada's level, for example, is roughly 26 percent higher than ours.

Household Income of Poor Children



Note: The chart shows the level of income at the 10th percentile of the country's distribution of children's household income as a percent of the level of income at the 10th percentile of the U.S. distribution.

Accounting for the differences. Demographic differences explain part of the story. For example, the high proportion of poor single mothers certainly raises the U.S. child poverty rate. But research has suggested that differences in demographics only partially explain the differences in child poverty rates across nations. Instead, the most important factors appear to be differences in taxes and the level of government assistance to low-income families. The United States, for example, provides less cash assistance to low-income families than most industrialized nations. Many European countries pay high levels of unemployment assistance for more than a year after people leave a job, no matter how short their period of employment. Others provide "family allowances"—special cash transfers to families with children.

Conclusion. Child poverty rates vary dramatically across nations, from less than 3 percent to more than 20 percent (using the relative measure). Differences in public policies account for a significant portion of this range. These policies, of course, come with tradeoffs: many European nations have high unemployment rates *and* low child poverty rates, due in part to their extensive system of income transfer programs. The situation in the United States is the reverse. Some poverty experts have criticized both models as being either "too expensive" (in Europe) or "too cheap" (in the U.S).

9-16-99

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

NAFTA Spurs Agricultural Trade with Canada and Mexico. As NAFTA enters its 6th year, the importance of the agreement for U.S. agriculture is more apparent than ever, according to a new report issued by the U.S. Department of Agriculture. While U.S. agricultural exports to non-NAFTA countries rose only 2.6 percent per year from 1994 to 1998, exports to Canada and Mexico rose 8.1 percent annually over the same period. Both U.S. exporters and importers are placing a greater emphasis on the North American market. In 1990, Canada and Mexico purchased 17 percent of U.S. agricultural exports and supplied 25 percent of imports; by 1998, the share of exports had risen to 25 percent and that of imports to 34 percent. The report argues that U.S. beef and pork trade has benefited greatly from NAFTA, with beef exports to Canada estimated to be twice as high as they would have been without the trade agreement. It finds that NAFTA has also facilitated the flow of U.S. and Canadian foreign direct investment in the processed food industry in North America, leading to the dissemination of new technology and efficiency gains for producers, as well as lower food costs and greater choices for consumers.

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Minorities Are Less Likely to Have Health Insurance. American minorities are less likely than whites to have health insurance, according to a report from the Commonwealth Fund. The report finds that among Americans aged 18 to 64, 14 percent of whites were uninsured in 1995 compared with 24 percent of blacks and 38 percent of Hispanics. Minorities are also less likely to be covered through work (69 percent of white workers have employer-sponsored coverage compared with 52 percent of black workers and 44 percent of Hispanic workers). Differences in socioeconomic status and type of jobs held may partially explain this discrepancy. For example, workers earning less than $10 per hour are less likely to be insured, and adults who work in large firms, are employed full-time, hold manufacturing or public administration jobs, or are trade union members are more likely to be covered through work. However, even within these categories, minorities are less likely to have employer-based insurance. The study finds that, after controlling for workforce and sociodemographic characteristics, blacks and Hispanics are 21 percent less likely than whites to have coverage through their employers. One possible barrier to minority health insurance mentioned in the report is the out-of-pocket cost associated with obtaining employer-sponsored coverage.

9-16-99

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Producer Price Index

****Embargoed until 8:30 a.m., Friday, September 10, 1999****

The producer price index for finished goods rose 0.5 percent in August. Excluding food and energy, producer prices fell 0.1 percent.

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Retail Sales (Tuesday)
Consumer Prices (Wednesday)
Industrial Production and Capacity Utilization (Thursday)
Housing Starts (Friday)

U.S. ECONOMIC STATISTICS

	1970-1993	1998	1998:4	1999:1	1999:2
Percent growth (annual rate)					
Real GDP (chain-type)	2.7	4.3	6.0	4.3	1.8
GDP chain-type price index	5.4	0.9	0.8	1.6	1.5
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.5	2.6	4.1	3.6	0.6
Real compensation per hour:					
Using CPI	0.6	2.5	2.0	2.9	1.5
Using NFB deflator	1.3	3.7	3.4	3.0	3.7
Shares of Nominal GDP (percent)					
Business fixed investment	10.9	11.0	11.0	11.0	11.2
Residential investment	4.5	4.3	4.5	4.6	4.7
Exports	8.2	11.3	11.3	10.9	11.0
Imports	9.2	13.0	13.1	13.2	13.7
Personal saving	5.2	0.3	-0.0	-0.5	-0.9
Federal surplus	-2.7	0.9	0.8	1.4	1.6

	1970-1993	1998	June 1999	July 1999	August 1999
Unemployment Rate (percent)	6.7**	4.5**	4.3	4.3	4.2
Payroll employment (thousands)					
increase per month			281	338	124
increase since Jan. 1993					19403
Inflation (percent per period)					
CPI	5.8	1.6	0.0	0.3	N.A.
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**Figures beginning 1994 are not comparable with earlier data.

New or revised data in **boldface**.
PPI data **embargoed until 8:30 a.m., Friday, September 10, 1999.**

FINANCIAL STATISTICS

	1997	1998	July 1999	August 1999	Sept. 9, 1999
Dow-Jones Industrial Average	7441	8626	11052	10935	11079
Interest Rates (percent per annum)					
3-month T-bill	5.06	4.78	4.55	4.72	4.68
10-year T-bond	6.35	5.26	5.79	5.94	5.97
Mortgage rate, 30-year fixed	7.60	6.94	7.63	7.94	7.88
Prime rate	8.44	8.35	8.00	8.06	8.25

INTERNATIONAL STATISTICS

Exchange Rates	**Current level**	**Percent Change from**	
	September 9, 1999	**Week ago**	**Year ago**
Euro (in U.S. dollars)	1.054	-1.4	N.A.
Yen (per U.S. dollar)	108.0	-1.1	-20.9
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	93.36	-0.3	-4.6

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	3.9 (Q2)	4.2 (Aug)	2.1 (Jul)
Canada	3.7 (Q2)	7.7 (Jul)	1.8 (Jul)
Japan	1.1 (Q2)	4.9 (Jul)	-0.1 (Jul)
France	2.1 (Q2)	11.3 (Jun)	0.3 (Jun)
Germany	0.6 (Q2)	7.1 (Jul)[2]	0.6 (Jul)
Italy	0.9 (Q1)	12.1 (Apr)	1.7 (Jul)
United Kingdom	1.2 (Q2)	6.1 (May)	1.3 (Jul)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics.
2/ Rate for former West Germany. Using OECD standardized unemployment data, the unemployment rate for unified Germany for July was 9.1 percent.

THE PRESIDENT HAS SEEN
9-16-99

THE WHITE HOUSE

WASHINGTON

September 12, 1999

MR. PRESIDENT:

Attached are the following weekly reports:

(A) Interest Rates and Stock Prices

(B) Update on Global Markets

(C) Weekly Economic Briefing

(D) OSTP

(E) Cabinet Affairs

Sean Maloney

Tab B - Copied Summers, Podesta

Tab C - Copied Baily, Podesta
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Copied pp.5-6 Sperling, Reed, HRC, Podesta
Copied p.7 HRC, Podesta

Tab D - Copied Lane, Podesta

Tab E - Copied Marshall, Podesta
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Copied p.4 Podesta
Copied p.6 Podesta

9-16-99

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

September 10, 1999

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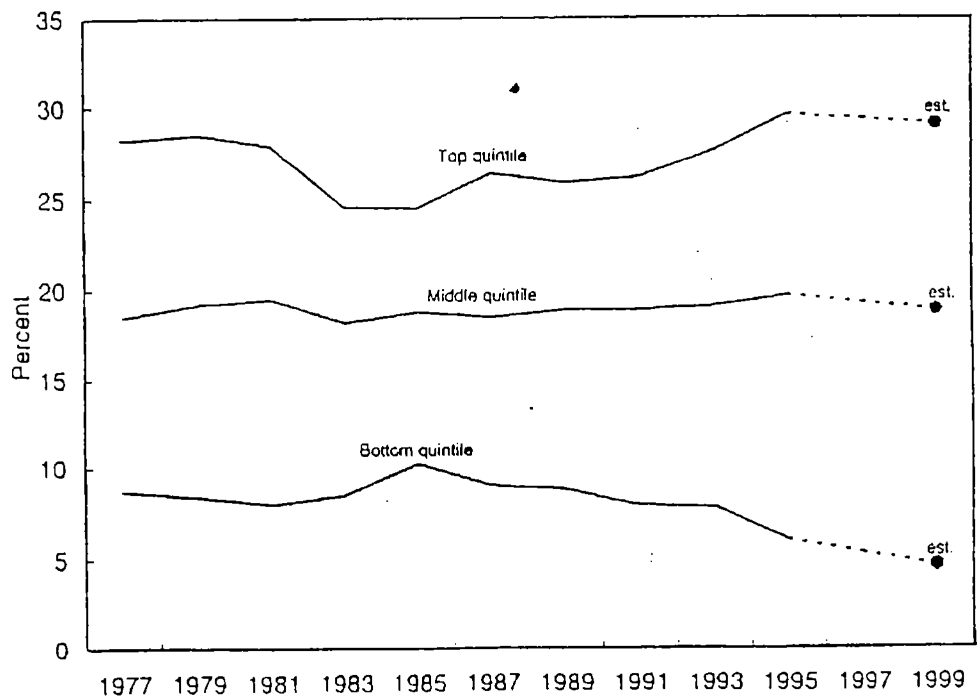
Podesta

CHART OF THE WEEK

Average Effective Federal Tax Rates



The Congressional Budget Office has just released estimates of average effective Federal tax rates for 1999. Federal taxes as a share of family income for the bottom fifth of families are the lowest they have been since 1977.

CONTENTS

"See, Jimmy? If they give a big tax cut to the wealthy, those guys'll feel good and have us come fix their roof and stuff."

9-16-99

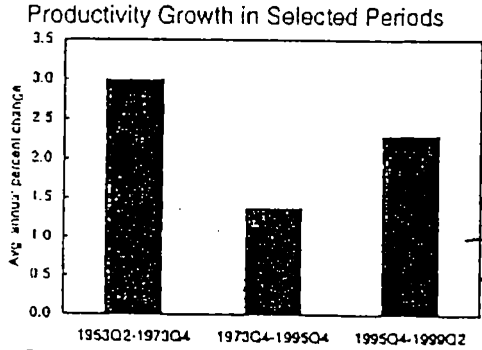
CURRENT DEVELOPMENT

The Role of Computers in Productivity Growth

Productivity growth in the computer and semiconductor industries contributes directly to aggregate productivity growth and, according to one estimate, has been the dominant source of the recent productivity spurt in the U.S. economy. Productivity growth in the manufacture of computers and semiconductors reflects the ability to produce faster processors, greater memory capacity, and larger disk drives without proportional increases in costs. But business investment in computers also adds to the quantity and quality of the capital stock, boosting productivity growth throughout the private sector. In the past, this latter effect on productivity growth was relatively small, but has recently increased.

