To: Mickey
Gene
John et al.

From: Bob Reich

Re: Conference

Date: December 6, 1992

Behind the official agenda for the conference should be a set of themes which frame the Clinton Administration's overall economic challenge--the structural reasons why the American economy has performed below par: the failure of our schools, inadequate worker training, the bias of US economic institutions toward short-term investment, the decaying public infrastructure, the failure of the US to pay adequate attention to our export performance, inadequate private investment, American technology's large reliance on the military, and so forth. The unofficial agenda also should emphasize what's good and strong in America, and how we can meet the challenge.

The press and the public are paying attention (as usual) to the business cycle (how much of a stimulus? What will happen to interest rates? etc.), and to the budget deficit narrowly conceived, instead of to these larger issues. The conference should be seen as an opportunity to reframe the debate and lay the groundwork for the BC economic agenda over the next four years.

The following are "thematic" chapters to a story which the conference should tell the American public. BC can emphasize the themes by, for example, summing up a particular session by reference to them. The people we select to make presentations, as well as BC's talking points, questions, and any debate, should enlarge upon these key themes, so that the overall story is told effectively.

I. The challenge ahead:

1. A cyclical "recovery" still leaves the larger "structural" agenda in place. Even when the economy gets back on track, it's important to remember that the long-term track we've been on since the mid-1970s isn't enough to improve the standard of living of most Americans. Jobs will return, but they won't yield high incomes.

2. America has been generating many new jobs during the past decade and a half, but not good jobs. The real incomes of college-educated Americans have been increasing at a healthy

clip; the real incomes of non-college-educated Americans have been stagnant or declining. The gap is widening.

3. Technological change, and global economic integration, are behind these long-term problems. Foreigners aren't to blame. Even if we didn't face foreign competition, uneducated and unskilled Americans would face declining incomes due to evolving technologies that supplant workers without skills but enrich the jobs of those with skills.

4. American industry, and financial markets, emphasize short-term profits at the expense of long-term investments. The private sector isn't investing as it should in worker training, technology, or factories and equipment. Instead, it's engaging in an endless series of short-term transactions. One culprit: The way we've organized our capital markets. Our short-termism is getting worse, as financial markets become more efficient.

5. A large and growing proportion of our nation's children are being inadequately fed, clothed, and educated. Our children are our nation's future.

6. Americans spend more on health care than any other nation, but get very little for our spending. The system is plagued by inefficiencies, and 35 million Americans have no access to it at all.

7. In sum, the public and private sectors are consuming too much and paying inadequate attention to investing in our long-term future. Business and government must shift direction.

II. Shifting direction from a consumption economy to an investment economy (and the financial legacy of the Reagan and Bush years)

8. There's an important difference between borrowing from the future in order to invest in future productivity, and borrowing in order to consume today. Public and private debt is high by historic standards, but the real problem is our failure to invest those borrowings in our future productivity--in machinery and equipment, people and infrastructure--the unique assets of a nation within an increasingly global and technological economy. (In the late 19th century, this nation was far more indebted than now, as a proportion of its national product, but we the borrowings in canals, railroads, telegraph systems, and other means of becoming so much more productive by the early 20th century that we could pay off the debt with ease).

9. The Cold War is over, but a substantial portion of our economy is still fighting it rather than improving our capacities to be productive and to improve our health. Relative to our past, and relative to other nations, we continue to invest a big portion of our resources (talent, machinery, etc.) in defense. We must find ways to convert from a defense-technology-industrial base to a commercially-competitive one.

10. Not all Americans are sacrificing proportionately to their ability to sacrifice. The total tax burden (including Social Security) has increased on the middle and lower-middle class, while decreasing on those at the top. Fairness requires that everyone sacrifice in proportion to their capacity to do so.

What's good and strong about America

11. America is still blessed with (a) the best university system in the world, (b) the most productive workers in the world, and (c) the greatest natural resources in the world. We can and should build on these strengths.

12. Our small businesses continue to be among the most innovative in the world. They account for most of the new inventions, and new jobs. Public policies should encourage innovative small businesses.

13. Our diversity is a source of strength. Within our borders are represented almost all the ethnic groups in the world. This rich diversity can serve as a foundation stone for our world leadership economically and politically.

14. The Cold War is over, which enables us to focus on the challenge ahead. The "peace dividend" mustn't be squandered on consumption (public and private), but must be directed at public and private investment.

15. America has a new opportunity for global leadership in the new international economy. The global economy isn't a zero-sum game in which we win or they win. Everyone can win if all sides (a) invest in their future, (b) coordinate global fiscal and monetary policies, (c) open themselves to global trade and investment. In addition, the First World will need to invest in the Second and Third.

THE ECONOMIC CONFERENCE
BRIEFING BOOK

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December 1992

THE ECONOMIC CONFERENCE
BRIEFING BOOK

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DAY TWO

AGENDA

ECONOMIC CONFERENCE
-DETAILED AGENDA-

SUNDAY, DECEMBER 13, 1992

6:30-8:00 p.m.: WELCOMING RECEPTION, CLINTON BALLROOM, EXCELSIOR

MONDAY, DECEMBER 14, 1992

8:00 PRE-CONFERENCE BRIEFING, ROBINSON CENTER

8:40 Mickey Kantor: Participant Briefing

8:55 BC, AG and Economic Team Enter

ASSESSMENT: DOMESTIC ECONOMY

9:05: BC Opening Statement.

9:20: *Bob Solow*: Macro Overview

9:35: *John Sculley*: Competitiveness and Education

9:40: *Alan Blinder*: The Need For an "Investment In People" Agenda.

9:45: *Marian Wright Edelman*: Children in Poverty

9:50: Questions or comments by BC/AG

10:00: *Alicia Munnell*: Investing in Infrastructure

10:05: *Michael Porter*: Private Investment

10:10: Questions or comments by BC/AG

10:15: *John White*: The Debt..

10:20: *Stuart Altman*: The Economic Consequences of Rising Health Care Costs.

10:25: *Harold Poling*: Health Care Costs and Competitiveness.

10:30: Questions or comments by BC/AG

10:40: *Alan Patricof*: The Small Business and Entrepeneurial Sector.

10:45: Questions or comments by BC/AG

10:50: STRETCH BREAK

11:10: PANEL DISCUSSION

12:00: QUESTIONS AND COMMENTS FROM FLOOR

12:15: QUESTIONS FROM TV/RADIO AUDIENCE

12:25: BC Wrap Up of Assessment

12:30: BREAK FOR LUNCH--PROCEED TO EXCELSIOR

2:00: LUNCH ENDS--PROCEED BACK TO ROBINSON CENTER

ASSESSMENT: INTERNATIONAL ECONOMY

2:30: BC Opens Assessment

2:35: *Rudi Dornbusch*: Global Overview

2:45: *Jeff Garten*: E.C.

2:50: *Glen Fukushima*: Asia

2:55: *Larry Summers*: FSU and Eastern Europe

3:00: BC/AG Questions and Comments about earlier presentations

3:10: *Paula Stern*: Mexico and Latin America

3:15: *Robert Browne*: Africa

3:20: PANEL DISCUSSION

3:45: QUESTIONS AND COMMENTS FROM FLOOR

4:00: BREAK

WORKING SESSION I: LIFETIME LEARNING

A. Preparation for School

4:30: BC Opens Session

4:35: *Lisbeth Schorr*: Government's Role.

4:38: *Heather Weiss*: Parents' Role.

4:41: *Arnold Hiatt*: Private Sector Role.

4:44: PANEL DISCUSSION

5:15: QUESTIONS AND COMMENTS FROM FLOOR

5:30: END QUESTIONS FROM FLOOR

B. Preparation for Work

5:30: BC Opens Session

5:35: *Hillary Pennington*: High School Path.

5:38: *Johnnetta Cole*: Financing the College Path.

5:41: *Paul Allaire*: Needs of the New Workplace.

5:44: PANEL DISCUSSION

6:05: QUESTIONS AND COMMENTS FROM FLOOR

6:15: QUESTIONS FROM RADIO AND TV AUDIENCE

6:30: BREAK FOR DINNER

7:30: DINNER: ART CENTER

TUESDAY, DECEMBER 15, 1992

8:00 CONFERENCE BRIEFING: ROBINSON CENTER

WORKING SESSION II: INVESTMENT FOR SHORT TERM GROWTH

8:30: BC Opens Session

8:40: *James Tobin, Allen Sinai* and *Charles McMillion*: Analysis of Short Term Forecast.

8:55: PANEL DISCUSSION

9:30: QUESTIONS AND COMMENTS FROM FLOOR

9:45: STRETCH BREAK (SWITCH PANELISTS)

WORKING SESSION III: INVESTMENT FOR LONG TERM GROWTH AND DEFICIT REDUCTION

10:00: BC Opens Session

10:05: *Felix Rohatyn*: Growth and Deficit Reduction

10:10: *Henry Aaron*: Cost of Deficits

10:13: *Isabel Sawhill*: Balancing the Two Deficits

10:16: *Bill Gray*: Impact of Cuts

10:19: PANEL DISCUSSION

11:00: QUESTIONS AND COMMENTS FROM FLOOR

11:15: QUESTIONS FROM RADIO AND TV VIEWERS

11:30: BREAK: SANDWICHES AVAILABLE

WORKING SESSION IV: ENVIRONMENT, NEW TECHNOLOGIES, AND ECONOMIC GROWTH

12:15: BC Opens Session, Introduces AG

12:20: AG Begins Discussion

12:25: *John Bryson*: False Choice -- business perspective.

12:28: *Frank Popoff*: False Choice -- business perspective.

12:31: *Lynn Williams*: False Choice -- labor perspective.

12:34: *Craig Fields*: Industries of the Future

12:37: PANEL DISCUSSION

1:30: QUESTIONS AND COMMENTS FROM FLOOR

1:45: STRETCH BREAK

WORKING SESSION V: THE CONNECTION BETWEEN REFORMING GOVERNMENT AND ECONOMIC GROWTH

2:00: BC Opens Session

2:05: *David Osborne*: Reinventing Government

2:10: *Doug Ross*: Reinventing Government

2:15 *Ernesto Cortes*: Economic Empowerment and Government Reform

2:20: PANEL DISCUSSION

3:00: QUESTIONS AND COMMENTS FROM FLOOR

3:15: BC CLOSES CONFERENCE

3:30: ADJOURN

4:00: CLOSING PRESS CONFERENCE: OLD STATEHOUSE

DOMESTIC ECONOMY:

MACRO - OVERVIEW

President-elect Bill Clinton

Vice President-elect Al Gore, Jr.	Mariam Wright Edelman *
Joan Claybrook	Robert Allen
Thomas Donahue	Kathryn Thompson
Calvin King	**Sec. of the Treasury Lloyd Bentsen**
Anne Markusen	Hugh McColl
Sec. of Labor Robert Reich	Marion Sandler
Jessica Tuckman Mathews	**Chair of CEA Laura Tyson**
John Sculley *	Frank Brooks
Andrew Shapiro	Alan Patricof *
Delano Lewis	Lacene Orvis
David Glass	Harold "Red" Poling *
Director of OMB Leon Panetta	**Economic Policy Advisor Robert Rubin**
Beth Renge	Robert Hurst
Alicia Munnell *	Betsy Henley-Cohn
Roy Vagelos	Robert Solow *
Sec. of Commerce Ron Brown	

Podium

* = Presenter

Other Presenters

1. Stuart Altman *
2. Alan Blinder *
3. Alan Patricof *
4. Michael Porter *

Donna Shalala	Carol Browner	Roger Altman	Alice Rivlin	Mack McClarty	HRC	Mickey Kantor	Presenter 1	Presenter 2	Presenter 3	Presenter 4
Anne Cohn Donnelly	Henry Cisneros	Doris Matsui	Madeleine Kunin	Vernon Jordan	Warren Christopher	John Emerson	Erskine Bowles	Mary Leslie	Team 32	Team 32

Assessment Panel

Name	Company	Category	St	Phone #
Mr. Robert Allen	AT&T	Telecommunicati	NJ	908-221-2000
* Mr. Stuart Altman ([illegible])	Brandeis University	Academia	MA	
* Mr. Alan Blinder ([illegible])	Princeton University	Academia	NJ	609-258-4000
Mr. Frank Brooks	Brooks Sausage Co.	Small Business	WI	414-947-0320
Ms. Joan Claybrook	Public Citizen	Non Profit	DC	202-833-3000
Mr. Thomas Donahue	AFL-CIO	Labor	DC	202-637-5221
* Ms. Marian Wright Edelman	Children's Defense	Non Profit	DC	202-628-8787
Mr. David Glass	Wal-Mart	Retail	AR	501-273-4000
Ms. Betsy Henley-Cohn	Joseph Cohn and	R/E,	CT	203-772-2420
Mr. Robert Hurst	Michigan Bell	Telecommunicati	MI	313-223-7173
Mr. Calvin King	Ark. Land and Farm	Agribusiness	AR	501-734-1140
Mr. Delano Lewis	C&P Telephone Co.	Telecommunicati	DC	202-392-3701
Ms. Anne Markusen	Rutgers University	Academia	NJ	908 932 4587
Ms. Jessica Tuchman	World Resources	Environment	DC	202-662-2501
Mr. Hugh L. McColl, Jr.	NationsBank	Commercial	NC	704-386-5663
* Ms. Alicia Munnell	Federal Reserve Bank	Government	MA	617-973-3385
Ms. Lacene Orvis	Caulkins Indiantown	Agribusiness	FL	407-597-2126
* Mr. Alan J. Patricof	Patricof & Co.	Small Business	NY	212-753-6300
* Mr. Harold A. Poling	Ford Motor Company	Auto	MI	313-322-7800
* Dr. Michael Porter ([illegible])	Harvard Business	Communications	MA	617-495-6309
Ms. Beth Renge	Renge Securities &	Investment	CA	415-955-2627
Ms. Marion O. Sandler	World Savings	Commercial	CA	510-446-6000
* Mr. John Sculley	Apple Computer, Inc.	High Tech	CA	408-996-1010
Mr. Andrew Shapiro	Yale Law School	Student	CT	203-776-8518
* Mr. Robert Solow	Harvard University	Staff		617-253-5268
Ms. Kathryn Thompson	Kathryn Thompson	R/E,	CA	714-380-1488/0112
Dr. Roy Vagelos	Merck & Co., Inc.	Healthcare	NJ	908-594-6775
* Mr. John White ([illegible])	Center for Business	Chemical	MA	716-383-1886

* Presenter

ASSESSMENT: DOMESTIC ECONOMY

Presenters:
Stuart Altman
Alan Blinder
Marian Wright Edelman
Alicia Munnell
Harold Poling
Michael Porter
John Sculley
Robert Solow
John White

Panelists:

Allen, Robert E. Basking Ridge, NJ
Chairman and Chief Executive Officer-AT&T
Has served with Bell Telephone system since 1958.
Boards: Bristol-Myers Squibb Company; PepsiCo; Federal Reserve Bank of NY, Wabash College.
Member: Business Roundtable, Business Council, US-Japan Business Council.

Primary concern: long-term deficit reduction.

Brooks, Frank B. Kenosha, WI
President and CEO, Brooks Sausage Company, Inc.
Former President and CEO, Chicago Economic Development Corporation
Recipient, 1980 Finance Achievement Award, Black Enterprise Magazine

Primary concern: equity investments for small businesses.

Claybrook, Joan B. Washington, DC
President, Public Citizen (since 1982). Public interest advocacy group focusing on public health and safety, civil rights and liberties, clean and safe energy sources, campaign finance reform, citizen participation in government. Founded by Ralph Nader.
Former Administrator, National Highway Traffic Safety Administration (1977-81)
Books: *Retreat from Safety: Reagan's Attack on America's Health (1984); Freedom from Harm: The Civilizing Influence of Health, Safety and Environmental Regulations (1986)*

Panel comments will focus on consumer perspective. Key interests for this panel: transportation; infrastructure; investment subsidies.

Donahue, Thomas R. Washington, D.C.
Secretary-Treasurer of AFL-CIO (since 1979)
Chairman of the U.S. Special Trade Representative's Labor Advisory Committee
Former Assistant Secretary of Labor for Labor-Management Relations
Director: Muscular Dystrophy Association; Urban League; African-American Institute
Chairman: USTR Labor Advisory Committee

Glass, David Bentonville, AR
President and CEO, Wal-Mart Stores, Inc.
Leader of America's No. 1 retailer
1986 and 1991 Retailer of the Year.

Primary concern: economic stimulation versus potential inflation.

Henley-Cohn, Betsy New Haven, CT
Chairman, Ansonia-Derby Water Coman
Chairman, Joseph Cohn & Sons, Inc., Atlantic Floor Covering, Inc.
Member, Committee of 200 (top business women in the U.S.)
Chairman 9th Square Tax District, City of New Haven

Hurst, Robert L. Detroit, MI
President, Michigan Bell Telephone (since June 1992)
Member, Economic Club of Detroit; Board and Strategic Planning Committee, Detroit Urban League; Chair, Henry Ford Hospital Board of Trustees.

Primary concern: "When will planning begin for the National Broadband Communications Infrastructure? Will the private sector be a part of the planning and implementation process?"

King, Calvin Brinkley, AR
President, Arkansas Land and Farm Development

Primary concern: Small family farmers, minority farmers and land owners, USDA policy, access to land for beginning farmers, involvement of non-profit organizations in loan servicing for agriculture.

Lewis, Delano E. Potomac, MD
President and CEO, C&P Telephone Company
Served in Peace Corps and on the Hill before joining C&P in 1973.
Former Board Member: Catholic University; United Negro College Fund.

Primary concern: Tax incentives for business (large/small); Investment tax credits - infrastructure support; Regulatory and legal issues re. telecommunications.

Markusen, Ann R New Brunswick, NJ
Director, Project on Regional and Industrial Economics at Rutgers University
Professor of Urban Planning and Policy Development
Books: *Dismantling the Cold War Economy (1992), The Rise of the Gunbelt (1991); Regions: the Economics and Politics of Territory (1987)*

Primary concern: trade and industrial policy,; problems involved with defense conversion.

Mathews, Ms. Jessica Tuchman		Washington, D.C.
Vice President, World Resources Institute.
Columnist, The Washington Post.
Served on AAAS, Congressional Office of Technology Assessment and National Academy of Sciences.
Co-founder and Member, Executive Committee, Surface Transportation Policy Project.

