# CHAPTER 5

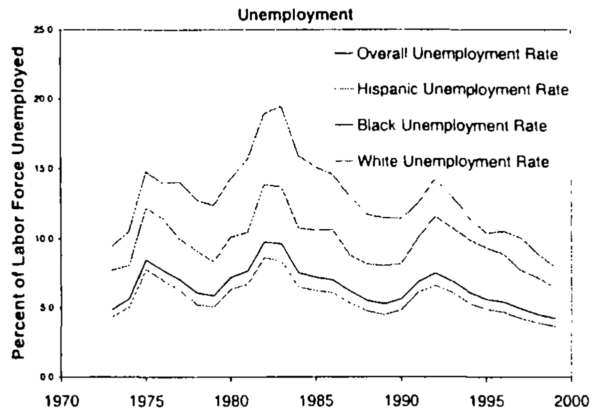
# LIVING IN THE NEW ECONOMY

THE CLINTON ADMINISTRATION FIRST came to office on a platform of "Putting People First." And indeed that pledge has been met. While the phrase "the new economy" typically brings to mind technological innovation and globalization, arguably one of the most important outcomes has been the change in the well being of the American people. By virtually any measure, Americans are better off today than they were eight years ago. Furthermore, as we highlight in the chapter, many of these improvements have benefited those who have been among the hardest to reach. Yet despite the dramatic gains, there is still more to do. Through a combination of public policy and continued economic growth the country can build upon its recent successes and tackle the remaining problems.

## Good News from the American Economy

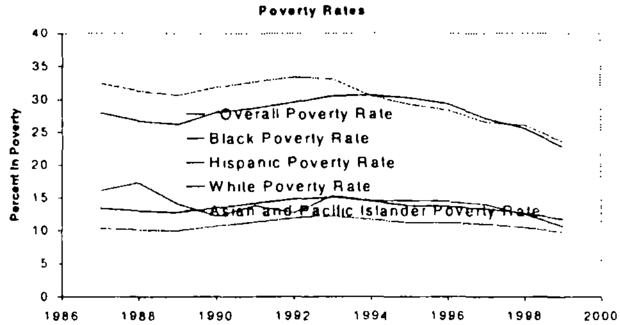
The record setting gains in the stock market and growth in the net worth of the wealthiest individuals have received much attention in the popular press. What is noteworthy about this economic expansion, however, is the breadth of its reach. The last few years in particular have brought tremendous gains to the poorest segments of our society.

- The gains in employment have been astounding. Since 1993, 22 million new jobs have been created and more Americans are employed than ever before. The unemployment rate has fallen to 3.9 percent, the lowest level since 1969 and black unemployment has reached 7.0 percent, the lowest level ever recorded.




At the same time, earnings increased substantially for African Americans. The earnings of full-time year-round black workers increased by $2,379 or 8.6 percent in just this past year, substantially closing the gap between the earnings of white and black males.

These gains in employment are echoed in growth in income and decreases in poverty. Median household income reached a new high of $40,800 in 1999, up 2.7 percent over the previous year, and 14.9 percent from 1993. Importantly, many of the most disadvantaged subgroups experienced the largest improvements. Median income for African American households increased by 7.7 percent in the past year and by 24 percent since 1993. The poverty rate for African Americans is now the lowest ever recorded. Female-headed households are another group that has often been left behind. This year, however, median income for female headed households increased by 4.8 percent for a total of 18.0 percent since 1993. For years poverty in central cities has seemed intractable, yet here too the situation is improving; residents of central cities experienced an above average increase in median income and the largest declines in poverty of any geographic area.




The strong economy coupled with Administration policies have lead to a long list of improvements in the quality of life for Americans. Low interest rates and a strong economy have helped more Americans than ever before afford a home. In the second quarter of 2000, 67.2 percent of American families owned a home up from 63.9 percent in the same quarter of 1993. Improvements in job opportunities, additional police officers, and tighter controls on guns have all contributed to a dramatic reduction in crime, with violent crime falling by 35 percent since 1993.

After years of decline, our public schools are improving. More young people are graduating from high school than ever before, and more are attending college. SAT math scores have reached their highest level in 30 years and verbal SAT scores have held steady despite an increasing number of non-native English speakers taking the exam.

Strides have also been made along the public health dimension. The number of teenage pregnancies has declined 14 percent since 1993, and smoking among teenagers declined for the first time in nearly a decade. The fraction of high school students who said they had smoked a cigarette in the preceding 30 days fell from 36.4 percent in 1997 to 34.8 percent in 1999. There is good news for both the youngest and oldest Americans. Infant mortality is down from 8.4 per thousand in 1993 to 7.2 in 1998. Deaths from heart disease, cancer, strokes and HIV are all down, and life expectancy is up. A child born in 1998 can expect to live nearly 76.7 years, up from 74.9 years just 10 years earlier.

While these statistics present a glowing picture of the new economy, more work remains to be done. Despite the tremendous recent gains, the incomes of minorities remain significant below those of whites and poverty is significantly higher. Infant mortality and life expectancy also differ substantially by race and ethnicity, as does access to a quality education. As the country moves into the new millennium, we must tackle these issues.

**Helping Families Help Themselves**

The new economy has been characterized by new technologies, new methods of communication, and new avenues of trade. However, it has also brought with it new ways of providing for the least well off Americans. With a strong economy and a policy of making work pay, more Americans than ever before are participating in the labor market, and the number on welfare has fallen dramatically. Low income families are receiving assistance in making the transition to independence through a network of social programs designed to help families bridge the gap from welfare to work. By placing the emphasis on helping working families, the administration has changed the tenor of social welfare policy.

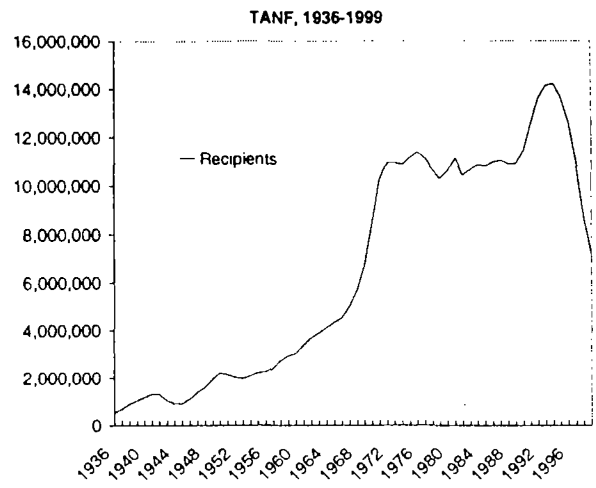
*Welfare Reform*

One of the most impressive achievements of the past eight years has been the reduction in the number of individuals receiving welfare. The administration began working towards welfare reform in 1993 by approving a number of waivers that allowed states to implement changes in their welfare programs on an experimental basis. As of August 1996, 43 states had implemented waiver programs and case loads had begun to fall.

These state level changes were followed by passage of the Personal Responsibility and Work Opportunity Act (PRWORA) in 1996. This Act dramatically changed the welfare system on a national level. It replaced the Aid to Families with Dependent Children (AFDC) program with a program of Temporary Assistance to Needy Families (TANF), established time limits on welfare receipt, and placed the emphasis on helping families leave welfare and enter the labor market. Families are aided in this transition through provisions that subsidize the earnings of low-income workers, offer assistance with child care, and ensure continued access to health insurance.

TANF differs from AFDC in several fundamental ways. Under the former AFDC program states set benefit levels, and received matching grants from the federal government to help with the cost of the program. In contrast, TANF provides states with block grants which they use to finance benefits and support other related programs. Under TANF states have much more flexibility in how the money is spent than they did under the former AFDC program. Second, the new system contains strict time limits and work requirements: Federal funds cannot be used to pay benefits to recipients who have received assistance for a lifetime total of five years, although states can exempt a small fraction of recipients from this requirement. Alternatively, states may set even shorter time limits. In 1999 38 states used the 60 month time limit. With respect to work requirements, TANF recipients must work in some capacity after two years of receiving benefits. Again states have a good deal of flexibility in implementing the rule and particularly in strengthening requirements. In 1999 28 states had welfare policies that imposed immediate work requirements in lieu of the two year limit. Finally, a third dimension in which TANF and AFDC differ significantly is the ability of states to design the parameters of the program to best suit their needs. While states always had the freedom to set benefit levels, TANF allows them to establish their own income disregards, income limits and asset tests. The majority of states have used this freedom to decrease the implicit tax on earnings. The AFDC program required reducing benefits dollar for dollar for any earnings above $90 per month if the individual had been enrolled in AFDC for one or more years. This "tax" creates a strong disincentive to work, as in many cases the AFDC participant could receive no increase in income from additional hours of work. Under TANF most states impose a more gradual benefit reduction rate to encourage greater workforce participation.

Following these changes, case loads have fallen dramatically. Since August of 1996 a total of 6 million individuals have left welfare. This represents a reduction of 49 percent




Looking back to 1993 to include the reductions that took place during the period of state waivers, the welfare caseloads fell by 7.8 million or 56 percent. Declines in some states have been even more dramatic. In Wisconsin, for example, the number of welfare cases fell by 70 percent between 1996 and 1999, and by 82 percent since 1993. **[Can anyone help us get estimated 2000 numbers before our deadline?]**

The 1996 reforms have undeniably been a success in reducing the number of individuals receiving welfare. However, reductions in case loads are not the only measure by which to judge the accomplishments of the policy. An important outcome is the well being of individuals once they leave the rolls. Because welfare reform was so recently implemented, little information exists about the outcomes of those who have left welfare. Much of what we know comes from studies conducted by a small set of individual states and counties, often including data from the state waiver experiments undertaken prior to PRWORA. This Report supplements this state-level information with new results from the 1996 panel of the Survey of Income and Program Participation (SIPP), providing some of the first evidence of the effect of welfare reform for a nationally representative sample. The majority of our results from SIPP are based on a sample of individuals who leave welfare and are observed for at least 12 months following the exit. Individuals are first observed in mos. of 1996 and survey data currently exists through the spring of 1998. We are therefore examining the experience of some of the early leavers after welfare reform, and are unlikely to observe the effect of binding time limits.

When considering the outcomes of the 7.8 million individuals who left welfare, one of the first issues that comes to mind is the incidence of recidivism—the number of individuals cycling on and off the rolls. Here again, the results are encouraging. Data from SIPP show that only 25 percent of the leavers in the sample return to welfare during the firsts 12 months after exit. The majority of those who do return do so quickly; 18 percent of those who exit return within the first 6 months of leaving while only 7 percent return during the second 6 month window. One would imagine that the probability of returning would continue to fall with the length of time off welfare.

A key component to successful exits from welfare is the ability to obtain a job and remain employed. Efforts to help individuals obtain jobs have tended to use one of two strategies. The first aims to get people employed as quickly as possible, assuming the work itself will teach the skills needed to remain in the labor force and eventually move to a better job. In this approach the focus is on maintaining some attachment to the labor force rather than on initial wages. The alternative approach uses more extensive training prior to entering the labor market. In this case labor market entry is delayed, but the initial job should be of higher quality. The first method is by far the most commonly employed, and initial evidence indicated that it was more successful.

However, a new study comparing outcomes across counties in California finds that over the long term the results for the two methods appear to be similar.

Although the increases in employment were not as dramatic as the declines in case loads, the gains in labor force participation are still substantial. Data from studies of several different states show that approximately 55 percent of those leaving welfare were employed in any particular quarter in the year subsequent to leaving welfare. Of those who took a job, 40 percent remained employed for a year and 70 percent worked during at least one quarter in the first year off welfare. On a national level, the outcomes are equally encouraging. Data from SIPP show that of those observed for 12 months after leaving welfare, 66 percent were employed at some point and 62 percent of this group (41 percent of the total) had earnings in all four quarters of the year. A large fraction of workers not only have earnings in all four quarters, but were in effect, continuously employed, and many of these were employed full-time. Thirty-two percent of welfare-leavers worked 50 weeks or more during the year, and 40 percent of this group worked 35 or more hours in every week.

Importantly, the rates of employment increased even among those who remained on welfare. In 1999, 33 percent of welfare recipients were working, compared to just 7 percent in 1992. The development of an attachment to the labor market for those currently on welfare bodes well for future exits for these individuals. In both groups of workers, the importance of the new economy should not be understated: The longer the economic expansion continues, the more job skills former and current welfare recipients will accumulate, and the better prepared they will be to weather an economic downturn.

There is a concern that welfare recipients who get jobs are likely to lose them soon after. In the sample of SIPP leavers who were working at some point during the 12 months following exit, 48 percent did leave a job during that period. However, when examining reasons for leaving a job, the most common explanation was "left for new job" reported by 22 percent of respondents.

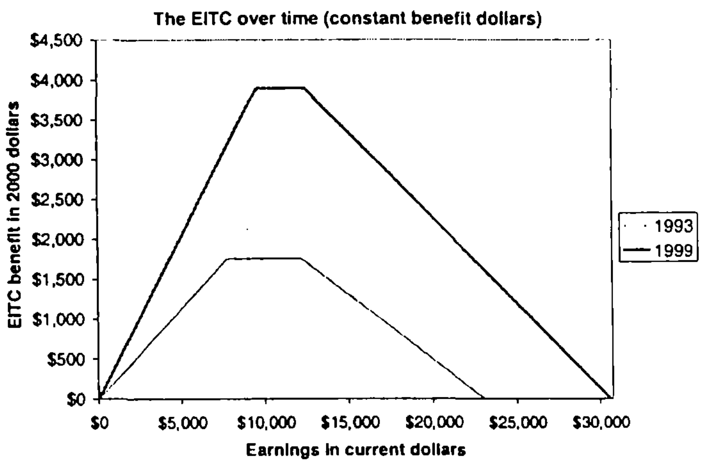
In addition to employment status, success after welfare can be gauged by the amount of earnings, and the potential for earnings growth. For the sample of SIPP leavers, median monthly household income plus food stamps for the year following exit was $1,401, compared to a statistically equivalent $1,468 in the two months preceding exit. For 44 percent of leavers, the total household income plus food stamp in the post-exit year was more than $50 higher than in the months before leaving, while for 49 percent it was at least $50 lower. One would not expect many of these new entrants to the labor market to have jobs that pay a very high wage, or even a wage that provides income above the poverty line. In fact, when looking only at earning and not household income, 48 percent of leavers who had any earnings at all had earnings below the poverty line in each of the 12 months following exit. When other sources of income are taken into account, however, this fraction with household income below the poverty line in every month falls to 29 percent. It is important to recognize that credits from the Earned Income Tax program (discussed in detail below) are not included in these calculations. While benefits from the EITC are not recorded in the SIPP data, the program provides a substantial subsidy to the earnings of low-income workers and would likely change incomes and poverty rates considerably.

More important to assessing the potential success of the employment relationship is the extent to which earnings grow over time. Comparing outcomes over just the first 12 months after exit, 39 percent of leavers had monthly earnings in the second 6 months that were $50 or more higher than in the first 6 months. Only 28 percent had a $50 or greater reduction in earnings over the two 6 month periods. Thus, a large fraction of former welfare recipients find jobs that provide earnings growth through increases in hours or wages or both.

*Making Work Pay*

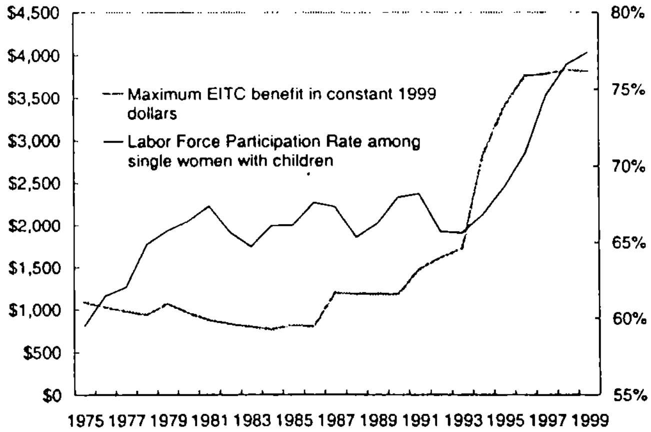
The transition from welfare to work is facilitated by a network of government support programs available to working families. In the past, families that left welfare often lost not only their cash assistance, but also faced other implicit taxes on their incomes through the loss of in-kind benefits, such as food stamps and Medicaid, and additional expenses incurred by working, such as the cost of child care and transportation. One study estimates that the implicit marginal tax rates—the decrease in the amount of government transfers for resulting from a one dollar increase in income--for AFDC recipients could range as high as 109 percent with the highest rates faced by those near the poverty line. In other words, earning one dollar more in the labor market would reduce benefits by $1.09 and total income by $0.09. PRWORA has attempted to reduce these "taxes" by expanding health insurance coverage to include many working families, increasing child care tax credits, and increasing the rewards from work through minimum wage policies and increases in the Earned Income Tax Credit (EITC). These programs also benefit low income working families who were not on welfare. By reaching out to this often neglected group and providing financial assistance, help with affordable child care and health insurance, the administration has worked to ensure that no group is left behind.

*EITC*: The EITC is one of the most successful programs targeted at low wage workers and is currently the largest cash transfer program in the country. Operating through the income tax system, the EITC provides a wage subsidy to low income workers with the amount of the subsidy depending on earned income and number of children. By increasing the wage rate the EITC creates stronger incentives for individuals to participate in the labor force. For a families with two or more children, wages are subsidized by 40 cents for every dollar of earned income until earned income reaches $9,540 (in 1999) for a maximum credit of $3,816. This tax credit is refundable so that even families who pay little or no tax can benefit fully from the program. Rather than eliminating the credit when earnings surpass this level, the credit remains at $9,540 for a period and then gradually reduced, phasing out completely at earned income of $30,565. This gradual reduction reduces the disincentive to work past the level at which the credit peaks.




The EITC has been expanded greatly since 1993 with increases in both benefits and in the scope of coverage. The 1993 expansions increased benefits for all eligible families, and particularly for those with two or more children. The expansion also allowed workers without children to claim a tax credit. As a result of these expansions, benefits paid through the EITC program increased from $18 billion in 1993 to nearly $32 billion in 1999, and the number of families receiving assistance from the program increased by one-third, from 15 million to nearly 20 million.

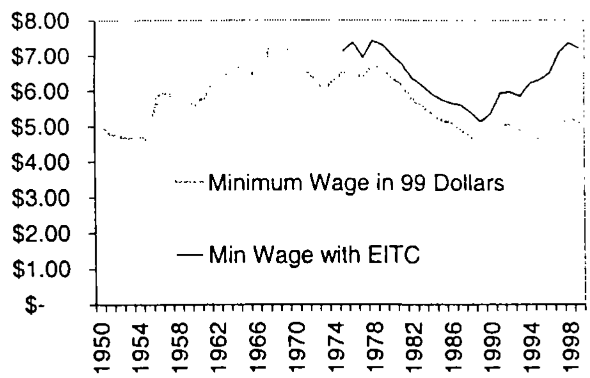
The wage subsidy has been effective in attracting more workers to the labor market. One study in particular estimated that the EITC alone was responsible for 34 percent of the increase in annual employment of single mothers over the period 1992 to 1996.




The EITC program also plays an important role in reducing the implicit marginal tax rate faced by those exiting welfare.

In addition to increasing the probability of employment, the EITC has done much to improve the well being of those who take advantage of the program. While the discussion above pointed out the difficulty former welfare recipients have in securing jobs that pay above poverty level wages, when the EITC is taken into account the earnings of many of these new workers increase substantially. In 1999, the EITC lifted 4.1 million individuals, including 2.3 million children, out of poverty. The program has also been effective in targeting benefits to the most needy. Estimates are that over 60 percent of EITC benefits accrue to families who have pre-EITC incomes below the poverty line.

*Minimum wage:* Operating in tandem with the EITC is the minimum wage. Although the EITC provides a wage subsidy, the minimum wage laws ensure that the subsidy is based on a fair wage. The real value of the minimum wage fell in the early 1990s hitting just 61 percent of its 1968 value in 1995. Subsequent Administration-backed efforts led to increases in the minimum wage in 1996 and 1997 [edit later: and additional increase of one dollar passed just this fall.] With this most recent increase, the minimum wage reaches 68 percent [edit later] of its 1968 level.




However, when combined with a possible 40 percent EITC subsidy, the true minimum wage for low income workers is $7.21, a figure nearly as high as the peak minimum wage rates in the 1960s.

*Child care:* For many parents, one of the most difficult aspects of employment is affording adequate child care. For low income families and new entrants to the labor market, the costs associated with child care sometimes make work impossible. In recognizing the cost of child care as barrier to work, PRWORA sought to increase the affordability of child care for low income families and to provide for more families. In doing so it combined various child care assistance programs already in existence to create the Child Care and Development Fund (CCDF) and substantially increased the funding. The CCDF provides states with block grants to subsidize approved child care arrangements. In 1999 states had access to a total of over $3 billion to use to improve and quality and affordability of child care. Unfortunately, despite the generous funding, the majority of states have waiting lists for benefits and many who qualify for the subsidies do not receive benefits. Estimates are that only 10 percent of eligible children are receiving benefits. According to one study, only 30 percent of families who left welfare and are now working as also receiving assistance with child care. [edit later: Proposal for $1 billion more in funding] However, despite the shortages, the number of children benefiting is large. In fiscal year 1998, an average of 1.5 million children received CCDF assistance in each month.

Although common sense and economic theory suggest that these subsidies will increase the probability that parents participate in the labor force, little evidence of the labor force participation effects of the program is available. This difficulty exits because most experiments of the effect of child care subsidies have also included other support programs such as health insurance and assistance obtaining employment and the effects of the different programs cannot be disentangled. An important issue along these lines is the extent that the subsidies allow parents who could not otherwise obtain care afford to do so. It is possible that by subsidizing child care the CCDF program crowds-out, or replaces, unpaid care. A mother who may have used a grandparent as a caregiver might choose a paid provider when she is offered a subsidy. If this is the case than the change in labor market participation as a result of the program will be small.

It is also unclear how the CCDF program affects the quality of care. If paid care replaces unpaid care, are children better off? Alternatively with a reduction in price, do parents demand higher quality care? The theoretical predictions are unclear. However, it is worth noting that the CCDF subsidies can be used only to purchase care from approved providers. In this sense it might improve the overall quality of care if parents substitute away from unlicensed providers.

*Food stamp program:* The food stamp program supplements family incomes to ensure that low income families receive adequate nutrition. Benefits are available to families with incomes up to 130 percent of the poverty line. The vast majority of benefits, 90 percent in 1999, go to families with children or elderly individuals. In 1999, 32 percent of benefits went to working families. Over the past few years, enrollment in the food stamp program has fallen dramatically from a high of 27.5 million participants in 1994 to 18.2 million in 1999. This decline is notable even among families with children. Only 51 percent of children in families with incomes below the poverty line received food stamps in 1999. Even among the very poorest---children in families with incomes below 50 percent of the poverty line---only 58 percent received food stamps in 1999, a decrease of 47 percent since 1993.