The importance of computers in aggregate productivity growth. Productivity in the non-farm private business sector grew at a 2.3 percent annual rate over the last 3½ years (see chart). Adjusting for the typical cyclical pattern of productivity, overall "trend" productivity growth is estimated to be about 2.0 percent per year over this period. This marks a 0.6 percentage point pickup in trend productivity growth over the 1.4 percent annual rate estimated for the previous 22 years.

Productivity Growth in Selected Periods



So far, the pickup in productivity has been mostly limited to the computer industry, which has seen a 40 percent annual growth rate in productivity since the end of 1995—double the rate recorded over the previous two decades. After accounting for cyclical factors and changes in measurement, trend productivity in the private business sector excluding computers shows very little acceleration. Although computers and semiconductors make up only about 5 percent of private output, the awesome acceleration in productivity growth in these industries more than makes up for their relatively small size. This localization of the productivity boom contrasts sharply with the experience of the productivity slowdown of the 1970s, when trend productivity slowed across most sectors of the economy.

The outlook for productivity growth. The outlook for productivity growth depends on the computer and semiconductor industries' ability to continue their recent pace of innovation and improvements in manufacturing efficiency, together with the effects from the use of growing stocks of computers throughout the economy. It is hard to predict whether the unprecedented pace of productivity growth in the computer and semiconductor industries observed over the last few years can be sustained. On the more positive side, the estimated contribution to productivity growth from the use of computers has increased relative to the previous 25 years and will remain at a high level for the near future. During the 1970-95 period, when the share of computers in the capital stock was very small, the contribution to the annual rate of productivity growth from the use of computers is estimated to have been only about 0.2 percentage points. But, the contribution has been growing and is estimated to have been about 0.4 percentage points per year over the last 3½ years, with the largest effects occurring this year.

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9-16-99

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SPECIAL ANALYSIS

Benefits for China of Greenhouse Gas Emissions Trading

A recent analysis by the Council of Economic Advisers finds that an international greenhouse gas emissions market would offer substantial economic opportunities for China. By adopting an emissions growth target under the Kyoto Protocol and participating in emissions trading, China could attract significant amounts of capital and technology to reduce its greenhouse gas emissions. By reducing its emissions, China would gain from selling unused emissions allowances to developed countries.

Creating a greenhouse gas market. The Kyoto Protocol calls for the design of an international trading system that will facilitate the transfer of capital and technology to the countries where emissions can be abated at least cost. A country that can abate greenhouse gas emissions at lower cost than others has the opportunity to attract investment for climate-friendly technology. By reducing its emissions, a country can then sell emissions allowances to countries with higher abatement costs. Ideally, an international greenhouse gas emissions market would be similar to the sulfur dioxide trading program in the U.S., which allows trading of permits to emit sulfur dioxide among electric utilities. In the U.S., power plants that can reduce emissions cheaply sell permits to plants for which emissions reduction is more expensive, resulting in estimated cost-savings of 25 to 43 percent. The principle of gains from trade in emissions allowances is basically the same as it is for trade in goods and services.

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In order to engage in trading, the Kyoto Protocol requires a country to have a greenhouse gas emissions target. It is broadly recognized that any such targets must be made compatible with a country's legitimate development needs. One way to do so would be for a developing country to set its target above current emissions levels, but below what emissions are forecast to be without additional abatement policies during the Protocol's first commitment period (2008 to 2012). Such an "emissions growth target" could provide for continued economic development, but with a lower emissions growth rate. To mitigate the risk that a target could end up being too stringent (or too lax), a target could be indexed to a country's economic performance between now and the 2008-2012 commitment period.

We shou[ld] get this appropria[te] clients ?

Economic gains for China. While China is making impressive strides towards lowering its greenhouse gas emissions intensity (emissions per unit of output), a variety of economic analyses and modeling efforts indicate that there are still many low-cost emissions abatement opportunities in China. Some analyses suggest that China has lower abatement costs than virtually any other country in the world. These international economic models can simulate an international emissions market by assessing the projected marginal cost of abating carbon dioxide emissions across countries and then estimating the extent of buying and selling until no further economic gains can be achieved through additional trades – i.e., they find the market clearing price for an emissions allowance.

Results from six international economic models indicate that by taking on an emissions target and actively participating in international emissions trading, China would find it economic to reduce emissions 14 to 24 percent below projected 2010 emissions levels and would be able to sell emissions allowances worth from $4 billion to over $14 billion annually.

Environmental gains for China. Efforts to abate carbon dioxide emissions will likely result in significant reductions in emissions of local air pollutants, such as sulfur dioxide and particulate matter, since both kinds of emissions are by-products of fossil fuel combustion. Local air pollution levels are a significant threat both to China's economy and to its citizens. Current pollution levels increase mortality rates, the incidence of chronic illness, and the number of hospital and emergency room visits. China's position as a low-cost producer in a global greenhouse gas emissions market offers a promising avenue for attracting investment in the energy and industrial technologies necessary to significantly address the high levels of local air pollution.

9-16-99

ARTICLE

Child Poverty Across Industrialized Nations

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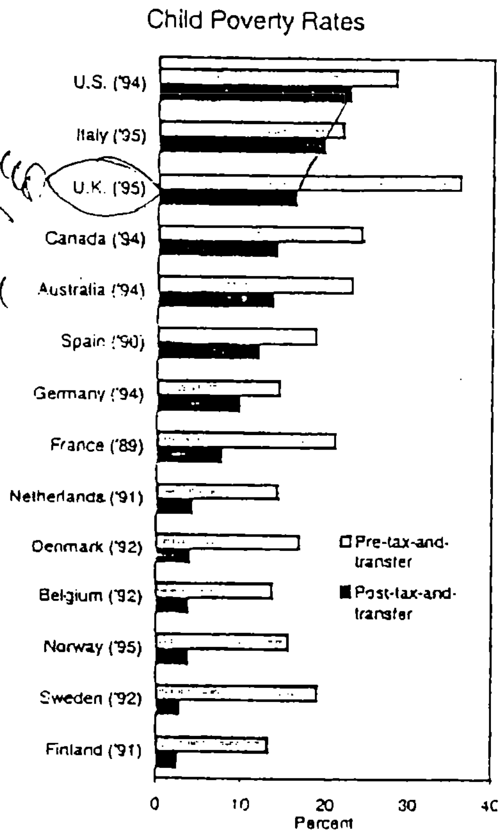
Podesta

Although the official U.S. child poverty rate declined from 22.7 percent in 1993 to 19.9 percent in 1997, child poverty remains more prevalent in the United States than in many other industrialized countries. A major reason is that government support for low income families is typically more generous in these other countries. However, there is a tradeoff. More generous policies may be associated with adverse labor market effects such as higher unemployment and less job creation.

Child poverty comparisons, relatively speaking. No official international standard exists for measuring poverty, but a common approach in making cross-country comparisons is to use a relative income measure. For example, a forthcoming study examines pre- and post-tax-and-transfer child poverty rates for a number of countries using a poverty threshold based on 50-percent-of-median household income (see chart). This threshold is similar to the official European Commission poverty definition of 50 percent of average household disposable income, but the use of medians rather than averages makes the statistics less sensitive to extremely large or small incomes.

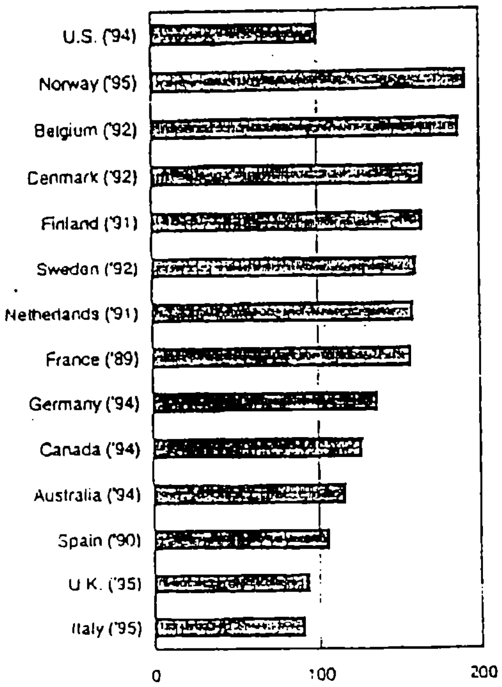


We should look at what they do — the unemployment pretty low

Unlike the money income concept used in the official U.S. poverty measure, the income measure used in the study reflects taxes and tax credits (including the EITC) and near-cash transfers (such as food stamps). Like the official U.S. measure, it excludes non-cash transfers such as public housing and publicly-provided health care. The estimated U.S. pre-tax-and-transfer child poverty rate is higher than that of most of the other countries, and it is reduced only modestly through taxes and transfers. In fact, the U.S. post-tax-and-transfer poverty rate is the highest among the countries shown.

Comparing absolute living standards. One reason for the relatively high U.S. child poverty rate is that half of U.S. median income is a high absolute threshold in comparison to other countries. Other countries would have higher child poverty rates based on the U.S. absolute threshold. A consistent measure based on the same absolute threshold does not exist. But, one available measure suggests that many poor children in the United States have limited resources relative to poor children in other countries. In particular, the chart shows that the dollar value of the household income available to the U.S. child at the 10th percentile of the U.S. income distribution is less than that of children at the 10th percentile of many other countries' distributions. Canada's level, for example, is roughly 26 percent higher than ours.

Household Income of Poor Children



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9-16-99

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United States	3.9 (Q2)	4.2 (Aug)	2.1 (Jul)
Canada	3.7 (Q2)	7.7 (Jul)	1.8 (Jul)
Japan	1.1 (Q2)	4.9 (Jul)	-0.1 (Jul)
France	2.1 (Q2)	11.3 (Jun)	0.3 (Jun)
Germany	0.6 (Q2)	7.1 (Jul)[2]	0.6 (Jul)
Italy	0.9 (Q1)	12.1 (Apr)	1.7 (Jul)
United Kingdom	1.2 (Q2)	6.1 (May)	1.3 (Jul)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics.
2/ Rate for former West Germany. Using OECD standardized unemployment data, the unemployment rate for unified Germany for July was 9.1 percent.