Primary concern: She will underscore her conviction that "there are win-win opportunities in taxing energy waste".

McColl, Jr., Hugh L.		Charlotte, NC
President and CEO of Nations Bank Company.
Board member of several education committees and strong supporter of education at all levels.

Primary concerns: Financial regulation, tax policy.

Orvis, Lacene E.		Indiantown, FL
CEO of Caulkins Indiantown Citrus Co. and Via Tropical Fruits, Inc.
Agricultural Committee Chair of Florida Council of 100

Primary concerns: Direction of NAFTA, GATT, other trade related programs.

Patricof, Alan J.		New York, NY
Patricof & Co. Ventures, Inc.
Has financed over 200 companies over last two decades and today manages over $1.5 billion on behalf of over 100 institutions.
Chairman of Entrepreneurs for Clinton/Gore
Contributed to position paper on small business/entrepreneurship

Primary concerns: what specific steps can be taken for job creation in the short term.

Renge, Beth San Francisco, CA
Trustee and Chair of The Legacy Fund for the Japanese American Citizens League
Board Member of Japan Society of Northern CA. and California Leadership
Former Chapter Treasurer of Japanese American Citizens League

Primary concerns: Rebuilding infrastructure.

Sandler, Marion O.
President and C.E.O., Golden West Financial Corporation and World S&L Association
(Golden West is the nation's third largest thrift)
Appointed to the Glass Ceiling Commission in 1992.

Primary concerns: health care costs, defense conversion. She wants to capitalize on "honeymoon period" with change.

Shapiro, Andrew L. New York
Author of *We're Number One!* , defending America's high status compared to other nations
Media coverage includes several national television shows, magazines and newspapers
Graduate of Brown University, planning to attend Yale Law School this fall
Presently working as staff member for The Nation and school teacher

Primary concerns: (1) How can the Clinton Administration truly meet the needs of the disadvantaged poor; (2) What are the President-elect's plans to address the economic concerns of young people?

Thompson, Kathryn G. Aliso Viejo, CA
Chairman and C.E.O., Kathryn G. Thompson Development Company (real estate, construction, development and management of residential,commercial and industrial property in Southern California)
Member, Advisory Committee on Construction Safety and Health, Occupational Safety Health Administration
1988 RNC Delegate

Primary concerns: bank lending regulation

Vagelos, Dr. P. Roy Rahway, NJ
Chairman, President and CEO, Merck & Co., Inc. (since 1985)
Former cellular physiologist and biochemist, National Heart Institute
Author of more than 100 scientific papers.
Member, President's Commission on Environmental Quality; Advisory Committee on Trade Policy and Negotiations.
Trustee, The Rockefeller University; University of Pennsylvania; Danforth Foundation.

Primary concerns: high tech industry and competitiveness.

DOMESTIC ASSESSMENT I:
THE MACROECONOMIC OVERVIEW

EVENT:
Listen to overview of the macroeconomic situation on the state of the economy (10 minutes) after which BC and AG will ask a few questions.

Presenter: ***Dr. Robert Solow*** is the 1987 winner of the Nobel prize in economics. He has been a professor at the Massachusetts Institute of Technology since 1950, specializing in theories of capital and economic growth. Under Kennedy, Dr. Solow served as Chief Economist for the Council of Economic Advisors. He was one of the original six Nobel laureates who endorsed Putting People First when it was first released.

GOALS:

1. A major goal of the Clinton-Gore economic agenda is to get our economy moving again to ensure sustained job growth. At the heart of the Clinton-Gore economic agenda, however, are actions to spur the long-term investments we need to increase the productivity of our people, and to increase the American standard of living.

2. This presentation explains why a long-term investment agenda is needed. It shows that U.S. productivity growth has lagged, and that sluggish productivity has had a real impact on the standard of living of the American family.

3. Demonstrate that the U.S. economy is burdened with significant structural problems, most particularly the twin deficits of the budget and weak public/private investment. These problems were created over a long time, and they will take a long time to solve.

ATTACHED:

- Summary of Solow Assessment
- Additional points to note and suggested questions for Solow
- Background:
  - Productivity, wages and family incomes
  - U.S. investment trends.
- Charts to be used by Solow
- Biographies on roundtable participants

SUMMARY OF ASSESSMENT BY ROBERT SOLOW: Professor Solow will use four or five charts to assess both the state of our short-term and long-term economic situation.

Short-Term Assessment:

Solow will make two points to underscore how weak this period is compared to previous recoveries:

- The economy has grown at only a fraction of the growth of previous recoveries.

- He will also use a chart -- "The Jobs Recession" -- to compare how weak payroll employment gain has been after the most recent recession compared to the average gain after the previous 7 recessions. He will then show that recent trends in GDP growth are not great enough at this point to bring back sustainable job growth.

Long-Term Assessment of Stagnating Standards of Living.

Solow will explain what our failure in productivity gains has meant to average American families. The American family would be making over $12,000 more per year if productivity had remained at the 1948-73 level for the last two decades. Solow may also point out that while the United States is still first in productivity, our rate of productivity growth has been well behind our competitors over the last four years. Finally, Solow will show that only the top 1% experienced dramatic income growth in the 1980s.

ADDITION POINTS/QUESTIONS TO NOTE:

1. **International Comparison**

American families know that their living standards have stopped rising. They must work longer hours, rely on two paychecks instead of just one, spend less time at home -- just to stay even with inflation. Did incomes in our major competitors like Germany and Japan also stagnate? Are they likely to surpass us in another ten years -- a very short span of time in the long sweep of history -- if we do nothing?

2. **Productivity Growth:**

Internationally, among 10 advanced industrial nations, the U.S. was 9th in productivity growth from 1980 to 1990. Japan's productivity growth rate has been three times as fast as the U.S. [OECD Quarterly National Accounts, 1992]. Is this because Japan is still at an earlier stage of its economic development than the United States, or does this reflect that we are truly lagging behind?

3. **What type of jobs?**

We know that during the last four years there was no private sector job growth. During the 1980s, there was substantial job growth -- as much as 17 million jobs -- while income growth was poor. Prior to the 1980s, have we ever experienced a period of significant job growth accompanied by little or no improvement in our standard of living?

BACKGROUND:

I. SAGGING PRODUCTIVITY/WAGES/FAMILY INCOMES

Weak productivity gains have slowed real wage growth, causing family incomes to stagnate.

1. <u>Productivity Growth has Slowed</u>: Service sector productivity is notoriously hard to measure and grows slowly. Manufacturing productivity grows faster because manufacturing processes are more amenable to the application of capital. And, for most of the postwar period, rising manufacturing productivity kept overall U.S. productivity moving ahead briskly, as noted below. Weakening investment and the erosion of the U.S. manufacturing sector over the last two decades has changed that. While manufacturing productivity has grown in recent years, the declining share of U.S. economic activity accounted for by that key sector has caused overall U.S. productivity growth to flatten out. (The share of GDP represented by the manufacturing sector has fallen to 19 percent now compared to 23 percent in 1980.) This table is from the <u>American Council on Capital Formation</u>.

<u>U.S. Productivity and Real Hourly Compensation Growth</u>
(Average Annual Rate)

	Productivity	Hourly Compensation
1959-1973	2.8 percent	2.9 percent
1974-1990	0.9 percent	0.7 percent

2. <u>Wage Growth has Slumped as Productivity Slowed</u>: As noted in the above table, hourly labor compensation, which includes benefits, closely tracks productivity gains - exactly as economic theory predicts. Thus, since productivity went flat two decades ago, real compensation has essentially gone flat for all workers too. The tiny 0.7 percent annual compensation gain since 1974 is an average figure. It disguises trends which have seen wage gains diverge depending upon skill level - with the wages of less skilled blue-collar workers essentially stagnating since 1973, and compensation to workers with more skills or education rising a bit faster. Even so, almost all families <u>feel</u> poorer. The cost of major middle-class purchases such as a college education for one's children, a house, or medical insurance have risen at roughly double the overall pace of inflation. That is why most families believe they are caught in a "middle-class squeeze."

3. Family Incomes Have Fallen in Recent Years: Real compensation tracks productivity closely, and so does real median family incomes. Family incomes grew handsomely until 1973 along with productivity and wages. Since then, real family incomes have grown only by tiny amounts annually as noted in the following table. Not surprisingly, the recession since 1989 has caused real family incomes to shrink. This table is based on Census Bureau data:

Median Real Family Income Growth (Annual Average Growth)

1947-1967:	2.8 percent
1967-1973:	2.6 percent
1973-1979:	0.6 percent
1979-1989:	0.4 percent
1989-1990:	-2.0 percent

II. INVESTMENT TRENDS

Economists universally agree that the most potent contributor to productivity growth is investment. Unfortunately, America has failed to make these long-term investments necessary for productivity growth. Getting this point across is one of the main goals of this session:

1. International Comparison

After adjusting for inflation, real U.S. domestic investment in plants and equipment has not increased significantly over the last two decades.

Real Rise in Plant and Equipment Investment, 1972-1991

France:	53.1 percent
U.S.:	60.5
Italy:	68.0
U.K.:	68.9
Germany:	73.3
Canada:	164.4
Japan:	209.9

Source: Council on Competitiveness

2. Domestic Investment Trend

U.S. investment activity has also lagged in the 1980's. The share of U.S. GDP being devoted to plant and equipment investment fell one quarter (net, inflation adjusted).

Source: Commerce Department

3. **Investment Grew Slowly Even During Eighties Recovery**

During the eighties recovery, the most potent type of investment, in equipment, grew only 5.7 percent annually. This growth rate was down over one-third from the 8.9 percent annual real growth rates in investment during the two previous recoveries (1970-73 and 1975-80). .

Source: Commerce Department

4. **U.S. Failed to Invest Adequately in Civilian R&D**

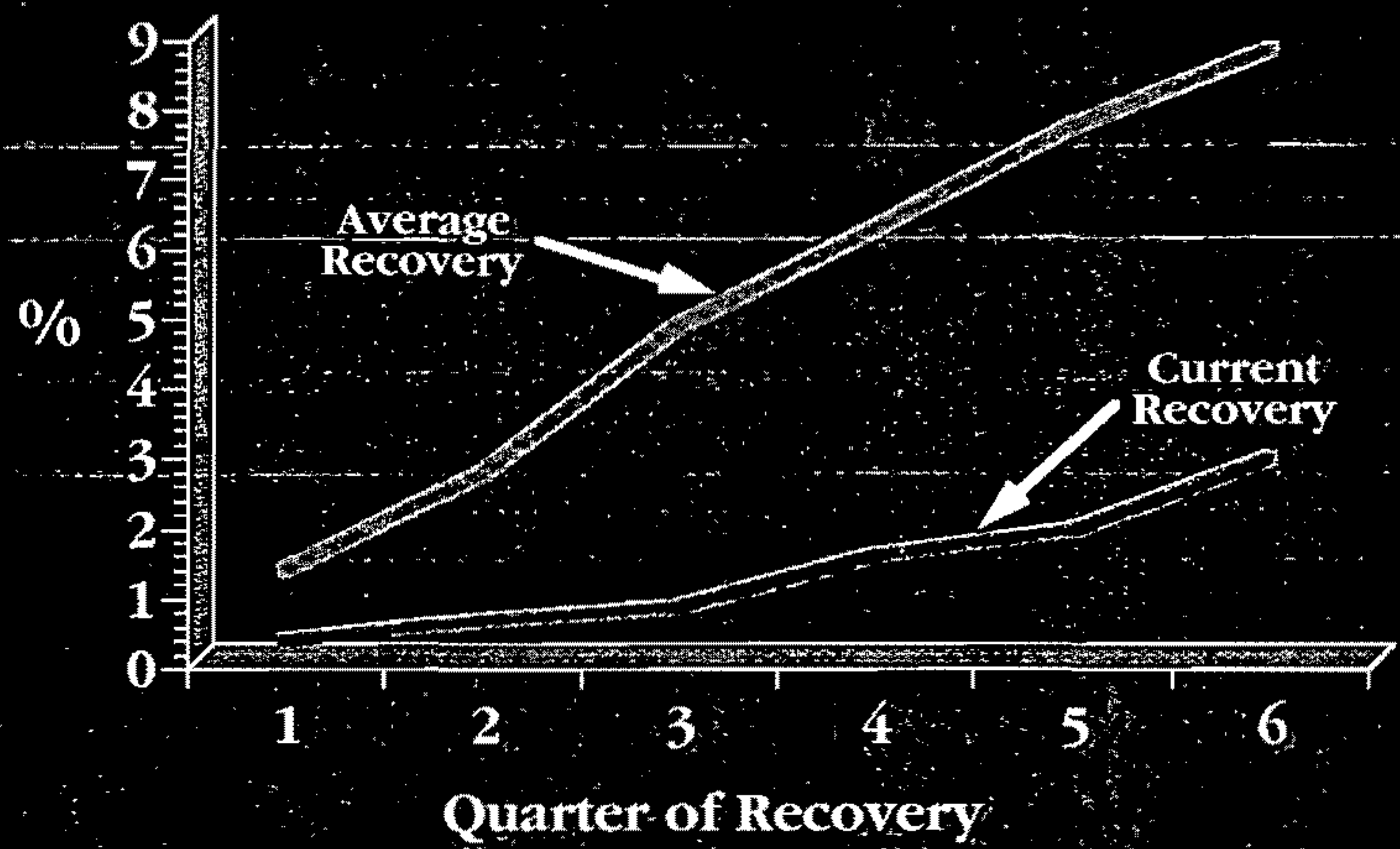
Civilian R&D is one of the most important contributors to productivity gains. Since 1970, the U.S. has been devoting a smaller share of GDP to civilian R&D spending than our competitors.

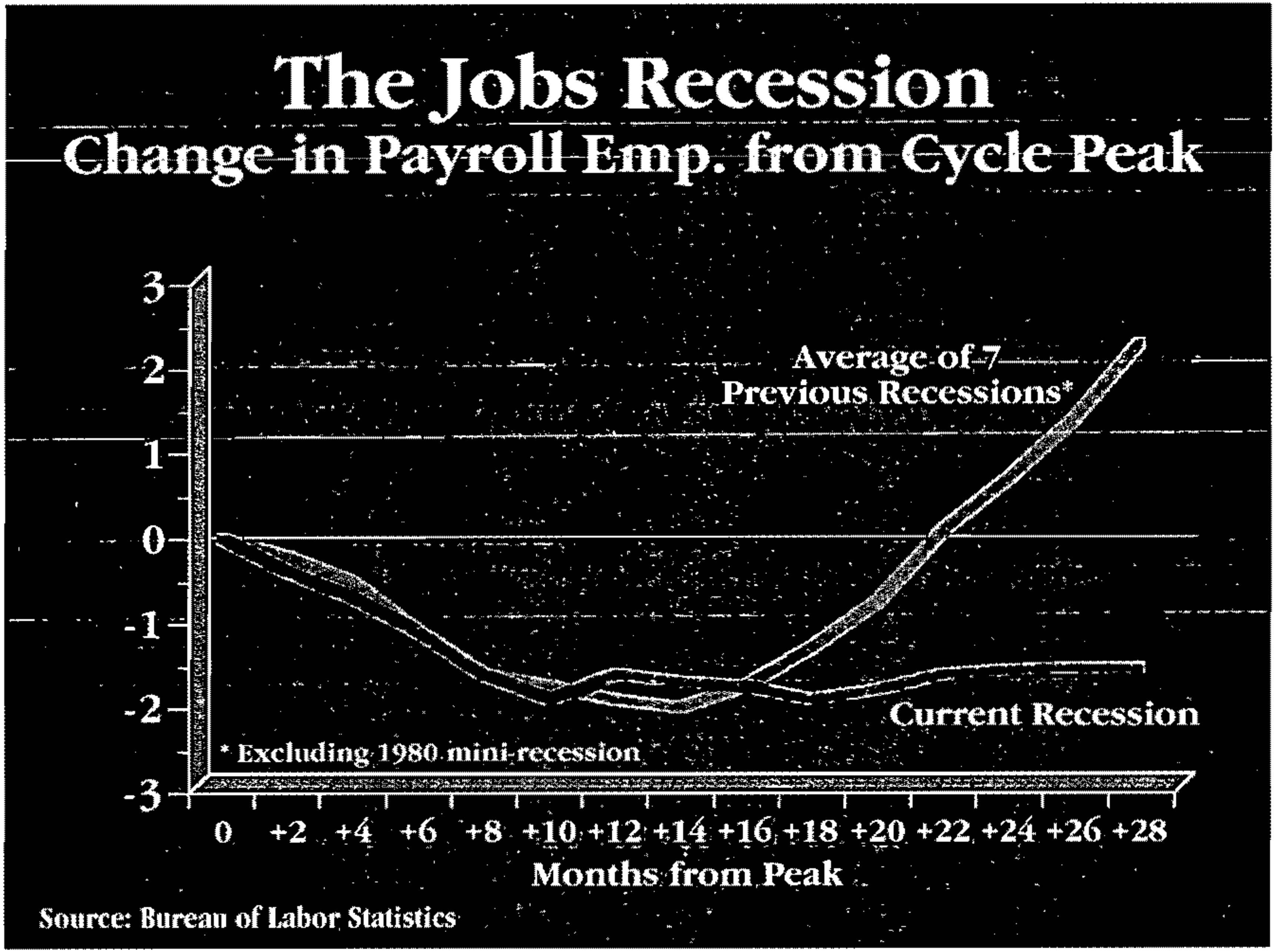
Share of GDP Devoted to Civilian R&D (1989)