This decline would be good news if families were becoming self-sufficient and did not need government assistance. However, there is a concern that many eligible families are not receiving benefits that they need. In particular, it is hard to imagine that those with incomes below 50 percent of the poverty line have sufficient resources that food stamps would not be a valued supplement. The decline in food stamps may connected to the decline in welfare participation. When families leave the welfare rolls they may believe that they are no longer eligible for food stamps, or alternatively they may not be informed of their eligibility by state welfare agencies. Newly working families may also find it difficult to retain benefits if they must miss work to be re-certified or if they have difficulty filling out the forms required to report changes in income. While a good deal of anecdotal evidence exists about the importance of various explanations for the decline in participation, we know of no study that has quantitatively assessed the validity or importance of these explanations. However, based on the sample of leavers in the SIPP data there does appear to be a sudden drop in the use of food stamps. Sixty-eight percent of those who exited welfare were receiving food stamp benefits while on the TANF rolls, compared to just 44 percent in the month immediately after exit. However, perhaps surprisingly, a similar decline is observed for those who leave welfare in the 1993 SIPP panel, well before the implementation of welfare reform. This comparison suggests that the drop in food stamp participation is not due to the institutional changes enacted by PROWRA.

Despite the drop in food stamp participation, there has been a sharp decline in food insecurity and hunger among Americans. Results from a recent survey found that the fraction of households in which someone went hungry fell to its lowest level ever recorded, 2.8 percent of the population--24 percent below the level in 1995 when the survey began. There is, however, a cautionary note: food insecurity (defined as being uncertain of having adequate food) for those with incomes between 50 and 130 percent of the poverty line actually rose. Furthermore, approximately one-third of those households with incomes below 130 percent of the poverty line—the income limit for food stamp eligibility--experienced food insecurity at some point, and over 10 percent experienced hunger. The figures are even larger for households with children.

*Health Insurance Expansions*: In the past, welfare participants who were successful in obtaining a job and exiting welfare typically lost their Medicaid coverage. This loss is likely to be costly and provides a strong incentive to remain on welfare. One of the important features of PRWORA was the expansion of Medicaid coverage and the creation of the State Children's Health Insurance Program (SCHIP), both of which provide health insurance coverage for children in low income working families. Because of the importance of these programs, they are discussed later in the chapter.

*Reaching out to Underserved Communities*

Providing opportunity and independence for American families, often requires more than a strong national economy and responsible welfare policy. In some areas poverty is so entrenched and the local economy so weak that programs specifically targeting these regions are needed. Some of the most intractable poverty in the country has been found in central cities. In 1967 when statistics for central cities were first recorded, the poverty rate for these areas was 15.0 percent compared to a nationwide rate of 14.2 percent. By this measure then, central cities were nearly as well off as the rest of the country. In contrast, poverty in non-metropolitan areas in 1967 was over 20 percent. Since that time, there has been a substantial shift in the incidence of poverty, with a worsening of conditions in the central cities, and an improvement in non-metropolitan areas. By 1993, the percent of central city residents living in poverty had reached 21.5 percent, its highest level ever, while the poverty rate in non-metropolitan areas declined somewhat to 17.2 percent.

Several factors are offered as explanations for the plight of central cities. The first is that central cities have social and demographic characteristics that make their populations particularly susceptible to poverty: The population of central cities is more likely to be illiterate, have low job skills, live in female headed households, and have little education, than the population of non-central cities. Secondly, residents of central cities often lack the social connections to help them find the jobs necessary to escape from poverty. These factors are associated with high levels of poverty regardless of area of residence and current policies to make work pay, discourage out of wedlock child-bearing, and improve schools in poor neighborhoods, are addressing these issues.

What appears to distinguish the situation in central cities from that in other areas are the limited job opportunities. Recent research has shown that the majority of job creation is taking place in suburbs rather than in inner cities. One study compared the number of low-skilled jobs in central cities and surrounding suburbs, with the number of low-schooled workers in each area, for four different cities. It found that the fraction of new job openings in the central cities and in the suburbs matched well with the fraction of people living in each area, but that once skill differences were taken into account, there was a spatial mismatch: the vast majority of new low-skilled jobs were concentrated in the suburbs, while the majority of low-skilled workers were in the central cities. Estimates from one study based on a small sample of cities found nearly 3 times as many new jobs per low-skilled worker in suburban areas than in central cities. For African Americans the situation is especially severe. Only 4 percent of low-skilled jobs were African American areas in central cities while 67 percent of low-skilled African Americans lived in these areas as did 42 percent of impoverished female-headed households. Furthermore, a recent HUD study found that between 1992 and 1997 not only was job growth was slower in the cities than in the suburbs, but that the job mix in cities is shifting toward high-tech jobs that are unavailable to low-skilled workers.

The difficulty central city residents face in finding employment is further heightened by transportation problems. Low-income workers, and welfare recipients in particular are unlikely to own cars. They must therefore rely on public transportation to commute to jobs. The suburbs are not well served by public transportation. The same study found that nearly half of low-skilled jobs in the suburbs were not accessible by public transportation. Furthermore, a reverse-commute, if possible at all, is extremely time consuming. While some cities and employers have chosen to provide transportation from the inner city to jobs in the suburbs, a more permanent solution is likely to be found in rebuilding the economies of central cities.

The administration has taken on this challenge and has developed a package of programs designed to improve the economic opportunities in distressed communities. The three main components of this package are the New Markets Initiative, Empowerment Zones (EZs) and Enterprise Communities (ECs), and the Community Development Financial Institutions Fund (CDFI fund). These programs provide an alternative means to helping American families. While TANF, food stamps, and other parts of the social safety net provide direct and often immediate assistance to needy families, these community redevelopment programs work towards longer term solutions to poverty and unemployment by assisting in the rebirth of distressed communities. The benefits from such programs, like the benefits from some employment based programs, take time to be realized. Despite the long term nature of expected gains, preliminary evidence from some of the earliest programs finds is just starting to be assessed. This evidence points to **[HUD can you help us get the early results on this? ]**

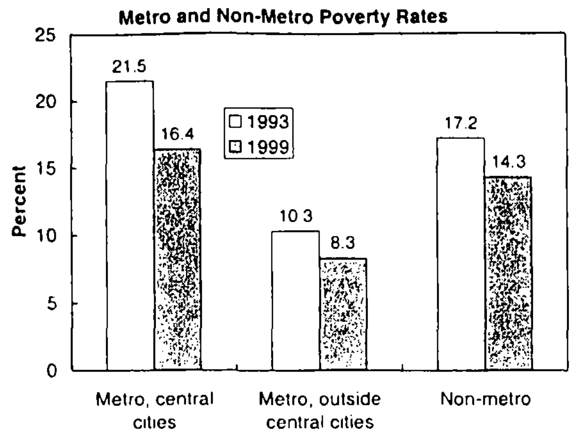
**Community Redevelopment Programs**

The administration's community development policies aim to assist distressed communities by encouraging investments from the private sector. These programs provide incentives such as tax credits and improving access to credit markets. At the foundation of this policy are empowerment zones and enterprise communities, typically referred to as EZs and ECs. In 1994, when these programs began, 105 cities were designated as EZs or ECs. The EZ and EC programs give communities substantial flexibility in developing new initiatives under the belief that problems can best be assessed and solved on a local level. The federal government helps by providing tax benefits and technical assistance to businesses expanding or locating new facilities in the target zones. It also provides grants to the communities themselves to support activities such as job training programs, day care centers, and community technology centers. Finally EZs and ECs can apply for waivers from federal regulations to help address specific economic problems.

The Community Development Financial Institutions Fund (CDFI) is similarly designed to encourage the development of new private markets in distressed communities. The CDFI does so by expanding the amount of capital available in these areas. CDFIs include community development banks, credit unions, venture capital funds and business loan funds. These institutions provide credit and other banking serves to a diverse set of clients including home buyers and small business.

Much of the New Markets Initiative is still before Congress [edit later]. However, an important component of the Initiative is the New Markets Tax Credit. This program offers a 25 percent tax credit designed to stimulate investments in distressed communities. It is anticipated that a wide variety of businesses will benefit from the program including retail stores, shopping centers, and small technology firms.

Through the combination of policies addressing both the long term and short term needs of the urban population, the quality of life for those living in central cities has improved dramatically. The unemployment rate in central cities has fallen from 8.2 percent in 1993 (July) to 4.8 percent in 1999 (July). This increase in employment has brought with it a reduction in poverty and an increase in median income. The poverty rate in central cities declined from 21.5 percent in 1993 to 16.4 percent in 1999, with the largest drop, a decline of 2.1 percentage points, coming in the past year. In fact, 80 percent of the total reduction in poverty from 1998 to 1999 was due to the reduction in central cities.




Median household income in central cities has also increased, rising 5 percent from 1998 to 1999 compared to a 2.1 percent increase for median incomes in metropolitan areas as a whole. For African Americans the gains were particularly striking. Median income for African American households in central cities increased by 13.9 percent in the one year period. Along with these economic gains has come a decline in the number of individuals on welfare. Case loads in central cities have declined by 40.6 percent from 1994 to 1999.

Despite these dramatic improvements, there is more to do. Poverty rates and unemployment are higher in central cities than elsewhere. In 1999 the national poverty rate was 11.8 percent compared to 16.4 percent in central cities. Furthermore, although dramatic, the 40.6 percent reduction in welfare was substantially smaller than the 51.5 percent decline nationwide. And there continues to be a mismatch between the skills of the urban work force and the demands of urban jobs. The administration's New Markets Initiative, EC/EZs and the CDFI fund provide hope for a fundamental change in the plight of inner cities, but these initiatives must be backed with other programs that focus on the future. As our new economy demands a more highly trained work force we must invest in our schools, where sufficient jobs cannot be brought to the inner cities we must provide transportation systems to move workers to jobs, and finally, we must continue to support policies that make work pay.

### Education in the New Economy

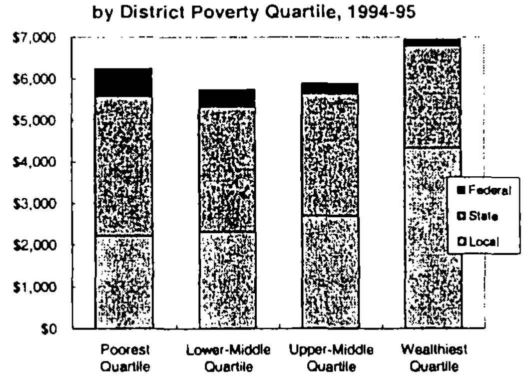
The rapidly expanding economy that has permitted these improvements in the well being of Americans is based in large part on information and technology growth. Continued growth therefore depends critically on a well-trained work force. The 2000 Economic Report focused on the demand for educated workers and the increasing economic returns to education. This year we examine America's public schools, noting recent changes in the ways in we educate our children and how we might best improve the quality of schooling we offer our children.

*A Role for Federal Education Policy*

In the United States, responsibility for elementary and secondary education has traditionally been left to the states and to local school districts. As a result, our public education system is extremely decentralized, and the federal role is limited. Given the structure, the federal government can best help local school districts by strategically targeting funds to where they will be most effective and by supporting and publicizing sharing best practices promising initiatives developed at the local level. In particular, the federal government has sought to improve access to education for the nation's poorest children and to help states improve the overall quality of their public schools. While economic incentives ought to induce parents to invest optimally in the education of their children, many poor families and communities lack the economic resources to do so. In these cases federal funds can play an important role.

Excluding school-based nutrition programs, the Federal government provides just over 6 percent of the funding for K-12 education. However, these funds are primarily targeted to new programs and to schools and school districts serving poorer students and can therefore have a larger impact than their magnitudes would suggest. While federal spending in the poorest schools does reduce the inequalities across districts it does not fully compensate for funding disparities related to local property tax bases and state funding for schools.

**Federal, State, and Local Revenues per Pupil, by District Poverty Quartile, 1994-95**




The largest single federal program for kindergarten through 12th grade (K-12) education is Title I, which allocates funds based on child poverty rates. The targeting of Title I funding towards schools serving poorer children increased significantly with the passage of the 1994 Elementary and Secondary Education Act. In the 1997-98 academic year, 96 percent of schools in the highest-poverty quartile received federal Title I funds, up from 79 percent in 1993-94. This quartile of schools contained 49 percent of the nation's poor children in 1997-98, and received 43 percent of all federal funds for K-12 education. These redistributional aspects of

Title I funding are typically significantly larger than any redistributional efforts on the state level.

There are many components to a quality education. While certainly parents, family, and communities play a crucial role, the discussion here is limited to features of the educational system more directly under the control of federal, state and local governments. We highlight in particular ~~those~~ aspects which current research suggests are most important and which are the subject of recently policy initiates. The analysis discusses the effect of class size on learning, teacher quality, the infrastructure of schools and equipment, and curriculum changes.

*Reducing class size*

Over the past decade, mounting evidence has shown that reducing class size can improve academic achievement, especially for students from disadvantaged backgrounds. Teachers in smaller classes can spend more time on individual instruction and review, and spend less time on student discipline and routine administrative tasks. Teachers of small classes may know their students better, interact with them more frequently and individually, and provide more frequent and in-depth feedback.

The effects of smaller class sizes appear to be significant and long lasting. A recent study of an experiment on class size in Tennessee found that students who were enrolled in smaller classes in kindergarten through grade 3 did better than students who were not in smaller classes

Better transition needed

even after returning to larger-sized classrooms in later grades. These students also did better on their SAT and ACT exams, and were more likely to take such college-entrance exams than students who never had the benefit of a small class. The results were especially strong for minority students—being in a small class in elementary school narrowed the difference in black/white probability of taking a college entrance exam in high school by 54 percent.

While the majority of research has concluded that students do better in smaller classes, reducing class sizes is expensive. Fully funding reductions in class size nationwide to 18 students per class would cost more than 5 billion dollars per year. Yet given the relationship between test scores and future earnings, the economic benefits of reducing class sizes will exceed these costs even if they lead to improvements of only 0.1 of a standard deviation in standardized test scores. Alternatively, this $5 billion could be spent on other improvements such as raising teacher salaries, renovating schools, lengthening the school year or upgrading textbooks and materials.

Meaning?

Paying for the needed reductions in class size is hampered by the current distribution of students and resources. A disproportionate share of the cost of class size reductions would be borne by schools serving poor students, since these schools currently have larger classes than more wealthy schools. Furthermore, there is little room at the state level for a reallocation of funds to assist poor schools. The majority of the inequality across school districts is attributable to differences in resources at the state level. Such cross-state differences can be best addressed through federal programs. In 1998, the administration proposed a seven-year Class Size Reduction Initiative to reduce class sizes nationwide to 18 students per class. In its first year, the program spent a total of $1.2 billion. These funds enabled school districts to hire 29,000 new teachers, reducing class sizes from an average of 23 students per class to an average of 18 students per class for 1.7 million children. In its second year, the program spent $1.3 billion.

reference report?

*The need for well-qualified teachers*

Reducing class sizes requires an increase in the number of teachers. This increase in demand is in addition to an already predicted surge in the number of teachers needed over the next decade. Between July of 2000 and July of 2008, the population aged 5-17 will increase by more than a million, while about three-quarters of a million teachers are expected to retire. Other teachers will leave the field of teaching for other occupations. Ignoring the effects of class size, the United States will need approximately 2 million new teachers over the next 8 years. Currently most occupations are seeing much sharper increases in starting salaries than the teaching profession, leading to an increase in the gap ~~of~~ between starting salaries for new teachers those for other occupations also requiring a college degree. This trend will make it difficult to find qualified applicants for the millions of new positions becoming available.

provide #s here.

Study quantifies impact of teacher.

One would expect the learning experience of a child to depend substantially on the quality of the classroom teacher. With sudden increases in the demand for teachers due to reductions in class size, it is difficult to maintain a consistently high level of quality in all classrooms. In 1996 California began a massive class-size reduction program, spending $1.5 billion per year with the goal of reducing class sizes statewide from an average of 28 students per class to a maximum of 20. By the 1998-99 school year, over 92 percent of California's students were in classes of 20 students or fewer. However, in grades K-3, where the class size reduction program was targeted, the percentage of teachers who were fully credentialed fell from 98 percent in the 1995-96 school year to 87 percent in the 1998-99 school year. This fall in the credentials of teachers was even greater in schools with the largest proportions of low-income children. Success of nationwide reductions in class size thus depend on the ability to attract and retain qualified teachers.

**Box 5 Teacher Compensation**

Changes in teacher compensation are a possible way to attract more highly motivated and skilled teachers to the profession, improving academic performance. The level of teacher pay is often cited as a problem in recruiting and retaining highly qualified teachers. In theory, higher pay will increase the pool of applicants for teaching positions, especially among the highly skilled and motivated, resulting in better teachers. However, simply raising teacher pay will also encourage lower skilled teachers already employed to stay in teaching positions.

Researchers have also examined proposals for altering the structure of teacher pay, such as paying teachers based on effort and skill as measured by student performance. Performance based pay would mean a significant departure from the traditional teacher pay systems, which base teacher pay on uniform schedules, providing higher pay for higher education, experience, and extra responsibilities. Under traditional pay systems, pay scales are based on objective criteria, and teachers with identical education levels, experience, and workloads receive the same pay. While this does eliminate potential disparities based on administrator's subjective criteria, it does not reward exceptional teachers—even with the same education and experience levels, different teachers are likely to have different results. In theory, providing compensation tied to the performance of the teachers or their students will spur teachers to higher performance, and attract people who feel that they are likely to benefit from such a system to the teaching profession. Performance awards would also provide clearer guidance to teachers who have been operating with unclear or multiple competing goals. Developing and implementing a school-based incentive pay system may complement the standards movement—since educational objectives are being more clearly defined and progress towards them is being more clearly assessed, linking pay performance is much more feasible than it used to be.

Yet, such performance-based pay systems for teachers must be very carefully designed. Student learning in a school involves the cooperative effort of many people. Incentives must be designed to create cooperative, not competitive, environments between teachers within a school. Educational achievement is also based on factors over which teachers have little or no control—such as family circumstances and previous education. Thus, incentive systems must reward teachers for the progress of students during the period they teach them, rather than absolute achievement levels. Incentives may also too narrowly focus attention on a few easily measurable indicators of educational achievement, when what is really desired is broader progress in many areas, some very difficult to measure. Yet another issue is whether incentive pay is effective at all, as it may undermine intrinsic motivations that effectively motivate teachers now.

*The Need for New Schools*

All students need safe, healthy, and modern places to learn. Communities across the country are struggling to address urgent safety and facility needs. The average public school was built or most recently renovated -42 40 years ago, and schools with more minority or poor students are more likely to be housed in older buildings. Many such older buildings require extensive upgrades of their electrical systems in order to install computers, upgrades made even more expensive by the widespread presence of asbestos in their walls.

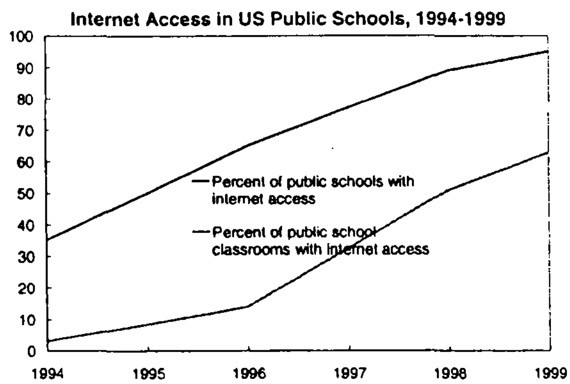
Increasing enrollments will put further pressure on aging educational facilities as will reductions in class size. The Department of Education estimates that $127 billion is needed to bring American's schools in good overall condition. Already, 39 percent of public schools in the U.S. contain temporary additions, one-fifth of which are in less than adequate condition. Schools with more minority students and schools with more poor students—the very schools whose students would benefit most from reduced class sizes—are more likely than other public schools to have temporary buildings. Their temporary buildings are also most likely to be in less than adequate condition. To help address these problems, the current federal budget includes $25 billion in school modernization bonds and $6.5 billion in loans and grants for urgent school renovation to modernize 6,000 schools and make emergency repairs to another 25,000 over the next five years.

Wait for [illegible]

*New Educational Technology and Internet Access*

As workplaces require more computer literacy from their workers, schools must prepare their students to enter the labor force with increasing familiarity with these technologies. Internet access can also be a tremendous resource in classrooms, giving students new incentives for learning and communicating, and connecting them to the resources of libraries, museums, and educational materials from around the world.

Between 1994 and 1999, tremendous strides were made in connecting public schools to the internet. The number of public schools with some connection to the internet nearly tripled between 1994 and 1999. B By 1999, 95 percent of public schools had some connection to the internet and 98 percent of public secondary schools were connected. The increases in internet connectivity were even sharper for classroom connections: increasing from 3 percent of public school classrooms in 1994 to 63 percent in 1999.

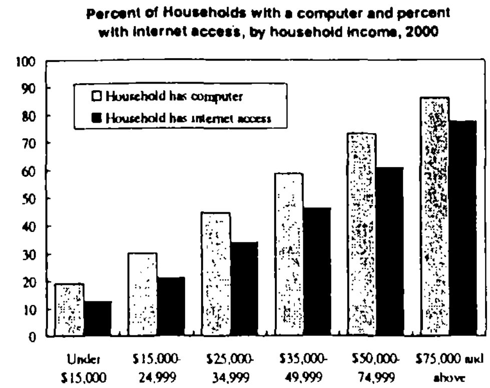



For computers to improve the quality of instruction teachers must know how to use the machines and how to integrate their usage into classroom instruction. Approximately one-half of the public school teachers with computers or internet access in their schools report using these resources for classroom instruction. Teachers who have received more professional development in using computers and the internet, younger teachers, and teachers in schools with fewer poor students were more likely to report using computers and the internet. Only one-third of teachers with access to computers and the internet said that they felt well or very well prepared to use computers and the internet and only one-fifth felt very well prepared to integrate educational technology into the classroom. Clearly, more investment in teacher preparation is needed.

The Federal government has helped local school districts make the transition to the digital age. Through its e-rate program, the Federal government has spent $5.3 billion as of September 2000 to connect school and library computers to each other and to the internet. These funds have been targeted to poor students: Schools with 75 percent or more of their students receiving free school lunch receive approximately ten times as much funding per student from the program as schools with the smallest percentage of poor students. Most of the funds have gone to establishing within-building connections between computers.

**Schools are reducing the Digital Divide**

Since 1993 computer use in America has grown ~~at an~~ enormous rate, revolutionizing the way Americans communicate, work and do business and computer knowledge and access is becoming increasingly important for success in today's society. Currently more than one-half of all US households have computers, and more than two-fifths have internet access in their own homes. However, internet access is not spread evenly among Americans. Its use varies greatly with income and education--people in households earning more than $75,000 per year are almost 4 times as likely to use the internet as people in households earning less than $15,000 per year.