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WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

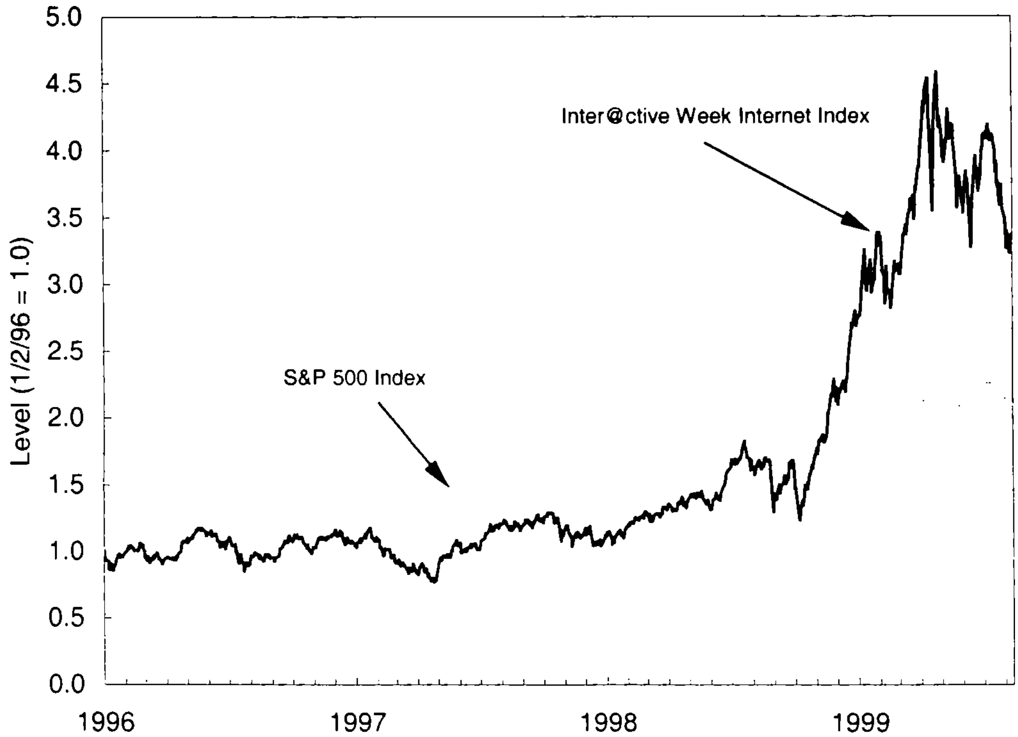
Prepared by the Council of Economic Advisers
with the assistance of the Office of the Vice President

Copied
Podesta
Baily

August 13, 1999

CHART OF THE WEEK

Internet Stocks and the S&P 500



Between 1996 and late 1998, the Inter@ctive Week index of Internet stocks performed no better than the Standard & Poor's 500 index. Since the beginning of October last year, however, the Internet index has more than doubled in value, despite recent retreats from much higher levels.

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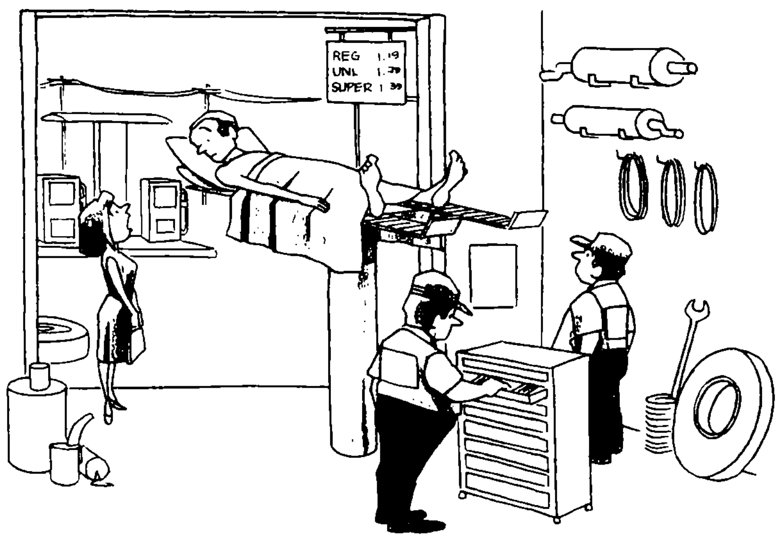


"I checked your company's medical plan again, and these guys *are* authorized through your HMO."

THE PRESIDENT HAS SEEN
8-17-99

EYES ONLY

TREND

Employment Changes in Manufacturing Industries

While the overall economy has performed strongly in this expansion, international factors have retarded manufacturing since 1997. This has led to significant employment declines in many of the durable goods industries that had been growing prior to 1997 and accelerated job losses in most nondurable industries.

1993-97: the durable divide. Between 1993 and 1997, manufacturing output grew at a 5.6 percent annual rate—faster than the rest of the economy, despite an increase in the manufacturing trade deficit. Because productivity growth was particularly rapid, employment growth was more sluggish. Nevertheless, manufacturing employment grew at an average annual rate of 0.8 percent and manufacturing employment increased by 769,000 between December 1992 and December 1997.

As might be expected in an expansion with particularly strong growth in investment, manufacturing employment gains were concentrated in durable goods (see chart on next page), with rapid advances over this period in motor vehicles and equipment, lumber and wood products, industrial machinery and equipment, fabricated metal products, and electronic and electrical equipment. Even in this period, however, employment growth in nondurables was sluggish. Indeed, labor-intensive industries heavily engaged in international trade, such as textiles, apparel, and leather and leather products (footwear), experienced significant employment declines.

1997-99: the global divide. More recently, the growth pattern has changed. Weak foreign demand and declining foreign currencies have brought manufacturing export growth to a halt. The volume of U.S. merchandise exports in the second quarter of 1999 was just 0.7 percent higher than it was in the fourth quarter of 1997, while merchandise imports increased by 18 percent. In the first 5 months of this year, the annualized trade deficit in manufactured goods has been \$270 billion—almost double the level prior to the Asian crisis.

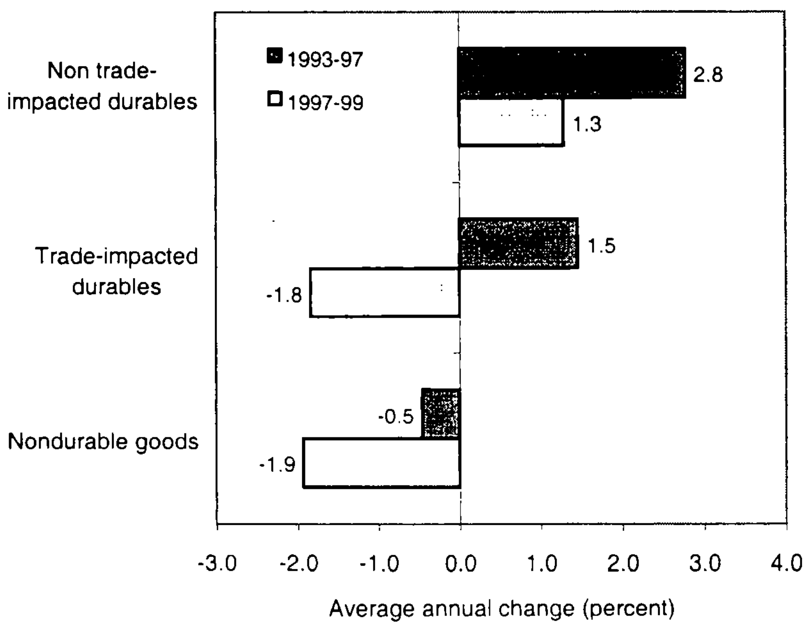
The most rapid employment declines since 1997 were again in labor-intensive sectors such as leather products, apparel, and textile mill products. In addition, however, many durable goods industries that had been doing well began to experience declining employment (trade-impacted durables in the chart). These include electronic and electrical equipment, industrial machinery and equipment, transportation equipment, and primary metals (including steel). Indeed, even employment in computer manufacturing fell by about 21,000 during this period.

Since machinery accounts for about half of all U.S. manufactured goods exports, durable goods manufacturers and their suppliers have clearly been adversely impacted by the export slump. Not only have they lost export sales directly but they have also been damaged indirectly as the decline in manufacturing capacity utilization (from 82.5 percent in the fourth quarter of 1997 to 79.4 percent in June) has depressed spending on industrial equipment. (In the second quarter, for example, expenditures on industrial equipment were only 2.6 percent above the level in the fourth quarter of 1997.) This weakness appears to explain why capacity utilization in steel remains low, despite the fact that steel imports have returned to near their pre-surge levels.

By contrast, manufacturers experiencing strong domestic demand growth have seen employment growth (non trade-impacted durables in the chart). Strong expenditures on construction have sustained employment growth in lumber and wood products; stone, clay, and glass; and furniture and fixtures. Similarly, buoyant demand for autos and trucks has maintained stable employment levels in motor vehicles and equipment despite strong import growth.

Implications. Manufacturing is an important provider of high-wage jobs, particularly for blue-collar men with a high school education. While rapid productivity growth in this sector is likely to limit the additional opportunities for such employment in the future, other developments can affect job availability. Increased exports, driven by foreign growth, would mitigate these employment declines. By contrast, higher domestic interest rates could depress industrial investment and construction spending and deal another blow to a sector that is already troubled.

Changes in Manufacturing Employment



THE PRESIDENT HAS SEEN
8-17-99

EYES ONLY

SPECIAL ANALYSIS

Can Competition Control Health Care Costs?

In most markets, competition is viewed as a powerful force for encouraging low prices, high quality, and innovation. However, distinctive features of the health care market—particularly differences in what providers and patients know and the diversity of individual health care needs—have led some to question whether more competition is beneficial. While unique features of the health care market may have weighed against the benefits of competition in the past and remain important today, recent developments in the health care industry appear to have shifted the balance in favor of competition.

Concerns about competition in health care. Prior to the mid-1980s, health insurance premiums were typically heavily subsidized by employers, which dampened individuals' sensitivity to cost and price differences. To the extent that employee contributions did not increase in line with costs, employees had an incentive to choose more expensive plans. Among providers, incentives to contain costs were poorly structured and resulted in little restraint on health care spending (encouraging, for example, a "medical arms race" among hospitals to provide more expensive equipment and facilities). Greater competition in such an environment could lead to excess capacity, higher costs, adverse patient health outcomes, and risk selection that isolates high-risk individuals into groups that insurers find prohibitively costly to serve.

The benefits of competition. Dramatic changes in the private health insurance environment have made competition more effective in controlling costs. In the past 15 years, employees have had to pay a larger share of health plan premiums, restoring price sensitivity. In addition, traditional fee-for-service health plans allowing for complete choice have given way to more tightly managed preferred provider organizations, resulting in cost containment. In the current environment greater competition can lower the costs associated with achieving any given quality of health insurance while giving consumers a choice of plans offering different menus of price and quality.