Japan:	3.0 percent
Germany:	2.8
U.S.:	1.9

Source: Council on Competitiveness

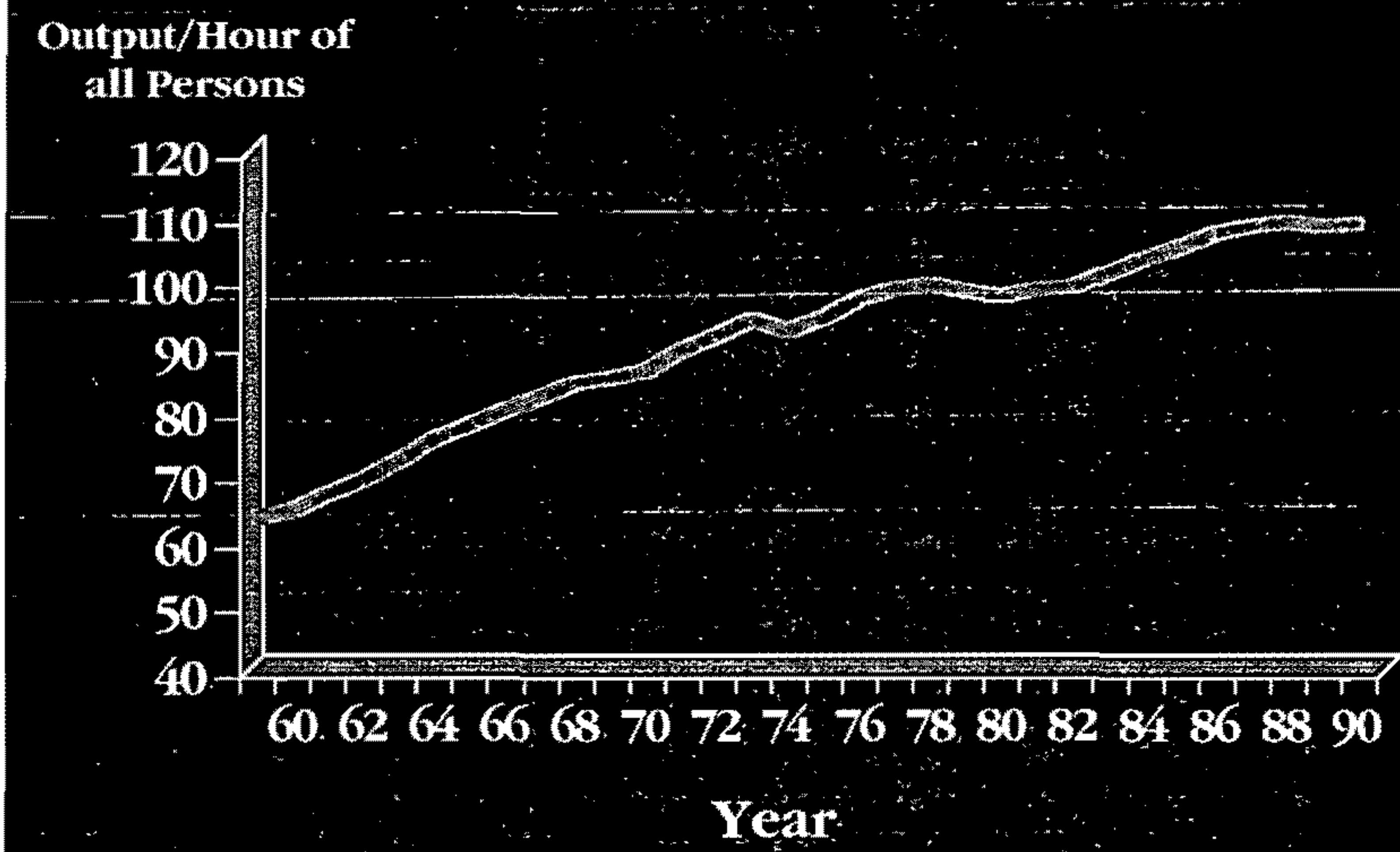
GDP Growth in Current and Average Recovery



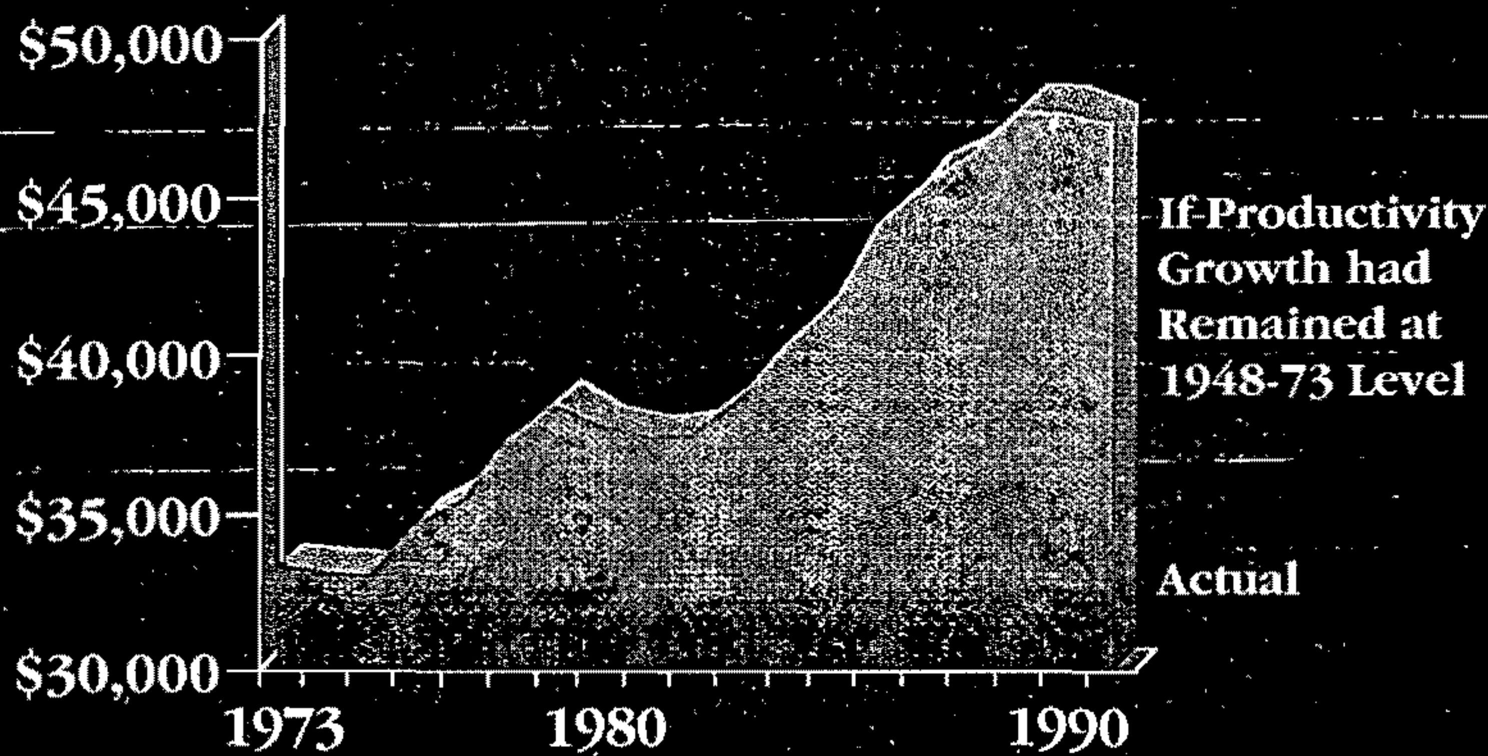


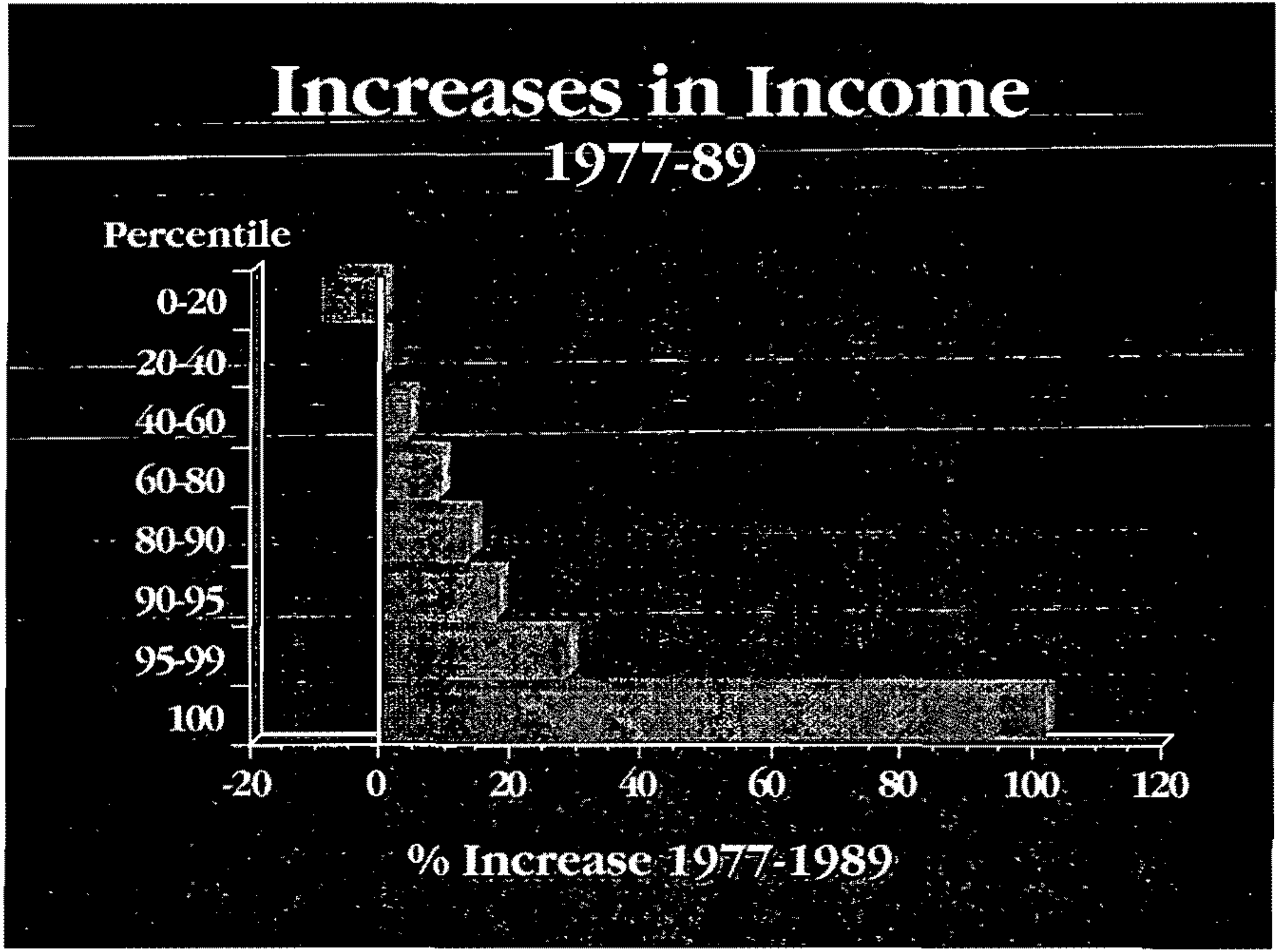
The Jobs Recession
Change in Payroll Emp. from Cycle Peak
3
2
1
0
-1
-2
-3
Average of 7
Previous Recessions*
Current Recession
* Excluding 1980 mini-recession
0 +2 +4 +6 +8 +10 +12 +14 +16 +18 +20 +22 +24 +26 +28
Months from Peak
Source: Bureau of Labor Statistics

U. S. Productivity



Family Incomes: What Could Have Been




Increases in Income
1977-89
Percentile
0-20
20-40
40-60
60-80
80-90
90-95
95-99
100
-20
0
20
40
60
80
100
120
% Increase 1977-1989

DOMESTIC ASSESSMENT II.

INVESTING in PEOPLE

DOMESTIC ASSESSMENT II: INVESTING IN PEOPLE

EVENT:
Assessments of U.S. investment in people, especially as it relates to preparing our children and workforce to compete in a global economy.

The assessment is divided into three sections which will each last five minutes:

1.	Competitiveness and Education:	Presented by **John Sculley**; Chairman and CEO of Apple Computer.
2.	Skills Gap and Structural Unemployment:	Presented by **Alan Blinder**, Ph.D; Professor of Economics at Princeton University
3.	Children in Poverty:	Presented by **Marion Wright Edelman**; President of the Children's Defense Fund.

GOALS:
- Develop a strong statistical case for why we need to invest more in people.
- Show the high rates of return of investments in people.
- Demonstrate that the US currently underinvests in people and conclude that investing in people is beneficial and necessary for US competitiveness.

ATTACHED:
- "Competitiveness and education assessment": summary of John Sculley presentation
- Additional background on competitiveness and education
- "The economics of investing in people": summary of Alan Blinder presentation
- Additional background on the economics of "Putting People First"
- "Children in poverty assessment": summary of Marian Wright Edelman presentation
- Additional background on children in poverty

For additional information, see briefing for Working Session I.

SUMMARY OF COMPETITIVENESS AND EDUCATION ASSESSMENT:

John Sculley will present 3-5 charts to make the following points:

- We are at a major turning point in the world economy as we shift from mass production and mass consumption to customization of goods and services and the decentralization of work. Success in this new, global economy lies in teaching the workforce math, science and critical thinking skills.

- The U.S. education system still concentrates on educating the students who actually graduate from college. Most other industrialized countries have an alternative path for the non-college bound, including vocational study and school-to-work transition programs.

- If we do not offer an education system which addresses the needs of all our students, and not just the elite who graduate from college, we will condemn our children to low skilled manual work that pays low wages. We cannot leave our children unprepared to participate as high skill workers in a global economy.

Additional Points To Make:

- We always hear about the performance of American students being well below other industrialized countries. For example, the dropout rate in South Korea is 10 percent, and virtually all of the 90 percent of South Korean students who graduate have mastered basic skills. The United States does not come close in either category. That means that our future workers are less well educated than workers who earn less than one-tenth what our workers earn. Have we priced ourselves out of the world labor market? (Ray Marshall and Marc Tucker, Thinking For a Living, 1992, p. 65)

- The Commission on the Skills of the American Workforce predicts that more than 70 percent of the jobs in America will not require a college education by the year 2000. What does that mean for the way we educate our young people?

Other Background:

- In a commonly cited study by the International Association for the Evaluation of Education Achievement, the United States ranked next-to-last in international math (algebra) achievement test scores among 15 countries. Belgium and New Zealand were among the countries that ranked higher. ("International Mathematics and Science Assessments: What Have We Learned?, National Center For Education Statistics, US Dept. of Education, January 1992)

SUMMARY OF THE ECONOMICS OF INVESTING IN PEOPLE ASSESSMENT:

Alan Blinder will present three charts to make the following points:

- During the last twelve years productivity has remained relatively stagnant and real wages have fallen significantly. These trends makes the case for a new approach -- an investment in people strategy.

- Rising wage inequality and an increased skills gap are driven by the increased internationalization of the U. S. economy and changes in the work place driven by the computer revolution. Increased automation has meant that good paying, unskilled and semi-skilled jobs have become scarce. This increased knowledge content of goods and services has put a large labor market premium on those able to recognize and solve problems. Thus, it is not surprising that educational wage differentials expanded sharply especially for young workers, during the 1980s. The gap in earnings between young college and high school graduates doubled in the 1980s. What you earn increasingly depends on what you learn.

- The real money incomes of the bottom fortieth percent of American families in 1989 were no higher than those of the analogous 40 percent of families a decade earlier. The real money incomes of the upper twenty percent of families in 1989 were almost 20 percent higher than those of the analogous families in 1979.

<u>Additional Points To Make</u>:

- In talking about a skills gap, we know that we need better-trained workers, but we also know that many employers are reluctant to invest in worker training because of the high mobility of the American workforce. What can we do to address this problem?

- We've heard a lot about this skills gap, but only 15 percent of employers report difficulty finding workers with the appropriate occupational skills. Some say that the reason that number is so low is that we have been slow in moving to the high-performance workplace. Do you think that's the case, or is there another reason for the apparent difference in opinion between someone like you, who is looking at this from a more academic perspective, and the business perspective?

- Today almost one of every five people who works full-time does not earn enough to support his or her family above the poverty line. The fraction of workers working full-time and making low wages (those that would be insufficient to raise a family of four above the poverty line) has increased for all workers and especially for young workers. I believe we need to increase the Earned Income Tax Credit for working families, but what else can we do to support parents, who are working 40 hours a week but still make less than the poverty line?

<u>Other Background</u>:

- Family income growth has been sluggish and unequal since the early 1970s. The economic expansion of the 1980s failed to benefit a substantial fraction of American households by enough to offset the losses incurred during the recession of the early 1980s. These families have fallen even further behind in the recent recession.

CHILDREN IN POVERTY ASSESSMENT:
Marian Wright Edelman will present three charts to make the following points:

- Young families are in trouble because of a devastating combination of profound changes in the American economy, government's inadequate response to families in trouble, and changes in the composition of young families themselves.

- 20.4% of American children live below the poverty line in spite of the fact that the U.S. is one of the most powerful and wealthiest economies in the world.

- The rate of children in poverty in the United States is more than twice that in Japan or any leading industrial country in Europe. (Marshall and Tucker, p. 65)

- America's children are not being adequately prepared to compete economically in an increasingly competitive world economy. We need to make a commitment that no child is left behind--all children must be prepared to start school and must be given a "healthy start". A number of investments that start our children off on the right foot in life have been proven to work and to save public dollars.

Additional Points To Make:

- Many of these programs like Head Start and WIC are becoming integrated with child-care programs. How can we better coordinate services in order to best serve our children?

- You showed that chart which indicates that every dollar the government spends on Head Start saves us at least $3 down the road. Now it's my understanding that the evaluation of the Perry Preschool Project in Michigan, which is considered to be the best study on this subject, says that there is a $6 return on every $1 invested. What are the factors that influence how high the rate of return is for Head Start-type programs? Does it largely depend on how many years the child is in the program?