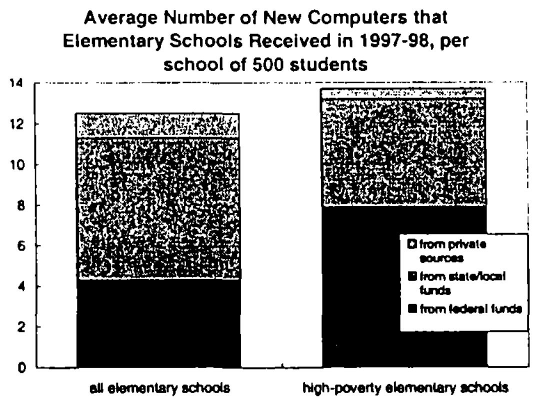



Adults with college degrees are nearly 6 times as likely to use the internet as adults who have not completed high school. There are also large differences by race. African Americans and Hispanics are substantially less likely than white and Asian Americans to use the internet. While some of this difference is due to differences in income and education, a recent study finds that approximately one-half of the difference in access is unexplained by these factors. As the level of technological literacy required by employers rises, there is an increased risk that individuals from disadvantaged groups who already face obstacles in the workplace will fall even further behind.

There is, however, good news along this front. African American, Hispanic, and lower-income Americans are connecting to the internet at faster rates than whites, Asians, or wealthier Americans. The most notable changes are occurring among school aged children, suggesting that the widespread availability of computers in the classroom is playing a role. Across all income and demographic groups, children aged 9-17 are more likely to use the internet than are older Americans. Over the last few years internet usage has grown faster among African American and Hispanic children than among white children, and faster among children in households earning less than $35,000 per year than among children from higher income households. Between 1998 and 2000, the gap in internet usage between black and white children decreased by 9 percent, although the gap in internet usage between Hispanic and white children grew by 9 percent. The gap between internet usage among children from households earning less than $35,000 per year and children from more wealthy households was unchanged.

have

Other federal programs also helped schools purchase new educational technology. In 1997-98, the most recent year for which such data is available, the federal government spent $688 million on increased access to technology in schools. These funds were used primarily for the purchase of computers and for professional development in using new technology. During the 1997-98 school year, federal funds paid for one quarter of new computers in schools. Federal funds were especially important in the acquisition of technology in high poverty schools, accounting for nearly 60 percent of funds for new computers in high-poverty elementary schools.




*Institutional Change*

Large investments in education are taking place—in hiring new teachers, in educational technology, in connecting schools nationwide to the internet, and in professional development for teachers. Yet the changes in American public schools which have happened over the past decade go far beyond increasing these investments. Dramatic changes are also taking place in the way that school resources are used. Organizational change has become a permanent part of the educational environment. The nature of change has moved from top-down mandates to site-based innovation and system restructuring including new ideas like schools as learning communities, the importance of professional development for teachers, and the central role of meaningful parental involvement. In the last decade, four major system-level strategies for delivering education have emerged: standards-based accountability, whole-school reform, market strategies, and shared decision-making. Each represents an attempt to address differing interests from a wide range of stake-holders including children, parents, teachers, school administrators, and legislators.

The dominant state-level strategy today is standards-driven accountability. It is hoped that establishing clear performance outcomes and systematically testing student progress, will stimulate teachers and students ~~stimulated~~ to focus their efforts in the right direction. Despite the popular appeal of standards and the widespread efforts to implement it, them many observers are reserving judgment on ~~its~~ their ability to generate widespread change. State after state has implemented standards for what all students need to learn in school. These standards have been followed by an increase in standards-based assessment, giving policymakers, parents, and students themselves more information for decision making.

Forty-nine states now have adopted statewide standards for what students should be studying in English, mathematics, science, and history and the social studies—thirty of the states implemented these standards after 1994. Forty-eight states have adopted state tests to assess student performance against these standards in reading and math—seventeen also assess student performance against science and social studies standards. Thirty-six publish some form of report card for each school, measuring school performance against a number of indicators, including assessment tests.

By implementing challenging tests with consequences that are enforced, schools can raise the expectations—and the motivation levels—of students, teachers, and parents. For many years, opinion surveys have shown that Americans believe our nation's schools are doing poorly—but that their own local schools are doing far better than the average. Experts warn that parents may not realize when their own children are falling behind. Standards-based assessments can ~~give~~ provide parents, teachers and other local decision-makers with objective information about how well students are learning—not only in comparison to other students in the same school, but to students at other schools as well. Furthermore, evidence suggests those countries and regions with standards and external assessments of student achievement have historically done better on comparison tests of student achievement.

The Federal Government has played an important role in spurring the standards movement by providing funds for developing voluntary national standards and granting more than $1 billion to help state and local education agencies in every state implement school reforms through the 1994 Goals 2000 Act. In addition, the Elementary and Secondary Education Act (ESEA) tied state standards implementation to continued receipt of Title I funds for poor schools. The legislation required that standards used in schools receiving Title I funds are the same standards used in schools not receiving Title I. This meant that states had to implement standards for all schools, or risk losing millions of dollars in Title I funds. The Federal government has also increased its assessment of American students' progress, better enabling us to evaluate these state-level reforms. In recent years, the Department of Education has expanded the National Assessment of Educational Progress (NAEP) to track student performance in each state. From the NAEP, we now have a tremendously valuable set of baseline indicators for 1990-1996 against which we will be able to measure student progress this decade and in future. This will help us evaluate student performance across states with widely differing state tests.

Along with implementing standards, schools and teachers have also made progress in developing and refining curricula. Over the past decade, educational researchers have formed a consensus on how best to teach reading to young children, ending the unproductive "reading wars". This consensus was summarized in the National Reading Panel's recent "Teaching Children to Read," and in the National Research Council's "Preventing Reading Difficulties in Young Children." These reports stress the importance of explicit instruction in the building blocks of written language (phonics), within the context of a broader educational program that interests children in reading for a variety of purposes and gives them ample opportunities to practice their reading skills.

*Giving Schools the freedom to innovate*

A persistent thread in the last decade of educational change has been the call for parental choice. Critics have argued that public schools have little incentive to improve, because they have a near-monopoly on schooling. Allowing parents to choose among alternatives would create a marketplace for education in which competition for per-pupil funds would force schools to improve.

Many states have answered these critics by allowing parents, teachers, or other interested parties to establish independent schools chartered by state or local education agencies. These charters give schools autonomy over their operations, and exempt them from certain state and local regulations (although not from standards-based assessment). Beginning with Minnesota in 1991, the number of states allowing such charter schools swelled to 36 states and the District of Columbia by the end of 1999. **[Could the Dept of Ed or anyone help use get more current** over 2,000 **numbers on schools and enrollments?]** By the beginning of the 1999-2000 school year, there were 1,605 charter schools in operation nationwide, and the number of such schools was growing by more than 40 percent per year.

Although charter schools represented less than 1 percent of all US public schools in 1999-2000, their rapid growth has made them the recipients of a great deal of attention, especially in areas where a significant percentage of students now attend these schools. Charter schools tend to be about a third the size of nearby public schools. Most enroll students of similar race and ethnic backgrounds as the students in their surrounding districts, although school districts with charter schools tend to have larger minority student populations than the national average. Most reported that they became charter schools to "realize an alternative vision of schooling." Nearly 90 percent reported that their students' achievement and their finances were monitored by their chartering agencies.

Charter schools have great potential as laboratories of educational innovation, allowing individual schools to experiment with a variety of different educational methods and student populations. It is hoped that successful charter school innovations will eventually spread back to the broader public education community.

**Innovation and Access in Health Care**

Another important aspect of any individual's well being is his health status. The quality medical care available in the United States is the best in the world, and recent medical innovations have further enhanced the quality of care. In addition to the benefits of a longer and healthier life accruing to individuals, improved health can also feed back to help the economy by reducing the number of sick days for employees and improving productivity. In this section we will illustrate a few of the more recent medical innovations, and discuss issues relating to access to health care.

*Innovation*

The past decade has seen dramatic innovations in medical care and treatment of individual conditions, and on a broader scale, in the relationship between patients and the medical system as a whole. A number of biomedical, pharmaceutical, and information technology advances have led to significant changes in the methods of treating people and in the health outcomes of individuals with those conditions. Health statistics reflect the impact of these advances. The treatment of heart attacks provides a powerful example of the role of innovation in improving health outcomes. Clinical trials of alternative acute heart attack management techniques have led to major changes in the treatment of heart attacks, and these changes directly accounted for approximately 55% of the decline in heart attack mortality between 1975 and 1995.

Not only are people living longer, but they are doing so with a lower incidence of disease and a higher quality of life. For example the rate of functional impairment has decreased. For the elderly there has been a significant decline is functional disability over the last xxx period and 24-41% of this decline has been attributable to innovations in medical care.

The health care industry has spawned dramatic technical changes in the last few decades. The number of new drugs that have been approved has increased rapidly: from 1995 to 1998, an average of 37.5 new drugs were approved each year, an increase of nearly 50 percent over the average rate of approval between 1989 and 1994, and a 65 percent increase over the period from 1985 to 1989. New biomedical knowledge has led to treatments for conditions that medicine could not previously address, to less invasive procedures, and to more accurate diagnostic techniques.

A few examples illustrate the benefits of these changes: More than four million Americans have Alzheimer's disease, the most common form of dementia. For centuries, people had to accept the progressive loss of intellectual and social abilities as an inevitable process for those afflicted. However, in 1976 a specific neurotransmitter was found to be associated with the incidence of Alzheimer's disease. Since that time there has made substantial progress in the treatment of Alzheimer's disease with many of the gains coming in the last 5 years. New drugs such as donepezil, introduced in 1996, are now widely available, and act to temporarily enhance cognitive functioning and delay disease progression. This development has brought new hope to many Alzheimer's elderly and their families. The value of such treatment is great; and potential savings generated from reduced formal or informal care-giving services, and delayed or avoided institutionalization can be as large as $63,000 annually per patient. A potential cure for Alzheimer's disease may be within reach as scientists identify the genes associated with Alzheimer's disease.

Cataract surgery provides another example. In the 1960s, cataract surgery required a large incision and, therefore, postoperative hospitalization for as long as a week. The invention of phacoemulsification, a process that breaks the cataract into tiny pieces that can be extracted by a small incision, has now made cataract treatment a ten-minute outpatient procedure. In addition, the change from eyeglasses, to contact lens, to inserted optic lenses (IOL) on operated eyes has greatly enhanced patients' post-operative vision. This advancement resulted in not only a better treatment, but the simplification of the process means that cataract surgery is performed by more physicians and is available to people who would previously have gone untreated. The increase in the number of cataract surgeries is substantial; among residents of one county studied in Minnesota, the rate of cataract extraction for individuals over 65 increased by four times from 1980 to 1994.

Not only were there important innovations in the treatment of diseases, but there were also significant improvements in the ability to diagnose disorders. The recent development of

Functional Magnetic Resonance Imaging (FMRI) provides an example of such a diagnostic advance. FMRI is an extension of MRI, which was developed in the late 1970s and widely diffused in the U.S during the 1990s. MRI, like CT-scans and X-rays, enables the observation of internal anatomical detail. However, FMRI improves significantly on these older diagnostic tools in that it does not use potentially harmful radiation and provides better resolution and greater contrast between normal and abnormal tissues. FMRI enables observation of entirely new internal processes. For example, physicians can obtain information about the functioning of the central nervous system, such as subtle increases of blood flow associated with activation of parts of the brain. The newer generation of MRI can detect chemical concentrations, and metabolic and water interaction; all of which can aid brain mapping and biochemical change mapping caused by different diseases. However, MRI, and FMRI are expensive improvements: MRI costs XX times as much as CT.

These examples provide specific illustrations of the value of recent medical innovations. A number of other critical advances have been made. For example, doctors can now transfer organs including hearts, lungs, livers and kidneys, none of which were possible a few decades ago, and the use of immonosuppresants has greatly increased the success of grafts. Modern telecommunication devices and speech recognition programs have been applied to compensate people with visual, hearing, and physical impairments, improving the quality of life of many people.

**Pharmaceutical Innovation and Costs**

While medical advances open the doors for new and improved treatments, they also contribute significantly to the increases in health care costs. Pharmaceutical innovations illustrate this phenomenon. The rate of pharmaceutical innovations has been accelerating: the number of new drugs introduced per year increased from 23 in 1990 to 53 in 1996, and an estimated 100 new drugs in 1998. These new drugs improve existing drug therapies or provide entirely new options for treating conditions. A few examples of the benefits of drug advances are new immunosuppressive agents that increase graft survival, and cholesterol reducing drugs that reduce the risk of heart attack. However, the accelerating innovation rates have been accompanied by an accelerating cost of drugs: spending on prescription drugs increased at an annual rate of 12 percent between 1993 and 1998, far faster than the 5 percent increase in overall health expenditures.

This growth in spending is due to a number of factors. One of these is that these new drugs are replacing cheaper older drugs. New drugs are priced two to four times higher than old drugs within the same disease subcategory. This higher cost of new drugs accounts for about 40 percent of the increase in drug costs. A second factor is that new drugs have very high utilization rates, and thus even without a price increase, they push medical spending higher. This accounts for about 40 percent of increased drug spending. Higher prices for existing drugs accounts for about 20 percent of the increase in the drug spending.

Because drugs provide improved health benefits while at the same time escalating costs, an important issue is how to evaluate whether those extra costs are better spent on drugs or other alternatives. Medical researchers attempt to estimate the cost effectiveness of a drug by measuring the benefits in terms of quality adjusted life years (QALY), which capture the gains from both longer life and quality of life. By comparing the cost per QALY of alternative treatments, the treatments can be ranked by their cost effectiveness. One study reviewed 228 cost-utility analyses and found that median cost per QALY was $11,000. While there is no standard threshold for cost effectiveness, $50,000 to $100,000 has often been used as a benchmark in the U.S.

However, cost-effectiveness does not mean cost saving. It appears that pharmaceutical innovations have concentrated on new and more expensive remedies, whether or not they are cost-effective. This continues to put pressure on health care costs, and thus on health insurance, pushing access to the benefits of pharmaceuticals out of the reach of some. Thus, the health care system must develop a greater understanding of how to create incentives that will spur cost-saving innovations, making improved health more affordable for all.

*The challenge of improving health insurance coverage*

As noted, the health care system in the United States is capable of providing the highest quality health care in the world. However, that health care can also be very expensive, particularly treatments for non-routine health care. Even routine health care costs are beyond the means of some people. Thus, there is a strong need for health insurance to allow people to benefit from this high quality health care.

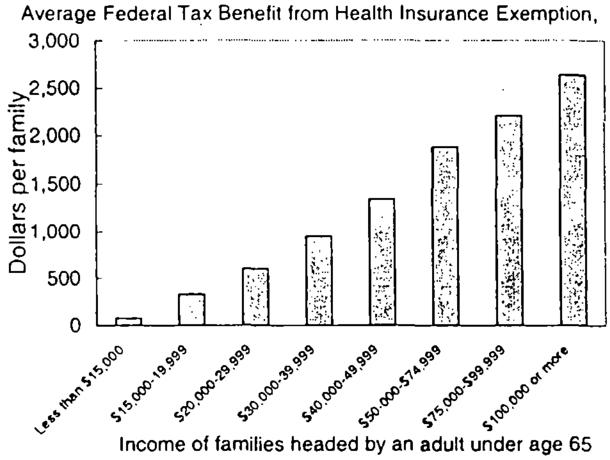
*The health insurance system and its coverage*

The American health insurance system relies primarily on employer-provided health insurance--about 63 percent of all Americans (74 percent of all insured people) are covered by an employer-based program. One reason for the dominance of employer-based group insurance is that the Federal tax code favors employer-based insurance. Insurance premiums paid by firms on behalf of employees are not included in the employees' taxable income, and employees' shares of health insurance premiums can be made with pre-tax dollars in firms with flexible spending plans. Because equivalent subsidies do not exist for employees who obtain insurance outside of work, this system encourages employer-sponsored plans.

There are several valuable aspects of this system. One benefit is that it encourages substantive risk pooling among a firm's employees, making insurance affordable and available for employees of all risk categories. In addition, firms can hire benefits administrators, who can evaluate different health insurance policies and act on behalf of the employees to ensure quality plans are offered to workers and that quality is periodically monitored. Firms can also take advantage of economies of scale to lower the insurance company's administrative costs, and thereby obtain lower prices.

Unfortunately, this system also possesses some inherent weaknesses. One problem is that the tax-preferred treatment of health insurance provides little benefit to low-income people who are most in need of assistance in making health insurance affordable; households with incomes low enough to have no tax liability receive no tax subsidy (See chart). In addition, those who do not obtain health insurance through their employer must find an alternative health insurance source. This includes not only the unemployed and the self-employed, but also people whose employers either cannot afford, or choose not to offer health insurance, and those who, even though offered health insurance, are unable to enroll because their share of the premium is more than they can afford.

Average Federal Tax Benefit from Health Insurance Exemption,

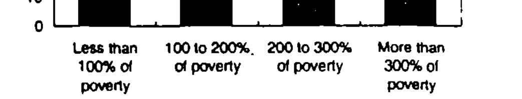



People without employer-provided health insurance and who do not qualify for publicly-funded programs must enter the individual insurance market if they want coverage. This market can present problems that limit affordable access. Some insurers may chose not to cover people with existing health problems, or sell policies that omit those problems from coverage. Insurers may also charge different premiums based on an individual's perceived risk; for example, older people may have to pay significantly higher premiums because they are more likely to experience health problems. In some cases, these premiums can be unaffordable. In addition, the cost of administering individual policies leads to higher administrative costs.

Publicly provided health insurance programs—Medicare, Medicaid, and SCHIP—provide an important source of coverage for many people. Created in 1965, Medicare and

Medicaid provide health insurance for elderly and low-income Americans. Over 36 million individuals received medical insurance through Medicare in 1998. Medicaid offers federal assistance to States that provide medical care to low-income Americans. Historically, eligibility for Medicaid was linked to eligibility for cash welfare. Beginning in the late 1980s, Medicaid has shifted toward a more general health insurance program that includes low-income working people. The 1996 Personal Responsibility and Work Opportunity Reconciliation Act, particularly, allowed Medicaid coverage to low-income families. Medicaid served over 41 million people in 1998. In 1997, the federal government created the State Children's Health Insurance Program (SCHIP) to target the growing number of uninsured children in families that have too much income to be eligible for Medicaid but too little to afford private insurance. SCHIP provides states with funding to provide health insurance through Medicaid, a non-Medicaid program, or a combination of both.

Chart x Health Insurance Coverage of Non-elderly People by Family Income.




This combination of employer-provided, individually purchased and publicly provided health insurance results in 42.6 million people without coverage. Not surprisingly, health insurance coverage is significantly related to income and employment characteristics. In families with income below the poverty line, 43 percent of adults did not have health insurance. In contrast, in families with income greater than 300 percent of poverty, only 9 percent of adults are uninsured. Fifty-six percent of uninsured non-elderly people are in families with incomes below

200 percent of poverty. The source of coverage also varies with income. More than 80 percent of families with incomes over 300 percent of poverty receive health care coverage through an employer. For families below the poverty line, meanwhile, Medicaid is the source of coverage for about X% of all families. Employees of small businesses (less than 100 employees) are also less likely to have insurance: one-fourth of small business employees are uninsured, compared to one-eighth of the employees in firms with 100 or more workers. This may be because small businesses are unable to take advantage of risk pooling as effectively as larger businesses. Part-time employees are much less likely to have coverage—32 percent of households with only part-time workers are covered. This decline is due in part to firms' restricting eligibility to exclude many part-time and temporary workers from health insurance coverage.

There are also significant differences in health insurance coverage across different racial and ethnic groups. Approximately 12 percent of non-Hispanic whites, 22 percent of blacks, 35 percent of Hispanics, and 21 percent of Asians and Pacific Islanders were uninsured in 1998.

*Issues in health insurance reform*

The need for health insurance reform is apparent from the large number of uninsured people. However, any proposal for reforming the health insurance system must address some specific challenges, including the possibilities of crowding out current health insurance, exacerbating adverse selection and difficulties encouraging participation by the uninsured.

"Crowding out" occurs when a policy that is designed to extend coverage to those currently uninsured cause some people who currently have insurance to switch to some other form of insurance. Another form of crowding out is when a policy causes an employer to stop offering coverage (or reduce its contribution) and thus forcing its employees to take advantage of the new government insurance or tax subsidy. When crowding out occurs, government dollars go not just to newly insured; some fraction of the money goes to those who had coverage and are now switching to a newly subsidized plan. If the new subsidy provides a much higher benefit than the value of the tax exclusion, then crowding out can be severe and the cost to the government of each net newly insured person can be pushed up substantially. Moreover, some employees may lose coverage and be unable to find replacement coverage, resulting in a smaller net increase in coverage, or possibly even a net decrease.

Studies of the Medicaid child eligibility expansions of the late 1980s and first half of the 1990s found that about 10 to 20 percent of the increase in Medicaid coverage was due to a reduction in private insurance coverage. Most of these studies examined Medicaid expansions that did not contain anti-crowd-out provisions. Because Medicaid covers mostly low-income people who are less likely to have private insurance, crowding out might be expected to be modest. The amount of crowding out will likely increase as eligibility for subsidies is extended up the income scale.

A second issue that any policy must consider is the risk of adverse selection. Adverse selection occurs when relatively low-risk individuals believe they do not benefit from the risk pooling provided by insurance, and therefore leave the risk pool. As these healthier people with lower health care costs leave the original pool, the average cost per person remaining in the pool will increase. When the costs and therefore the premiums for insurance begin to climb, still more people will elect not to purchase health insurance and there can be a spiral of rising premiums and declining enrollments. This could lead to prohibitively high premiums for those still desiring to purchase health-care insurance. Adverse selection can affect both the group and the non-group markets. The existing tax subsidy for employment-based group health insurance encourages healthy workers to remain in the group pool, because the subsidy for individually purchased insurance is smaller. If an alternative policy makes individual insurance more attractive, healthy people may decline employer-based coverage for individual coverage priced to suit them, leading to adverse selection in the group pool. In response to restrictions on individual rating, healthy people may also leave the individual market and not carry any health insurance, leading to adverse selection in the individual market. Even if young, healthy individuals find low-premium policies that reflect their lower risk rather than choosing to drop insurance altogether, higher risk people might still face prohibitively high premiums because the market becomes segmented into different risk pools.

Studies of insurance choices by employees offered multiple health insurance plans have shown that adverse selection occurs in the health insurance market. One study of government employees found that premiums for plans with more generous benefit levels increased much faster than premiums for plans with lower benefit levels, and found that this change was due to the worsening health status of the people selecting the generous benefit plan. A study of a second example where employees were offered a choice of several plans observed that healthy employees were less likely to choose the more generous benefit plan, and that the premium for the most generous plan became so expensive that the employer dropped it from the options.

A final consideration in designing any policy to extend health insurance is encouraging participation by the targeted group. For example, a policy with a modest co-payment may be implemented to prevent over-utilization by the insured. However, for individuals at low-income levels, even such modest costs may dramatically decrease enrollment and utilization. This may especially affect families without health-insurance problems, who could risk remaining uninsured to pay for more pressing needs such as food and housing. In addition, a complex application process designed to determine eligibility may have the unintended side effect of dramatically reducing coverage for otherwise qualified individuals. A subsidy that is received only after expenses have been paid may also deter individuals who do not have the funds to pay the insurance premiums up front.