The effect of price on switching among health plans. The projected success of competition as a strategy for controlling health costs depends in part on the willingness of consumers to switch health plans in response to a change in plan premiums. Evidence that consumers are very sensitive to out-of-pocket premiums and are willing to switch health plans in response to small changes comes from a study of what happened at University of California campuses after 1994, when they stopped paying the full premium for most health plans and subsidizing the cost of the most expensive plan. The study found that individuals facing monthly premium increases of as little as $10 were roughly five times as likely to switch plans as those whose premiums remained constant.

EYES ONLY

Attention to adverse selection remains important. Potentially, the switch to a less expensive plan in response to higher premiums could go too far, given limits on what beneficiaries and insurers know about each other and the diversity of individual health care needs. This is illustrated by what happened when Harvard shifted to a voucher system in 1995, in which beneficiaries were paid a fixed contribution irrespective of which plan they chose. Harvard experienced cost savings of 5 to 8 percent of baseline health spending, due largely to lower insurer profits as a result of increasing plan choice and more stringent bargaining. However, this change increased the price to employees in the most generous plan by over $500 annually. Most individuals switched away from this plan, so that the provider of this policy experienced rising expenses beyond what was projected. Within 3 years, this health care option was driven out of the market.

Conclusion. In the current health care environment, increasing price sensitivity and requiring providers to bid competitively for contracts to provide health care should prove beneficial. While issues such as adverse selection cannot be ignored, recent research suggests that the cost savings from increased competition are likely to be enough to generate net benefits. In the case of competitive bidding, reductions in the cost of providing care are transferred to the organization soliciting the bids, with some of these savings passed on to patients. Such an incentive structure should lead to shifts away from costly plans and create additional savings. With the right structuring of incentives, competition can achieve desired cost objectives without unduly sacrificing quality.

EYES ONLY

SPECIAL ANALYSIS

Labor Market Explanations for a Lower NAIRU

[This material was discussed at Wednesday's economic briefing, but was not contained in the written material for that briefing.]

One of the most notable features of the current expansion is how long the unemployment rate has remained below 5 percent without triggering rising inflation. A new study highlights four changes in the labor market that may have lowered the unemployment rate consistent with stable inflation (the NAIRU).

Demographics. The maturing of the baby boom and rising educational attainment of the labor force could reduce the amount of unemployment associated with frequent job changes by younger and less-educated workers (because they represent a smaller fraction of the labor force) and hence lower the aggregate unemployment rate. The study estimates that the changing age composition of the labor force can account for an estimated 0.4 percentage point of the decline in the overall unemployment rate since the mid-1980s. Because it has been going on for decades, increasing average educational attainment appears to be a less plausible explanatory factor for *recent* changes in the NAIRU.

Growth in the prison population. The study notes that nearly 2 percent of the adult male population is currently incarcerated and that the prison population has almost doubled in the past decade. To the extent that convicted criminals had weak employment histories (and hence high unemployment rates) prior to their arrest, their removal from the labor force would lower the unemployment rate without much impact on labor market tightness. The study estimates that the increase in the incarcerated population can account for roughly a 0.3 percentage point decline in the male unemployment rate, and a 0.17 percentage point decline in the overall unemployment rate, since 1985.

Improved matching. The rise of the temporary help industry and, since 1993, the expanded provision of job search assistance (JSA) to unemployed workers could have reduced frictional unemployment by matching unemployed workers to job vacancies more quickly and more efficiently. The study finds that JSA is unlikely to affect a large enough number of workers to significantly affect the aggregate unemployment rate. By contrast, it finds that the rise of the temporary help industry may account for as much of the decline in unemployment since the mid-1980s as do demographic shifts.

Weak unions and worker anxiety. Finally, the study examines the "weak backbone hypothesis," which holds that workers have become more reluctant to press for wage gains. It points to declining union membership and the watershed Professional Air Traffic Controllers Organization (PATCO) strike in 1981 as evidence that the threat of unionization is now so low in many industries that the labor market has passed a "tipping point" beyond which unions and the threat of unionization have very little influence on wage setting. Although worker anxiety is frequently advanced as a source of wage restraint, the study concludes that worker surveys do not reveal widespread insecurity and there is little evidence of a link between insecurity and wage growth.

Implications. Demographic shifts and the rise of the temporary help industry appear to be the major labor market developments that have allowed the economy to achieve sustained low unemployment rates. While it remains an open question whether they are the main reason for the improved inflation-unemployment trade-off during the current expansion, they are unlikely to be reversed in the near future. Thus, they would be a force operating to maintain the high-pressure labor markets of this expansion that have begun to bring benefits to low-wage workers and disadvantaged families as well as the rest of the labor force.

EYES ONLY

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Do Local Communities Benefit from Foreign Direct Investment? Investment by foreign manufacturing firms in American communities raises wages by more than an equivalent amount of domestic investment, but that investment may come at a cost to government budgets, according to a recent study. The study found that attracting a representative foreign manufacturing firm increased wages for all jobs in the industry in the same county by 2.3 percent, compared with 0.3 percent for a new domestic firm. However, state and local governments often offer incentives to attract firms, and the study finds that attracting foreign firms is associated with larger reductions in real per capita local government revenues and expenditures than attracting new domestic firms. Also, increased foreign investment is associated with lower public school enrollment and a shift in spending away from education toward public safety and transportation.

Can New York Bank on Wall Street? A recent study by the Federal Reserve Bank of New York addresses concerns that a future downturn in the securities industry would be quite disruptive to the New York City economy. The study reports that the securities industry is disproportionately large in New York City. It accounts for 4.7 percent of total employment (roughly 10 times the national average) and generates 19 percent of total earnings. In some way, 14 percent of all New York City employment depends on the securities industry. The study also notes that Wall Street was a large factor in New York City's two major downturns in the 1970s and early 1990s. However, it finds that other factors might soften the blow of a decline in securities market employment. Specifically, several sectors that were hard hit in earlier downturns (including manufacturing and real estate) appear to be on more solid footing in this expansion. Other fast-growing industries not tied to the financial sector might also cushion the effects of securities industry job losses.

State Regulators Highlight Problems with Day Trading. This week, state securities regulators issued a report based on a 7-month investigation of the day-trading industry. Day trading is a strategy in which individuals make numerous small stock trades each day trying to exploit small movements in share prices. The day-trading industry consists of specialty firms where customers go to make such trades using proprietary software. The report, released by the North American Securities Administrators Association (NASAA), concluded that day-trading firms are misleading in their advertising and ought to screen potential customers better. It also questioned the practice at some firms of arranging inter-customer loans to meet margin calls. These practices seem to be aimed at evading legal restrictions on investment firms' lending to customers—restrictions that are meant to prevent customers from investing beyond their means. The report contained an independent analysis of accounts at one Massachusetts firm where at least 70 percent of traders lost money and only 11.5 percent showed the ability to conduct profitable short-term trading. However, this firm had been shut down last year by state authorities and may not be representative of the industry.

EYES ONLY

INTERNATIONAL ROUNDUP

IEA Sees Tighter Oil Markets. With supply constrained and a recovery in demand underway, oil markets are set to tighten, according to the International Energy Agency (IEA). Demand is expected to grow beginning in the second half of this year, and oil demand in 2000 is forecast to be about 1.8 million barrels per day, or 2.4 percent, higher than 1999 levels. On the supply side, OPEC ministers have been quoted in the press saying that they do not anticipate raising output quotas at their next meeting in September. OPEC compliance with recent cutback agreements was 91 percent in July, and continued compliance will keep OPEC supplies constrained. Meanwhile, non-OPEC oil supply is expected to increase much less than demand, following a small decrease this year.

World Bank Sees Commodity Markets Vulnerable to Y2K Bug. Anticipation of the Y2K technology bug could disrupt global commodity markets, according to the World Bank's most recent *Global Commodity Markets* report. Demand for essential commodities is expected to increase as consumers stockpile basic staples such as fuels and foods and speculators buy in anticipation of higher prices—though some producer response should be expected as well. Stocks of most commodities appear to be sufficiently large to prevent significant price increases, but oil markets may be vulnerable, not only because of the supply considerations discussed above but also because oil production is highly technology intensive, which heightens the risk of production disruptions, especially for producers like Russia and Nigeria that might lack the resources to fix problems. The report also warns that Y2K-related transportation disruptions could lead to local imbalances. For example, efforts by importers to stockpile goods before the end of 1999 could put strains on shipping capacity. Also, low-valued or bulky commodities such as grains and timber may be crowded out by high-valued commodities and manufactures, leading to price volatility as surpluses build in exporting countries and shortages develop in importing countries.

OECD Reviews Mexico's Regulatory Restructuring. In its new report *Regulatory Reform in Mexico,* the OECD praises the regulatory reforms that have helped transform Mexico from an inward-looking economy to an open and market-based economy over the last 15 years. The report emphasizes that reforms have produced major benefits by reducing prices and increasing quality and choice for Mexican consumers and businesses. It notes that privatization and the elimination of red tape have encouraged firms to invest in new technologies. The report finds that the Mexican economy is now more adaptable, allowing it to rebound more quickly and at lower cost from major economic crises. However, it observes that further reform is needed in some sectors, notably telecommunications, where prices remain very high. It recommends improving regulation of dominant firms after privatization, enhancing the efficiency and coherence of regulations at state and local levels, and increasing regulatory transparency to boost investment, market entry, and innovation. And it stresses the importance of securing the benefits of the program through sustained policy stability and strengthened public administration.

EYES ONLY

RELEASES THIS WEEK

Producer Price Index

****Embargoed until 8:30 a.m., Friday, August 13, 1999****

The producer price index for finished goods rose 0.2 percent in July. Excluding food and energy, producer prices were unchanged.

Retail Sales

Advance estimates show that retail sales rose 0.7 percent in July. Excluding sales in the automotive group, retail sales rose 0.3 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 (Thursday)

EYES ONLY

U.S. ECONOMIC STATISTICS

	1970-1993	1998	1998:4	1999:1	1999:2
Percent growth (annual rate)					
Real GDP (chain-type)	2.7	4.3	6.0	4.3	2.3
GDP chain-type price index	5.4	0.9	0.8	1.6	1.6
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.5	2.6	4.1	3.6	1.3
Real compensation per hour:					
Using CPI	0.6	2.5	2.0	2.9	1.5
Using NFB deflator	1.3	3.7	3.4	3.0	3.3
Shares of Nominal GDP (percent)					
Business fixed investment	10.9	11.0	11.0	11.0	11.2
Residential investment	4.5	4.3	4.5	4.6	4.6
Exports	8.2	11.3	11.3	10.9	10.9
Imports	9.2	13.0	13.1	13.2	13.5
Personal saving	5.2	0.3	−0.0	−0.5	−0.8
Federal surplus	-2.7	0.9	0.8	1.4	N.A.