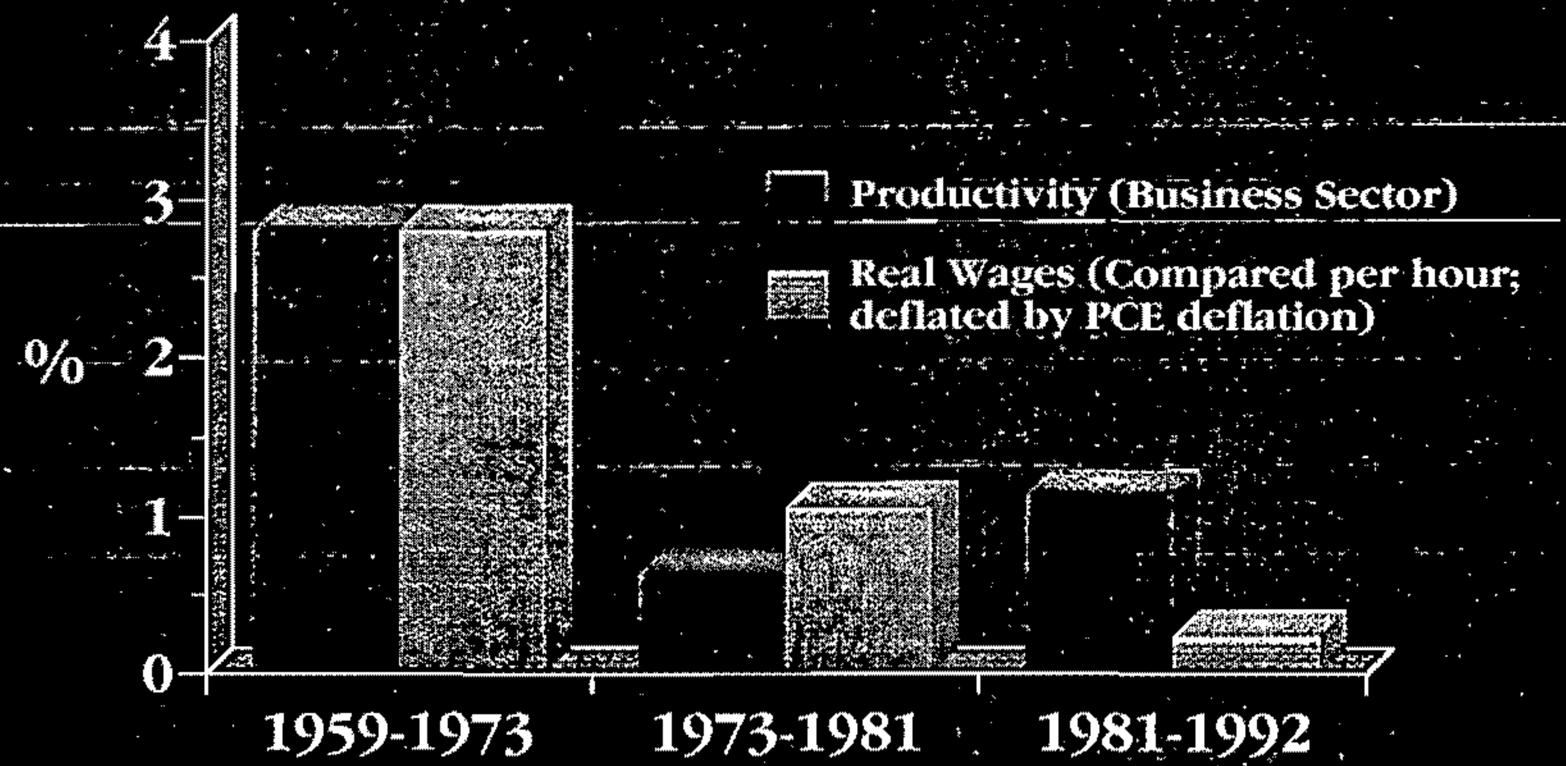
Other Background:

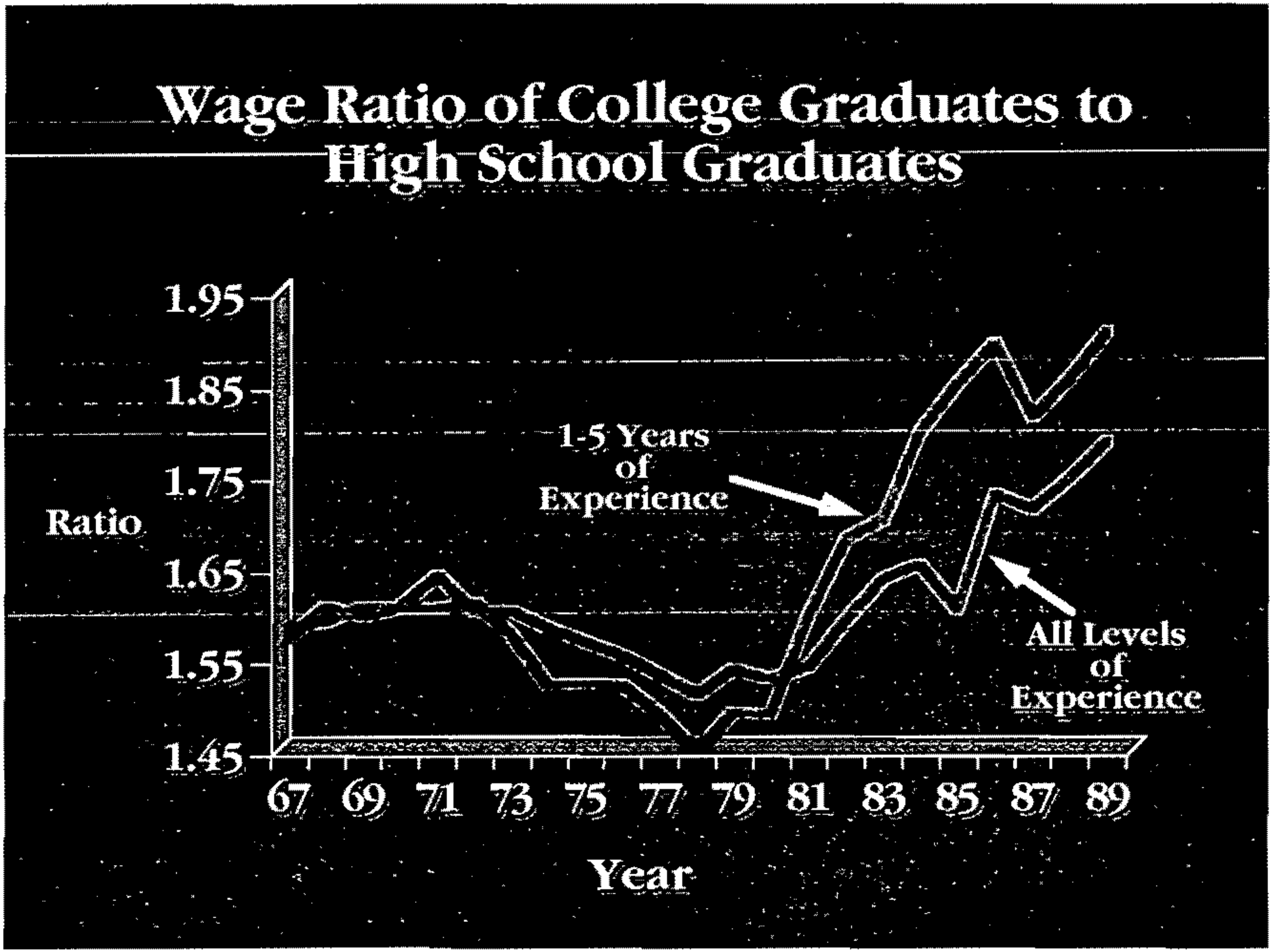
- More than one in every five children,(more than 14 million) are growing up poor. One in four children is raised by just one parent. Half a million a year are born to teenage girls who are ill-prepared to accept the responsibility of motherhood. Furthermore, the child poverty rate has been increasing steadily over time; the child poverty rate has been higher in every year since 1980 than in any previous year since 1965.

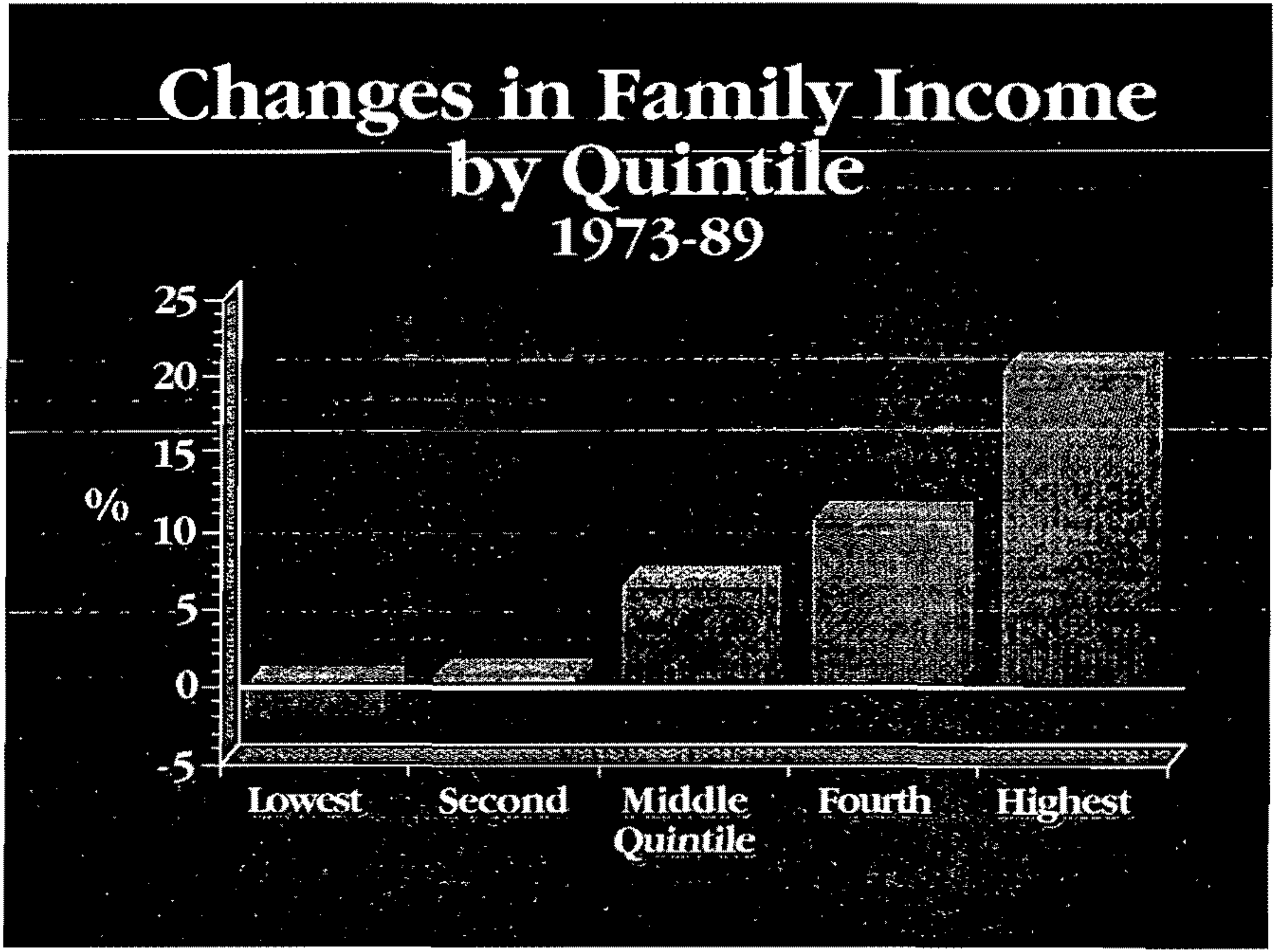
- The American infant mortality rate is scandalously high relative to those of other advanced industrial nations. Many American children and mothers receive inadequate medical care and live in deprived material conditions.

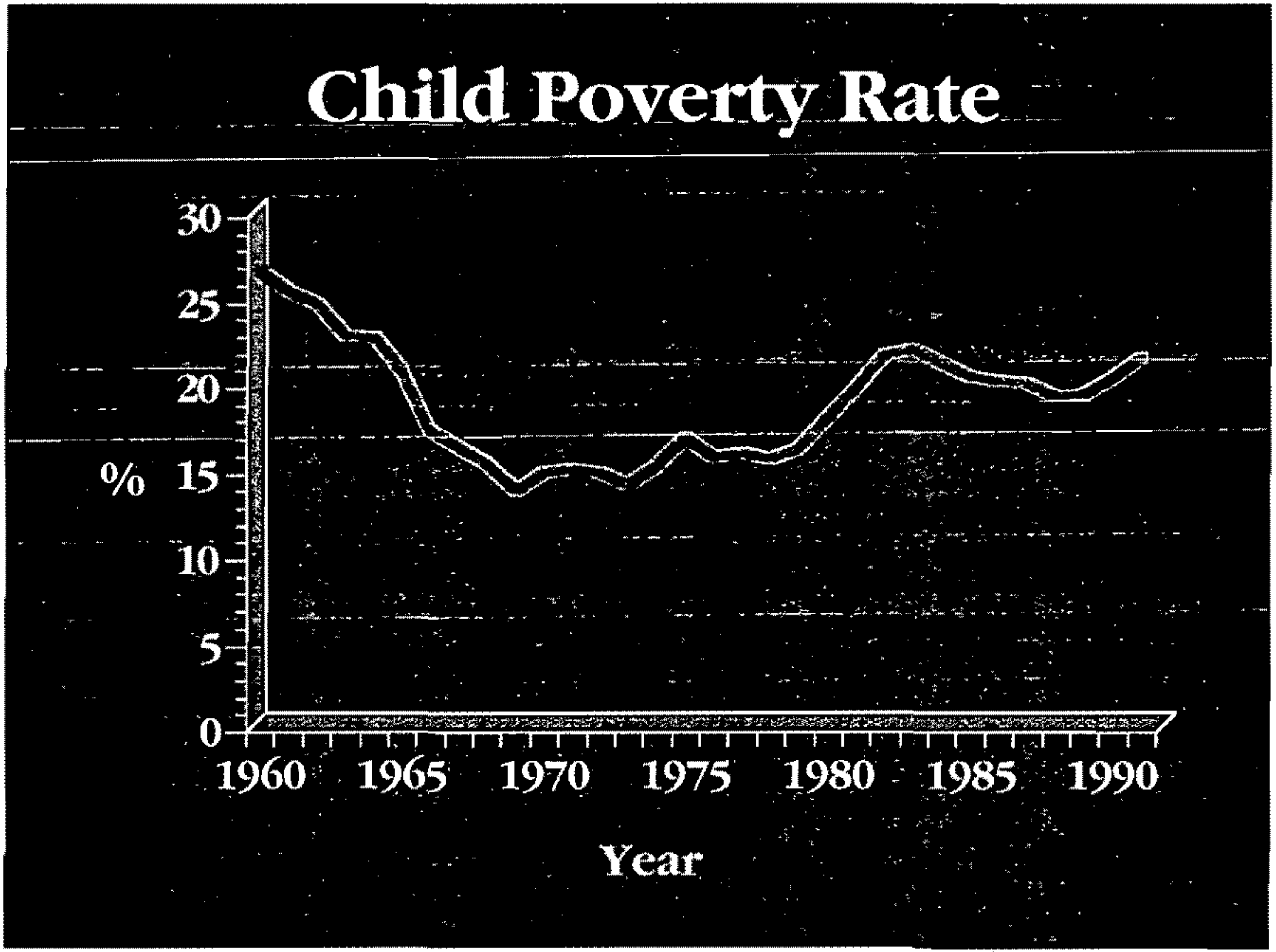
- Every dollar on immunizations saves us $10, and every dollar on WIC saves $3.

Growth Rates of Productivity and Real Wages



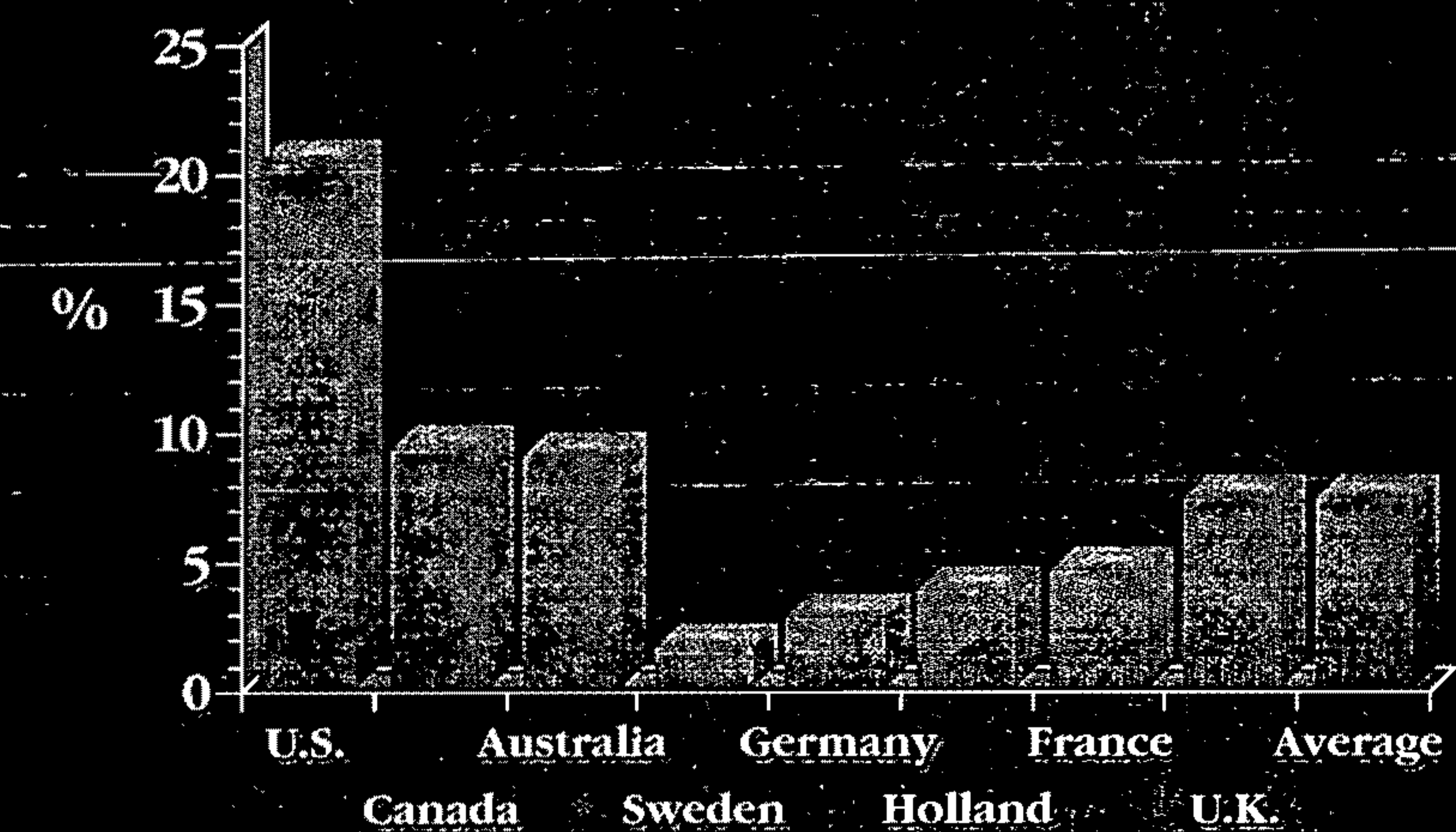

Wage Ratio of College Graduates to High School Graduates
1.95
1.85
1.75
1.65
1.55
1.45
Ratio
1-5 Years of Experience
All Levels of Experience
67
69
71
73
75
77
79
81
83
85
87
89
Year