*Meeting the challenge of covering more people*

The Administration has taken steps to extend coverage to more people. Particularly noteworthy successes have been the expanded eligibility for Medicaid, and the creation of the SCHIP. In addition, the Health Insurance Portability and Accountability Act of 1996 limits exclusions for pre-existing conditions in employer health insurance plans and for people converting to individual insurance. The Administration's Family Care proposal would enable more low and moderate income families to be covered by extending publicly provided insurance to the parents of children covered by SCHIP.

Although much has been done to ensure access to health care for millions of individuals, a number of challenges lie ahead. Prescription drugs have become a significant health care expenditure for many, particularly for the elderly. Helping individuals afford needed prescription medications is a priority. We must also contend with the growing elderly population and the forecasted increase in the need for long-term care. And finally, we must continue to work towards providing access to the health care system for the millions of Americans who remain uninsured.

**Building Livable Communities**

As the new economy presents greater options and opportunities for Americans, it also poses critical challenges for ensuring the sustained livability of our developing communities. Throughout much of the 20th century the population has shifted from central cities to suburbs and this trend has accelerated in the last decade. From 1990 to 1999 the suburban population grew by nearly 19 percent, compared to population growth of only 6 percent for central cities. This rate of increase is striking, relative to the rates of growth during the 1980s: 19 percent in the cities and only 6 percent in the suburbs. However, the new economy has witnessed a change in the pattern of job location as well. Inner cities are no longer the source of the majority of job growth. Rather, new jobs and new industries are springing up on the fringes of cities, often in "technology parks" or "research corridors." In 1997 57 percent of metropolitan-area jobs were located in suburbs, up from 55 percent in 1992.

These new "edge cities" have the potential to offer the best of both worlds to American families: the amenities and quality of life people seek from the suburbs, and the availability of jobs formerly associated with the central city. However, there are also drawbacks to this trend, and a satisfactory outcome requires that communities invest now in developing plans to channel this growth along avenues that ensure that the attractive aspects of the area are not spoiled by rapid growth. With this new growth comes the need to balance economic considerations with their social and environmental consequences.

*Economic Forces Driving Suburbanization*

Economists have noted the positive relationship between the density of economic activity and a region's productivity. In the past, many of the gains from agglomeration were due to access to natural resources and means of transportation. In contrast, the agglomeration economies of today are often based on a clustering of firms in the same industry that gain from the sharing of ideas, consumers, and specialized pools of skilled workers. Familiar examples include the mutual funds cluster in Boston, the oil and gas cluster in Houston, and the computer and related electronics cluster in Silicon Valley. **[Add evidence.]** Often freer from traditional ties to specific locations, new economy firms are able to choose from a wider array of potential business sites.

The outcome of their choices has led to a further distinction from past periods of industrialization. With current development occurring on the outskirts of cities, rather than in the central cities themselves, development is consuming land at a rate twice that of population growth. An average of 2.3 million acres of land is being consumed annually, and a significant share of this is residential development on lots of one acre or more in fringe suburbs or smaller cities. Such growth is commonly known as "urban sprawl."

Sprawl, defined as dispersed development beyond metro centers, often stretches along established highways and throughout rural areas. Identified by low-density residential and commercial settlements, sprawl often requires reliance on automobiles for transportation, including long-distance commutes. Powers over land-use and transportation are often fragmented among different local and regional governments, resulting in little coordinated influence on land use decisions. Often sprawling communities are divided by great fiscal disparities and distinctly zoned land uses.

Several economic explanations exist for this form of suburbanization. First, for many of these young, growing firms, urban areas may exhibit diseconomies that offset any benefits associated with the central city. The building stock in most central cities is old, and it may be costly to upgrade existing facilities to current technological standards. Rents in revitalized or redeveloped urban areas may be too expensive for new firms to afford to locate there. Similarly, existing building codes may make new construction prohibitively expensive, and in many cases it may be more cost effective to "start from scratch" in a new area. **[Does HUD or anyone else have good data on this?]** The drawbacks of urbanization may also accrue to potential employees. Firms in the new edge cities may be more attractive to workers seeking to live near work and yet avoid the congestion and pollution of an urban area. Finally, by locating near similar firms, firms can generate new externalities and benefit from shared resources. In the most well-known examples, firms in Silicon Valley, California; Cambridge, Massachusetts; and the Research Triangle of North Carolina benefit from access to pools of specialized high-tech labor.

*Challenges of new growth.*

The rapid economic growth of technology centers in edge cities and suburban areas provides benefits to local communities in terms of jobs and tax revenues. For example, between 1995 and 1999 sales tax revenues in the city of San Jose increased by 40 percent. However, if left unchecked this growth can also bring significant costs. Many suburban communities are becoming increasingly congested and in danger of losing the very attributes that made them attractive places to live and work. Increasing population strains existing public resources like schools and parks. Affordable housing is moving farther away from available jobs, increasing average commuting distances. The resulting traffic problems, worsened by limited public transportation, make commuting difficult and time-consuming and increase the demand for new road construction. Car ownership and the availability of public transportation can help; however, the problems of spatial mismatch persist.

The effects of rapid growth affect the environmental quality of these regions, as evidenced in their water quality, air quality, and land use patterns. Increases in paved surfaces, including roads, buildings, and parking lots, can contribute to a deterioration of water quality as well as to an overall loss of greenspace. This loss of greenspace leads to a less effective natural drainage, poorer water quality, and a dramatic increase in the potential for flooding in some areas. For example, residents along California's Russian River have witnessed their fourth major flood in three consecutive years. Hydrologists attribute such events in part to urbanization's effects on stream flow: downstream runoff into streams and rivers increases as impervious surfaces from development increase. **[EPA or others, can you share further specifics or statistics, perhaps on a national level?]** Increased traffic not only affects commuting and quality of life, but also ambient air quality, as emissions can lead to elevated levels of ozone and particulate matter. While national air quality trends have improved over the last 10 years, as of September 1999, 121 metropolitan areas still did not meet the national standards for air pollutants. This pollution in turn affects the health of residents, especially those in sensitive segments of the population. For example, incidence of pediatric asthma, aggravated by particulate matter, $SO_2$, and ozone, has increased 55 percent between 1982 and 1996.

*Economic Dimensions and Solutions*

One of the difficulties with ensuring appropriate development is that the costs and benefits of the development are typically borne by different entities; decisions benefiting private individuals may have adverse public effects, but these social costs are unlikely to be weighed by private decision makers. For example, individuals may prefer homes on large private lots, distant from both city centers and major highways. However, these homes require new roads, more driving, and the installation of public utilities. If a large number of individuals chose to live in such homes, the negative externalities that the decision generates – increased traffic, air pollution, and impervious surfaces – can outweigh the benefits each individual receives. The results of such decisions are evident in many areas of the country, and are particularly vivid in Atlanta Georgia, despite planning efforts to remedy them.

**Atlanta, Georgia: Challenges to Smart Growth**

Ranked by some as the nation's most sprawl-threatened large city, Atlanta continues to expand at a phenomenal pace. From 1980 to 1998 Atlanta's population grew almost 68 percent, with almost all of this growth occurring beyond the city limits. According to some studies, the Atlanta metropolitan area loses 500 acres of greenspace, forest, and farmland each week. This means that greenspace is disappearing to development faster than in any metropolitan area in history, and the city is suffering its consequences: water quality of the Chattahoochee River and Lake Allatoona is deteriorating, and air quality is in violation of clean air standards. Traffic congestion costs from lost time and wasted fuel are estimated at an overwhelming $1.5 billion a year. With an average work commute by car of 37 minutes (which is estimated to stretch to 45 minutes in 20 years, given continued growth), Atlanta residents may enjoy new economy benefits, but are clearly suffering the resulting costs of seemingly boundless sprawl. Motorists in Atlanta lead the nation in miles driven per person per day, totaling over 100 million miles daily.

The Atlanta Regional Commission is attempting to limit and coordinate this expansive growth. These governments are opposing a perimeter highway proposal for the reason that it threatens urban investment and encourages further sprawl. The ARC, supported by the state government, is trying hard to provide and encourage alternatives to single-motorist car transportation.

However, the momentum of sprawl continues and Atlanta faces a serious challenge to channel future growth toward building sustainable, attractive communities.

Economists would argue that the true cost of building a new home should include the costs of the associated externalities. However, quantifying these social and environmental burdens is considerably more difficult than merely identifying the private costs of development. There are, however, positive steps that can be taken in this direction. For instance, many studies have found that the additional tax revenue received from new development does not necessarily cover the installation of roads and utilities and the provision of public services to new residents. If new development were required to bear the full cost of services, including infrastructure, the resulting pattern of development would be less likely to have the characteristics of urban sprawl. Many governments have begun to assess impact fees on new construction to correct these subsidies.

Communities are beginning to use other kinds of economic incentives to achieve outcomes more consistent with smart growth. For example, some communities, such as South Bend, Washington, have imposed fees on impervious surface area to encourage development that has a less detrimental effect on water quality and flooding potential. Other communities are using toll roads to improve traffic patterns. San Diego charges motorists on I-15 higher prices during congested times than for driving during off-peak hours. The use of electronic transponder technology to identify motorists and collect tolls makes this system possible without the significant slowdowns caused by toll collection plazas. Other communities use transferable development rights to provide incentives for maintaining land in agriculture and other uses that maintain open space and provide ecological benefits.

The Clinton-Gore Administration's $9.3 billion Building Livable Communities program is encouraging "smart growth." It has set forth several principles to help guide policy efforts on a local level and to encourage greater planning and coordination over larger regions to resolve existing negative externalities. The Livable Communities initiative seeks to sustain prosperity and expand economic opportunity, to enhance the quality of life, and to build a stronger sense of community. Dedicating funds for regional smart growth efforts including Better America Bonds for state, local, and tribal governments, the initiative aims to preserve green spaces, ease traffic congestion, restore a sense of community, promote collaboration among neighboring municipalities through regional governance, and enhance economic competitiveness. As demonstrated by what Vice President Gore termed "a wave of local innovation," initiatives on the state and local levels are beginning to have real impacts on communities. Examples of such progress include the State of Maryland and the City of Chattanooga, Tennessee.

**Examples of Smart Growth**

Many governments are making significant efforts to encourage smart growth. For example, Maryland has established the following goals in its smart growth program: to preserve its most valuable remaining natural resources, to support existing communities and neighborhoods by targeting state resources to development in areas where the infrastructure is already in place, and to save taxpayer dollars by avoiding the unnecessary cost of building the infrastructure required to support sprawl. The program also ensures that the State will regularly evaluate the program's effectiveness. Earning federal grant money, reprioritizing within the state budget, and designing financial incentives for businesses, local governments, and homeowners, the State has been able to leverage funds necessary to emerge as a leader in the smart growth community, while preserving local decision-making authority.

Similarly, the smart growth success of Chattanooga, Tennessee, affirms the conviction that Americans can enjoy both economic prosperity and a high quality of life. Chattanooga was once home to heavily polluting iron foundries, textile mills, and chemical plants. However, through thoughtful economic development efforts, Chattanooga has become a model for other cities seeking environmentally sound urban renewal. The city now prides itself as a "laboratory" for sustainable development projects involving rezoning, reclamation, revitalization, and redevelopment. Illustrating how older cities can thrive in the new economy, Chattanooga boasts a 22-mile "Riverwalk" with picnic areas, a sculpture garden, waterfront housing developments, an electric-bus public transit system, footbridges, and an arts district.

Many of the areas of new and rapid growth are characterized by the combination of an educated workforce that places emphasis on the quality of life, and favorable economic conditions. Therefore, they have both the constituency to demand change, and the resources necessary to implement it. There is evidence that business and community leaders are already recognizing the costs and impacts of sprawl and acting to mitigate the negative effects. In areas such as the Washington, DC Beltway, Boston, San Francisco, and Seattle, leaders are acting to improve land use and transportation decisions and enhance environmental quality. The success of these endeavors will depend on the ability of these communities to make hard choices and find creative solutions to the challenges of urban sprawl.

Replacement Text for Chapter 5:

Introduction  Insert #1 (add after first paragraph, delete the rest of the original introduction)

The private sector has demonstrated great entrepreneurial dynamism and technological sophistication in bring us the New economy. But we need to recognize that for all their virtues, even in a New economy, private markets alone will not guarantee that all our national goals will be met. Private markets can create wealth, but they will not ensure that all citizens, even those able to find jobs, will have adequate incomes. Nor will private markets ensure that all citizens have access to quality education and healthcare. Similarly, while private markets can generate growth, they will not ensure that growth will reach all communities. Nor will purely private markets  necessarily deal with the negative side effects of growth on the environment and urban congestion.

Many of our most difficult national challenges will require government intervention through policies that assist individuals and communities in danger of being left behind. In this chapter, therefore, we consider policy areas which have a major impact on the opportunities given to all Americans to create a better life for themselves and their children.  In particular, we outline recent reforms in our welfare system, and policies designed to improve our educational system, expand health insurance coverage and ensure smart growth.  In each case, we describe the considerable progress that has been made and present the tasks that remain to be accomplished.

While the New Economy may not automatically meet these challenges, the faster growth it has generate does make meeting them considerably easier. In addition, the innovations that have occurred in information technologies, organizational redesign and policy provide better tools with which to meet them. Accordingly, in each section of the chapter, we pay particular attention to the contributions such innovations have and can play in improving the quality of life for all Americans.  For example, in the welfare system, new policies that make work pay have dramatically reduced the number of families receiving cash assistance while increasing the number employed. In education, schools have worked to implement higher standards for students and teachers and have brought aspects of the New economy into the classroom through the increased use of computers. In health care, innovations in medical technology and managerial practices have increased the quality of care and helped rein in costs. Finally, across our communities some are taking advantage of new techniques to combat problems of congestion and pollution and ensure smart growth practices. In this chapter we elaborate on these and similar policies than have helped grow our workforce, sustain strong economic growth, and improve the quality of life for all Americans.

Good News Insert #1

Many Americans lack health insurance coverage and access to adequate medical care.

Innovative policies have helped us share many of the gains of the New economy, reduce the number of individuals on welfare, and improve employment opportunities for all. But new policies may be needed to contend with future changes in the economy. A slowing of economic growth may be felt most severely by those who have most recently begun to share in its virtues. Those most recently employed may lose their jobs and accompanying benefits such as health insurance. State, local and Federal governments may feel pressure to cut back on investments in education if revenues decline. And localities currently willing to invest in smart growth policies may neglect these policies in times of fiscal tightness. Thus, continued improvements in the well-being of the American people depend on both sustained economic growth and active public policy. As America moves into the new millenium we must confront these issues.

Helping Families Insert #1

The New Economy is popularly characterized by new technologies, new methods of communication, and new avenues of trade. But it also brings innovative ways of providing for the least well-off Americans. Substantial changes have taken place in the organization of our welfare system and in the incentives it provides. These innovations, and in particular policies designed to increase the benefits of work, such as child care subsidizes, and increases in the earnings welfare recipients can keep, have changed the tenor of American social welfare policy. Public policy now emphasizes employment and investment in the skills of those who are less well-off. In doing so the Administration has helped low-income families leave welfare and enter the labor market thereby ensuring a more equitable distribution of gains from the New Economy.

Helping Families Insert #2

Our success in helping families leave welfare is tempered by the realization that many families are still dependent on public assistance. As time limits for TANF being to bind, we must focus on how to best help those who have been unable to secure employment. Furthermore, that many of those who have left the welfare rolls are no better off financially than they were while receiving benefits. Investments in job skills, a continued strong economy, and policies that ensure an acceptable wage can all help these individuals succeed in the labor force. Finally, when the economy does begin to slow, we must be prepared to help those who lose their jobs. If former welfare recipients are among the last hired, they may be among the first laid-off and run the risk of returning to public assistance. These challenges are not insurmountable but require the commitment of government and the help of the private sector to reach workable solutions.

Education Insert #1

As we seek to train young people to join the new economy, we must look for innovations in the provision of education that will increase the quality of the education that all experience. These innovations include a committed effort to reduce class size, investments in teachers aimed at increasing their effectiveness in the classroom, new higher standards for schools, the widespread adoption of computer technologies in classrooms, and new charter schools that provide parents with a choice with respect to their children's educations but retain public accountability.

Education Insert #2

The leadership provided by the Federal government and the funding made available to schools work to improve schools in a number of ways. Among the priorities of both teachers and administrators are reducing class size, hiring new teachers, providing training for both new and veteran teachers, modernizing schools, equiping schools with new technology and developing new standards and accountability.

Education Insert #3

In addition to the E-rate program, in 2000 the Federal government spent $766 million on education technology programs through Title III of the Elementary and Secondary School Act (ESEA). $425 million of this amount was provided through the Technology Literacy Challenge Fund. Schools also used portions of their Title I funding to invest in technology. These funds were used....

demand

Education Insert #4 This decline indicates that the for well trained teachers is outstripping the supply and that continued increases in this demand will likely make it more difficult for schools to find qualified instructors. Ultimately the benefits of nationwide reductions in class size will depend on the ability of the profession to attract and retain greater numbers of talented teachers.

Education Insert #5 There are many excellent schools in the United States, however the quality of schools is not uniformly excellent. Because what students learn in schools is crucial in determining the options available to them after leaving school, and more broadly, to the productivity of our nation, we must provide *all* children with excellent opportunities to learn. We have therefore invested in a high quality public education system. While much of the financing for public schools comes from State and local governments, the Federal government has worked for a more equitable distribution of resources across schools, and to help states and localities provide high quality education.

**Rewarding Effective Teachers**

Traditionally, teacher salaries have been based on education levels, experience, and responsibilities. These systems leave little room to reward the most effective teachers. Recently some school districts and states have experimented with alternative performance based pay systems. These new methods of providing compensation to teachers may help improve the quality of instruction along several dimensions. First, by establishing specific criteria performance-based awards can help clarify and prioritize goals, thus providing better guidance for teachers. These rewards can also provide teachers with additional motivation to work to achieve these goals. And importantly, tying teacher compensation to performance may help attract and retain talented people to the teaching profession, if they know that their hard work and skills will be rewarded.

However, to be effective performance-based pay systems must be carefully designed. Because student achievement depends on many factors that teachers cannot control, such as family circumstances and previous education, fair performance-based incentive systems should reward teachers for gains in student achievement, rather than for absolute levels of student achievement. Furthermore, because student learning involves cooperative effort, incentives must be designed to create cooperative, and not competitive, environments among teachers. For example, team-spiritedness might be enhanced by basing **a portion of** the awards on school-wide achievement rather than the achievement of individual classes. Finally, the standards used to assess performance must be carefully constructed. Measures such as gains in student test scores, increases in attendance, and increases in graduation rates have all been employed.[i] [ii]

The design of these school-based performance awards systems varies widely across sites. In some cases awards are given directly to teachers, in other cases the rewards benefit entire schools. To provide a sense of the types of incentives used by districts we highlight two programs. In Charlotte-Mecklenburg, North Carolina awards were based on a broad array of student outcomes including subject mastery, drop-out rates, and absenteeism. Schools received points for meeting annual improvement goals and teachers in these schools benefited directly. In the highest performing schools (classified as "exemplary") certified staff members each received $1000. Certified staff in schools with slightly lower gains ("outstanding" schools) received $750. In contrast to the equal division of awards within schools in Charlotte-Mecklenburg program, the program implemented at the Vaughn charter school in Los Angeles results in awards that vary substantially across teachers. At Vaughn teachers are provided with the opportunity to receive cash bonuses in each semester for effective performance in a number of areas including the teaching of specific academic subjects and more general skills like classroom management and lesson planning. Performance is assessed through self-evaluations, peer review and reviews by administrators. For a veteran teacher, performance related awards can total up to $13,100 per year.

While little evidence is available on the effect of these programs on student outcomes, one study of a performance-based award program in Dallas, Texas does show positive effects on student achievement. Studies of the effect on teachers found that many school-based performance-based award systems helped improve cooperation among teachers but that programs varied in their effectiveness in increasing teacher motivation. Teachers in many programs also reported that they felt increased pressure at work and worked longer hours. The system at Vaughn has helped attract new recruits and many current teachers were pleased with the program. However, there are also some problems. One teacher complained that the peer review process with differing amounts paid to teachers, "pits teacher against teacher." These difficulties indicate that additional research and experimentation might be useful in attempting to develop optimal compensation strategies.

## Ensuring Gains are Maintained

Effective teachers, adequate facilities, and well-constructed standards, can help students learn more, however, these investments are of little value unless students retain what they have learned. Numerous studies have demonstrated that knowledge and skills deteriorate while children are away from school, specifically during summer vacations. Drawing their conclusions from an analysis of many previous studies, one group of researchers found that children lost an average of one month's worth of learning over summer break.

Much of the federal government's role in educational policy has been aimed at helping children in low-income families receive a quality education, thus mitigating the effect of family income on schooling outcomes. Absent the effects of public schools, it appears that family characteristics play a larger role. Many studies have noted that the deterioration of skills associated with summer vacation was the largest for children in low-income families. These differences appear to be particularly large for reading: students from middle class families were found to have experienced a small gain in test scores over the summer while students from low-income families fell behind, creating a gap between the two groups in reading skills that is equal to approximately 3 months of schooling.

These differences suggest that public schools can do even more to help children from low-income families succeed. One possibility is to lengthen the school year. If students were to attend school year-round, there would be less opportunity for skills to depreciate. Alternatively summer enrichment programs targeting low-income communities can help poor children overcome some of the disadvantages they face at home and in their neighborhoods. In addition to changes in the school calendar, communities can offer after school enrichment programs.

Both after school and summer learning programs can also be a boon for working parents, particularly for lower-income parents who may have difficulty arranging alternative care for their children. Not only can such programs give parents peace of mind that their children are in a safe, enriching environment, but they can also allow working parents to invest in their jobs and gain important labor market skills that can further benefit their children through increases in familial income and exits from welfare.

The Administration has worked to assist local communities develop after school activities through its 21st Century Community Learning Centers Program begun in 2000. This program has funded more than 3600 after school and summer programs and the Administration has proposed significant increases in the program's budget for the 2001 fiscal year. Preliminary evaluations indicate that these programs have had beneficial impacts on the academic and social behaviors of participating children.

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[i] School-Based Performance Award Programs: Design and Administration Issues Synthesized from Eight Programs.

**Note to MT: Please do NOT change "Vice President Gore" to "The Vice President." "VP Gore" is correct and desired style, requested by POTUS speechwriters and approved by Staff Secretary. Also, HOPE is correctly all CAPS. It should NOT be changed to Hope Scholarships.**

## ECONOMIC REPORT OF THE PRESIDENT

*To the Congress of the United States:*

I am pleased to report that the American economy today is strong. We are enjoying the longest economic expansion in U.S. history, with more than 22 million new jobs since 1993, the lowest unemployment rate in 30 years, the lowest female unemployment rate in 40 years, the lowest Hispanic and African American unemployment rates ever recorded, and the highest home ownership rate in history.

This economic expansion has been not only unusually long, but also broad and deep. For the first time in decades, wages are rising at all income levels. We have the lowest child poverty in 20 years and the lowest poverty rate for single mothers ever recorded. Since 1993, the average family's income has gone up more than $6,000 and, for African American families, even more. The number of families who own stock has grown by 40 percent.