	1970-1993	1998	May 1999	June 1999	July 1999
Unemployment Rate (percent)	6.7**	4.5**	4.2	4.3	4.3
Payroll employment (thousands)					
increase per month			28	273	310
increase since Jan. 1993					19243
Inflation (percent per period)					
CPI	5.8	1.6	0.0	0.0	N.A.
PPI-Finished goods	5.0	0.0	0.2	−0.1	**0.2**

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

New or revised data in **boldface**.
PPI data **embargoed until 8:30 a.m., Friday, August 13, 1999**.

EYES ONLY

FINANCIAL STATISTICS

	1997	1998	June 1999	July 1999	August 12, 1999
Dow-Jones Industrial Average	7441	8626	10704	11052	10808
Interest Rates (percent per annum)					
3-month T-bill	5.06	4.78	4.57	4.55	4.66
10-year T-bond	6.35	5.26	5.90	5.79	6.08
Mortgage rate, 30-year fixed	7.60	6.94	7.55	7.63	8.15
Prime rate	8.44	8.35	7.75	8.00	8.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level August 12, 1999**	**Percent Change from Week ago**	**Percent Change from Year ago**
Euro (in U.S. dollars)	1.064	-1.5	N.A.
Yen (per U.S. dollar)	115.8	1.6	-20.8
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	95.01	0.8	-5.6

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	4.1 (Q2)	4.3 (Jul)	2.0 (Jun)
Canada	3.2 (Q1)	7.6 (Jun)	1.5 (Jun)
Japan	0.1 (Q1)	4.9 (Jun)	0.0 (Jun)
France	2.3 (Q1)	11.3 (Jun)	0.5 (Apr)
Germany	0.8 (Q1)	7.2 (May)[2]	0.4 (Jun)
Italy	0.9 (Q1)	12.1 (Apr)	1.4 (Jun)
United Kingdom	1.2 (Q2)	6.2 (Apr)	1.4 (Jun)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics.
2/ Rate for former West Germany. Using OECD standardized unemployment data, the unemployment rate for unified Germany for May was 9.1 percent.

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WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

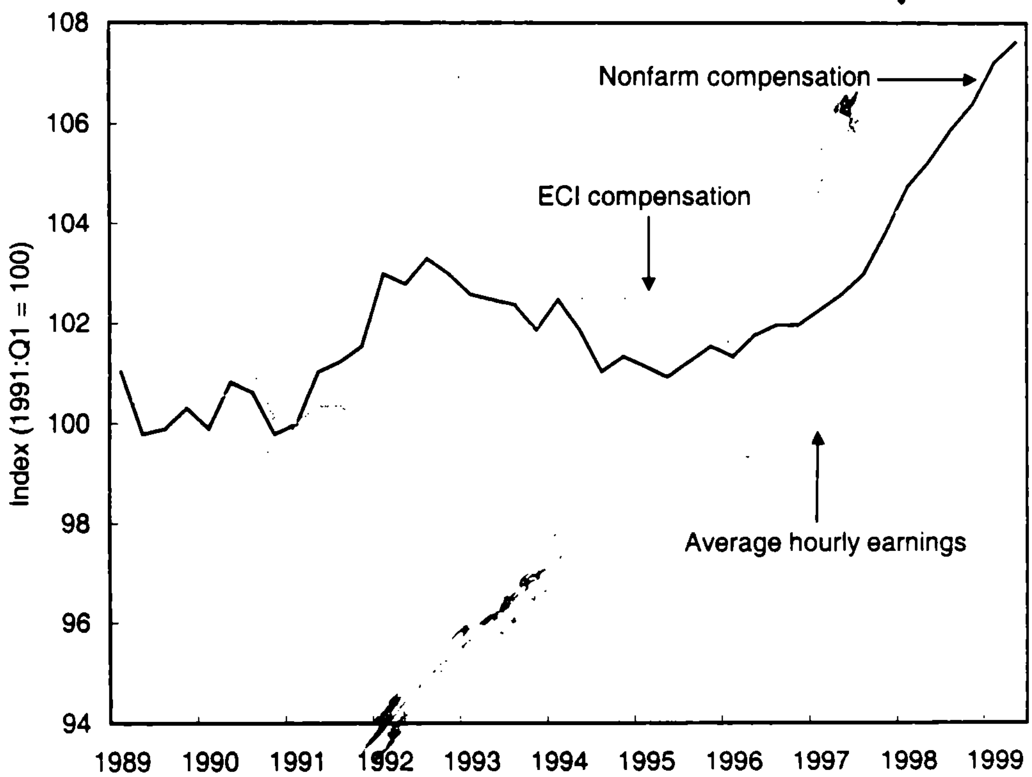
Prepared by the Council of Economic Advisers
with the assistance of the Office of the Vice President

copied entire report: CEA/Podesta
pg 7 top. HRC/Reed/Podesta
bottom. Reed/Riley/Podesta

August 6, 1999

CHART OF THE WEEK

Three Measures of Real Wages



Over the past few years, both average hourly earnings of production or non-supervisory workers (reflecting the wages of about 80 percent of private employment) and nonfarm compensation (which includes non-wage benefits) have increased faster than compensation measured by the employment cost index (ECI). The ECI is based on a constant mix of industries and occupations, while the other two reflect changes in the composition of jobs. Thus, the job-mix seems to be shifting toward higher-paying jobs.

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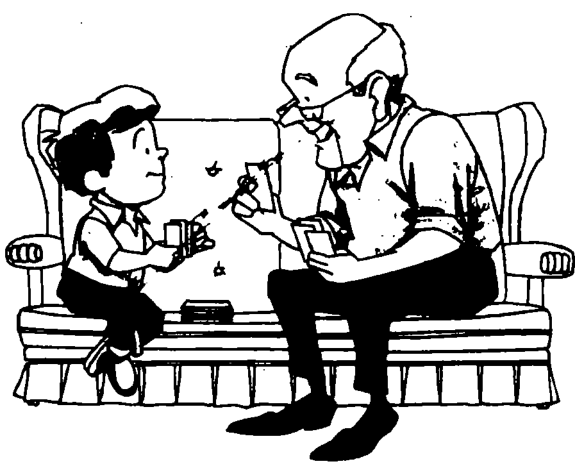
DEPARTMENTS



"Some would say I'm retired, but I like to think of myself as a stay-at-home grandfather."

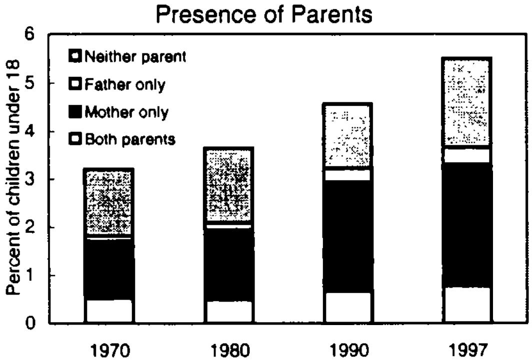
SPECIAL ANALYSIS

Balancing Work and Childcare: the Role of Grandparents

The past decade has witnessed a marked increase in grandparent involvement in raising grandchildren. An examination of this involvement over the last three decades suggests that intergenerational ties may have strengthened. Recent studies have examined the reasons for these trends and their implications for labor force participation.

Trends in living arrangements of grandchildren. Over the last three decades, the share of children under age 18 living in a household headed by a grandparent has risen by more than 70 percent to 5.5 percent of all children in 1997 (see chart). The driving force in the 1990s has been an increase in the share of children living in households with neither parent present. Between 1980 and 1990, by contrast, the increase came from children living in grandparent-headed households with just a single parent present. The share in such households with the father as the single parent present, while small, continued to grow in the 1990s.

Grandchildren in Grandparents' Homes by Presence of Parents



Interactions between caregiving and labor force participation. The rise in female labor force participation has created a greater overall demand for grandchild care that extends beyond living arrangements. Among grandparents caring for grandchildren in a non-custodial relationship, the employment of the grandchild's parents and the desire to help the grandchild's parents financially are commonly cited reasons for providing care. In addition, in a sample of working mothers aged 19-26 with a youngest child under 5 years old, nearly 25 percent utilized grandmothers as the principal caregiver. Evidence from another study suggests an intergenerational labor-force tradeoff: among women aged 51-54, 73 percent of those without grandchildren were engaged in some form of work, whereas among those caring for grandchildren, only 54 percent were in the labor force.

Impact on work and families. Evidence that caregiving is associated with labor market outcomes such as reduced hours, increased absenteeism, and missed promotions has largely been based on studies of caregiving for elderly parents or infirm spouses rather than grandchildren. While some of the effects found in this research may be present in grandchild care, other factors could be at work as well. First, grandchild care may be seen more as an opportunity than as a burden and therefore contribute to the attractiveness of retiring. Second, because employer-provided health insurance rarely covers grandchildren, the need to keep working to maintain dependents' health insurance is not the issue it could be in other caregiving situations. Third, grandchild care may allow a middle-generation individual to participate in the labor force or obtain schooling, both of which may have positive long-term effects.

Conclusion. Grandparents face an intergenerational tradeoff between work and caregiving. Choosing to provide care for a grandchild is associated with decreased labor force attachment of the grandparent but increased attachment of the middle-generation child. By participating in grandchild care, retirement-age individuals play a key role in shaping the economic well-being of future generations.

SPECIAL ANALYSIS

Farm Program Costs and the WTO

Until recently, the United States was comfortably below the limits set on trade-distorting farm supports in the Uruguay Round Agreement on Agriculture. But the recent rapid increase in farm program payments is eroding that cushion.

Trends. After record-low expenditures in 1996, Federal spending on agriculture through the Commodity Credit Corporation (CCC) is rising. The CCC's net expenditures were $4.6 billion in fiscal year 1996, $7.3 billion in 1997, and $10.1 billion in 1998. CCC net expenditures could reach $18.4 billion in 1999. USDA projects a subsequent decline, but such projections are highly uncertain. A share of these annual expenditures, along with certain other forms of support, count against the United States' Uruguay Round commitment.

Uruguay Round commitments. In total, 28 WTO members, including most major agricultural producers and traders, have made binding commitments to reduce so-called "amber box" trade-distorting supports (such as market price support payments, storage payments, marketing loans, and some forms of crop insurance) according to fixed schedules. Like other developed countries, the United States agreed to a 20 percent cut over 6 years from a 1986-88 base level. For the United States, the base level "aggregate measure of support" (AMS), which quantifies amber-box programs, was $23.9 billion. For 1999, the U.S. ceiling is $19.9 billion.