Changes in Family Income
by Quintile
1973-89
%
25
20
15
10
5
0
-5
Lowest
Second
Middle
Quintile
Fourth
Highest

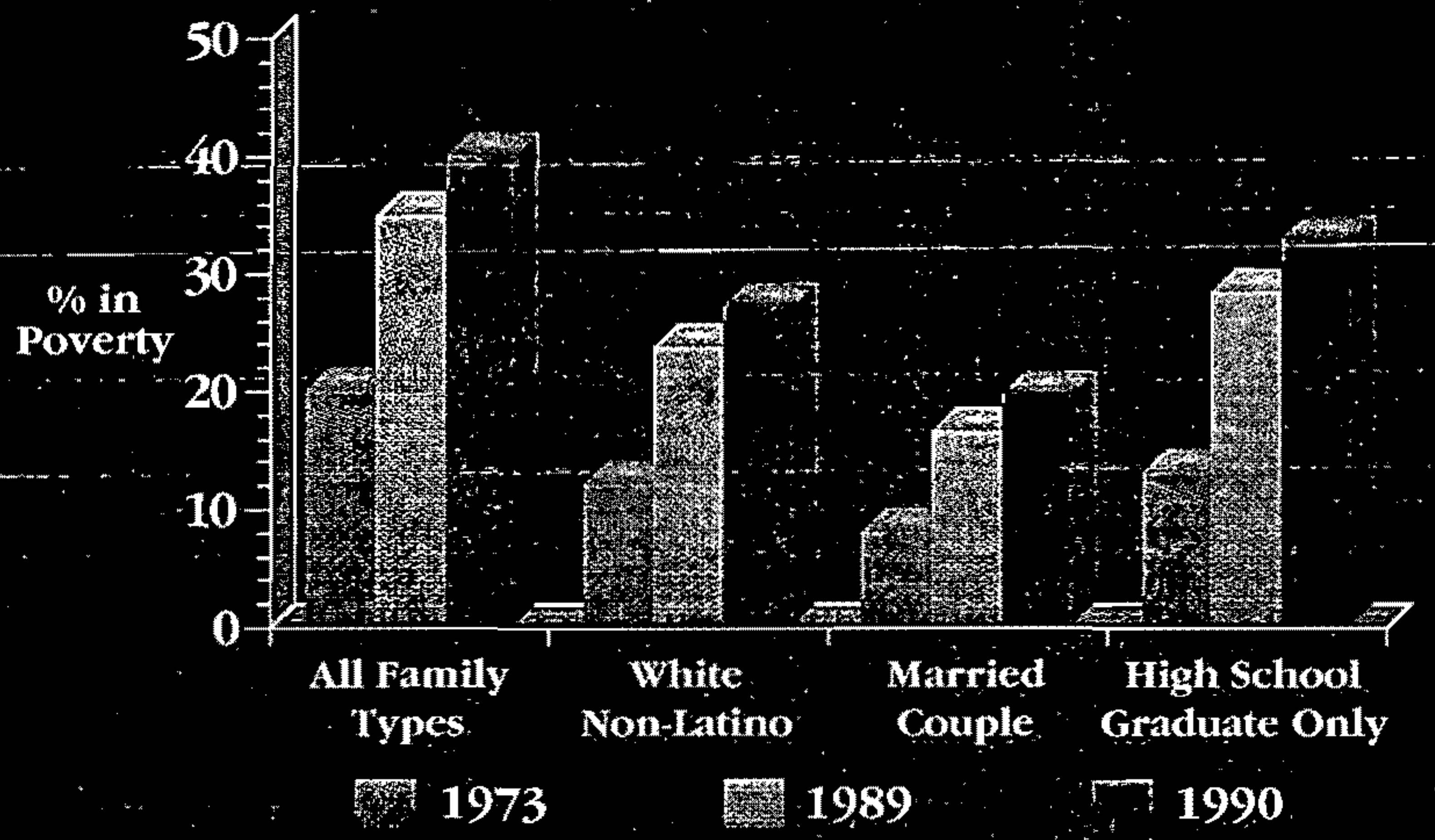

Child Poverty Rate
%
30
25
20
15
10
5
0
1960
1965
1970
1975
1980
1985
1990
Year

An International Look at Child Poverty

Percentage of Children Living Below Poverty Line in mid-1980's



Poverty Rates of Children in Young Families, by Characteristics of the Family Head 1973, 1989 & 1990



Sound Investments

$ 1 on childhood immunizations	*Saves*	$10 in later medical costs
$ 1 on comprehensive maternity care for pregnant women	*Saves*	$3.38 in later health costs
$ 1 on food and nutrition counseling for pregnant women	*Saves*	$ 3.13 in Medicaid costs due to low-birthweight babies
$ 1 for quality preschool education like comprehensive Head Start	*Saves*	At least $3.00 in later special education, crime, welfare and other costs
$ 1 for comprehensive job training, education, and support services through the Job Corps	*Saves*	$1.46 in later crime,welfare, and other costs and lost tax revenues

DOMESTIC ASSESSMENT III:

PUBLIC + PRIVATE INVESTMENT

DOMESTIC ASSESSMENT III: PUBLIC AND PRIVATE INVESTMENT

EVENT:
Assessments of U.S. private and public investment trends, and the ways in which these trends affect U.S. competitiveness.

The assessment is divided into two sections, each of which will last five minutes.

1. Public Investment: Presented by **Alicia Munnell**, Ph.D

   Senior Vice President and Director of Research for the Federal Reserve Bank of Boston. She has served on advisory boards for the World Bank, MIT, the Economic Policy Institute and AEI.

2. Private Investment: Presented by **Michael Porter**

   Professor of Business Administration at Harvard Business School since 1973. He is a leading authority on competitive strategy and served on President Reagan's Commission on Industrial Competitiveness. He directed a pro bono study of the Massachusetts economy in 1991. Some of his publications are: <u>The Competitive Advantage of Nations</u>; <u>Competitive Strategy; Techniques for Analyzing Industries and Competitors</u>; and <u>Capital Choices: Changing the Way America Invests in Industry</u>.

GOALS:
- Demonstrate that public investment "crowds in" rather than "crowds out" private investment.
- Demonstrate that the U.S. is underinvesting in plants and equipment and R&D, and suffering in terms of growth as a result.
- Demonstrate that countries with the highest investment rates also have the highest growth rates.

ATTACHED:
- Public sector investment assessment: summary of Alicia Munnell presentation
- Possible questions for Munnell
- Background information on infrastructure
- Private sector investment assessment: outline of Michael Porter presentation
- Summary of Michael Porter study on private sector investment
- Possible questions for Porter
- Possible points of contention (presented in question/answer form)
- Key elements of Clinton-Gore plan
- Charts that might be used
- Biographies of roundtable participants

PUBLIC INVESTMENT ASSESSMENT:
(Summary of Munnell presentation)

The increasing focus on infrastructure issues reflects the lack of attention to both public and private investment during the 1980s, when most of the nation's output went for current consumption.

Experts concerned about continued low levels of productivity growth argued for shifting resources from consumption to investment.

Public capital investment in the U.S. is not only low compared to historical levels but also falls well below that in other developed countries.

The argument for increased public, as opposed to exclusively private, investment rests on three premises:

1. The drop in public capital spending reflects more than demographic and other developments such as the completion of the interstate highway system and the education of the baby-boomer generation; **a serious decline has occurred in the stock of productive infrastructure.**

2. This decline represents a real economic loss. For example, the state of our transportation infrastructure is beginning to serve as a drag on economic performance. **Recent research suggests that greater public capital not only enhances the quality of life but also leads to increased private sector output.** Public capital enhances the productivity of private capital, raising its rate of return and encouraging more investment. One study on the relationship between public capital and employment growth showed that public capital had a positive, statistically significant effect on employment growth at the state level.

3. **Numerous investment opportunities have been identified with high ratios of benefits to costs.** For example, cost-benefit studies reported by the CBO (1988) indicate that the return to projects designed to maintain the average condition on the federal highway system could be as high as 30 to 40 percent.

Voters are willing to pay for more infrastructure investment, as expressed in bond elections and other referenda. Eighty percent of infrastructure bond proposals submitted to the voters between 1984 and 1989 were approved and the margin exceeded 66 percent on average.

Improved construction design and pricing should not be considered an alternative to infrastructure investment, but rather a policy to be pursued in concert with a major capital investment initiative.

Three specific suggestions for identifying those areas with the biggest payoffs:

1. Federal matching grant rates must be reduced; states and localities must bear at least half the costs to ensure that the money is spent sensibly.

2. One profitable investment area is aviation. The U.S. has the best aviation industry in the world; airlines need to earn enough money to buy planes, and for airlines to be profitable, airports must be safe and relatively uncongested.

3. A major infrastructure initiative, combined with a significant deficit reduction effort, raises the importance of carefully considering the introduction of a capital budget at the federal level.

POSSIBLE QUESTIONS FOR MUNNELL:

Q. As we proceed with our Rebuild America plan, what exact definition of infrastructure should we use? How has this definition changed?

Q. Do you agree with the Federal Highway Administration's projection that $50 million worth of annual public capital investment between 1990 and 2009 will be required from all sources <u>just to maintain</u> highways and bridges at their current level? [<u>1991 Status of the Nation's Highways and Bridges</u>, Federal Highway Administration, 11/91]

Q. What role do you see the private sector taking in the development of high-tech infrastructure (high-speed rails and national information network)?

Q. What is the best evidence that public investment "crowds in" private investment? Are there clear historical examples?

BACKGROUND INFORMATION ON INFRASTRUCTURE:

- Highway travel is expected to grow by 65-100% over the next 30 years. [Office of Technology Assessment; Federal Highway Administration, 11/91]

- Estimates of <u>total additional</u> public infrastructure investment needed per year range from $45 billion to over $100 billion. [<u>The Public's Capital</u>, 7/89, University of Colorado, Harvard University]

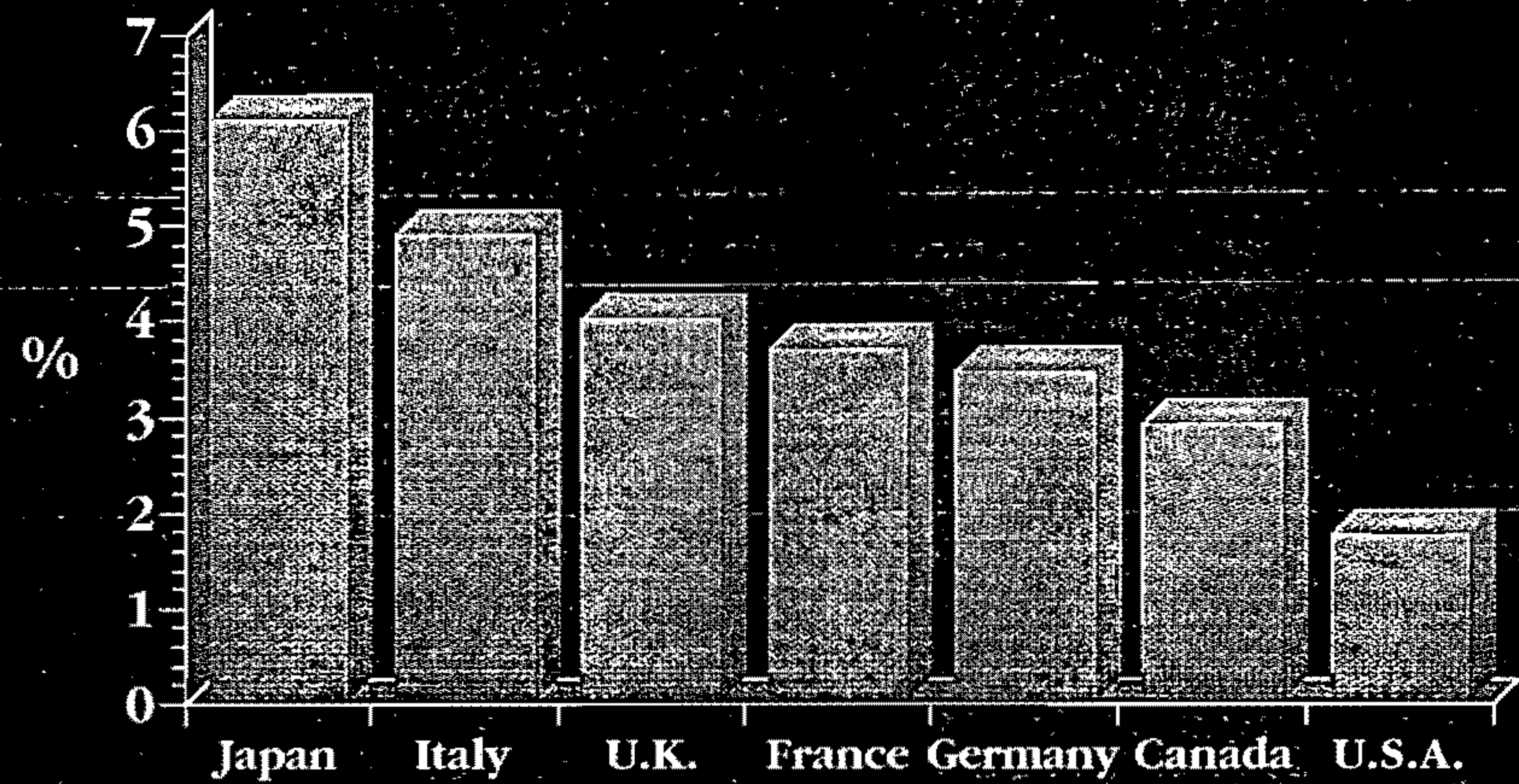
- $1 billion of spending on highway and bridge construction results in an estimated total output in the economy of $2.4 billion and employment of an estimated 52,000 persons. [CRS Report for Congress, 5/10/90]

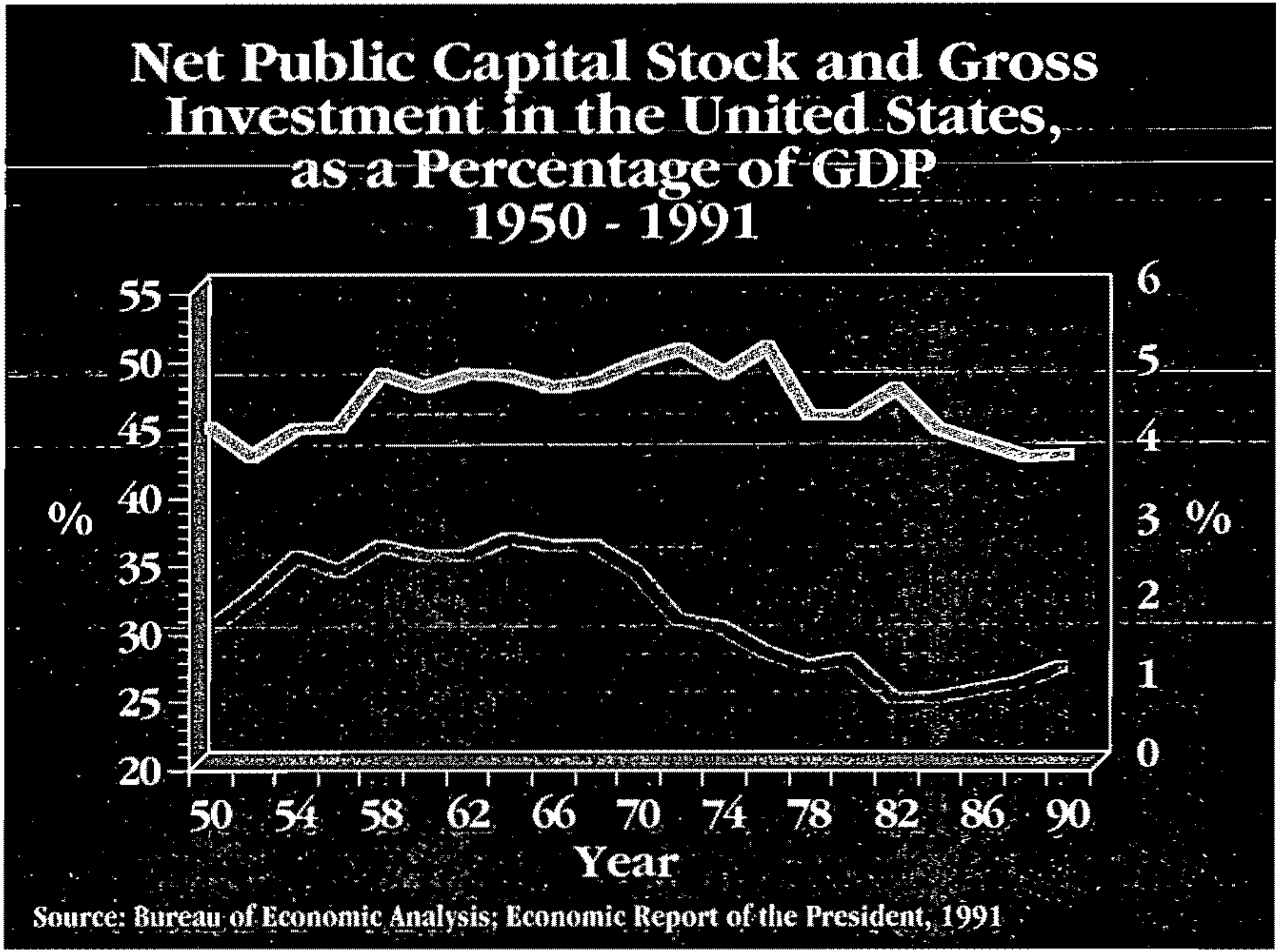
- Delaying needed highway improvements can increase costs as much as 200%. [Federal Highway Administration, 11/91]

- By 1994, Japan, Germany, and France are all expected to have fully operational advanced telecommunications networks that can carry voice and data information concurrently. Because the rate of American telecommunications dropped an average of 8 percent a year in the 1980s, such systems are expected to be less than half complete in the U.S. by 1994. [New York State Urban Development Corporation]

- Though maglev (high-speed trains) was invented by two American scientists in 1960, the U.S. invested of only $3 million in research between 1966 and 1975 and then abandoned the effort. Meanwhile Japan invested $1 billion. Demonstration trains are already operating in Japan and Germany. [New York State Urban Development Corporation]

Public Investment as a Share of GDP
1990




Net Public Capital Stock and Gross Investment in the United States, as a Percentage of GDP
1950 - 1991
%
55
50
45
40
35
30
25
20
6
5
4
3 %
2
1
0
50
54
58
62
66
70
74
78
82
86
90
Year
Source: Bureau of Economic Analysis; Economic Report of the President, 1991

PRIVATE SECTOR INVESTMENT ASSESSMENT:
(Outline of Porter presentation)

Porter will make the following points in his presentation (see attached charts):

- The foundation of a nation's competitiveness is based on the capacity of a nation's firms to continuously innovate and upgrade. Upgrading requires sustained investment in specialized assets, knowledge and skills.