Our current economic strength is the result not of chance, but of a choice the American people made eight years ago. At that time, ten million of our fellow citizens were out of work. Interest rates were high. The deficit was $290 billion and rising. And the federal debt had quadrupled in the previous 12 years, imposing a crushing burden on our economy and on our children.

The American people chose to change direction, and empowered by that choice, Vice President Gore and I put in place a new economic strategy: fiscal discipline, greater investment our people, and expanded trade. The result of that three-part strategy has been eight years of prosperity and progress. Continuing with this proven strategy is the best way to keep our prosperity and progress going.

### THE ADMINISTRATION'S ECONOMIC AGENDA

Our strategy has been based, first and foremost, on a commitment to fiscal discipline. By first cutting and then eliminating the deficit, we have created a virtuous cycle of lower interest rates, greater investment, more jobs, higher productivity, and higher wages. In the process, we have gone from the largest deficits in history to the largest surpluses in history. We have extended the Medicare Trust Fund—which, when I was elected President, was scheduled to go bankrupt in 1999—to 2025. And we've paid off $362.5 billion in debt.

Second, our strategy has focused on investing more in education, health care, science and technology, to strengthen our people's capacity to make the most of the new opportunities of the 21st Century. We have doubled funding for Head Start, provided after-school and mentoring to more than a million young people, and begun putting 100,000 new, well-trained teachers in the early grades to lower class size. Thanks to these investments, and a new stress on higher standards and accountability, reading, math and SAT scores are up. And with the largest expansion of college aid since the GI Bill, more students than ever are going on to college.

We've also invested in our people with targeted tax relief, to help Americans meet the challenges of work and child rearing. Last year alone, our HOPE Scholarship and Lifelong Learning tax credits helped 10 million families pay for college. Our Earned Income Tax Credit helped 15 million families work their way into the middle class. And 25 million families will get $500 child tax credit. The typical American family today is paying a lower share of its income in federal income taxes than at any time during the past 35 years.

Every year since 1993, we have increased funding for long-term research and development—investments that lead to more economic growth, more high-wage jobs, more cures for diseases, and a cleaner environment. Funding for the National Institute of Health, for instance, has nearly doubled over the past seven years.

Meanwhile, we have continued to make important investments in our nation's communities. Our Empowerment Zone tax credits are bringing new business and new jobs to our hardest pressed communities -- from the inner cities to Appalachia to the Mississippi Delta to our Native American reservations. With the help of 100,000 new community police officers and common-sense measures like the Brady Law and the assault weapons ban that keep guns out of the wrong hands, crime has fallen to a 25 year low. Under the Children's Health Insurance Program, 2 million previously uninsured children now have health coverage.

Third, our economic strategy has focused on opening markets around the world. Today, with more than 300 new trade agreements, including the North America Free Trade Agreement and the Uruguay Round agreements, American workers and firms are competing in more markets than ever before, and our economy is stronger for it.

CONTINUING OUR ECONOMIC STRATEGY

Last year, we took important new actions to secure our economic future, guided by the same three-part strategy. We normalized trade with China, a move that will open China's markets to American products from wheat to cars to consulting services, and ensure that our companies will be more able to sell goods without moving factories or investments there. Congress also passed, and I signed, a 2001 budget that maintains our commitment to fiscal discipline. Under this new budget, we will continue to pay down more debt. And if we stay on this path, we can make America debt-free by 2012 for the first time since Andrew Jackson was President in 1835, thereby keeping interest rates low and prosperity going.

The 2001 budget also continues our strategy of investing in our people. It includes the largest-ever increase in funding for the National Science Foundation and major increases in funding for education. With over $1.2 billion dedicated to school renovation, thousands of local school districts will finally be able to give our children the classrooms they deserve. We've increased by 25 percent funding to meet our goal of hiring 100,000 new, highly-qualified teachers to reduce class size. We've nearly doubled funding for after-school programs to help more than 1.3 million students, while increasing support for teacher training, and for turning around failing schools. And to open the doors of college even wider – so that more of our young people can walk through them – we have increased the maximum Pell Grant to an all-time high of $3,750 – up nearly $1,500 since 1993.

The new budget also includes our historic New Markets and Renewal Communities Initiative, the most significant effort ever to help hard-pressed communities lift themselves up through entrepreneurship and access to new capital. With our New Markets tax credit, 40 strengthened Empowerment Zones, and 40 renewal communities, this initiative will spur billions in private investment in communities that have not yet shared in our great economic revival.

This is a unique moment in U.S. history, a time of unrivaled prosperity and progress, with few internal crises or external threats. We have the responsibility to use our good fortune wisely. If we maintain our current economic strategy, we can sustain our prosperity, expand the circle of opportunity, meet the long-term challenges of this new century, and provide our children the chance to live their dreams.

THE WHITE HOUSE
JANUARY 12, 2001

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## 4-6 p.m.

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# CHAPTER SIX

## CONCLUSION: ACHIEVEMENTS AND CHALLENGES IN THE NEW ECONOMY

The past 8 years have been a period of extraordinary achievement for the U.S. economy. Supported by sound policies and strategic investments in the future, the U.S. has experienced an economic expansion unprecedented for its length, breadth and depth. This expansion is not only the longest ever recorded – it has also been astounding in sharing the benefits widely, raising Americans' average incomes to record highs, and creating opportunities for groups that have traditionally been left behind.

This expansion has not just meant that the economy growing in sheer size. It has also entailed the economy becoming dramatically more information-intensive, more productive and more innovative. Today's economy utilizes new, more efficient business practices; and has redefined many relationships between suppliers, manufacturers, financiers, and customers. The cumulative result of these trends and their interactions has been a "New Economy" that is currently providing Americans the benefits of high growth, low inflation, high productivity, rising incomes, and low unemployment.

A policy strategy centered on fiscal discipline, investment in education and technology, and opening new markets has been the key to ensuring that the government supported and fostered the flourishing of innovation and entrepreneurship in our economy. The combination of private sector innovation, of Americans' hard work, and of sound policies and investments in the future has created a vibrant economy. Over the last 8 years, the economy has grown at the robust rate of 4.0 per year on average. Inflation has remained near its lowest rate since the 1960s. Meanwhile, productivity growth has increased rather than decreased over the course of the expansion: it grew 3.7 percent over the past 2 years and a stunning 5 percent in just the last 4 quarters.

Importantly, this prosperity has been remarkably equitably shared in this expansion compared to other previous long expansions. There have been solid, across-the-board income gains, with some of the strongest gains realized at the bottom of the income distribution. The bottom 20 percent of the income distribution saw the largest income growth of any group – 16.3 percent since 1993. In all, over the past eight years, the economy has created more than 22 million jobs. More than 80 percent of those jobs have been high-quality jobs paying above-median wages. Median family income has increased by $6,338 since 1993 rising to $48,950 in 1999. Since 1993, seven million Americans have moved out of poverty. Homeownership reached 67.7 percent – the highest on record. Unemployment is at its lowest level in more than 30 years. Unemployment rates for African Americans and Hispanics are at their lowest rates on record.

This Economic Report of the President attempts to describe the phenomena that are collectively known as the "New Economy." It examines the driving forces of innovation, organizational change and sound policy that have created the New Economy. The report further analyses the effects those forces have had on macroeconomic performance, on business practices, and on our ability as a nation to address various challenges such as poverty, education, and the long term welfare of all our citizens. In addition, the Report examines those areas where economic growth on its own may not meet all the challenges and where targeted government policies can play a useful role to ensure that the circle of opportunity is expanded to include as many as possible.

The U.S. today stands at a unique juncture in history. It enjoys unprecedented prosperity and as such faces a unique set of opportunities as well as challenges. Used wisely and cautiously, our prosperity can be harnessed to continue to strengthen research and development to drive long-term innovation and further productivity increases; to improve the education and training of the workforce; and to improve our ability to provide for the long-term needs of our increasingly aging population by shoring up Social Security and Medicare for the future. The right path is to continue the polices of the last 8 years which has created a virtuous circle in which fiscal prudence helps keep interest rates attractive for investment, and strong productive investment generates a healthy and growing economy with ever larger budget surpluses.

However, it must be acknowledged that today's strong economy is far from invulnerable. The virtuous circle can be easily broken if fiscal discipline is abandoned and priorities are placed on large tax cuts rather than long term investments for the country. A large tax cut could overstimulate demand and make it much harder to avoid overheating and an eventual recession. This would be particularly detrimental at a time when the country faces such a significant demographic challenge: Over the next 40 years, the population aged 65 and over will rise from its current share of about 12.5 percent of total population to nearly 21 percent. Retirement and health programs for the elderly will take up an increasing share of Federal outlays. Per-capita costs of Social Security and Medicare are expected to rise in the future, implying an even more dramatic increase in spending on the elderly. Spending on Social Security and Medicare as a share of GDP will more than double over the next 40 years from around 6 percent of GDP in 2000 to nearly 13 percent in 2040.

Today's New Economy provides a precious opportunity to continue to build for the future, secure the well-being of our older generation, and make the right investments to continue fueling the engine of innovation, enterprise, and productivity in our economy. Defining and pursuing the right priorities for continuing the expansion will be critical to the Nation's long-term welfare.

**Technology's Role in the New Economy**

At the heart of the new economy is a bubbling cauldron of innovation. In particular, advances in computing, information storage and communications technology have proliferated in recent years – yielding whole arrays of new products, services and industries. What has been special about this most recent period, however, is that in addition to these separate paths of innovation, there has been a great convergence of technologies – telecommunications, information technology, and the Internet – that have enabled a whole new range of capabilities not previously imagined.

As a result of these powerful innovations interacting with one another, the economy has become "lighter" in recent years, shifting toward products embodying more knowledge capital and less physical capital. Spending on information technology (IT) has played a leading role in the acceleration of economic growth. Although it accounts for just 8.3 percent of GDP, it accounted for almost a third of output growth between 1995 and 1999. Investment in information processing equipment and software as a share of all private non residential fixed investment increased from 13.8 percent in 1993 to 41.5 percent in the third quarter of 2000. Between 1990 and 1997, the number of IT firms more than doubled, a 140 percent increase.

Technological innovation has been particularly important for two reasons. First, the IT-producing sector is highly productive, and the growth of this sector has led to increased performance in the U.S. economy as a whole. Second, the adoption of IT has led to performance gains in other sectors of the economy, making other inputs more productive by changing the way firms do business. Manufacturing plants are increasingly automated, while workers are given more flexible job assignments and stronger incentive pay. Supplier relationships are becoming more closely integrated through use of computer systems that coordinate the various aspects of production and warehousing, allowing firms to reduce inventories dramatically. Firm boundaries are also shifting rapidly, as firms outsource non-core businesses and move toward flexible, collaborative relationships like strategic alliances with suppliers, customers, and even rivals.

But technology alone is not the answer. It is only when it is used wisely by firms that it becomes a transforming agent. Performance improvements are most likely to be realized when firms use IT to bring about changes in basic business practices, job-design, organizational structure, interactions with customers and suppliers and human resource practices such as incentives and decision making authority.

One example of technology's ability to enable changed business practices is how the Internet is now being used to reduce costs for procurement. Online business to business exchanges now offer a range of transaction tools such as buyer and seller auctions, billing, insurance, information and other custom services that allow firms to achieve greater efficiency in procurement. One on-line exchange claims to have saved customers $2 billion during its five years of operations. These kinds of improvements, in turn, can help make the economy more resilient: the more efficient procurement and inventory management enabled by technology has led to a greatly reduced tendency toward inventory overhang – thus reducing the tendency towards recession in periods of declining growth.

**The Role of Policy in Supporting the New Economy**

While innovation and entrepreneurship are at the heart of the New Economy, they have been fostered in the U.S. by the right government policies. Firstly, government policy has played a critical role in providing the fuel needed to run the New Economy. The budget deficit had ballooned to $290 billion in 1992, the largest ever, and was projected to grow to more than $455 billion by fiscal year 2000. This budget deficit placed a huge drain on investment capital and productivity rates in the economy were anemic. However, with the program of fiscal discipline led by President Clinton and Vice President Gore, there have been eight consecutive years of fiscal improvement. The surplus in fiscal 2000 was $237 billion – the largest surplus since 1948.

These sizable surpluses mean that the government, rather than draining away resources from private investment, is freeing them up. And indeed, there has been a dramatic increase in investment. From the first quarter of 1993 to the third quarter of 2000, investment grew at 13 percent a year. This long investment boom has been a key to the increasing productivity growth over the course of the expansion, which in turn has enabled the economy to continue on a path of strong yet non-inflationary growth.

The explosion of the New Economy was also helped in the U.S. by strong, pro-competitive policies that allowed innovations to flourish. The Telecommunications Act of 1996, for example, opened up competition between local telephone companies and long distance providers and cable companies – unleashing a flood of innovation in the information and communications technology sectors that has been a key driver of the New Economy. The Act also provided guidelines that would ensure that the benefits of increased competition would also be harnessed to increase the circle of opportunity: Through the E-rate, which was established by the Act, schools and libraries gained access to discounted telecommunications and Internet connections. This, paired with a massive increase in Federal funding for education technology – soaring to $769 million in fiscal year 2000 from just $23 million in fiscal 1994 – lays a long term investment in the technologically-skilled work force needed to sustain this economy.

**Globalization and the New Economy**

Globalization has also played a crucial role in promoting the technological innovation and facilitating the organizational restructuring that has yielded a New Economy. By forcing more competition and specialization, globalization induces innovation, higher productivity and stronger growth. Producers gain by specializing in what they do best. With open markets, they are able to use the best and most cost-effective inputs from global sources to lower their costs and improve productivity

Meanwhile, improvements in communications and information technology have spurred deeper integration between the United States and the World Economy. Indeed, it is no coincidence that the New Economy has emerged in the United States at the same time as U.S. participation in the global economy has reached new heights, as globalization and recent advances in information technology are integrally linked.

Over the past 8 years, fostering globalization and its benefits has been a high priority. Over 300 trade agreements have been signed, including passage of the North America Free Trade Agreement (NAFTA), the Uruguay Round multilateral trade agreements, permanent normal trade relations with China, agreements in telecommunications, information technology equipment, and financial services, and a moratorium on tariffs on e-commerce. At the same time, a focus of U.S. trade policy has been to ensure that agreements safeguard global natural resources and respect our values, including our commitment to core labor standards.

The effects of globalization and improved communications and technology are evident in U.S. international transactions. Trade in capital goods has soared since 1996, with particularly strong growth in trade in items central to the New Economy, such as computers, semiconductors, and telecommunications equipment. There has also been strong export growth in services that reflect the value of U.S. innovation, such as professional, business and technical services, and financial services.

**Harnessing the New Economy**

The power of the New Economy clearly has the ability to deliver many benefits for Americans. However, it is not necessarily true that it will spontaneously provide benefits to all people. That is where policy makers have played a critical role in harnessing the dynamism of the New Economy to benefit groups that traditionally have been left behind.

A robust economy that creates 22 million new jobs certainly provides broad reaching benefits. Unemployment rates for African-Americans and Hispanics have hit record lows during this expansion. But in addition to these pure market effects of a high-pressure economy, there are additional means that can be important to empower and assist struggling families. These have included raising the minimum wage twice, expanding the Earned Income Tax Credit, additional child care subsidies, and extensions of health insurance coverage provide assistance to low income working families. Together with the effects of the strong economy, these measures have helped 7.7 million people move out of poverty since 1993. As more people move off of welfare, and out of poverty, and into the job market, this in turn has a positive feedback effect on the economy as a whole – lessening the burdens on the public and increasing the productive force in the economy.

In addition, innovations in technology can help improve the delivery of many social services including health care and education. Innovations made possible by new technologies are yielding new treatment methods that can directly improve the quality of life for many. In education, new programs bring computers and Internet usage to the classrooms, help improve teacher effectiveness, reduce class size, and narrow the digital divide.

Despite the vast improvements in the quality of life experienced by many Americans several challenges remain. Welfare rolls dropped by 7.8 million between January 1993 and December 1999, and the number of individuals receiving welfare benefits is down by 56 percent from January of 1993. But there are still substantial disparities in economic well-being across regions, with minorities and residents of central cities and rural areas suffering disproportionately high rates of poverty and unemployment.

Our health care system also presents numerous challenges. We need to continue to control health expenditures to ensure that care is affordable to all. Issues related to managed care and the appropriate way to align incentives so that health care is not overly restricted or overly prescribed. Even with these issues under control, many Americans may continue to lack health insurance coverage and will therefore be unable to take advantage of the quality of care available to the majority of individuals. Finally, the new economy has allowed certain geographical regions to experience enormous growth in jobs and population. This growth, when left unchecked, has led to sprawl and serious environmental consequences.

Even at a moment of great prosperity, there continue to be great challenges ahead. There is a unique opportunity now to harness the power of the high-tech, high-productivity, high-growth New Economy to continue the prosperity and to use it to improve the lives of all

Americans. The challenges of the future – whether they be saving Social Security, improving education, expanding health care coverage, or paying down the national debt – are significant and will require concerted effort. The tools and capabilities of the New Economy, combined with the right, targeted policies, can provide a powerful solution toward addressing these challenges as a Nation.

# CHAPTER 5

# LIVING IN THE NEW ECONOMY

This Administration came to office on a platform of "putting people first." The Administration has kept that pledge.Although the phrase "New Economy" typically brings to mind technological innovation and globalization, arguably one of the most important changes from the old economy to the new has been an improvement in the well-being of the American people. By virtually any measure, Americans are better off today than they were 8 years ago.

Replace with "Introduction insert #1" on attached sheet

~~On its own the New Economy, for all its entrepreneurial dynamism and technological sophistication {**I wanted here to sharpen the focus between private markets and public action**}, cannot solve all the Nation's problems. Many of our most difficult challenges require government intervention, through policies that assist individuals and communities in danger of being left behind. One of the guiding principles of our Nation is that all people deserve the opportunity to create a better life for themselves and their children. New policies designed to reform welfare, improve our educational system,, and expand health insurance coverage seek to extend the benefits of the booming economy and of technological change to those Americans who have not already felt them directly. For the most part these policies have been successful. In particular, many of these policies have benefited populations that historically have been among the hardest to reach.~~

~~Under this Administration, the Federal Government has made investments in America that focus on the country's future. Programs that help people enter and remain in the labor force, and that invest in the education of our youth, help individuals acquire the skills they need to be successful and ensure that our economy will have the skilled, productive labor force it needs to continue growing. Investments in smart growth in rapidly developing regions will help sustain economic development and the quality of life Americans enjoy.~~

~~**[Except for welfare to work, the examples in this section don't show how policy has effected change. Simply adding "Policies to . . ." will correct that problem in the last three examples.]** The Administration's policies reflect both the technological and the organizational~~

~~innovations of the New Economy. Our system of providing for the poorest Americans has been fundamentally changed. No longer are families punished financially for leaving welfare and returning to work. Programs that make work pay have dramatically reduced the number of families receiving cash assistance while increasing the number of people employed. **[Sentence is vague—it can be made more specific by citing, say, use of computers in schools.]** The education sector has become much more technologically advanced and set higher standards for learning. In the health care sector, innovations in information technology and managerial {**and financing?**} practices have increased the quality of care and helped lower costs. Our communities are taking advantage of new techniques to combat problems of congestion and pollution and ensure smart growth practices. These and similar policies are working to train and grow our work force, sustain strong economic growth, and improve the quality of life for all Americans.~~

## Good News from the American Economy

Record-setting gains in the stock market and growth in the net worth of wealthy individuals have received wide media coverage. But the most noteworthy aspects of the recent economic expansion are its duration and its reach. The last few years in particular have brought tremendous gains to all segments of our society.

Employment gains have been dramatic. Between January 1993 and October 2000, 22.4 million new jobs were created.[1] In 1999 the unemployment rate reached 4.2 percent—the lowest level since 1969. Just as important, it has stayed low, remaining below 5 percent to 41 months at the time of this writi {**j~~ust as important, it has stayed low—backing up the "duration" point just above~~**}At the same time wages have been increasing. After declining steadily from 1986 to 1994, real hourly wages for private sector workers rose by ~~7.2~~ ~~8.9~~ 7.0 percent between 1994 and 1999.[2] These gains in employment and wages are echoed in growth in income and decreases in poverty. The median household income reached a new high of $40,800 in 1999, an increase of 2.7 percent in real terms since 1998 alone, and a total increase of 13.3 percent from 1993. In 1999 the poverty rate fell to 11.8 percent, its lowest level since 1979, and 3.3 percentage points below the 1993 rate of 15.1 percent.

many
Unlike ~~ma~~ previous expansions, these gains were shared by Americans at all income levels. Between 1998 and 1999, real income grew by 4.4 percent for those (yes) [**households?**] at the 20th percentile and by 3.5 percent for those at the 80th percentile. (A household at the 20th percentile is one whose income is higher than that of the poorest 20 percent of all households, and lower than that of the richest 80 percent.) From 1993 to 1999 the respective growth rates were 15.0 percent and 14.2 percent.[3] In addition, the most disadvantaged groups tended to experience the greatest improvements in financial well-being.

* ¶ In 1999 Unemployment for African Americans and Hispanics fell to the lowest levels on record ~~between 1993 and 1999~~. African Americans saw their unemployment fall from 13 percent in 1993 to 7.0 percent in 1999,[4] while Hispanics saw their unemployment ~~jobless~~ rate drop to ~~5.6~~ 6.4 percent.[5] Earnings have also increased, particularly for African Americans. Between 1998 and 1999 the median earnings for full-time African American male workers increased by $2,379, or 8.6 percent—a dramatic rise for a single year. With this sharp increase, the earnings ratio for African American males compared with white American males rose to 0.81, the highest level ever recorded (Chart 5-1).[6]

move to * above (in same paragraph, start new ¶ w/ Unemployment

* Household incomes for African Americans and Hispanics have also risen to all-time highs. The median income for African American households increased 7.7 percent between 1998 and 1999 (it is up 23.9 percent since 1993), climbing to $27,910. The median for Hispanics rose to $30,735, an increase of 6.1 percent between 1998 and 1999 (and 16.5 percent since 1993). [7]

Along with these record increases in income have come record declines in poverty (Chart 5-2). In 1999 ~~1998-99~~ the poverty rate for African Americans reached an all-time low of 23.6 percent, and the decline in poverty between 1998 and 1999 was the largest one-year decline ever recorded. Hispanics also experienced a record drop in poverty. At 22.8 percent, the poverty rate for this group is now at its lowest since 1979. [8]

In the past, economic gains have often had limited impact (sounds less strong) ~~little effect~~ on households headed by women. During this Administration, however, the strong economy and a social welfare policy that emphasizes work have brought substantial benefits to this group. In March 1993 just 56.8 percent of women maintaining a family on their own were employed; this figure rose to 63.4 percent in March 1998 and 65.2 percent in March 1999.[9] This increase in employment corresponded to an increase in income. Between 1993 and 1999 the median income for these households increased by 22.4 percent, with 4.9 percentage points of that increase occurring between 1998 and 1999 alone.[10] The poverty rate for households headed by females also fell, dropping from 38.7 percent in 1993 to 33.1 percent in 1998 and 30.4 percent in 1999.