U.S. performance. For 1995-1997, the U.S. AMS averaged about $6 billion, primarily for dairy, sugar, and peanut supports. In 1998, however, low market prices resulted in higher commodity payments, especially for corn, wheat, and soy. The projected AMS for 1998 is $9 to $10 billion and that for 1999 will likely be higher, even before including amounts from any currently proposed emergency farm aid legislation. Moreover, the totals for 1995-1998 do not include non-product specific support, such as crop and revenue insurance, because such support did not meet a *de minimus* threshold of 5 percent of the total value of agricultural production.

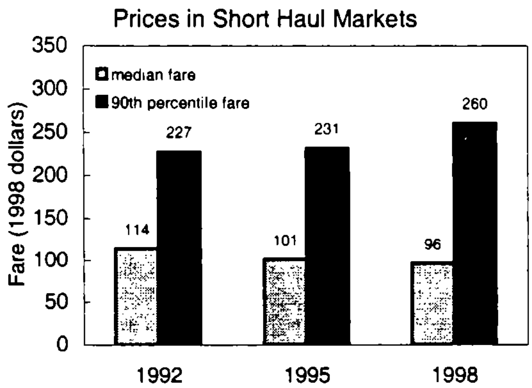
The non-product-specific "wild card." Non-product-specific support could play an important role in determining whether foreigners might allege that the United States has not met its WTO commitments. If such support exceeds the 5 percent threshold of roughly $10 billion, the entire category would then be included in the AMS. Among other factors, the amount of crop and revenue insurance subsidies, which already account for a substantial share of all U.S. non-product-specific support, could be critical.

Conclusion. If farm program spending continues to rise, the distinction between amber-box support and so-called "green box" non- and minimally trade distorting support (such as research and extension, pest and disease control, domestic food aid, and income support payments that are de-coupled from prices or production) will become even more important. There are no WTO limits or reduction commitments if support qualifies for the green box. To the extent that spending on any new farm programs or policy instruments, including government-backed risk management tools, can be tailored to meet green-box provisions, the United States stands less chance of being accused of overshooting its AMS ceiling.

ARTICLE

Why Are Fares Flying Higher for Business Travelers?

Are recent trends in the airline industry threatening the lower fares and increased service that followed airline deregulation in 1978? A recent report from the National Research Council's Transportation Research Board finds evidence that leisure travelers continue to benefit from low fares, while prices paid by business travelers have been rising.



Increased fare dispersion. This finding of divergent trends for different groups of consumers comes from an analysis of trends in fare dispersion. The Board presents evidence that on short haul routes (those less than 750 miles), the median fare (in 1998 dollars) declined from $114 in 1992 to $96 in 1998 (see chart). By contrast, the fare at the 90th percentile rose from $227 to $260 over the same period.

Airline pricing. The disparity in fares paid for essentially the same seat on any given flight reflects the widespread use of fare restrictions by airlines to separate travelers into different groups based upon their willingness to pay for tickets. Leisure travelers who plan ahead can generally get significant discounts off of the fares charged to last-minute business customers. Although this practice seems "unfair" to those paying higher fares for potentially the same seat, the cost to the airline of providing a seat to a business traveler is higher. An airline that wants to serve business customers must reserve some capacity for the last-minute business traveler, and that capacity sometimes goes unused even though it could have been sold earlier to another leisure traveler.

Competing explanations. Two different explanations have been suggested to explain why airline fares for business travelers are increasing even though fares for leisure travelers appear to be declining.

- Tighter capacity. One explanation for the increase in fares to business travelers is that airline capacity has become tighter as the economy continues to expand. As capacity becomes scarce, holding additional capacity empty for business travelers becomes increasingly costly, and business fares would be expected to increase. The Board found some evidence for this view, noting that between 1992 and 1997, the load factor for domestic carriers (a mileage-weighted ratio of passengers to seats) has risen from about 63 percent to about 69 percent.

- Insufficient competition. An alternative explanation for the increases in business fares relative to leisure fares is insufficient competition from low-cost carriers. For example, the Board found that in markets where Southwest Airlines is present, its fares are substantially below those of the incumbent airlines for both leisure and business travelers. In addition, unlike the incumbent airlines, Southwest has not sharply increased the disparity between its business and leisure fares over the 1992-1998 period.

Implications. In light of these findings, the Transportation Research Board has recommended that increasing efforts be made to ensure that airport facilities remain readily available to new entrants like Southwest and other low-cost carriers. For example, the Board notes that administrative limits (such as slot controls designed to control congestion) have also blocked new airlines from particular airports. The report recommends that airlines pay a fee to fly into congested airports during peak hours to control congestion rather than using slot mechanisms to control the number of arrivals and departures. The report also finds that limited access to airport gates can be an obstacle to entry, and that Federal rules and airport funding should be designed to encourage sufficient gate supply for new competitors.

Conclusion. While airlines may have legitimate business reasons for charging different prices for seats on the same flight, they may also be able to exploit such opportunities when competition is limited. Appropriate policies to allow competitive entry can help ensure that the benefits of airline deregulation are achieved.

8-10-99

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

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Career Academies Show Positive Results. Career academies represent one of the fastest-growing high school reforms in the nation, combining elements of the school restructuring and school-to-career movements. Organized as schools-within-schools, career academies use classroom- and work-based learning centered around an occupational area to help students gain the necessary skills to make successful transitions to post-secondary education, employment, or a combination of the two. A recent study of 10 career academies in disadvantaged areas around the country found that each was successful in establishing partnerships with a group of local employers and developing a range of career-awareness and work-based learning activities. The percentage of academy students participating in career-awareness activities outside of the school was more than twice as high as that of the control group. The gains in in-school career activities, employment during high school, and participation in high-quality work-based learning were more modest. The study found that increasing the quantity and quality of academy activities remains a challenge, as does fuller integration of classroom- and work-based learning.

A New Explanation for the Education Wage Differential among Men. Common explanations for the widening wage differential between college- and high-school-educated workers include increased technology in the workplace, immigration, and decreased unionization. But a new study finds a different explanation, at least for men, in the forces of supply and demand. In particular, since the mid-1970s male college graduates have benefited from relative pay gains because younger generations of men have been attending college at smaller rates than their predecessors, thereby decreasing the supply of college-educated workers in each successive cohort. Thus, steadily increasing demand for college-educated workers would lead to an increased relative wage. According to the study, this relative earnings gain for younger college-educated male workers is the reason for the rise in the wage differential between college- and high school-educated workers from 25 percent in the mid-1970s to 40 percent in 1998. While the earnings differential has remained the same for older workers over the past 25 years, it has doubled for younger workers.

Online Shopping Rate Shows First Decline. The latest findings from an ongoing survey of Internet users found that the percentage who made purchases online decreased for the first time last quarter. Between April 1998 and March 1999 the percentage of users who made online purchases grew from 47 to 74 percent, but it then dropped slightly to 71 percent last quarter. These findings are based on a sample drawn from a private firm's database of Internet users who have volunteered to participate in online research. Of course, continued growth in Internet usage should keep the volume of Internet purchases rising even if the percentage stops growing. The survey found that three-quarters of buyers are making multiple purchases, and 95 percent of online shoppers say that they plan to buy the same amount or even more online in the future. CDs, books, computer software and hardware, and airline tickets were the top items purchased.

INTERNATIONAL ROUNDUP

OECD Releases Latest Science and Technology Indicators. After a decline in R&D spending in OECD countries in the early 1990s, investments have recovered since 1995, according to the OECD's semi-annual *Main Science and Technology Indicators.* This reversal is apparent in the United States, where the rate of growth of gross domestic expenditure on R&D jumped to 6.5 percent in 1998 (it was –0.2 percent as recently as 1994). The ratio of R&D expenditures to GDP increased from 2.5 percent in 1994 to 2.8 percent in 1998—well above the 1.8 percent average rate for the EU. Although the public sector is the primary source of R&D financing in smaller OECD countries such as Portugal and Iceland, the business sector is the main source in R&D-intensive countries like the United States, Japan, Korea, and Sweden. Business R&D funding represents more than 65 percent of total R&D expenditures for these countries. OECD governments have shown an increased interest in health- and environment-related R&D programs, as the share of spending for such programs in total government budgets grew steadily in the 1990s.

World Carbon Emissions Fall in 1998. Last year, global emissions of carbon from the combustion of fossil fuels declined for the first time since 1993, according to a report by the Worldwatch Institute. The report estimates that emissions fell 0.5 percent to 6.32 billion tons. The decline occurred even though the world economy grew 2.5 percent in 1998. During the last 2 years, the amount of carbon emissions required to produce $1,000 of income fell by 6.4 percent. The report cites improved energy efficiency, falling coal use, and the growth of information technology and service industries that are not major energy users as explanations for the decline in carbon emissions. The de-linking of economic growth and carbon emissions was particularly dramatic in China, which grew 7.2 percent in 1998 while experiencing a 3.7 percent drop in emissions. In the United States, emissions rose only 0.4 percent in 1998, while the economy grew 3.9 percent. However, U.S. emissions in 1998 were still 10.3 percent above 1990 levels, compared with the Kyoto Protocol target for greenhouse gas emissions of 7 percent below the 1990 level by 2010.

Mexico Imposes Tariffs on U.S. Beef. In response to an anti-dumping petition against beef imports from the United States, the Mexican Secretary of Commerce and Industry announced this week that it would place tariffs of up to 215 percent on various U.S. beef products. This ruling comes following a preliminary determination by Mexico that U.S. producers were sending beef products across the border at artificially low prices and causing injury to the Mexican beef industry. Tariff amounts range from 5 percent to 215 percent across different product categories. Within these categories, however, four specific U.S. corporations were granted substantially lower tariffs than other U.S. producers. Mexico is the second largest importer of American beef, accounting for roughly 15 percent of the total value of U.S. beef exports in the January-April 1999 period.

RELEASES THIS WEEK

Employment and Unemployment

****Embargoed until 8:30 a.m., Friday, August 6, 1999****

In July, the unemployment rate was unchanged from June at 4.3 percent. Nonfarm payroll employment rose by 310,000.

Productivity

Nonfarm business productivity rose 1.3 percent at an annual rate in the second quarter. Manufacturing productivity rose 4.9 percent.

Leading Indicators

The composite index of leading indicators increased 0.3 percent in June, following an increase of 0.3 percent in May.

NAPM Report on Business

The Purchasing Managers' Index declined 3.6 percentage points to 53.4 percent in July. (A reading above 50 percent indicates that the manufacturing economy is generally expanding.)