- Forms of investments include physical assets, intangible assets (e.g. R&D, employee training, development of supplier relations).

- The United States is investing less than Germany and Japan in equipment and civilian R&D.

- Countries that invest a large share of their income grow rapidly. The United States has one of the lowest investment rates of any developed countries. As a result, over the past thirty years, the United States has a lower productivity growth rate than the United Kingdom, Canada, France, Germany, Italy and Japan.

- U.S. private investment is lower because both the macroeconomic environment and the U.S. system for the allocation of capital do not encourage these types of investments.

SUMMARY OF MICHAEL PORTER STUDY:
(Capital Choices: Changing the Way America Invests in Industry)

Michael Porter recently completed a study on the U.S. system for allocating capital. He concluded that "many American firms invest too little in those assets and capabilities most required for competitiveness (such as employee training or R&D), while others overinvest in areas (such as unrelated acquisitions) that add little to the country's long-term economic strength." The problem, according to Porter, is a "flawed U.S. system for allocating investment capital to companies and to specific projects within companies."

Evidence of investment problem:

- Many U.S. industries are declining relative to Germany and Japan.

- Investment in plants and equipment, civilian R&D, corporate training, relationships with suppliers, and start-up losses to enter foreign markets is lower in the U.S. than in Japan or Germany.

- American CEOs believe that their companies have shorter time horizons than their competitors.

- The average holding period of stocks has declined from over seven years in 1960 to about two years today.

Recommendations for systemic reform:

To address these problems, Porter recommends reforms in several areas:

1. **Improve the macroeconomic environment:** Increase private and public sector savings, and create a stable macroeconomic environment.

2. **Expand true ownership throughout the system:** Outside owners should take larger stakes and play a more active and constructive role in the companies. Also, ownership should be expanded to directors, managers, employees, and even customers and suppliers.

3. **Better align the goals of capital providers, corporations, directors, managers, employees, customers, suppliers and society:** For example, by creating incentives for long-term equity incentives, the government could encourage investors to look for companies with attractive prospects five or more years in the future.

4. **Improve the information used by investors:** Require disclosure of information that would help investors judge the long-term prospects of a company, such as patents, the education and training profile of employees, or the share of sales represented by new products.

POSSIBLE QUESTIONS FOR PORTER

Q. What are some of the steps that the U.S. can take to lengthen the time horizons of U.S. companies?

Q. What will happen if our major competitors continue to out-invest us in plant and equipment by as much as 2 to 1?

POSSIBLE POINTS OF CONTENTION:

Q. How do you avoid pork barrel projects?

A. The easiest way is to give the President a line item veto. Beyond that, it will be essential that President-elect Clinton send a clear message to Congress at the front end that pork barrel politics will not be tolerated. Additionally, quantitative determinations should be used when possible to determine what levels of expenditures are appropriate in what projects and what geographic areas.

Q. How will environmental concerns factor into infrastructure investment decisions? By improving and expanding our highways, won't we be encouraging more travel, thereby creating more pollution?

A. We will make smart infrastructure investments which will result in energy-efficient and environmentally sound transportation. Better highways will result in less congestion, and other technologies (such as high-speed rail) will move more people, quicker, with less pollution. In addition, our other commitments to energy and environmental policies will remain strong.

KEY ELEMENTS OF CLINTON-GORE PLAN:

Public Investment

- Create a Rebuild America Fund with a $20 billion federal investment each year for four years.
- Put public records, databases, libraries, and educational materials on line for public use (national information network).
- Develop high speed rail networks and high-tech short-haul aircraft.

Private Investment

- Provide a targeted investment tax credit to encourage investment in new plants and equipment.
- Create a permanent research and development tax credit to reward companies that invest in new technology.
- Offer a 50 percent tax exclusion to those who take risks by making long-term investments in new businesses.

Private Investment in the U.S. Economy

The Foundations of National Competitiveness

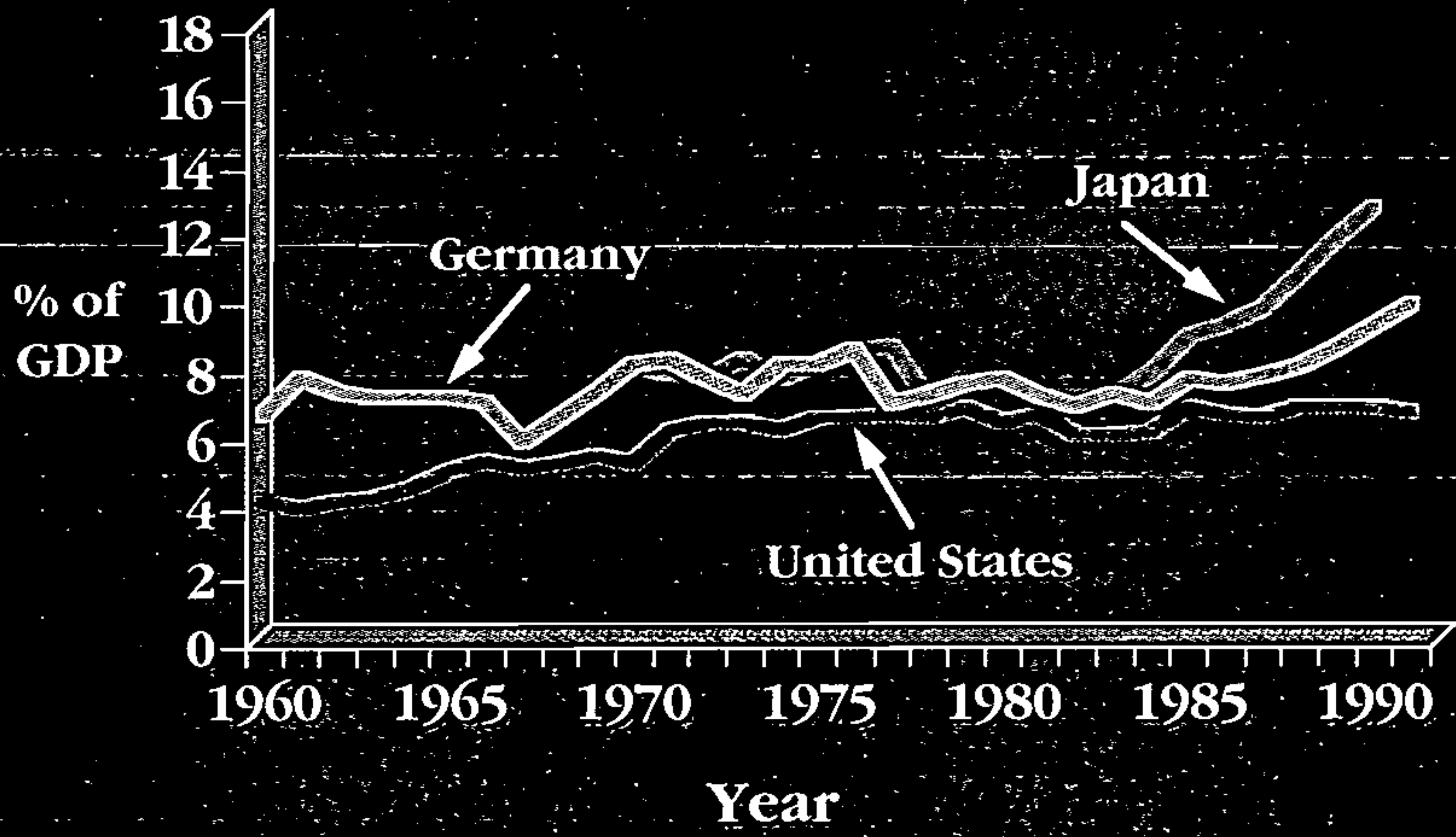
- The Productivity With Which a Nation's Resources are Deployed

- National Productivity Depends on the Capacity of a Nation's Firms to Continuously Innovate and Upgrade
- Upgrading Requires Sustained Investment in Specialized Assets, Knowledge and Skills

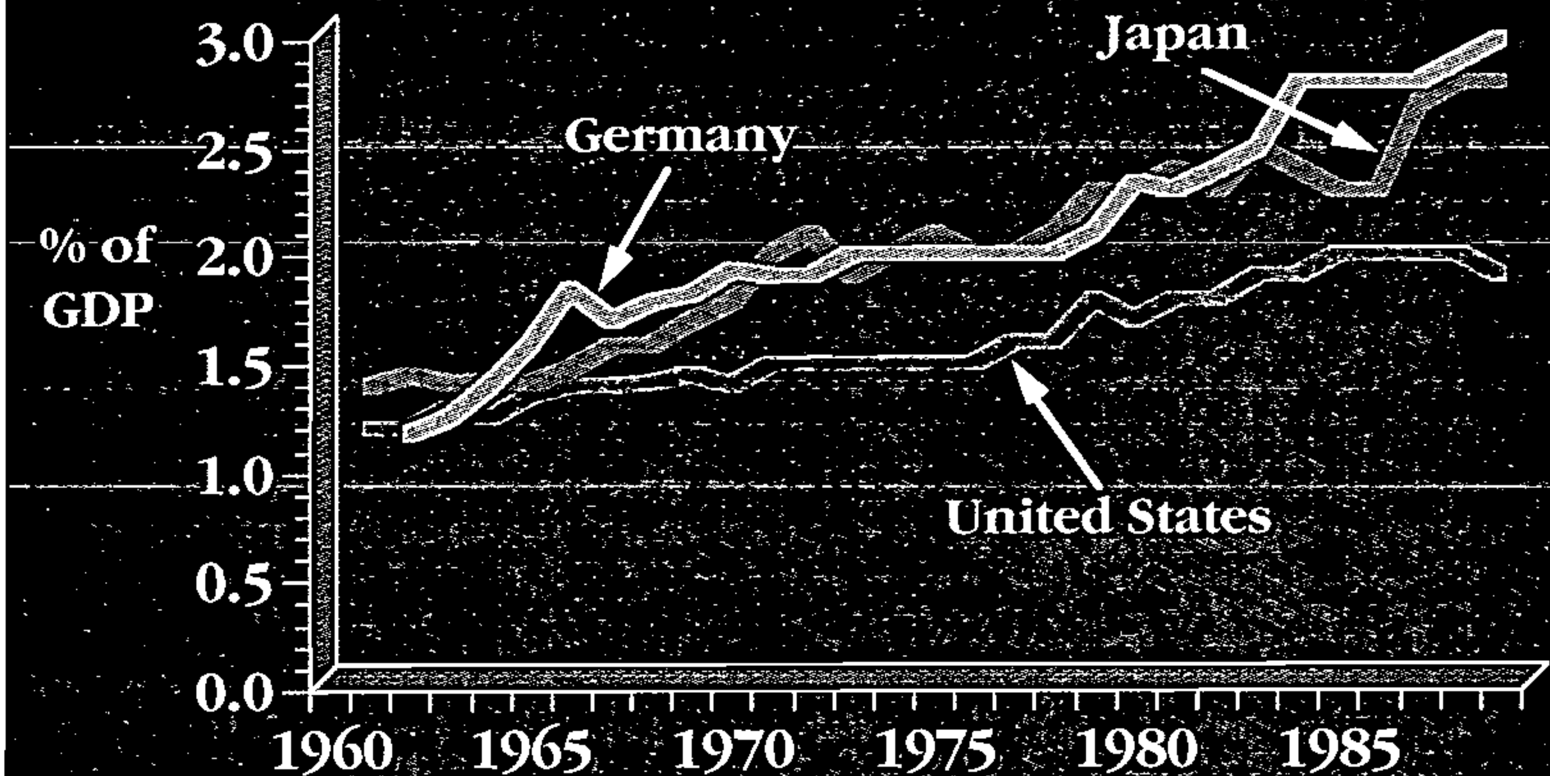
Forms of Investment

- Physical Assets
- Intangible Assets
  - R&D
  - Advertising and Marketing
  - Employee Training / Skills Development
  - Information Systems
  - Organizational Development
  - Development of Supplier Relationships
- Positional Assets
  - Market Entry Costs

Investment in Producers' Durable Equipment



Investment in Non-Defense Research and Development



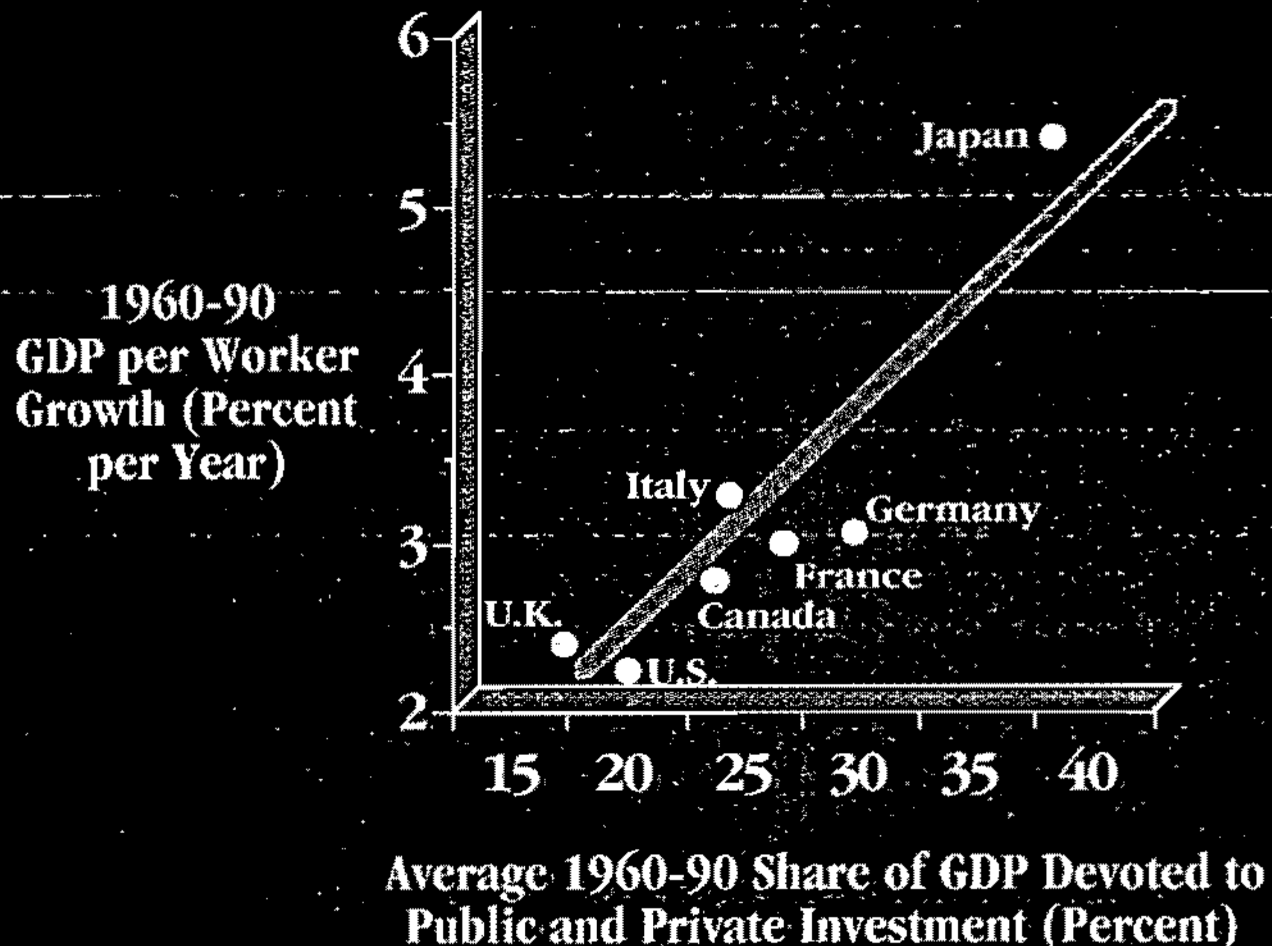
Source: National Science Foundation and Organization for Economic Cooperation and Development

Comparative Private Sector Investment, 1990

($ Billions)

	U. S.	% GNP	Japan	% GNP
Physical Capital	$524	10.00%	$586	18.90%
Industry-funded R&D	74	1.40%	80	2.60%
	$598	11.40%	$666	21.50%
Estimated Corporate Training	120	2.20%	180	6.00%
Total Private Investment	$718	13.60%	$846	27.50%

Growth and Investment for the G-7
(1960-1990)



Causes of Lower U. S. Private Investment

- The Macroeconomic Environment
  - Pool of Investment Capital
  - Policy Stability
- The Allocation of Capital

DOMESTIC ASSESSMENT IV:

THE DEFICIT

DOMESTIC ASSESSMENT IV:
THE DEFICIT

EVENT:
Assessment by John White on the impact of the federal debt and ballooning budget deficits (5 minutes).

Presenter: ***John White*** was just named Director of the Center for Business and Government at the Harvard Kennedy School of Government. From 1988-1991, he served as corporate Vice President of Eastman Kodak Company. He was the Chairman of the Board and CEO of Interactive Systems Corporation from 1981-1988, and from 1978-1980, he was the Deputy Director of the Office of Management and Budget. After drafting the economic plan for the Perot campaign, White endorsed the Clinton Gore plan.

GOALS:

- Stress the importance of the deficit to America's long-term productivity and growth. As this is an assessment, the discussion should not get bogged down in specific prescriptions.