Within this group are those most likely to have been affected by welfare reform: low-income single mothers and their children. (Low income is defined here as an income below 200 percent of the poverty line.) Analysis of a recently completed survey indicates that ~~According to a recently released survey~~, between 1997 and 1999 the ~~number~~ percent of ~~working~~ low-income single mothers who were employed increased from 59.7 percent to 65.2 percent. ([illegible]) Children as well as their mothers benefited from this change.[11] Between 1998 and 1999 the poverty rate for children fell by 2 percentage points, to 16.9 percent, the lowest level since 1979 and the largest percentage-point decline since 1966. Poverty among African American children declined by even more in absolute terms, falling by 3.6 percentage points to 33.1 percent. Since 1993 the ~~overall~~ all poverty rate for children has fallen by 5.8 percentage points.

(there aren't really supportive policies other than not cutting Social Security)

Our oldest Americans have also benefited from economic growth ~~and supportive policies~~. In 1999 the poverty rate among the elderly fell below 10 percent for the first time ever. With the elimination of the Social Security earnings test for those aged 65 and over, older Americans will likely participate in the labor force in greater numbers, further improving their financial status. For years, residents of our ~~inner~~ central cities **{Emily and I are unsure whether it should be "inner" or "central" here and later; "inner" is more familiar but may not fact-check (or be the same thing)}** have seen little change in their poverty levels, yet here, too, the situation is improving. **[Dates? Figures?]** ~~Inner~~ Central-city residents experienced an above-average increase in median income and the largest declines in poverty of any geographic category.[12]

(Use central throughout)

The gains experienced by Americans over the past 8 years have not been limited to financial gains but include a long list of improvements in the quality of life. Low interest rates and a strong economy have helped more Americans than ever before become homeowners. In the third quarter of 2000, 67.7 percent of American families owned a home, up from 63.7 ~~64.7~~ percent in the first ~~same~~ quarter of 1993 and surpassing the Administration's goal, set in 1995, of 67.5 ___ percent ~~[give figure?]~~.[13][14] Improvements in job opportunities, in combination with Administration initiatives to hire additional police officers, strengthen gun laws, and increase local resources to improve public safety, have contributed to a dramatic reduction in crime, with the overall crime rate falling to its lowest level in 26 years.[15]

Incorrect statement

Our public schools today are also showing improvements on several fronts. Si~~nce 1992, readin~~g ~~and mathematics scores on the National Assessment of Educational Progress (NAEP~~) ex~~amination have increased for fourth, eighth, and twelfth graders, including those students in schools with the highest poverty rates~~ ~~{is this what a "high-poverty school" is?}~~.[16] More young people are graduating from high school than ever before, and more are attending college.[17] Average math scores on the Scholastic Aptitude ~~{isn't the A for "Achievement" nowadays?}~~ Test (SAT) ~~math scores~~ have reached their highest level in 30 years, and average verbal SAT scores have held steady [~~maybe this is not a good thing to say? Be more specific~~] even though the number of non-native English speakers taking the exam has increased.[18] Minorities have also made notable academic achievements. Among high-school graduates aged 18-24, the proportion of African-American and Hispanic students continuing their education at a 4-year college is at a record high.[19]

Improvements have also been made in the public health arena.
The health of Americans has also been improving. The birth rate among teenagers declined 17 percent between 1993 and 1999 ~~{is this a "health" issue?}~~.[20] * Between 1997 an 1999 Smoking among teenagers declined. This was the first time ~~for the first time~~ in nearly a decade f~~rom 1997 to 1999~~.[21] The proportion of high school students who said they had smoked a cigarette in the preceding 30 days that declined ~~fell over that period from 36.4 percent to 34.8 percent~~. * move bracketed text to * [Infant mortality is down from 8.4 deaths per thousand in 1993 to 7.1 ~~7.2~~ per thousand in 1998.] Death rates ~~s~~ from heart disease, cancer, stroke, and AIDS are all down, and life expectancy has improved. A child born in 1998 can expect to live nearly 76.7 years, up from 75.4 in 1990 ~~74.9 years just 10 years earlier~~.[22]

Although these statistics present a glowing picture of the New Economy and the well-being of the Nation as a whole, more work remains to be done. Despite the recent gains, the incomes of minority groups remain significantly below those of whites and their poverty rates significantly above. Infant mortality and life expectancy rates also differ substantially by race and ethnicity, as does access to a quality education. Certain areas of the country continue to experience unemployment rates of more than 10 percent and distressingly high {**~~there will always be "above-average" poverty somewhere~~**} levels of poverty. ~~As America moves into the new millennium, we must confront these issues~~.

Add "Good News insert #1"

**Helping Families Help Themselves**

Replace with "Helping Families insert #1" on attached sheet

The New Economy is popularly characterized by new technologies, new methods of communication, and new avenues of trade. But it also brings innovative ways of providing for the least well off Americans. [**The rest of the paragraph does not show how the New Economy provides innovations. The information is also redundant to the paragraphs above.**] Low-income families are receiving help in becoming or remaining independent of public assistance through a network of programs designed to increase the benefits of work. By placing its emphasis on employment and investing in the skills of those who are less well off, the Administration has changed the tenor of American social welfare policy and helped ensure a more equitable distribution of the gains from the New Economy.

### *Welfare Reform*

One of the most impressive achievements of the past 8 years has been the reduction in the number of Americans receiving welfare, along with an increase in e~~mployment among curre~~nt ~~and former welfare recipients~~ {**"the number of Americans who have moved from welfare to work"**} ok. The Administration has worked hard for welfare reform b~~egan working toward welfare reform in 199~~3. ~~One of its firs~~t In doing so it allowed a record number of States to **~~steps was to allow States to [re waivers: is "record number" correct? That is, had such waivers ever been granted before~~**]implement changes in their welfare programs on an experimental basis, through waivers from Federal welfare regulations and caseloads began to fall. As of August 1996, 43 states had received waivers and set up alternative programs that emphasized work and parental responsibility. ~~Caseloads soon began to fall~~.[23]

There were some waivers prior to 1993

These changes at the State level were followed by changes at the national level, in particular the bipartisan Personal Responsibility and Work Opportunity Reconciliation Act signed by the President in 1996. This act replaced the Aid to Families with Dependent Children (AFDC) program with one that provides needy families with temporary assistance, established time limits for receiving welfare benefits, and shifted the program's emphasis from simply providing assistance to helping families leave welfare and enter the labor market.[24] Policies that offer tax credits to subsidize the earnings of low-income workers, provide assistance with child care, and expand eligibility for health insurance support the welfare-to-work transition.

The new program, Temporary Assistance for Needy Families (TANF), differs from the AFDC program in three fundamental ways. First, it gives States much more discretion in using Federal

OK

funds ~~[??]~~. Under the AFDC program, States set eligibility and benefit levels and received matching funds from the Federal Government to help with the cost of the program. The new program provides States with block grants that are used to finance cash benefits, job preparation, and other worker support programs. States now have much more flexibility in spending, and they have used this flexibility to meet the particular demands of their constituencies. [~~examples?~~] for example by allocating additional funds to child care subsidies by allowing welfare recipients to keep a greater fraction of their earnings. States are also eligible for performance bonuses for moving individuals into jobs, increasing participation in the food stamp, Medicaid, and children's health insurance programs, providing child care, and **[what does this phrase mean? It could be misinterpreted]** increasing f~~amily~~ the percent of children in married couple families. f~~ormation and stability~~. States can also receive bonus awards for reducing out-of-wedlock births.

Second, the new system imposes time limits and work requirements on welfare recipients. In general, States can no longer use Federal funds to pay benefits to recipients who have received assistance for more than 60 months during their lifetime. States can exempt some recipients from this requirement, set even shorter time limits, or use their own funds to continue support beyond the 5-year limit. In 1999, 38 States used the 60-month time limit, and the remainder implemented other policies (8 states have shorter time limits, 3 currently have no time limit, and others intend to use longer periods).[25] Recipients must also work in some capacity after receiving benefits for 2 years, but States have flexibility in deciding how to implement this rule—, particularly in terms of strengthening it. In 1999, 28 States had welfare policies that imposed immediate work requirements rather than the 2-year requirement.[26]

Finally, States can now design the parameters of their program to suit the needs of their residents. Although States have always had the freedom to set benefit levels, the new program allows them to to set income and asset limits for eligibility as well and to establish their own methods of calculating the income of potentially eligible families. The majority of States have used this freedom to decrease the implicit tax on earnings. The AFDC program reduced benefits dollar for dollar for any earnings of more than $90 per month after 12 months of work. This 100 percent "tax" created a strong disincentive to work, as many participants did not see their income increase after they went to work. Many States now use a more gradual benefit reduction rate to encourage greater work force participation. They are also investing in a wide range of supports to help welfare recipients and other low-income working families enter the work force and succeed on the job.

*The Effects of Welfare-to-Work Programs*

Since August 1996, caseloads have fallen dramatically (Chart 5-3). The average monthly national caseload has declined by 6 million, a reduction of ~~40~~ 50 percent .[27] Including reductions that took place during the period of State waivers, caseloads have fallen by 7.8 million, or 56 percent, since 1993. Declines in some states have been even more dramatic. In Wisconsin, for example, the number of welfare recipients fell by 70 percent between 1996 and 1999, and it has fallen by 82 percent since 1993.

The 1996 reforms have undeniably been successful in reducing the number of people receiving welfare. But reductions in caseloads are not the only measure by which to judge the reforms: the well-being of the millions of former welfare recipients is also important. Much of what we know about outcomes for welfare leavers comes from studies undertaken in individual States. To date over 30 States have conducted studies monitoring the outcomes of those who have left welfare. In addition, some of the data from State waiver experiments undertaken before the nationwide welfare reform have implications for current programs.[28]

Available data on the results of welfare reform often differ from State to State and do not represent nationwide averages. This Report therefore supplements this information with new results from the U.S. Bureau of the Census's {~~who conducts this survey?~~} Survey of Income and Program Participation (SIPP),[29] providing some of the first evidence on the effects of welfare reform for a nationally representative sample. The ~~majority of these~~ results from SIPP are based on a sample of people who were observed for at least 12 months after leaving the welfare rolls. These individuals were first observed between December 1995 and March 1996 and were reinterviewed every 4 months until November 1998 or February 1999, depending on the month of the initial interview. The new data cover the experiences of some of the earliest beneficiaries of welfare reform and may not reveal the effects of the time limits on receiving benefits or the long-term impact on families.

One of the most important issues in evaluating welfare reform is the incidence of recidivism--that is, the ~~number of individuals~~ cycling of individuals on and off the rolls. Both SIPP data and a synthesis of State studies show that approximately 25 percent of those who leave welfare returnwithin 12 months. (Most studies of recidivism, including those cited here, ~~exclude those who stay off the rolls for less than a month.)~~ do not count transitions of less than two months as true welf exits or entrances The majority of those who do return do so quickly: the SIPP data show that 18 percent of those who exit return within the first 6 months of leaving and only 7 percent during the second 6-month window. Further, the number of those returning to welfare declines with time. In Maryland 25 percent of former recipients returned to welfare within 12 months, but only 10 percent returned in the next 12 months, and just ~~2~~ 1 percent in the third 12-month period.[30]

## *Helping Welfare Leavers Find and Keep Jobs*

A key component to success after welfare is the ability to obtain a job and remain employed. The Administration provided a total of $3 billion in fiscal years 1998 and 1999 in the form of Welfare-to-Work grants[31] to help States and local communities move long-term welfare recipients and noncustodial parents into jobs. The Administration also implemented the Workforce Investment Act, which allows States to provide job assistance to low-income workers (Box 5-1).[32]

**Box 5-1. The Workforce Investment Act**

The Workforce Investment Act of 1998 was the result of a bipartisan effort by the Congress and the Administration. The law requires that basic job and career information and assistance be available to all Americans and creates a system developed around one-stop career centers in order to knit together multiple programs at the local level. The law also provides for intensive assessment, counseling, job search assistance, and training for low-income individuals and dislocated workers on a priority basis.

The law initiates three reforms that are designed to maximize training choices: individual training accounts, systems for identifying eligible training providers and their programs, and State and local Consumer Reports Systems containing extensive information on programs and their performance. These reforms were designed so that trainees will have the opportunity and the purchasing power to enter the training program of their choice rather than be channeled into one of a handful of locally contracted programs. The reforms provide a high level of reliable information that will empower trainees, allowing them to make informed choices.

Welfare-to-work programs generally use one of two approaches to helping welfare leavers find jobs. The "work first" approach aims to get people employed as quickly as possible. It assumes that work itself will ~~teach~~ give inexperienced workers the skills (human capital) they need to remain in the labor force, ~~after which they can~~ and move to increasingly better jobs. This approach focuses on maintaining an attachment to the labor force rather than on initial wages. The alternative approach relies on comparatively extensive education and training before welfare leavers enter the labor market. It keeps them out of the work force longer in the expectation that, once they enter the labor market, they will find better jobs than they could otherwise.

The work-first approach is by far the more commonly employed, and studies of initial ~~evidence indicates~~ outcomes indicated that it ~~is~~ was the more successful: employment levels and earnings ~~are~~ were higher in areas that have used it. However, a new study comparing outcomes across counties in California over a 9-year period finds that results for the two approaches are similar in the long term.[33] A separate study comparing the outcomes of 11 different welfare-to-work programs over a 2-year period found that the most successful approach combinedan emphasis on work with assistance in completing the General Education Diploma (GED). [34]

Employment levels among former welfare recipients have increased substantially since the 1996 reform.[35] Administrative data from studies conducted in several different States show that between 62 and 75 percent of those leaving welfare were employed at some point in the following year, and approximately 40 percent were employed in all four quarters.[36] Results are similar at the national level. SIPP data show that 66 percent of welfare leavers were employed at some point in the following 12 months, and 43 percent had earnings in all four quarters. However, many of those working all four quarters were employed less than full time. Only 32 percent of welfare leavers worked 50 weeks or more during the year, and just 40 percent of this group (12.8 percent of all leavers) worked 35 or more hours in each ~~every~~ week. Thus, although labor force participation has increased significantly among former welfare recipients, there is still considerable room for further gains.

Importantly, employment rates increased even among those who remained on welfare. In 1999, 33 percent of welfare recipients were working, compared with just 7 percent in 1992.[37] Developing an attachment to the labor market even while on welfare is important, because it increases the probability of success after welfare is no longer an option.[38]

The importance of the booming economy to these successes should not be understated. Theories of human capital accumulation and the tenets behind work-first programs suggest that time spent working increases productivity, job skills, and wages. The long economic expansion and historically low unemployment rates have given current and former welfare recipients the chance to accumulate work experience that would be expected to ~~will~~ serve them well in a future downturn. The longer the expansion continues, the better prepared they will be. to weather the consequences

## *Earnings*

Although employment is important in and of itself, so, too, are earnings. Welfare leavers are unlikely to thrive in the workplace if they are no better off financially than they were before leaving the welfare rolls. Evidence from State studies indicates that, at least initially, few leavers are significantly better off. Median quarterly earnings for those who found employment varied from $2,000 to $3,000, or approximately $700–$1,000 per month. In Wisconsin the majority of leavers had lower incomes (earnings plus food stamp benefits) after exiting welfare than they had while receiving welfare benefits. For the sample of SIPP leavers, the median monthly household income plus food stamps for the year following exit was $1,605, compared with $1,509 in the 2 months preceding exit. For 44 percent of leavers, total household income plus food stamps in the year following exit was more than $50 per month higher than in the months before; for 49 percent it was at least $50 lower.

The idea behind work-first programs is that an initial job will lead to earnings growth over time. Because many former welfare recipients find employment in low-wage industries such as food services, their prospects for earnings growth may not seem extremely bright.[39] Yet 39 percent of SIPP leavers had monthly earnings in the second 6 months after leaving welfare that were $50 or more higher than in the first 6 months. Twenty-eight percent saw a reduction in earnings of $50 or more over the two 6-month periods immediately following exit. Thus, over one-third of former welfare recipients did find jobs that provide earnings growth through increases in hours, wages, or both.

Income gains from the Earned Income Tax Credit (discussed in detail below) are not included in these calculations. Although its benefits are not recorded in the SIPP data, the earned income credit provides a substantial subsidy to low-income workers, and including its effects would improve incomes and poverty rates considerably. Although its figures do not focus specifically on welfare leavers, the Census Bureau estimates that in 1999 the fraction of households with after-tax incomes of less than $10,000 a year falls from 9.9 percent to 9.3 percent when the Earned Income Tax Credit (EITC) is factored in.[40] At a maximum of $3,880 for a low-income worker with two children, the EITC could add up to $323 per month to a family's income.

*Making Work Pay*

A network of government support programs facilitates the transition from welfare to work. In the past, families leaving welfare often lost not only their cash assistance but alsoother benefits such as food stamps and Medicaid. At the same time they incurred explicit payroll taxes and additional expenses associated with work, such as child care and transportation costs. One study found that the implicit marginal tax rate—the net amount ~~lost from a one-dollar increase in income to~~ paid in taxes, forgone benefits, and expenses from a one-dollar increase in income—for AFDC recipients could easilyexceed 50 percent.[41] In other words, earning one dollar more in the labor market increased their disposable income by less than 50 cents.

The Administration's welfare reform proposals have attempted to reduce these implicit taxes by increasing the rewards from work, through a higher minimum wage and an increased Earned Income Tax Credit, through increased subsidies for child care, and through expanded health insurance coverage to include working families not previously eligible for public programs.[42] The Administration has also worked to help single parents collect the child support paymentsdue them. These programs do more than help ease the transition from welfare to work; they also benefit working families who may have never received welfare. By reaching out to both groups, the Administration has worked to ensure that no working family is left behind.

*The Earned Income Tax Credit.* Operating through the income tax system, this credit provides a wage subsidy for low-income workers. The amount of the subsidy depends on how much the family earns and on ~~the number of dependents~~ whether there are zero, one, or two or more children. By effectively increasing the wage rate, the Earned Income Tax Credit offers those eligible an added incentive to participate in the labor force. In 2000, families with two or more children received a subsidy of 40 cents for every dollar of earned income up to ~~$9,720~~ $9,700, for a maximum credit of ~~$3,888~~ $3,880. This tax credit is refundable, so even families who pay little or no income tax can benefit fully from the tax provision. Rather than falling to zero when earnings surpass this level, the credit remains at ~~$3,888~~ $3,880 until earnings reach ~~$12,690~~ $12,700 and then gradually declines. It is phased out completely when earned income reaches $31,152 (Chart 5-4).[43] The gradual reduction reduces the disincentive to earn income beyond the level at which the credit peaks.

more than 2 children does not give a higher benefit; one dependents other than children yield no increase

The Earned Income Tax Credit has been expanded greatly since 1990, with increases in both benefits and scope of coverage. The 1993 expansions increased benefits for approximately 15 million families, in large part by raising the subsidy for families with two or more children.[44] The

yes
1993 {~~1993 correct?~~} expansion also, for the first time, allowed workers without children to claim a tax credit.[45] As a result of both the 1990 and 1993 expansions, credits paid through this provision increased from $15.5 billion (~~in 1999 dollars~~) in 1993 to nearly $32 billion in tax year 1999.[46] At the same time the number of families receiving assistance from the program increased by one-third, from 15 million to just over 19 ~~nearly 20~~ million.[47] The program now pays out more than the combined amounts distributed through the TANF and food stamp programs.[48]

This wage subsidy has been effective in attracting more workers into the labor market (Chart 5-5).[49] According to one estimate, ~~in 1992–96~~ the Earned Income Tax Credit alone was responsible for 34 percent of the increase in ~~{what is annual employment as opposed to just employment?}~~ annual employment among unmarried mothers.[50] between 1992 and 1996

(Need to be [illegible] 34% of total [illegible]
[illegible] working at [illegible] the year)

In addition to increasing the probability of employment for ~~that~~ low-income people ~~will find jobs and keep them~~, the Earned Income Tax Credit has done much to improve the well-being of those who take advantage of it. (doesn't help job search) Many former welfare recipients have trouble securing jobs that pay enough to raise their incomes ~~them~~ above the poverty level. But when the credit is taken into account, the earnings of many of these new workers rise substantially. In 1999 the credit lifted 4.1 million individuals, including 2.3 million children, out of poverty. The provision has also been effective in targeting benefits to the most needy. Estimates are that between 50 and 60 percent of its benefits accrue to families with incomes below the poverty line.[51]

***Minimum wage.*** The minimum wage operates in tandem with the Earned Income Tax Credit: the credit provides an effective wage subsidy, and the minimum wage laws ensure that that subsidy is based on an acceptable wage. The real value of the minimum wage declined substantially from 1992 to 1995, falling to just 71 percent of its peak value in 1968 ~~value~~.[52] Subsequent Administration-backed efforts led to increases in the minimum wage in 1996 and 1997. Even with these most recent increases, however, the minimum wage in 1999 was equal to less than 80 ~~2000 was equal to only 77~~ percent of its 1968 level (after controlling for inflation).

However, when the minimum wage is combined with a possible 40 percent subsidy from the Earned Income Tax Credit, the true minimum wage for workers with two or more children and earnings of less than $9,700 ~~$9,540 is~~ $7.21 an hour (Chart 5-6). This hourly rate is nearly as high in real terms as the peak minimum wage rates of the 1960s. Even so, an individual working full-time at the minimum wage would have a yearly income of just $14,188 ~~$14,116~~ (including the credit), well below the poverty line of $16,895 for a family of two adults and two children.

<insert Chart 5.6: Minimum wage with EITC chart here>

*Child care.* For many parents, one of the most difficult barriers to employment is finding affordable, good-quality child care. For low-income families and new entrants to the labor market, the costs of child care may make working impossible. Recognizing these costs as a barrier to work, the Administration has fought to make child care more affordable for low-income families and to provide assistance with child care expenses to a greater number of families. As a result, funding for child care has increased by XX percent since 19XX ~~more than doubled [dates?]~~, and the various existing child care programs have been combined to create the Child Care and Development Fund. The fund provides States with block grants for the purpose of subsidizing approved child care arrangements. In fiscal year 2000 ~~2001, under the Administration's proposed budget~~, States had ~~will have~~ access to more than $3.5 billion through this program. These funds are ~~can be~~ used not only to make child care more affordable but also to improve the quality of that care.[53]

Estimates suggest that 1.75 ~~over 2~~ million children benefited ~~will benefit~~ from the Child Care and Development Fund in 1999 ~~fiscal year 2001~~. Despite this substantial investment, however, many States have waiting lists for benefits, and many families who qualify for the subsidies do not receive benefits. According to one study, only 30 percent of families who have left welfare and are now self-supporting are receiving assistance with child care.