MAJOR RELEASES NEXT WEEK

Retail Sales (Thursday)
Producer Prices (Friday)

U.S. ECONOMIC STATISTICS

	1970-1993	1998	1998:4	1999:1	1999:2
Percent growth (annual rate)					
Real GDP (chain-type)	2.7	4.3	6.0	4.3	2.3
GDP chain-type price index	5.4	0.9	0.8	1.6	1.6
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.5	**2.6**	**4.1**	**3.6**	**1.3**
Real compensation per hour:					
Using CPI	0.6	**2.5**	**2.0**	**2.9**	**1.5**
Using NFB deflator	1.3	**3.7**	**3.4**	**3.0**	**3.3**
Shares of Nominal GDP (percent)					
Business fixed investment	10.9	11.0	11.0	11.0	11.2
Residential investment	4.5	4.3	4.5	4.6	4.6
Exports	8.2	11.3	11.3	10.9	10.9
Imports	9.2	13.0	13.1	13.2	13.5
Personal saving	5.2	0.3	−0.0	−0.5	−0.8
Federal surplus	-2.7	0.9	0.8	1.4	N.A.

	1970-1993	1998	May 1999	June 1999	July 1999
Unemployment Rate (percent)	6.7**	4.5**	4.2	4.3	**4.3**
Payroll employment (thousands)					
increase per month			**28**	**273**	**310**
increase since Jan. 1993					**19243**
Inflation (percent per period)					
CPI	5.8	1.6	0.0	0.0	N.A.
PPI-Finished goods	5.0	0.0	0.2	−0.1	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, August 6, 1999**.

FINANCIAL STATISTICS

	1997	1998	June 1999	July 1999	August 5, 1999
Dow-Jones Industrial Average	7441	8626	10704	11052	10794
Interest Rates (percent per annum)					
3-month T-bill	5.06	4.78	4.57	4.55	4.61
10-year T-bond	6.35	5.26	5.90	5.79	5.88
Mortgage rate, 30-year fixed	7.60	6.94	7.55	7.63	7.89
Prime rate	8.44	8.35	7.75	8.00	8.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level August 5, 1999**	**Percent Change from Week ago**	**Percent Change from Year ago**
Euro (in U.S. dollars)	1.079	0.7	N.A.
Yen (per U.S. dollar)	114.0	-1.1	-21.1
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	94.28	-0.8	-5.9

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	4.1 (Q2)	**4.3** (Jul)	2.0 (Jun)
Canada	3.2 (Q1)	8.1 (May)	1.5 (Jun)
Japan	0.1 (Q1)	4.7 (May)	0.0 (Jun)
France	2.3 (Q1)	11.4 (Apr)	0.5 (Apr)
Germany	0.8 (Q1)	7.2 (May)[2]	0.4 (Jun)
Italy	0.9 (Q1)	12.1 (Apr)	1.4 (Jun)
United Kingdom	1.2 (Q2)	6.2 (Mar)	1.4 (Jun)

U.S. unemployment data **embargoed until 8:30 a.m., Friday, August 6, 1999.**

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

2/ Rate for former West Germany. Using OECD standardized unemployment data, the unemployment rate for unified Germany for May was 9.1 percent.

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THE PRESIDENT HAS SEEN
8-2-99

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

July 30, 1999

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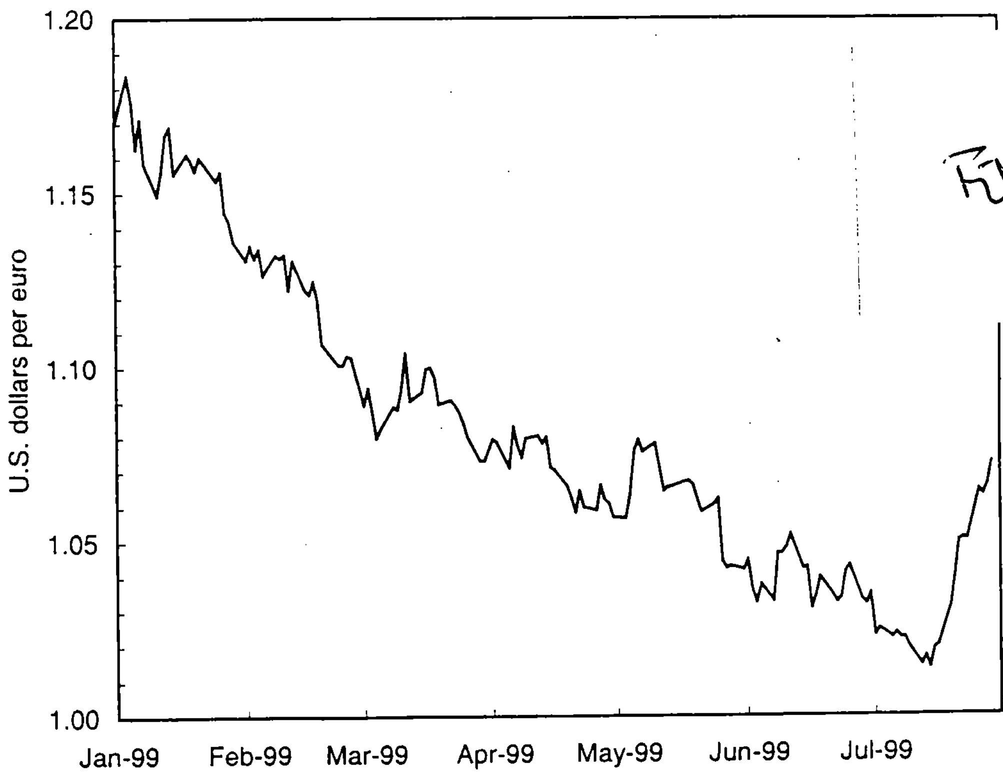
CHART OF THE WEEK

Euro Rebounds before Reaching $1.00



File

Since the euro was introduced, its foreign exchange value has slid, coming close to $1.00 in mid-July. In the past 2 weeks, however, the euro has rallied to rise above $1.05. A range of reasons has been offered for the rebound, including a heightened perception of economic strength in the euro zone and the possibility that the European Central Bank would adopt a bias toward higher interest rates.

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CURRENT DEVELOPMENT

SPECIAL ANALYSES

DEPARTMENTS

"Eight years of unprecedented expansion, and yet the kid sector has failed to participate."

8-2-99

CURRENT DEVELOPMENT

GDP Scorecard: Second Quarter 1999

Real GDP is estimated to have increased at a 2.3 percent annual rate in the second quarter of 1999. Strong gains in consumption and equipment investment were partially offset by declines in stockbuilding and net exports. The price index for GDP increased at a 1.6 percent annual rate—somewhat higher than the 1.1 percent annual rate of increase over the previous four quarters.

Component	Growth*	Comments
Total consumer expenditures	4.0%	Although consumption has slowed from the 5½ percent pace over the previous four quarters, consumers' spending ran further ahead of their income, dropping the saving rate to–1.1 percent.
Producers' durable equipment	15.3%	As has been typical in this expansion, most of the strength was in computers or other information processing equipment.
Nonresidential structures	-1.2%	Construction of industrial buildings continues to fall. Office building construction leveled off in the second quarter after a solid gain in the first.
Residential investment	5.1%	Although housing starts fell sharply in the second quarter, residential investment was supported by commissions on existing home sales.
Inventories (change, billions of 1992 dollars)	$19.3	The pace of stockbuilding was much lower in the second quarter than in the first. Inventories are now extraordinarily lean with respect to sales. CEA expects renewed stockbuilding to boost GDP growth in the second half.
Federal purchases	-3.2%	The drop reflects continued declines in Federal employment and budget authority.
State & local purchases	-0.1%	Road construction did not suffer the normal seasonal drop in the first quarter. Reciprocally, it failed to post the normal seasonal increase in the second.
Exports	4.5%	Coming after only a 0.5 percent gain over the previous four quarters, the gain in exports suggests a rebound in foreign GDP.
Imports	9.7%	Most of the increase was in capital goods, especially computer-related equipment.

*Percent real growth in the second 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.

<u>SPECIAL ANALYSIS</u>

Wives' Earnings and Family Income Inequality Revisited

New research on the impact of wives' earnings on family income inequality has confirmed earlier findings that over the broad sweep of three decades increases in wives' labor force participation and earnings have, on balance, moderated inequality. However, the new research finds that in more recent years wives' earnings have had a neutral effect on the distribution of income across families.

Conflicting forces. Married women's earnings have risen dramatically during the past three decades as their time devoted to paid work has risen substantially and their hourly wages have increased. As male earnings stagnated during this period, wives' earnings have been the main source of growth in family income. The impact on family income inequality has reflected two conflicting effects:

- <u>Reduced inequality in wives' earnings</u>. Although married women's earnings are less equally distributed than those of married men (largely because more women have zero earnings), the inequality in wives' earnings has declined over time as more have taken paid employment (and the proportion with zero earnings has declined). This effect has tended to moderate family income inequality over time.

- <u>Increasing correlation with husbands' earnings</u>. Wives' and husbands' earnings have been positively correlated throughout the past three decades, and the increase in labor force participation has been greatest among wives of high-earning husbands. In addition, more highly educated, higher-wage men tend to marry more highly educated, higher-wage women. As a result, the correlation between husbands' and wives' earnings increased between 1976 and 1990, increasing inequality among married couples.

How it all adds up. The new study confirms earlier research findings that the changes in wives' earnings over the entire period after 1967 made the married-couple family income distribution more equal than it would otherwise have been in 1994. This equalizing effect was smaller (but still existed) when all families, including single-parent ones, were included. However, the equalizing effect virtually disappears for married couples (and becomes slightly *dis*equalizing for all families) for the period after 1979. The correlation between wives' and husbands' earnings did not begin rising until the mid-1970s. Before that time, therefore, the declining inequality of married women's earnings dominated the picture; but from 1979 until at least 1994, it was balanced by the increasing correlation between wives' earnings and those of their husbands.

Conclusion. The impact of increases in wives' earnings and labor force participation on family income inequality depends on a complex set of interactions. Recently, the rising correlation between wives' and husbands' income (and its aggravating effect on inequality) has become important enough to offset other factors, leaving little net effect.

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SPECIAL ANALYSIS

Effects of WIC on Birth Outcomes

Relative to many other industrialized countries, the United States has surprisingly high rates of low-weight births, pre-term births, and infant mortality, particularly among blacks. Research on the impact of the Special Supplemental Food and Nutrition Program for Women, Infants, and Children (WIC) finds that WIC participation leads to significantly better outcomes in important measures such as birth weight for black infants—though not for whites.

The WIC program. WIC is specifically designed to combat the negative birth outcomes that are often associated with the socioeconomic status of the mother and conditions during pregnancy (such as smoking, drug use, and inadequate prenatal care and nutrition). It is a national clinic-based program that provides a variety of nutritional and health-related goods and services to pregnant and postpartum women, infants, and children under the age of 6. The program had 7.4 million participants in 1998 and an appropriation of $3.9 billion in FY 1999. To be eligible, participants must have a low family income (at or below 185 percent of the poverty level) and a demonstrated "nutritional risk" factor (such as anemia, low weight, or drug-use). One estimate is that roughly 50 percent of income-eligible women were covered by WIC in the early 1990s.