- Show Americans how much the CBO baseline that was used by both Clinton and Perot has worsened since each put out their respective plans, due to changes in economic and technical assumptions, and RTC financing actions by Congress.

- Explore the different components of spending that are driving the rise of the deficit -- health care and interest spending.

ALSO IN THIS BRIEFING
- Summary of assessment

- Additional points to note and possible questions for White

- Charts that might be used

- Biographies on roundtable participants

SUMMARY OF JOHN WHITE'S ASSESSMENT ON THE DEFICIT:

White's presentation may be one of the high points of the first day. The main chart he will show is one that points out the change in the baseline assumptions since Perot and Clinton released their respective plans.

The main goal here is for White to show that the government's official deficit projections have gotten worse since Putting People First and the Perot plan was put out. Both of those plans relied on the January 1992 CBO baseline -- the most authoritative baseline at the time they were released. The chart will show that most of the increase in the most recent (although not officially released) deficit baseline since then has been due to (1) the failure of Congress and the Administration to deal with the S&L bail-out; and (2) to changing economic and technical assumptions. Initially, CBO projected that more assets would be purchased in FY 1993 (increasing the deficit), with many of the assets sold in later years (lowering the deficit). Furthermore, the sluggishness of this recovery has lowered both current and future revenue estimates.

White may also show charts prepared by Chairman Panetta's staff that show the shifting of the composition of the deficit over periods of time. The key point here is critical: while the deficit has been increasing, it has not been increasing because there has been too much increase in discretionary domestic investment. Instead the chart shows that increases have been in health care costs and interest payments on the national debt.

White may also explore a matter we have been recently discussing: whether a better measure of our economic health than just the deficit number, is the debt/GDP ratio.

POINTS TO NOTE/QUESTIONS FOR JOHN WHITE

1. In 1992, America spent $880 billion on health care. CBO projects that health care costs will consume 18 percent of GDP by the year 2000, or almost $1.7 trillion dollars. By comparison, in 1965, health care expenditures consumed only 6 percent of GDP in 1965. In the next five years, health care spending will increase faster than any other part of the budget. [CBO]

2. Bob Reich points out that the current Debt/GDP ratio was the same now as it was in the mid-1950s. Yet, in the mid-1950s, productivity and growth were far higher. Why do you believe this is? Does this support the view that what counts most is not just how much you borrow, but what you are borrowing to invest in? At that point, we were rebuilding our educational system, the national highways and preparing for the space race.

3. The logic of using a debt/GDP ratio is, I understand, that what really counts for a nation, like a family, is not how much debt you have per se, but how much you are in debt compared to your income. Yet, some Americans may feel skeptical when they hear economists using different -- and more confusing -- deficit measurements. What are the types of targets that would be reasonable in judging what is an appropriate debt/GDP ratio?

4. I know that in addition to the federal deficit we have also seen a strong increase in personal debt as percentage of disposable income. Indeed, the ratio has gone from 65% in 1974 to 93.9% in 1991 according to the Department of Commerce. How much of the problem in our national savings problem do you see as emanating from increased private debt as a ratio of personal disposable income?

BACKGROUND

Long-term Deficit Reduction and Why It's Important
Source: "Why Deficits Matter" by David Wyss of DRI/Mgraw Hill

While there is debate over how quickly the new administration should aim to reduce the deficit, there is general consensus by economists that a long-term commitment to deficit reduction is critical to America's competitiveness in the world economy. Here are some major points you might want to raise in the discussion:

- **DEFICITS IMPEDE INVESTMENT** With large budget deficits, an increasingly large percentage of the federal budget must go to paying just the interest costs on the debt alone. In the 1980's, consumer spending rose from 62.8 percent of GDP in 1979 to 66.9 percent in 1989; at the same time, gross business fixed investment fell from 13 percent to 10.8 percent. In short, a shift away from an investment-led economy to a consumer-led economy.

- **DEFICITS KEEP PRODUCTIVITY LOW** The large percentage of GNP going to interest costs on the deficit mean less available funds for investments in the major components of economic growth like education and technology.

- **DEFICITS EAT INTO PRIVATE SAVINGS** As federal budget deficits have ballooned over the last 20 years, the country's savings rate has declined. The personal savings rate dropped to 3.3 percent in 1987 from the postwar average of 7.5 percent. Corporate savings over the same time period fell to under 1 percent during the 1980's, as compared to the post war average of 2.9 percent of GDP. In sum, consumption instead of savings and investment dominated consumer and business trends.

- **DEFICIT AND DEBT KEEP FAMILY INCOMES LOW/REDUCE JOB PROSPECTS** High government borrowing and the low levels of private and corporate savings and low private and public investment leads to lower productivity rates, which translates into lower real wage gains, lower family income, and bleaker job prospects.

- **DEFICITS PUT AMERICA AT A COMPETITIVE DISADVANTAGE** Heavy borrowing, much of it from foreign sources, meant that our share of world markets dropped, the trade deficits with several countries widened, and contributed to the severe decline of America's manufacturing sector in the 1980's.

- **DEFICITS RAISE LONG-TERM INTEREST RATES** The influx of foreign capital borrowed by the U.S. Treasury to finance the deficit caused American long-term interest rates to rise, again impeding investment, and pushed up interest rates abroad, slowing the international flow of capital.

Center for Strategic and International Studies:
The Strengthening of America Report

In its section on "Getting our Fiscal House in Order", the CSIS Commission, co-chaired by Senators Nunn and Domenici, argues that controlling the deficit and reforming the country's tax system ought to be the country's top two priorities. Specifically, the Commission argues, the deficit must be reduced to:

- **INCREASE SAVINGS AND INVESTMENT.** The drop in savings during the 1980's, largely caused by the deficit and static real family income, has already cost America about 15 percent of its capital stock.

- **THE DEFICIT TAKES AN INCREASING PERCENTAGE OF THE FEDERAL BUDGET.** Federal spending has jumped from $500 billion in 1970 to $1.5 trillion in 1992, with over $902 billion of that spending going to mandatory programs (entitlements). Measures such as payroll taxes, intended to cover the costs of these expenditures, are failing to keep up with the growth of these entitlements.

- **CAUSES:** If not reversed, the path of slow growth, rising health care costs and aging population mean that the deficit will get worse than current projections in the latter half of this decade.

- **AVOID DEFICIT GIMMICKS** The Commission argues <u>against</u> the so-called past "silver bullets" often cited as main ways to balance the budget:

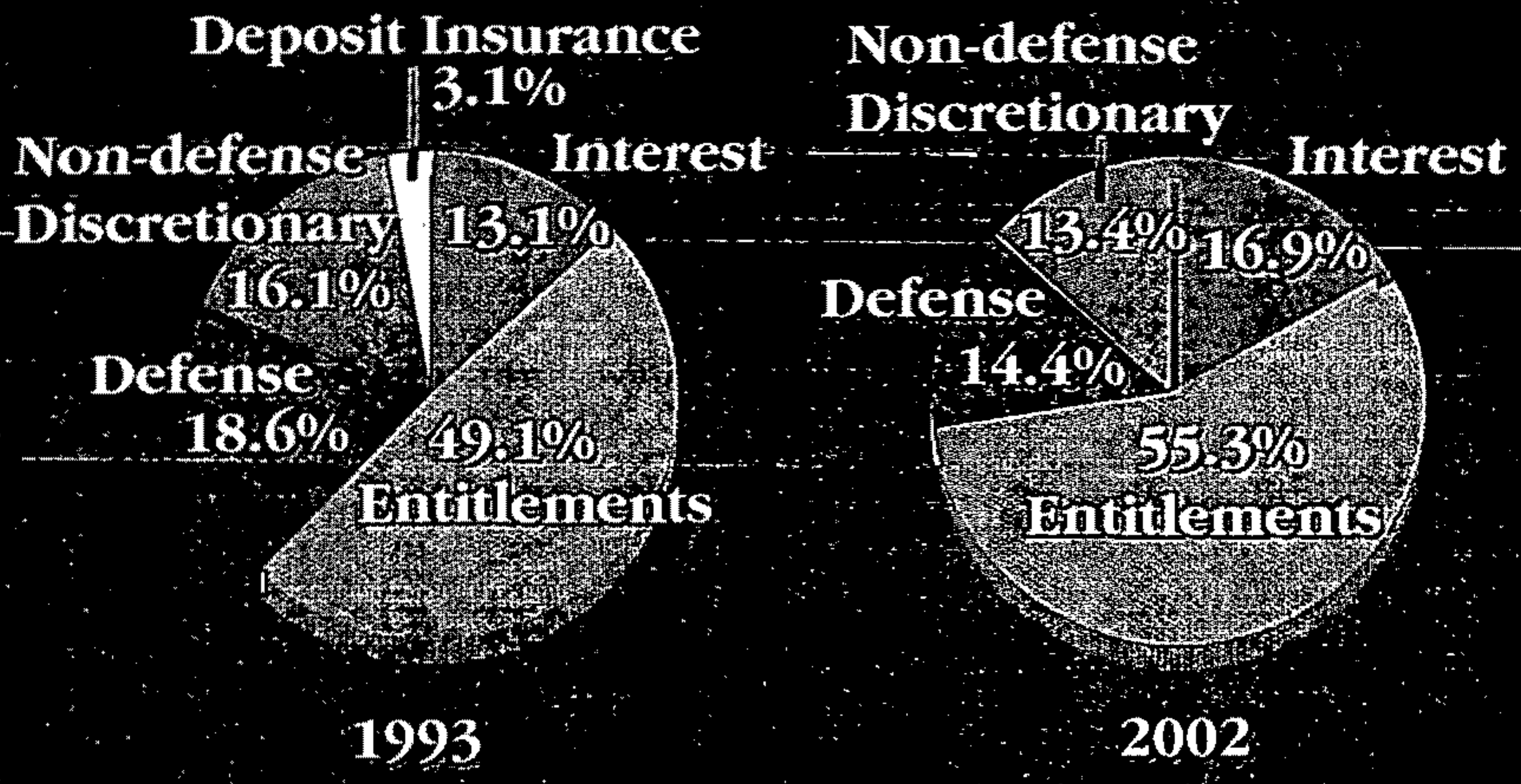
    - Laws: Gramm-Rudman-Hollings and similar laws to balance the budget, including
    - Line item veto: President can't trim more than 2 % of discretionary spending with this measure.
    - Bi-ennial budgeting: too confusing and not responsible.
    - Agency consolidation: not significant savings.

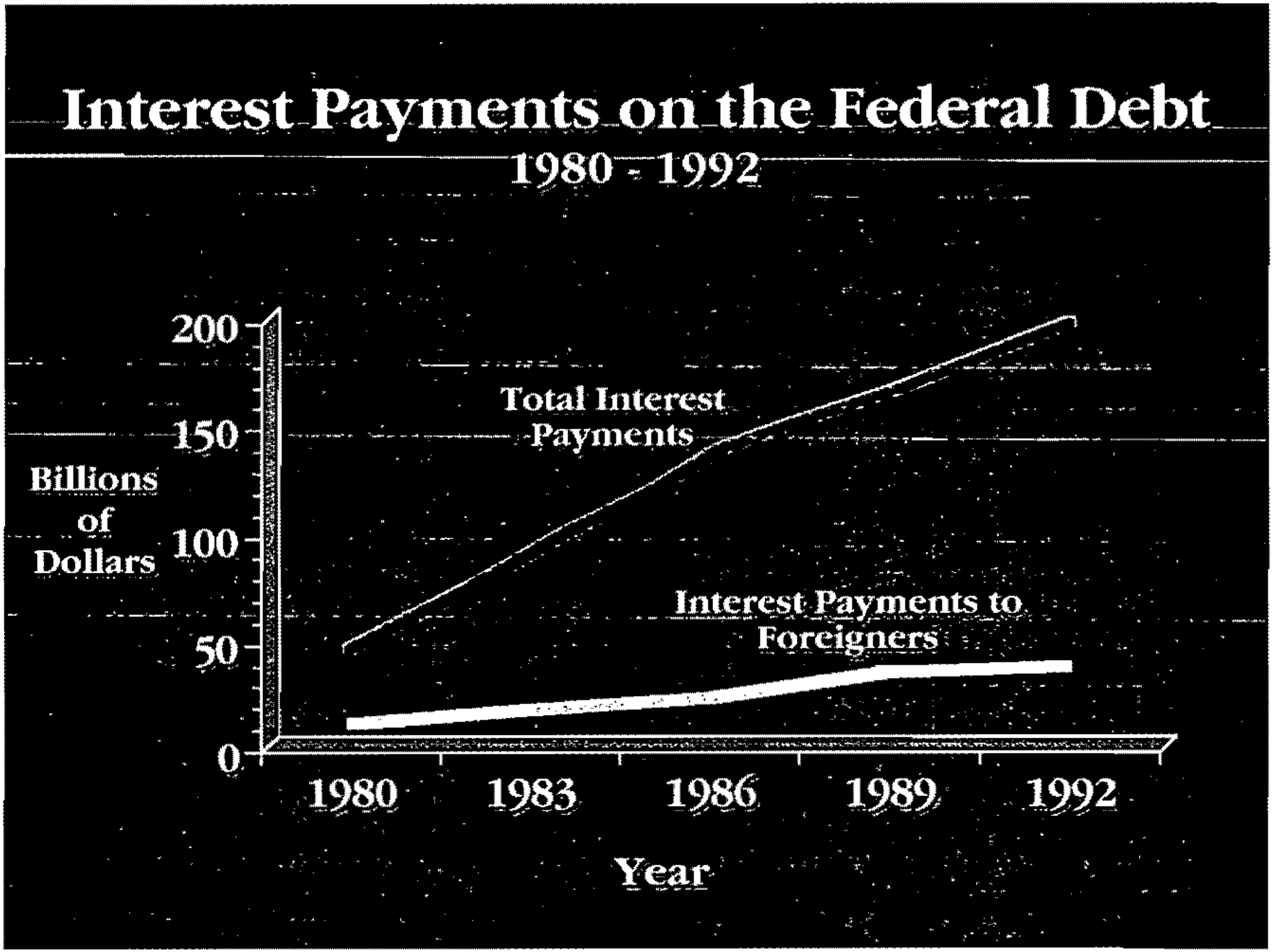
- **PRESCRIPTIONS:** The Commission presents two "hard line" choice to balance the budget by the year 2002 without touching the Social Security Trust Funds, which can be pursued separately or together:

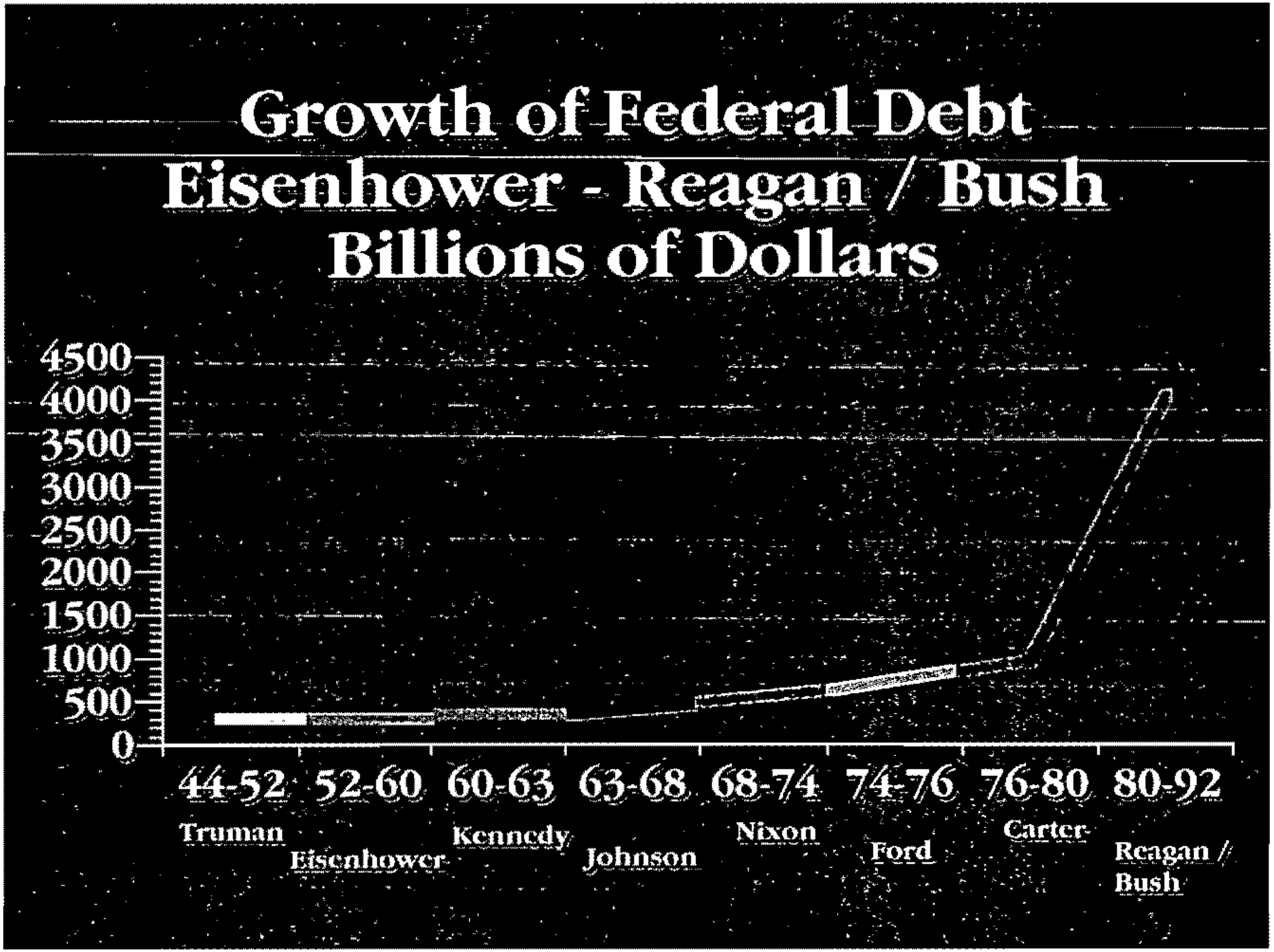
    - <u>Cut spending</u>: defense cuts, eliminate COLAs except for the poor; caps on mandatory spending (no inflation adjustment).