***Food stamp program.*** The food stamp program supplements family incomes to help ensure that low-income families receive adequate nutrition. Benefits are available to families with incomes up to 130 percent of the poverty line. In fiscal year 1998 the vast majority of benefits (nearly 90 percent in dollar terms) went to elderly individuals and families with children.[54] In 1999, ~~32~~ 27 percent of participating households had earned income. ~~benefits went to working families~~. Since 1994 enrollment in the food stamp program has fallen dramatically, from a high of 27.5 million participants to 18.2 million in 1999. Of concern, however, is the fact that the participation rate for eligible families declined from 71 percent in September 1994 to 62 percent in September 1997.[55] This decline is particularly marked for families with children. [**T~~he rest of the paragraph was phrased to suggest th~~at** Not corr it is children we were referring to **~~children receive food stamps. Are the changes to "families with children" correct?]~~** In 1999 only 51 percent of f~~amilies that included~~ children in families with ~~and had~~ incomes below the poverty line received food stamps. Even among the very poorest f~~amilies with~~ children in families ~~—those~~ with incomes less than 50 percent of the poverty line—only 58 percent received food stamps in 1999, down from 76 percent in 1993.[56]

Several factors could be responsible for the decline in participation. Changes in the laws governing the program have excluded Some immigrants from the program and restricted the amount of benefits that able-bodied workers may receive. Limitations on the value of assets an eligible family may hold may also exclude some needy families. And the strong economy and the growing number of workers with jobs may have helped reduce the need for food stamps. But these factors alone cannot explain all of steep decline in participation rates, and it is likely.. that some eligible families are not receiving the benefits they need (and are entitled to receive), especially families just leaving the welfare rolls. Rules governing participation in the program are often a factor here. ~~Some~~ States require that wage-earning food stamp recipients have their incomes recertified at regular intervals, typically ~~sometimes~~ as often as every three months and even more frequent in some states. For low-wage earners without much time off, this requirement could well be a substantial deterrent to participation. A recent study underscored this concern, attributing a large portion of nonparticipation ~~largely~~ to the costs to recipients of regular recertification.[57] (largely implies it was the most important factor)

In response to these recent trends, the Administration has implemented a series of changes in the regulations governing the food stamp program. These changes substantially reduce the need for recertification for those leaving welfare and the newly employed, and streamline the application process. States can also receive bonus awards under the TANF program for **~~[raising?]~~** high participation rates for low-income working households and for overall increases in participation. To date, $20 million has been allocated for these awards. Finally, the Administration has provided funding for educational and outreach campaigns aimed at e**~~nhancing [Can this term~~ be s~~implified, perhaps to "improving nutrition, especially for children"?]~~** ~~nutritional security~~.[58] improving nutrition for low-income families and the elderly

awards exist for both level and change

*Child support programs.* Child support payments from noncustodial parents are an important source of income for poor children. In 1997 child support lifted an estimated half a million children out of poverty.[59] Child support is particularly important for families leaving welfare. Women who leave welfare and do not receive child support have more than a 30 percent chance of recidivism after six months. For those receiving even small amounts of child support (0-$100 per month), that figure drops to ~~9~~ 10 percent.[60]

An important component of the Administration's policies to help working families is ensuring that single and divorced parents receive the child support payments they are entitled to under the law.. Between fiscal years 1992 and 1999 the dollar value of child support collections increased in real terms by more than two-thirds, from $9.5 billion to nearly $16 billion (in 1999 dollars). During the same period the number of child support cases involving collections increased from ~~2.8~~ 2.6 million to 6.1 million.

However, much of the money collected never reaches the custodial parent. Many States reduce TANF benefits dollar for dollar when a noncustodial parent provides support, reducing the incentive for noncustodial parents to provide for their children. The President has proposed legislative changes that would make it easier for States to pass along a portion of child support payments to custodial parents receiving assistance. This change would give parents an incentive to cooperate with the system. Some States, such as Wisconsin, are already experimenting with this type of policy, with some success. Results show that noncustodial parents are more willing to pay child support when they know that at least some of the money will ~~go to the custodial parent.~~ benefit their child. Utlimately more wide-spread use of this policy should increase collections of child support payments.

(Not an incentive, just a help)

~~As an added incentive for cooperation with laws governing child support,~~ The Administration has also put in place policies that reach out to low-income noncustodial parents. Some $125 million has been requested for grants designed to help fathers find and keep work **{is this correct?}** ("Fathers Work" grants). Responsible fatherhood initiatives funded through the Department of

Labor complement this policy, helping noncustodial parents not only find work and pay child supportbut also reconnect with their children.

*Access to health insurance.* Historically, individuals and families leaving the welfare rolls have lost their Medicaid coverage as they did so. During the 1980s a series of Medicaid expansions and the introduction of Transitional Medicaid Assistance ~~Coverage~~ began providing health insurance benefits to former welfare recipients and low-income families, easing the transition to work. Prior to the 1996 welfare reform a Federal mandate required that States cover all pregnant women and allowed some children not receiving welfare to enroll in Medicaid. This group included children under the age of 6 in families with incomes below 133 percent of the poverty line, and children between the ages of 6 and 19 in families with incomes below 100 percent of the poverty line. Many States opted for even broader coverage, setting higher income thresholds and covering children of all ages. Adults could obtain Medicaid for up to 12 months under the Transitional Medicaid Assistance ~~Coverage~~ program or through State programs for the medically needy. The 1996 legislation expanded Medicaid coverage to single parent and ~~unmarried [mothers?]~~, some two-parent families, and families leaving welfare provided their incomes were sufficiently low. In 1997 the State Children's Health Insurance Program (SCHIP) was created to provide health insurance for ~~target all~~ children in low-income families. ~~These programs are~~ The SCHIP program is discussed in detail later in the chapter.

Add "Helping Families Insert #2"

***Reaching out to Underserved Communities***

(Change inner city to central city)

Providing opportunity and independence for American families sometimes requires more than a strong national economy and responsible welfare policy. Areas where poverty has become entrenched and the local economy is weak may need additional assistance. Some of the most intractable poverty is found in America's central ~~inner~~ cities and rural areas. Because these areas are home to large numbers of Americans—in 1999, [~~correct year?~~] yes 30 percent of the country's population lived in the central ~~inner~~ cities and 20 percent in rural areas[61]—this situation is cause for great concern.

In 1967, when statistics for these areas were first recorded separately, the poverty rate for inner cities was 15.0 percent, compared with a nationwide rate of 14.2 percent. In contrast, poverty in rural areas was over 20 percent. By this measurethe inner cities were nearly as well off as the rest of the country, but rural areas suffered from disproportionately high rates of poverty. Between 1967 and the early 1990s, however, the incidence of poverty shifted: conditions in the central ~~inner~~ cities worsened, and nonmetropolitan areas saw a slight improvement. By 1993 the proportion of central ~~inner~~-city residents living in poverty had reached an all-time high of 21.5 percent, and the poverty rate in rural areas had declined slightly to 17.2 percent— well above the national poverty rate of 15.1 percent ok ~~in both cases~~. Since 1993, however, the situation has improved dramatically. In 1999, the poverty rate for central ~~inner~~ cities was 16.4 percent and that in rural areas stood at 14.3 percent. Yet these rates remain well above the national average [of 11.8 percent ~~**give national average here?**~~].

The strong national economy and current policies to make work pay, discourage out-of-wedlock births, and improve schools in poor neighborhoods can be expected to provide some relief, [no ~~**especially in inner cities?**~~]. But given the persistently high poverty rates in these areas, additional strategies may be required. To reach out to residents of these areas, the Administration has enacted a series of programs that directly target communities.

*Central* ~~*Inner*~~ *cities*: Central ~~Inner~~ cities are often more attractive to low-income workers than outlying suburbs. Inner-city residents have ready access to public transportation and shopping, and city governments often provide more generous support services than governments in other locales.[62] But cities often have one key drawback(?) ~~limitation~~: limited (not necessarily fewer, just not enough or not the type needed) ~~fewer~~ job opportunities. Recent research shows that most job creation today is taking place in the suburbs. One study by the Department of Housing and Urban Development (HUD) found that from 1992 to 1997 job growth was slower in the cities than in the suburbs ~~in 1992–97~~ and that the job mix in cities is increasingly shifting towardhigh-technology industries, which works against low-skilled workers.[63]

The difficulty central ~~inner~~-city residents face in finding employment is further heightened by problems with discrimination and transportation ~~transportation and by discrimination~~. Low-income workers, and welfare recipients in particular, are unlikely to own cars and must rely on public transportation. Yet a recent study found that nearly half of all low-skilled jobs in the suburbs are not accessible by public transportation.[64] Compounding this situation is the fact that minority workers in the inner city still face discrimination in housing and employment markets. A recent study found that minorities have difficulty renting and purchasing housing in the suburbs and are less likely to be hired by the white-owned firms that predominate there.[65] The cost of housing in the suburbs may also make it difficult to move to homes near suburban jobs.

From a policy perspective, several approaches are available to address the mismatch between where low-skilled workers live and where they can find work. The first—and perhaps most difficult—is to rebuild the economies of our central ~~inner~~ cities. The second involves seeking ways to overcome the transportation hurdles that central ~~inner~~-city commuters face. The third approach is to help low-income families obtain housing in areas where jobs are available. Providing training is yet another way to address this issue—that is, improving workers' skillsand thus their employability at a range of jobs. The Administration has pursued policies that incorporate all four approaches.

When this Administration took office, a number of programs already addressed underserved communities. The long-standing problems in these areas, however, clearly called for additional policy measures. The Administration developed a number of strategies for rebuilding inner-city economies, including Empowerment Zones and Enterprise Communities. Since 1995 over $1 billion has gone to 78 designated urban areas under these initiatives, supplemented by over $10 billion leveraged through other Federal grants, State and local government spending, and private sector funding. The Empowerment Zone and Enterprise Community programs aim to assist communities by encouraging investment from private businesses through tax credits, wage subsidies, and improved access to credit markets.

To help solve commuting problems, the Administration's Transportation Equity Act for the 21st Century established a new Job Access and Reverse Commute Program designed specifically to connect low-income persons to employment and support services. Similarly, the Bridges to Work program provides placement, transportation, and retention services in a select group of cities. In addition, the Administration has made owning a car easier for low-income families receiving temporary assistance or food stamps, by givingStates the flexibility to raise the limit on the value of a car counted as an asset for welfare eligibility purposes[66].[67] HUD programs also address transportation problems by subsidizing low-income families in both public and private sector housing. HUD's housing voucher program helps over 1.6 million families pay the rent for apartments in the private market. This portable form of assistance helps families locate near jobs.

Two Administration housing initiatives focus on improving employment outcomes for low-income families. The Moving to Opportunity demonstration program combines intensive counseling with voucher assistance to help families move from high-poverty public housing projects to private housing in low-poverty areas. The Welfare-to-Work voucher program provides housing subsidies and services to families eligible for temporary assistance to help adults in the family obtain and keep jobs.[68] Limited preliminary evidence from Moving to Opportunity programs in Baltimore and Boston suggests that the program also helps children as has ~~is successful in~~ been successful in improving educational outcomes ~~for children~~.[69].

*Rural communities*: Like the inner cities, many of America's rural communities face high rates of poverty and unemployment.[70] But these communities also face a number of unique problems. First, they tend to have smaller, less diversified economies than do the central ~~inner~~ cities and thus can be severely affected by the closing of only one or two industrial plants.[71] Second, many rural communities are geographically isolated from major markets, making it hard for residents to find jobs and for businesses to reach their customers.[72] Third, rural communities often offer little in the way of public transportation, so that commuting problems are likely to be more acute than in urban areas. Although recent advances in telecommunications promise to reduce some of ~~this~~ these disadvantages rural communities also lag behind urban communities in access to this technology.[73] Finally rural governments often lack the economies of scale needed to make investments in public services economical.[74]

A variety of programs exist to help these communities. Technical assistance, grants, and loans offered through the Rural Utilities Service provide assistance with basic infrastructure needssuch as electricity, telecommunications, and water and waste facilities. The Rural Housing Service assists rural communities with community facilities and housing. Its programs provide housing assistance to families with moderate and low incomes; it also helps communities develop and improve facilities such as fire stations, libraries, and hospitals.

The Rural Business-Cooperative Service cultivates partnerships between the private sector and community-based organizations.[75] It also provides technical assistance and funding for projects that generate employment. Rural businesses also get a boost from the Empowerment Zone and Enterprise Community initiative, as many of the areas these programs target are located in rural communities. Finally, the Telecommunications Act of 1996 is addressing the digital divide by providing funds to help schools and medical facilities in low-income communities (both rural and urban) develop modern communications infrastructure.[76]

At the regional level the Administration has supported several initiatives addressing the problems of rural development, including a Task Force on the Economic Development of the Southwest Border, the Mississippi Delta regional initiative, and the Denali Commission in Alaska. These initiatives coordinate Federal, State, and local development assistance to areas with historically high poverty rates and limited employment opportunities.

*Results*: These programs, coupled with the strong national economy and policies aimed at making work pay, have led to substantial improvements in the quality of life for those living in inner cities and rural areas. The unemployment rate in the Nation's inner cities fell from 8.2 percent in 1993 to 5.3 percent in 1999, while unemployment in rural areas declined from 5.9 percent to 3.7 percent.[77] Increased employment has meant reductions in poverty and increases in median incomes (Chart 5-7). As noted above, the poverty rates in both central cities and rural areas f[ell] significantly between 1998 and 1999 ~~The poverty rate in the inner cities fell from 21.5 percent in 1993~~ to ~~16.4 percent in~~ in central cities ~~1999~~, with the largest drop, in central city rates, 2.1 percentage points, occurring in the last year. This change was so large and affected so many people that it ~~These figures have a significance that goes far beyond the affected neighborhoods~~: ~~inner cities~~ accounted for 80 percent of the total reduction in poverty from 1998 to 1999 .[78] ~~Poverty in rural areas also fell substantially, from 17.2 percent in 1993 to 14.3 percent in 1999~~.

The median household income in the ~~inner~~ central cities has also increased, rising 5 percent in real terms from 1998 to 1999—more than double the 2.1 percent increase in the median income in metropolitan areas as a whole.[79] As was the ~~ee~~ situation for the gains for the nation as a whole, th[e] gains in incom[e] for ~~For~~ African Americans ~~the gains~~ in central cities were particularly striking. After adjusting for inflation, the median income for African American households in inner cities increased by 13.9 percent ~~in 1998–99~~ between 1998 and 1999. These economic gains have been accompanied by a decline in the number of people on welfare. Caseloads in the largest ~~inner~~ central-city areas declined by

40.6 percent between 1994 and 1999.[80] Increases in the median household income in rural areas were less dramatic than those in the cities, rising just 0.9 percent in real terms ~~in 1998–99~~ between 1998 and 1999.

*Despite these clear improvements in the well-being of our poorest communities, much remains to be done. Poverty rates and unemployment are still higher in our inner cities and rural areas than elsewhere. It is too soon to judge the effectiveness of the Administration's community-based policies,, but reaching out to these communities demonstrates a willingness to seek creative solutions to some of the Nation's most pressing problems.* un-italic

**Education in the New Economy**

~~Educatio~~ Education insert #5

Investments in human capital play an important role in the New Economy. By investing in our young people, we support continued growth of the economy. T~~he most direct way to invest in~~ h~~uman capital is through education and training~~ ~~{**what other ways are there??**}~~. Last year's *Economic Report of the President* focused on the demand for educated workers, postsecondary education, and training. This year's *Report* examines America's public elementary and secondary schools—institutions crucial to the development of our future work force. Not all communities can afford to offer their students the best possible education. In reducing this inequality, the Federal government can play a crucial role. And by promoting educational innovations such as more standardized curricula and the increased use of technology in the classroom, the Federal Government is working to improve the quality of schooling and to create the more productive work force needed for future economic growth.

Many factors go into producing a quality education. Parents, families, and communities rank among the most important contributors to the education of children. But the discussion here focuses on those components of the education system that are more directly under the control of Federal, State, and local governments, and highlights the effects of class size, teacher quality, and school infrastructure and equipment. I~~mproving the quality of~~ Strengthening these inputs to the education process is key to improving educational outcomes.

*A Role for Federal Education Policy*

Insert "Education Insert #1"

The Federal Government has long sought to improve access to education for the Nation's poorest children and to help States ensure that their public schools are of high quality. Federal funds ~~target primarily local communities, where they~~ primarily help implement needed reforms, expand new programs,[81] provide access to new technology,[82] and pay part of the cost of education for students with disabilities.[83] Many Federal education programs are targeted to schools and school districts serving students from lower-income families.[84] By directing funds to these important areas, the Federal investment in schooling can have an impact greater than the expenditure itself would suggest.

In the United States, primary responsibility for elementary and secondary education rests with the States and with local school districts. Excluding school-based health[85] and nutrition programs, the Federal Government provides just a little more than 6 percent of all funding for kindergarten, elementary, and high school education.[86] However this figure belies the disproportionately large impact federal dollars can have on schools. Federal spending in the poorest schools reduces inequalities across school districts but does not fully compensate for the overall pattern of funding disparitiescreated by differences in local property tax bases and State funding levels (Chart 5-8). ~~[Give date] The~~ A study of 1994-1995 data found that the Federal Government spent more than four times as much per student in the poorest quartile of school districts as in the wealthiest quartile, but that the wealthiest school districts still had the highest level of expenditure per student.[87]

The largest single Federal education program for kindergarten through 12th grade (K-12) is Title I,[88] which ~~allocates additional~~ provides funds ~~[what are these funds in addition to?]~~ to schools based on the number of ~~[correct?]~~ poor children ~~enrolled~~ (not necessarily enrolled) and the child poverty rate in the local area.[89] [Correct?] Under the 1965 Elementary and Secondary Education Act, Title I funds are to be targeted to schools serving the poorest children. ~~But the mandate expanded~~ The targeting of funds to poor schools improve significantly with the passage of the Improving America's Schools Act in 1994, which reauthorized the 1965 law. In the 1997–98 academic year, 96 percent of the schools with the highest poverty levels received Title I funds, up from 79 percent in 1993–94.[90] In addition, in 1997–98 the ~~poorest~~ highest-poverty quartile of school districts received 43 percent of all Federal funds for K-12 education and 50 percent of Title I funds—amounts that reflect theshare of the Nation's poor children in these districts (49 percent). At the same time ~~the poorest~~ these school districts received less than a quarter of all State and local funds. Clearly, Federal funds in general and Title I funds in particular are a critical resource for improving equality in education.[91 92 93]

Replace with "Education Inserted #2"

**[Transition needed here. Would something like "How do schools and school districts use Federal funding to improve education? Among the priorities of both teachers and administrators are reducing class size, hiring new teachers and providing training for those already teaching, modernizing schools, accessing new technology, and developing standards and accountability. School choice?]**

*Reducing Class Size*

For decades the merits of ~~broad-based~~ various educational spending programs, including those aimed at reducing class size, have been the subject of much debate. Are they in fact effective in improving student achievement? Mounting evidence ~~has begun to show~~ is showing that smaller classes are beneficial, especially for disadvantaged students and those in the early grades.

The most compelling evidence comes from the Project STAR (Student-Teacher Achievement Ratio) experiment in Tennessee. To determine to what extent smaller classes improve academic outcomes, Tennessee authorized and financed an experiment that randomly assigned students and teachers in grad K-3 ~~randomly~~ to classes with a standard number of students (22–25) or to smaller classes (13–17).[94] The results showed ~~significant improvement~~ better performance for children in the smaller classes: ~~from kindergarten through grade 3~~ these children did better on standardized tests of reading and math than students in larger classes.

A follow-up study showed that the students enrolled in smaller classes in the early grades continued to do better on standardized tests in middle school than other students. These students a~~lso scored higher on their standard college entrance examinations while in high school and~~ were also more likely to take ~~these exams~~ college entrance exams in high school. The results were especially strong for minority students. For example, white students have a higher probability of taking a college entrance exam than African American students. But when the probabilities were calculated for white and African American students who were placed in small classes in elementary school, this difference narrowed by 54 percent.[95] Some 46 percent of white students and 40 percent of African American studentswho had been in small classes took a college entrance exam; the corresponding figures for students in

standard ~~traditionally~~, sized
~~traditional~~l classes were 45 and 32 percent.

the experimental design and the outcomes it generated
The quality of {~~clear results from?} this experiment~~ persuaded many scholars that reductions in class size can improve educational outcomes for children. Teachers in smaller classes can spend more time on individual instruction and review, and less on student discipline and routine administrative tasks, than teachers in larger classes.[96] Teachers of small classes arealso more likely to get to know their students, interact with them frequently on a one-to-one basis, and provide frequent, in-depth feedback.[97] Results are now emerging from programs in other States (~~such as the SAGE program in Wisconsin~~) that reinforce the conclusions of the Tennessee study.

Reducing class size is expensive, however. Onestudy estimates that reducing class size in grades 1-3, to an average of 18 students, would cost an ~~estimated~~ $5 billion per year.[98] Despite the expense, the expected gains in students' future earnings appear to be large enough to make the investment worthwhile.[99] [In 1998 the Administration proposed a 7-year Class Size

~~nationwide~~ ~~maximum~~ The ~~current~~ goal is for an ~~maximum~~ ~~and~~ average

move up bracketed text

Reduction Initiative to reduce class sizes in grades 1-3 to a ~~national average~~ of 18 students per

nationwide

class. In its first 2 years the program ~~has~~ enabled school districts to hire 29,000 new teachers, reducing class size for 1.7 million children.]

an estimated

*The Importance of Teachers*

The quality of teachers may play an even more important role than class size in improving student outcomes. Parents, students, and professional educators agree that teacher effectiveness is a significant factor in student achievement, and several recent studies support this conclusion. These studies find that differences in teacher~~characteristics~~s have significant effects.[100] Further, several of these analyses show that some measurable characteristics, such as holding a master's degree, are not necessarily indicative of a teacher's ability to enhance student performance. And although a teacher's effectiveness appears to increase with experience in the first years of teaching, these gains to seniority do not continue beyond three to five years. {~~so what characteristics *do* matter?~~}

These results suggest that much of the difference in the effectiveness of teachers stems from differences in hard to measure attributes such as talent and motivation, indicating that direct observation may be the best way to assess teaching ability

Many schools are finding it difficult to attract and retain highly effective teachers. Some of this difficulty likely stems from the existing pay scales in public schools. In the last several decades, teachers' salaries have fallen relative to those in other occupations. A large majority of public school teachers are women, and for this group in particular, the rewards of teaching have fallen relative to other opportunities. In 1940 fewer than 40 percent of women with a college degree earned more than the average female teacher.[101] By 1990 this fraction had risen to 60 percent. This trend continued throughout the 1990s; ~~simply because~~ starting salaries in most occupations increased at a much sharper rate than did starting salaries in the teaching profession.[102] One study found that from 1994 to 1998 the average salary for people with a master's degree in nonteaching fields increased by 32 percent in real terms, while the real increase in the average salary for teachers was less than 1 percent.[103] Other factors that affect job quality for teachers, such as crowded classrooms, unsafe schools, and limited opportunities for professional development and advancement, also affect schools' ability to attract and retain teachers.