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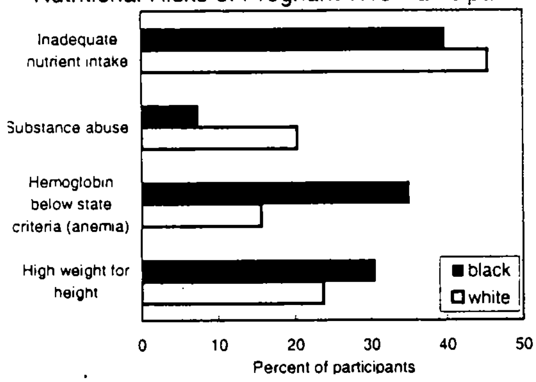
Research findings. Evaluating WIC's effectiveness is complicated by selection issues. On the one hand, women most in need of services may be the ones who choose to participate, making the program appear more effective than it might be for others. On the other hand, women who pay particular attention to their health may be the ones who seek additional assistance, in which case the program may appear to be less effective than it might be for others. However, a new study that pays particular attention to these selection issues provides some of the strongest evidence to date on the effectiveness of the program.

Its results suggest that prenatal WIC participation increases birth weights for black infants by 5 to 13 percent. The study also finds a statistically significant increase in gestational length of 1.4 percent, a reduction in the likelihood of a pre-term birth of 5 percent, and significant reductions in the likelihood of a neonatal and infant death. However, the new study for the most part found no significant effect of WIC on birth outcomes for whites. This last finding is consistent with previous research, which has found smaller or no effects for whites.

Accounting for racial differences. The study suggests possible explanations for why WIC appears to have a stronger effect for blacks. First, it may be the case that prior to any WIC intervention, white mothers are, in ways unobservable to the researcher, healthier at the time of their pregnancy, so that the marginal impact of WIC may be smaller for them. Second, some evidence suggests that black and white women differ in the risk factors that make them eligible for the

Nutritional Risks of Pregnant WIC Participants



program (see chart), suggesting the possibility that the program may be more effective at combating the ill effects of some risk factors than of others.

Implications. The new study provides strong evidence that WIC is effective at improving birth outcomes, at least for a needy subgroup of the population. As welfare caseloads decline and fewer expectant mothers receive assistance through the traditional welfare system, the importance of WIC could increase.

8-2-99

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Anne
As by Cathy

Child Support Enforcement is Working Better Than We Think. Although the share of single mothers receiving child support has remained roughly the same (about 30 percent) over the past 20 years, child-support enforcement has actually improved, according to an Urban Institute study. The study finds that a shift in the composition of single mothers away from divorced or separated mothers toward never-married mothers has masked improvements in the receipt rate for both groups. Between 1976 and 1997, the receipt rate of never-married mothers increased from 4 to 18 percent while that of previously married mothers rose from 36 to 42 percent. However, the proportion of never-marrieds (with their lower receipt rates) increased from 17 percent in 1976 to 46 percent in 1997. The study estimates that over half of the rise in child support rates for never-married mothers and a third of the rise in child support receipt rates for previously married mothers can be attributed to greater enforcement efforts and the expansion of funding for child support enforcement.

Study Examines the Gender Gap in Retirement Income. On average, single women have less wealth and income in retirement than single men. In addition, women aged 65 and older are about twice as likely to live in poverty as are similarly-aged men. A number of studies have examined widowhood as an important determinant of these differentials, but a new study looks at differences in work histories, since women earn less on average than men, are concentrated in female-dominated fields, and work fewer years during their prime. The study finds that the first two of these factors significantly lower a single woman's retirement wealth and that the three combined can explain 85 percent of the retirement wealth gap. The authors conclude that if women's earnings continue to climb as they have over the past decade or so, future cohorts of women approaching retirement will enjoy higher well-being, both absolutely and relative to men. Continuation of the slow but steady observed fall in occupational segregation should contribute further to that improvement.

Recent Studies Show Sharp Differences in Well-Being in the DC Region. The District of Columbia ranks last in a recent ranking of the best states for raising children, well below its neighbors Maryland (7) and Virginia (23). This finding is complemented by a new Brookings Institution study finding that metropolitan Washington is prosperous but deeply divided. Signs of overall prosperity include a remarkably low regional unemployment rate and a growing number of jobs, partly due to the exploding technology industry; rising capital investment; and housing, retail, and office markets that are among the hottest in the country. However, the western areas (including parts of Northwest DC) typically enjoy wealth and prosperity while the eastern parts suffer from high rates of poverty. DC and Prince George's County are home to a disproportionately high percentage of the region's poor citizens, single mothers, and struggling schools. The area is also racially segregated, with 70 percent of the area's African American population living in DC or Prince George's County. Most of the region's job growth took place in the western parts and outside of the Capital Beltway.

INTERNATIONAL ROUNDUP

OECD Warns Against Complacency in South Korean Restructuring. In its recent survey of the South Korean economy, the Organization for Economic Co-operation and Development noted that the country has been remarkably successful in overcoming the financial crisis at the end of 1997. The OECD concludes that supportive macroeconomic policies and progress in structural reform have laid the foundation for positive growth in 1999. However, the survey warns that the success to date should not lead to complacency about the necessity of fully implementing the new framework put in place after the crisis and in making additional improvements. A priority emphasized by the OECD is further progress in establishing a healthy, market-based financial system. The OECD also argues that much needs to be done to restructure the corporate sector, using the new governance framework that has been put in place. Events this week surrounding the restructuring of Daewoo, Korea's second largest chaebol (business conglomerate), have focused attention on the country's commitment to structural reform. After falling almost 15 percent over the previous 5 trading days, the Korean stock market rose over 6 percent on Tuesday, in part apparently on news that the government has strengthened its commitment to push corporate reform and that the restructuring of Daewoo would proceed apace. Meanwhile, the latest production data show that South Korea's industrial output rose 29.5 percent from a year earlier in June, the largest such increase since August 1988.

European Central Bank Keeps Interest Rates Unchanged. The Governing Council of the European Central Bank (ECB) decided at its July 29 meeting to keep interest rates unchanged, despite speculation earlier this week that an interest rate hike might be announced. The speculation was fueled by the recent remarks of ECB president Wim Duisenberg indicating that a reassessment of the ECB's interest rate policy might be appropriate once economic growth starts to accelerate. As discussed in the Chart of the Week, Duisenberg's comments were probably one factor contributing to the recent rise in the euro. In addition, positive market sentiment regarding the prospects for euro area output growth has been reflected in a narrowing of the gap between United States and euro area bond yields (as well as in the appreciation of the euro). The most recent ECB Monthly Bulletin discusses how new data point to a stabilization of overall output growth in the euro area in early 1999 and to an economic recovery in the second part of 1999 and into the year 2000. Press reports also indicate that the most recent German and French business confidence indexes were stronger than expected. On the monetary side, rapid credit expansion and sustained growth of the monetary aggregates at rates above the ECB's reference rate of 4.5 percent per year have raised concerns in some quarters about future price stability. For the present, however, the ECB has not decided to raise rates.

RELEASES THIS WEEK

Gross Domestic Product

According to advance estimates, real gross domestic product grew at an annual rate of 2.3 percent in the second quarter.

Employment Cost Index

The employment cost index for private industry workers rose 3.3 percent for the 12-month period ending in June.

Advance Durable Orders

Advance estimates show that new orders for durable goods rose 0.3 percent in June, following an increase of 0.8 percent in May.

Consumer Confidence

Consumer confidence, as measured by The Conference Board, fell 3.4 index points in July, to 135.6 (1985=100).

MAJOR RELEASES NEXT WEEK

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

U.S. ECONOMIC STATISTICS

	1970-1993	1998	1998:4	1999:1	1999:2
Percent growth (annual rate)					
Real GDP (chain-type)	2.7	4.3	6.0	4.3	**2.3**
GDP chain-type price index	5.4	0.9	0.8	1.6	**1.6**
Nonfarm business (NFB) sector:					
Productivity (chain-type)	1.5	2.7	4.3	3.5	N.A.
Real compensation per hour:					
Using CPI	0.6	2.6	2.2	2.6	N.A.
Using NFB deflator	1.3	3.8	3.8	2.6	N.A.
Shares of Nominal GDP (percent)					
Business fixed investment	10.9	11.0	11.0	11.0	**11.2**
Residential investment	4.5	4.3	4.5	4.6	**4.6**
Exports	8.2	11.3	11.3	10.9	**10.9**
Imports	9.2	13.0	13.1	13.2	**13.5**
Personal saving	5.2	0.3	-0.0	-0.5	**-0.8**
Federal surplus	-2.7	0.9	0.8	1.4	N.A.

	1970-1993	1998	April 1999	May 1999	June 1999
Unemployment Rate (percent)	6.7**	4.5**	4.3	4.2	4.3
Payroll employment (thousands)					
increase per month			321	-5	268
increase since Jan. 1993					18895
Inflation (percent per period)					
CPI	5.8	1.6	0.7	0.0	0.0
PPI-Finished goods	5.0	0.0	0.5	0.2	-0.1

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

New or revised data in **boldface**.

FINANCIAL STATISTICS

	1997	1998	May 1999	June 1999	July 29, 1999
Dow-Jones Industrial Average	7441	8626	10854	10704	10791
Interest Rates (percent per annum)					
3-month T-bill	5.06	4.78	4.50	4.57	4.59
10-year T-bond	6.35	5.26	5.54	5.90	5.88
Mortgage rate, 30-year fixed	7.60	6.94	7.15	7.55	7.70
Prime rate	8.44	8.35	7.75	7.75	8.00

INTERNATIONAL STATISTICS

Exchange Rates	**Current level July 29, 1999**	**Percent Change from**	
		Week ago	**Year ago**
Euro (in U.S. dollars)	1.072	2.0	N.A.
Yen (per U.S. dollar)	115.2	-1.8	-19.1
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	95.06	-1.2	-4.5

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	4.1 (Q2)	4.3 (Jun)	2.0 (Jun)
Canada	3.2 (Q1)	8.1 (May)	1.6 (May)
Japan	0.1 (Q1)	4.7 (May)	-0.4 (May)
France	2.3 (Q1)	11.4 (Apr)	0.5 (Apr)
Germany	0.8 (Q1)	7.2 (May)[2]	0.4 (May)
Italy	0.9 (Q1)	12.1 (Apr)	1.6 (May)
United Kingdom	1.2 (Q1)	6.2 (Mar)	1.3 (May)

1/ For unemployment data, rates approximating U.S. concepts as calculated by the U.S. Department of Labor, Bureau of Labor Statistics.
2/ Rate for former West Germany. Using OECD standardized unemployment data, the unemployment rate for unified Germany for May was 9.1 percent.