This challenge will become particularly difficult in coming years. Between July 2000 and July 2008, the number of children aged 5–17 will rise by nearly 1 million,[104] significantly increasing the need for teachers nationwide. Yet in this same period, about 750,000 teachers are expected to retire,[105] and ~~others~~ many are likely to leave the field to pursue other occupations. Given these statistics, the United States will need an estimated 2 million new teachers in the next 8 years.[106] The demand for teachers will be heightened by mandates to reduce class size. Decreasing the number of students per class to a nationwide average of 18 in grades 1-3 will require staffing an estimated 100,000 additional classrooms.[107]

These increases in the demand for teachers will make it increasingly difficult to maintain consistently high teacher quality in all classrooms. The magnitude of the challenge is already becoming clear. In 1996 California began a massive program designed to reduce class size in the early grades (K-3). Expenditures for the program, which seeks a statewide class size reduction from an average of 28 students to a maximum of 20, are running $1.5 billion per year. The State has been largely successful in achieving its goal: by the 1998–99 school year, more than 92 percent of California's students in the targeted grades were in classes of 20 or fewer students.[108]

But the percentage of fully credentialed teachers instructing these classes fell from 98 percent in the 1995–96 school year to 87 percent in 1998–99. [Although one study of the California experience found little impact of teacher certification on student outcomes, other analyses have concluded that credentials greatly ~~matter~~. Regardless of the importance of certification, however, increases in the demand for teachers may affect the availability of talented instructors.[109] The ultimate benefits of nationwide reductions in class size will depend on the ability to attract and retain greater numbers of highly qualified teachers and to providing mentoring, training, and other support to those just entering the profession.] [Box 5-2]

see Education insert #3 on attached page

This Administration has supported investments in teachers. Its Class Size Reduction Initiative requires that teachers hired with Federal funds available under the program be fully certified. The initiative allows school districts to spend up to 25 percent of their allocated funds ~~allocation~~ on professional development and testing for new teachers (for content knowledge, to meet State certification requirements, or both). Districts that have met the appropriate goals for reducing class size in the early grades have the option of using their entire allocation for activities to improve teacher quality. **[Correct?]**The Teacher Quality Enhancement Grant program i~~s aimed at reforming State licensing systems and establishing support systems for new teachers~~ helps states improve the quality of teaching. To date it has helped prepare about 3,000 new teachers for high-need school districts, and it will help prepare many thousands more in coming years. Funding for this program—th~~e largest Federal professional development program in the budget—~~increased from \$275 million in 1993 to \$~~667~~ 335 million in fiscal year ~~2001~~ 2000.[110] [111]

**[~~Please indicate where in the text this box should be referenced~~]**

**Box 5-2. Rewarding Effective Teachers**

Replace with box on attached sheet

Some proposals for improving educational quality involve rewarding teachers with bonuses based on performance—a change from traditional systems that base pay on education, experience, and responsibilities. Performance-based pay systems may improve the quality of instruction by providing teachers with an additional incentive to achieve certain specific goals. In addition, establishing criteria for performance-based awards can help clarify and prioritize these goals, providing better guidance for teachers. Tying teacher compensation to performance may also help attract talented people to the teaching profession; such individuals may be more willing to become teachers if they know their hard work and skills will be rewarded.

Performance-based pay systems must be carefully designed. Because student achievement depends on many factors that teachers cannot control, such as family circumstances and previous education, teachers should be rewarded for gains in student achievement rather than for absolute levels of achievement. Furthermore, because learning involves cooperative effort, incentives must be designed to create a cooperative rather than a competitive environment for teachers. One way to foster such team spirit is to base awards on the achievements of an entire school rather than on the success of individual classes. Performance standards should not be based solely on a few easily measurable indicators of educational achievement but should focus on gains in important skills. The school can also coordinate its efforts to meet performance standards with other important goals.[112]

School-based performance awards were introduced in Kentucky and North Carolina in 1991 and in Maryland in 1996. Studies have found that the success of these programs varies according to how well they are designed and implemented. Well-designed programs were successful in focusing attention on goals, channeling organizational resources to meeting those goals, and motivating teachers. Even the best of these programs increased the pressure felt by teachers, however.

*The Need for Modern Schools*

Besides class size and teacher effectiveness, the physical condition of classrooms and educational materials may well affect~~s~~ the quality of the educational experience. In the most severe cases it co[uld] affect the safety of students. Communities across the country are struggling to address the problems of aging schools. In 1999 the average public school was 40 years old, and schools in largely poor or minority districts are even older.[113] Many of these aging buildings have outdated electrical systems that must be upgraded for computers, and asbestos in the walls of some schools increases the cost of such upgrades.[114] Some buildings need to be renovated extensively to accommodate disabled students. Many schools will need more classrooms as enrollments increase and average class size is reduced, putting additional pressure on aging facilities.

The National Center for Education Statistics estimates that getting America's schools into ~~top~~ good physical condition will require an investment of $127 billion.[115] Some 39 percent of our public schools already have temporary additions, about one-fifth of which are in less than adequate condition. Schools with a relatively high proportion of poor and minority students[116]~~—the very schools where students would benefit most from smaller classes~~—are more likely than other public schools to have temporary buildings, and thus will have the most difficulty housing additional classes. To help address these problems, current spending proposals provide $1 billion in grants for emergency school renovations. In addition, there is bipartisan support for $25 billion in school modernization bonds over the next 5 years.[117, 118]

*New Educational Technology and Internet Access*

Today's workers are increasingly required to be computer literate, and. schools must be able to teach students the skills they will need to work with computers and other new technologies. In addition, Internet access is becoming an important classroom resource, helping students learn by connecting them to libraries, museums, and educational materials around the world.[119] Internet access has become increasingly widespread in American classrooms over the past 8 years, and Federal programs, especially the E-rate program, have played a large role. The E-rate program provides up to $2.25 billion per year to off-set the cost of telecommunication services, internet access, and internal connections to schools and libraries. Between 1994 and 1999, tremendous strides were made in connecting public schools to the Internet (Chart 5-9). With the help of ~~this~~ the E-rate program the ~~The~~ number of public schools with Internet access nearly tripled between 1994 and 1999, by ~~which year some~~ 1999 95 percent of all public schools were on line. Increases in Internet connectivity within classrooms were even more dramatic. In 1994 only 3 percent of public school classrooms had Internet hookups; by 1999 that figure had risen to 63 percent.[120]

<insert Chart 5.9: Internet access chart here>

The Federal Government has helped local school districts make the transition to the digital age, committing $5.7 billion over the last three years through its E-rate program to connect school and library computers to each other and to the Internet (Box 5-3).[121, 122] These funds have targeted schools with a high proportion of low-income students. Schools where 75 percent or more of students are eligible for free school lunches receive approximately 10 times as much funding per student from the program as schools with the smallest percentage of such students.[123]

**Box 5.3 Reducing the Digital Divide**

Since 1993, computer use in America has grown at an enormous rate, revolutionizing the way Americans communicate, work, and do business. Access to a computer—and knowing how to use it—are increasingly important for success in today's society. Currently more than half of all U.S. households have computers, and more than two-fifths have Internet access at home. But computer use varies greatly with income and education. People in households earning more than $75,000 per year are almost four times as likely to use the Internet as those in households earning less than $15,000 per year. Adults with college degrees are more than eight times as likely to use the Internet as adults who have not completed high school. Race is also a factor.. African Americans and Hispanics are substantially less likely than white and Asian Americans to use the Internet. A recent study finds that income and education explain only around half of this difference. Individuals from disadvantaged groups that already face obstacles in the workplace are at risk of falling even further behind if they lack computer know-how.

There is encouraging news, however. African American(s)?, Hispanic, and low-income Americans with access to ~~are connecting to~~ the Internet at faster rates than whites, Asian Americans, or wealthier Americans. Notable changes are occurring among school-age children, suggesting that the widespread availability of computers in the classroom is playing a role. Across all income and demographic groups, Internet usage among children aged 9–17 is higher than the national average. And over the last few years Internet usage has grown faster among African American and Hispanic children than among white children, and faster among children in households earning less than $35,000 per year than among children from wealthier households.[124]

Other Federal programs have also helped schools purchase new educational technology. I~~n the~~ 1~~997–98 school year {correct?}, the most recent for which data are available, Federal education programs spent $688 million (in addition to the E-rate program funds) on increased access to technology in schools. Much of the funding ($425 million in the Technology Literacy Challenge~~ F~~und)[125] went to help States implement statewide technology programs~~. These funds were used ~~primarily~~ to purchase computers and train staff in using new technology (Chart 5-10). During the 1997–98 school year, Federal funds paid for one-fourth of all new computers in schools. Federal funds were especially important in helping elementary schools with high levels of low-income students acquire technology, accounting for nearly 60 percent of new computers in these schools.[126]

Replace with "Educat insert E on attach sheet

For computers to improve the quality of instruction, teachers must know how to use them and how to integrate them into classroom instruction. A recent study found that 53 ~~the~~ percent ~~only half~~ of all public school teachers with computers or Internet access used these resources "t~~o a moderate or~~ l~~arge extent~~" for classroom instruction.[127] Teachers who have received more professional development in using computers and the Internet, ~~younger teachers~~, and teachers in schools with relatively few low-income students were the most likely to report using computers and the Internet. Newer teachers were also more likely to use computers "a lot" to create instructional materials

Despite the growth in the number of classrooms with computers Only one-third of teachers with access to computers and the Internet said that they felt well or very well prepared to use them, ~~and only one-fifth felt very well prepared to integrate educational technology into the classroom "to a moderate or large extent."[128 129] Such studies~~ These results clearly show that more investment in teacher preparation is needed. The Federal Government has addressed this issue through its Preparing Tomorrow's Teachers to Use Technology grant program. This program supports 352 partnerships[130] among colleges, educational agencies, high-technology companies, and nonprofit organizations, providing training for teachers in integrating technology into the classroom T~~hese partnerships are providing 3 years o~~f tra~~ining for 200,000 new teachers in integrating technology into the classroom. In its 2001 budget the Administration has requested an additional $150 million for this~~ program.[131132]

*Standards and Accountability*

Over the last decade, changes have taken place in America's public schools that go far beyond increasing the investments just described. Among the most important changes are new ways of improving OK {??} accountability for educational outcomes and of giving parents and students more choice in selecting a public school. (do you want the charter school section folded into the standards section? As of now they are separate but this makes sense to put them together)

One of the most important strategies at the State level today is standards-driven accountability. Initiatives that establish clear performance outcomes and systematically test student progress aim to help teachers and students focus their efforts on those areas needing the most work. Spurred in part by legislation passed in 1994 (the Improving America's Schools Act and the Goals 2000 **{is this the full name?}** Act), State after State has implemented standards for what students need to learn in school. ~~Since that time 29[133] [134] States have implemented standards for core academic subjects.~~[135] As of October 2000, 48 States and the District of Columbia had adopted such standards statewide, with the majority of states adopting standards Since ~~after~~ 1994 The establishment of these standards has been followed by an increase in standards-based assessment. Forty-eight states and the District of Columbia now administer tests to assess student performance relative to these standards in reading and math, and 17[136] States do so for science and social studies as wel. Thirty-six states currently publish some form of report card for each school, measuring school performance against a number of indicators, including student assessments, ~~tests.~~[137]

Both the standards themselves and the assessments based on them have been controversial. Many argue that classroom instruction is now geared toward preparing students for the exams--that teachers are, in effect, "teaching to the test." ~~Broad-based tests of these sorts are relatively new in the United States, but not in other countries. Cross-country comparisons show a positive correlation between student achievement and the existence of standards and external assessments and suggest that the imposition of standards may increase learning {OK?}.~~[138] OK

However, When implemented correctly, such assessments can help improve the quality of the educational experience--and educational outcomes--in several ways. First, tests that are challenging and well constructed can help raise the expectations of students, teachers, and parents. These expectations can motivate ~~put pressure on~~ all parties to improve their performance. Second, by clearly outlining the material to be covered and the degree of mastery required, these measures of accountability may help teachers focus on what are generally agreed to be the most important topics. Finally, these tests provide parents, teachers, and students with information that highlights those areas in which students are less than fully prepared.[139]

The Federal Government has played an important role in the standards movement. Since 1994 it has devoted more than $2.6 billion to helping agencies in every State implement school reforms through the Goals 2000 Act. Even before that legislation was passed, the government supported the development of voluntary national standards that States could use as a basis for their own standards.[140] In addition, the 1994 Improving America's Schools Act tightened Title I accountability at the school and district levels by requiring States to hold students in Title I ~~students~~ schools to the same challenging standards as other students and to assess all students against these standards.

The Federal Government has also increased its efforts to track student progress, undertaking evaluations that help in assessing State-level reforms.[141] In recent years the Department of Education has expanded the National Assessment of Educational Progress program to track student performance in each State. Thanks to these assessments ~~this program~~, a valuable set of baseline indicators which can help researchers and educational professionals evaluate the effectiveness of new policies the teaching methodology now exists for measuring student progress. [see box 5-4 The Individuals with Disabilities Education Act Amendments of 1997 further require that children with disabilities be included in State and district-level assessment programs, so that the performance of these children will be measured as well.[142]

**[Please indicate where this box should be referenced in text]**

New box, see attached sheet

**Box 5-4 Ensuring That Gains are Maintained**

~~Effective teachers, adequate facilities, and well-constructed standards can help students learn more, but it is equally important to ensure that students retain what they have learned. Recent studies have found that, during vacations and breaks, some students lose some of the skills and knowledge they have acquired. One study showed that although children from low-income and children from high-income families achieved similar gains on standardized tests during the school year, the former fell behind during summer break, while the latter maintained~~

the same test scores or continued to improve. These differences suggest an important role for public schools in helping children from low-income families succeed. By providing enrichment programs over the summer and after school, our public schools can help poor children overcome some of the disadvantages they face at home and in their neighborhoods.

These after-school and summer learning programs can also be a boon for working parents. Not only do they provide peace of mind for parents who know their children are in a safe, enriching environment, but they also allow working parents to invest more in their jobs, benefiting their own careers and further helping their children.

Neighborhood school facilities represent a large capital investment for any community, and they are often not used to their full potential. Many schools sit empty when they could be serving as community centers,offering access to theI Internet and adult education classes, for example. This Administration has worked to help communities develop after-school activities through its 21st Century Community Learning Centers Program. Through this program, the number of communities offering after-school activities in their classrooms has expanded from only a handful to over 3,600.

*Increasing Public School Choice*

A persistent thread during the last decade of educational change has been the call for parental choice in their children's education. Allowing parents to choose among different public school models would likely benefit students as each is offered a ~~type of inst~~ model of instruc most closel suiting their needs ~~benefit both educators and parents as well as the children themselves~~. In responding to parental demand, educators would offer the most effective educational models and innovations. Parents would be able to choose the school that offers the best fit for their child's learning skills and interests.

Many States have responded to the demand for choice by allowing parents, teachers, and other interested parties to establish independent public schools chartered by State or local education agencies. These charter schools are given autonomy over their operations and are exempted from certain State and local regulations (although not from standards-based assessment) in exchange for strict public accountability and results. Charter schools have great potential as laboratories of educational innovation, allowing individual schools to explore ~~experiment with~~ a variety of educational methods ~~and student populations~~ while remaining publicly accountable.

The Administration has strongly supported the development of charter schools, having overseen the passage of the first charter school law in 1994 ~~1998~~ and signing the Charter School Expansion of 1998. 19xx. [~~add date~~] In 1991 Minnesota became the first state to allow charter schools, and by the end of 1999, 36 states and the District of Columbia allowed ~~had opened~~ such schools. At the beginning of the 2000–01 school year, 2,069 charter schools were operating nationwide, up from just 34 at the start of the 1993–94 school year.

Although charter schools currently represent only 2 percent of all U.S. public schools,[143] their rapid growth has brought them a great deal of attention, especially in areas where a significant percentage of students now attend these schools. Charter schools tend to be about one-third the size of nearby conventional public schools. Most enroll students from the surrounding neighborhoods, so that students are often of the same race or the same ethnic background {??}. School districts with charter schools tend to have larger minority student populations than the average school district.[144]

### *Helping Students Make the Transition from Secondary School to College*

Federal programs are also helping students make the transition from secondary schoolto college or work ~~and beyond~~. The Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR UP) bring together middle schools with a high proportion of poor students together with local colleges and universities. These partnerships helped prepare more than 250,000 students for college in fiscal year 2000. The programs provide entire classes of students and their families with academic enrichment programs; information about choosing a college, applying for financial aid, and preparing for college entry; and in some cases will provide college scholarships. TRIO {~~spell out?~~} programs such as Upward Bound are currently offering services to help ~~help~~ 730,000 low-income, first-generation college and disabled students prepare for and succeed in college [~~annually?~~]. And after 6 years of receiving seed money from the Federal Government, all States have instituted local school-to-work programs to benefit secondary school students as they prepare for their working lives.[145]

(sorry, it really is just called TRIO)

Over the past 8 years, Federal assistance to Americans investing in their college education has also increased. Direct Pell grants haverisen from a maximum of $2,300 per student per year to $3,300. The HOPE Scholarship ~~Hope {Scholarship? is it not "HOPE"?}~~ and Lifetime Learning tax credits have also reduced the cost of education for American families. Fees and interest rates on student loans have been reduced, and restructuring the Federal student loan program has saved billions in taxpayer dollars.[146]

**Innovation and Access in Health Care**

next page

The American health care system today reflects the successes and the promise of the New Economy. Americans are healthier now than they were just 10 years ago. Between 1990 and 1998 life expectancy at birth rose approximately 1.3 years, and life expectancy at age 65 rose more than half a year.[147] The rate of chronic disability among the elderly declined by 1.3 percent **{percentage pts?}** annually between 1982 and 1994.[148] Medical innovations are in part responsible for these improvements, as well as factors such as improved nutrition and exercise. Yet health care continues to present challenges that demand an ongoing role for the government.

A stream of technological innovations has raised the quality of care and improved health outcomes. Innovative diagnostic tools and new treatments have improved the medical system's ability to treat many diseases. These innovations enable physicians to identify health problems more accurately and to offer treatments that are less invasive and promise better outcomes. One good example is the use of drug therapy to treat some conditions that formerly required surgery.

These improvements in treatment are expensive, however, and overall health care costs have risen as people demand more and better care. The pressures on rising expenditures are exacerbated by traditional fee-for-service insurance, which offers no incentives for patients or providers to limit their health care consumption. Managed care has evolved as an organizational innovation to control rising health care expenditures. It creates incentives for both patients and providers to make efficient health care consumption choices—to utilize treatments, especially costly technological innovations, only when they are medically necessary.

attached is a new box on summer school & the Administration's 21st Century Community Learning Centers Prog

**Box 5-x. Rewarding Effective Teachers**

Traditionally, teacher salaries have been based on education levels, experience, and responsibilities. These systems leave little room to reward the most effective teachers. Recently some school districts and states have experimented with alternative performance based pay systems. These new methods of providing compensation to teachers may help improve the quality of instruction along several dimensions. First, by establishing specific criteria performance-based awards can help clarify and prioritize goals, thus providing better guidance for teachers. These rewards can also provide teachers with additional motivation to work to achieve these goals. And importantly, tying teacher compensation to performance may help attract **and retain** talented people to the teaching profession, if they know that their hard work and skills will be rewarded. Insert #1

However, to be effective performance-based pay systems must be carefully designed. Because student achievement depends on many factors that teachers cannot control, such as family circumstances and previous education, fair performance-based incentive systems should reward teachers for gains in student achievement, rather than for absolute levels of student achievement. Insert #2 Furthermore, because student learning involves cooperative effort, incentives must be designed to create cooperative, and not competitive, environments among teachers. For example, team-spiritedness might be enhanced by basing **a portion of** the awards on school-wide achievement rather than the achievement of individual classes. Finally, the standards used to assess performance must be carefully constructed. Insert 3 & 4 Measures such as gains in student test scores, increases in attendance, and increases in graduation rates have all been employed.[i] [ii]

comment on high-stakes testing

The design of these school-based performance awards systems varies widely across sites. In some cases awards are given directly to teachers, in other cases the rewards benefit entire schools. To provide a sense of the types of incentives used by districts we highlight two programs. In Charlotte-Mecklenburg, North Carolina awards were based on a broad array of student outcomes including subject mastery, drop-out rates, and absenteeism. Schools received points for meeting annual improvement goals and teachers in these schools benefited directly. In the highest performing schools (classified as "exemplary") certified staff members each received $1000. Certified staff in schools with slightly lower gains ("outstanding" schools) received $750. In contrast to the equal division of awards within schools in Charlotte-Mecklenburg program, the program implemented at the Vaughn charter school in Los Angeles results in awards that vary substantially across teachers. At Vaughn teachers are provided with the opportunity to receive cash bonuses in each semester for effective performance in a number of areas including the teaching of specific academic subjects and more general skills like classroom management and lesson planning. Performance is assessed through self-evaluations, peer review and reviews by administrators. For a veteran teacher, performance related awards can total up to $13,100.

how is it structured?

While little evidence is available on the effect of these programs on student outcomes, one study of a program in Dallas, Texas does show positive effects on student achievement. Studies of the effect on teachers found that many school-based performance-based award systems helped improve cooperation among teachers but that programs varied in their effectiveness in increasing teacher motivation. Teachers in many programs also reported that they felt increased pressure at work and worked longer hours. The system at Vaughn has helped attract new recruits and many current teachers were pleased with the program. However, there are also some problems. One teacher complained that the peer review process with differing amounts paid to teachers, "pits teach against teacher." These difficulties indicate that additional research and experimentation might be useful in attempting to develop optimal compensation strategies.

We need a statement emphasizing the need for higher base salaries, before incentives.

## Ensuring Gains are Maintained

Effective teachers, adequate facilities, and well-constructed standards, can help students learn more, however, these investments ~~are of little~~ lose their value unless students retain what they have learned. Numerous studies have demonstrated that knowledge and skills deteriorate while children are away from school, specifically during summer vacations. Drawing their conclusions from an analysis of many previous studies, one group of researchers found that children lost an average of one month's worth of learning over summer break.

Much of the federal government's role in educational policy has been aimed at helping children in low-income families receive a quality education, thus mitigating the effect of family in~~come~~ characteristics on schooling outcomes. ~~Absent the effects of public schools, it appears that family characteristics play a larger role.~~ Many studies have noted that the deterioration of skills associated with summer vacation was the largest for children in low-income families. These differences appear to be particularly large for reading: students from middle class families were found to have experienced a small gain in test scores over the summer while students from low-income families fell behind, creating a gap between the two groups in reading skills that is equal to approximately 3 months of schooling.

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These differences suggest that public schools can do even more to help children from low-income families succeed. One possibility is to lengthen the school year. If students were to attend school year-round, there would be less opportunity for skills to depreciate. Alternatively summer enrichment programs targeting low-income communities can help poor children overcome some of the disadvantages they face at home and in their neighborhoods. In addition to changes in the school calendar, communities can offer after school enrichment programs.

Both after school and summer learning programs can also be a boon for working parents, particularly for lower-income parents who may have difficulty arranging alternative care for their children. Not only can such programs they give parents peace of mind that their children are in a safe, enriching environment, but ~~they~~ can also allow working parents to invest in their jobs and gain important labor market skills that can further benefit their children through increases in familial income and exits from welfare.

The Administration has worked to assist local communities develop after school activities through its 21st Century Community Learning Centers Program ~~begun in 2000.~~ This program has funded more than 3600 after school and summer programs and the Administration has proposed significant increases in the program's budget for the 2001 fiscal year. Preliminary evaluations indicate that these programs have had beneficial impacts on the academic and social behaviors of the children.

[i] School-Based Performance Award Programs: Design and Administration Issues Synthesized from Eight Programs.