    - <u>Raise Taxes</u>: a value added tax; a 50 cent gas tax; environmental "green" taxes and other consumption-based taxes; increase in the AMT. Restructure income tax code to reward savings.

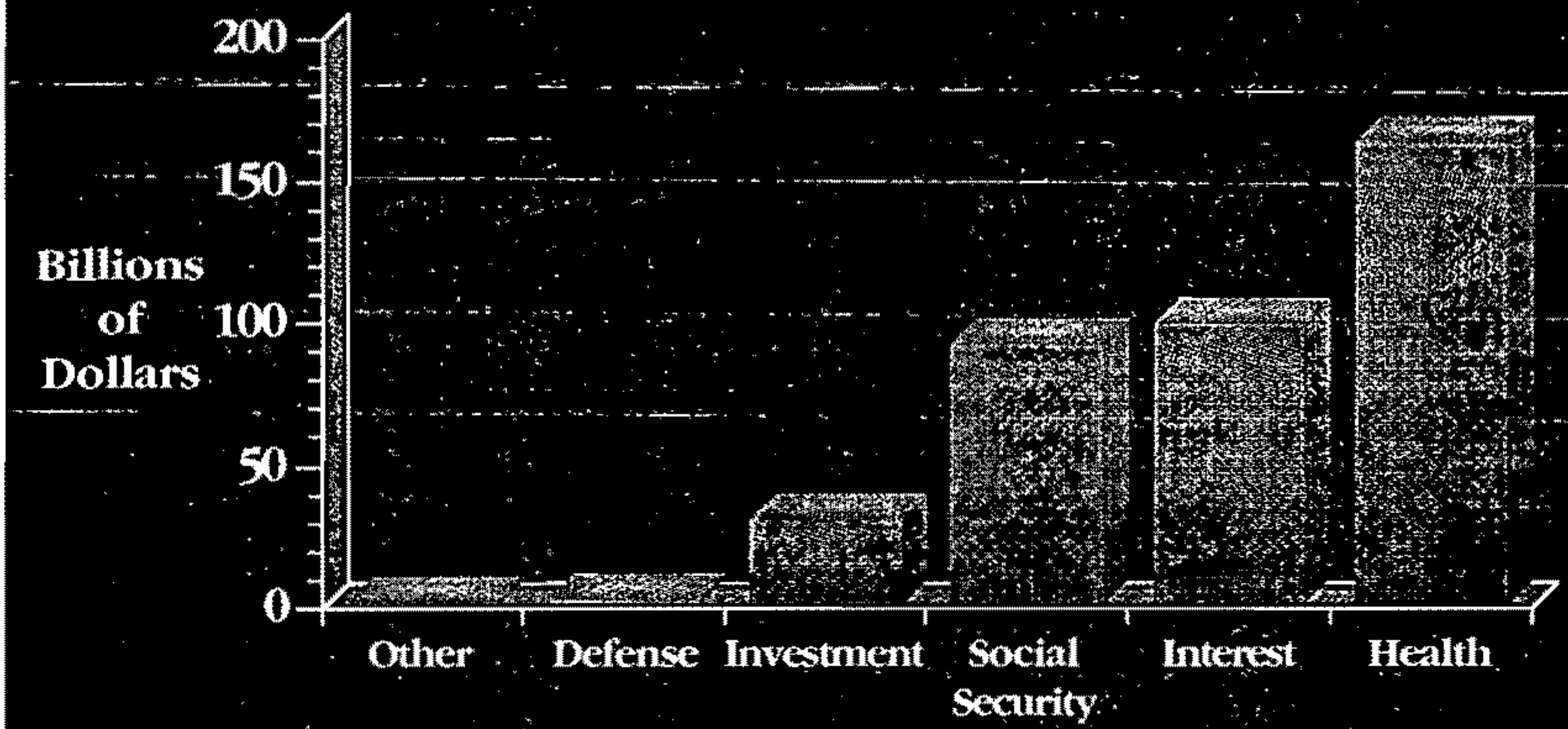
Major Categories of Spending
Fiscal Years, Percent of Total




Interest Payments on the Federal Debt
1980 - 1992
Total Interest Payments
Interest Payments to Foreigners
Billions of Dollars
200
150
100
50
0
1980
1983
1986
1989
1992
Year

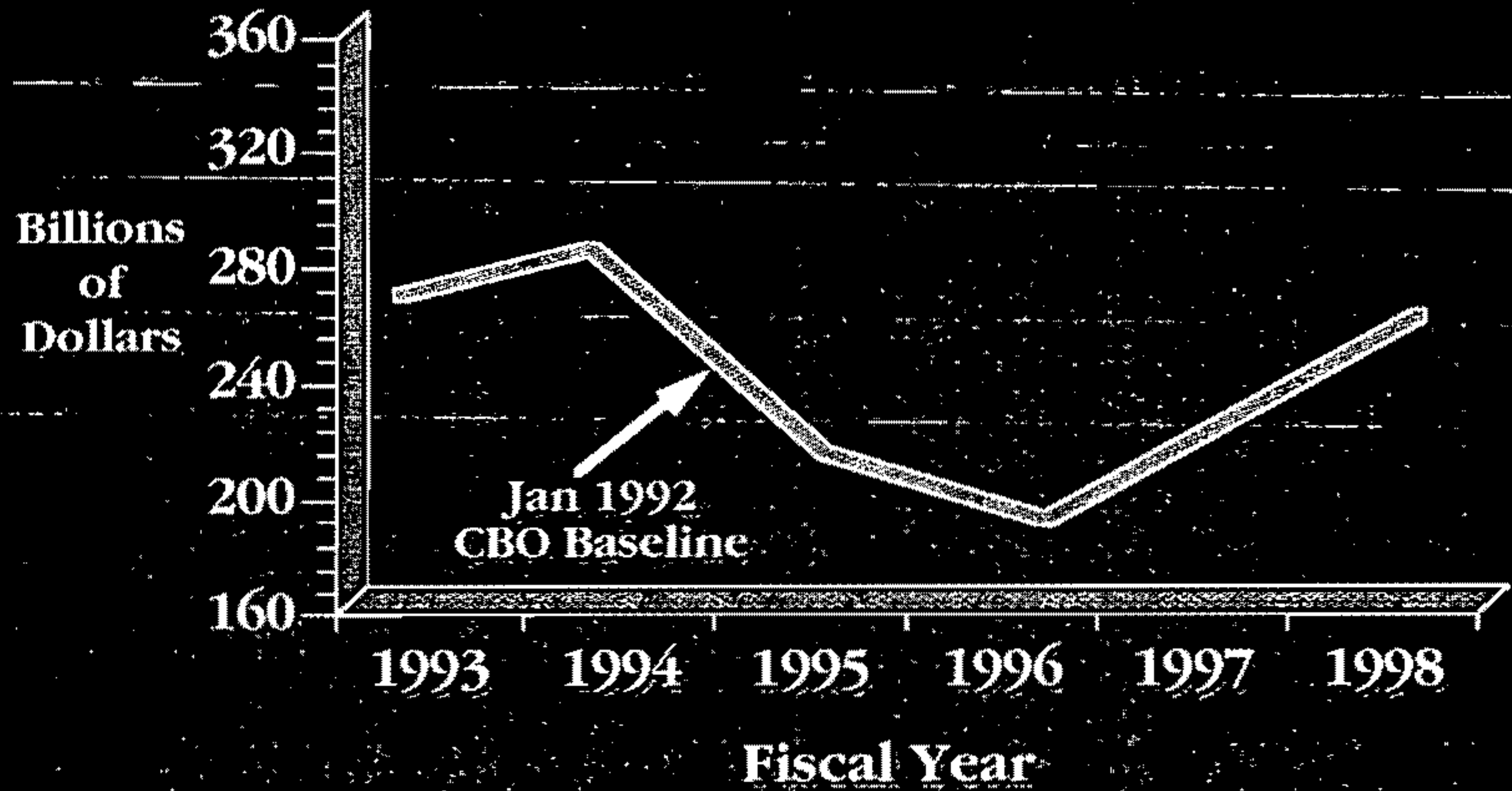

Growth of Federal Debt
Eisenhower - Reagan / Bush
Billions of Dollars
4500
4000
3500
3000
2500
2000
1500
1000
500
0
44-52
52-60
60-63
63-68
68-74
74-76
76-80
80-92
Truman
Eisenhower
Kennedy
Johnson
Nixon
Ford
Carter
Reagan / Bush

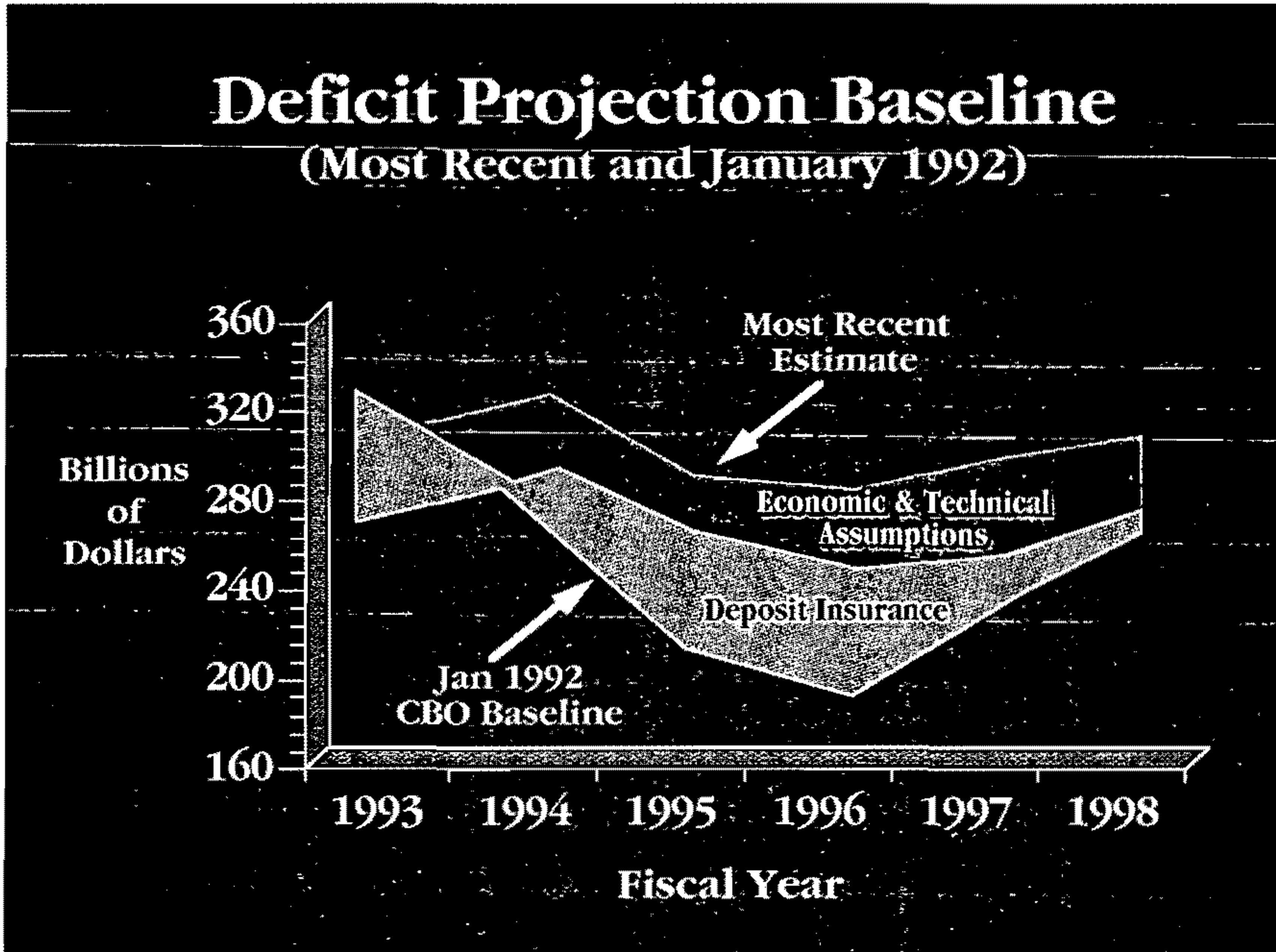
Estimated Increases in Spending From 1993 to 1998 by Major Budget Category



Deficit Projection Baseline

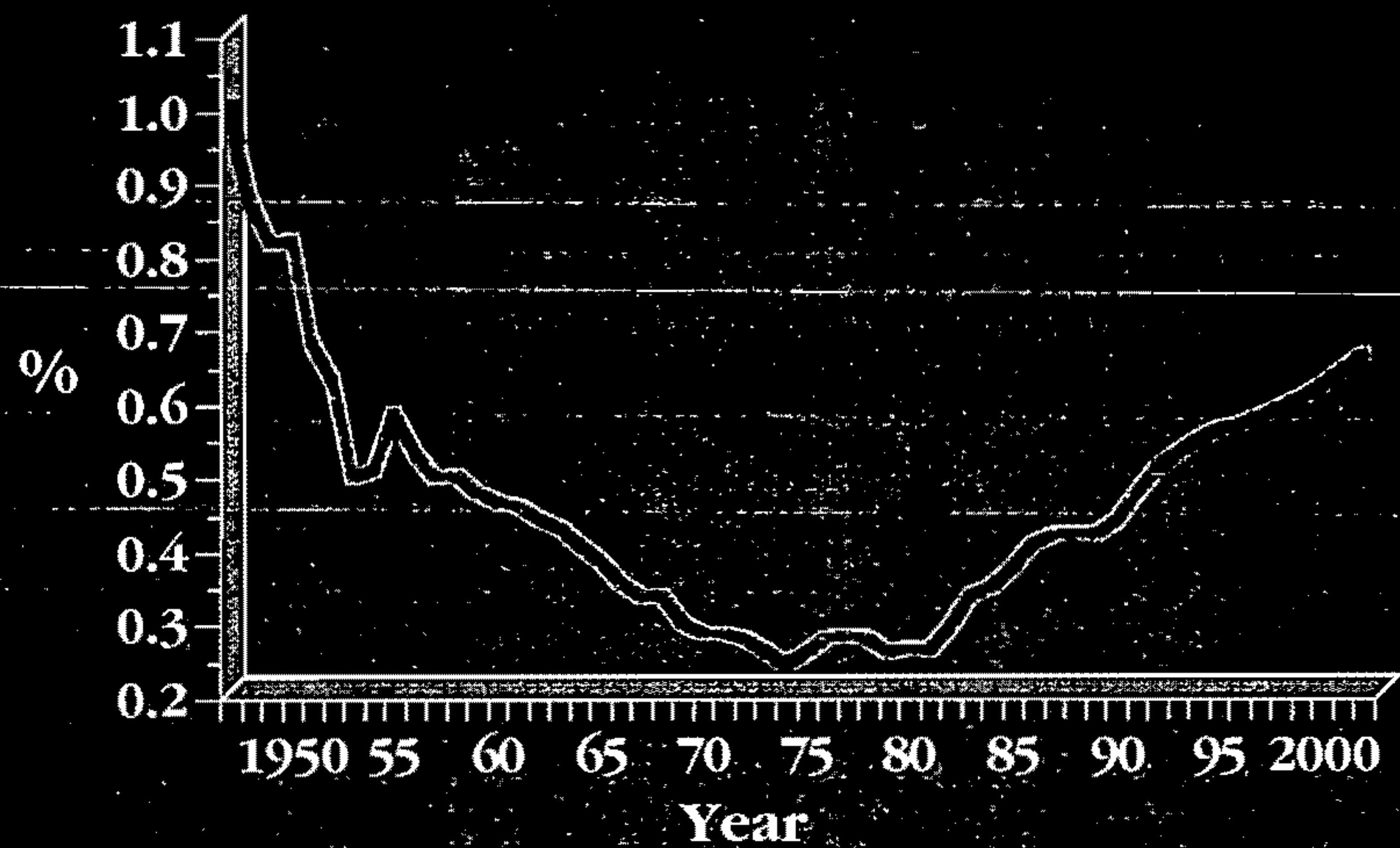
(January 1992)





Deficit Projection Baseline
(Most Recent and January 1992)
Billions of Dollars
360
320
280
240
200
160
Most Recent Estimate
Economic & Technical Assumptions
Deposit Insurance
Jan 1992 CBO Baseline
1993
1994
1995
1996
1997
1998
Fiscal Year

Debt/GDP Ratio



DOMESTIC ASSESSMENT V:

HEALTH CARE

DOMESTIC ASSESSMENT V:
HEALTH CARE

EVENT:
This presentation will examine the crisis in rising U.S. health care costs and the effects which these costs have on the U.S. economy.

This assessment is divided into two sections, which will each last five minutes:

1. The Burden of Rising Health Care Costs:

   Presented by **Stuart Altman**: Professor of National Health Policy, The Heller School, Brandeis University

2. Health Care Costs and U.S. Competitiveness

   Presented by **Harold Poling**: Chairman and C.E.O. of Ford Motor Company

GOALS:
- To identify the economic implications of the rising health care costs in the United States -- both for the budget deficit and for the competitiveness of U.S. firms.
- To establish a clear connection -- using the example of the U.S. auto industry -- between health care costs and the decreasing competitiveness of U.S. products in the global marketplace.
- To make it clear that the status quo is unacceptable.

ATTACHED:
- Summary of the presentations
- Questions: Additional points to explore with the presenters
- Background:
  - Congressional Budget Office's, <u>Economic Implications of Rising Health Care Costs</u>, October 1992.
  - Major tenets of the Clinton/Gore health care plan, as outlined during the campaign.
- Possible points of contention
- Charts that might be used
- Biographies of roundtable participants

SUMMARY OF ASSESSMENT:

1. **The Burden of Rising Health Care Costs:**

Professor Altman, who has published extensively on the subject of controlling health care costs, will use a variety of charts to illustrate the increasing share of U.S. product consumed by rising health care costs and the corresponding effects these have had on the federal budget deficit.

- Medicare and Medicaid are the fastest growing portions of the budget; if their growth is not contained -- and they continue to be financed through budget deficits -- they will raise interest costs alone on the federal debt by $91 billion by 2002.

Altman will stress that this burden has been intensifying with no commensurate benefit to the economy or to the standard of living of U.S. workers. Health care costs now consume almost 15% of our nation's product, yet 37 million people remain uninsured and over 60 million do not have adequate insurance. [1992 Green Book]

- In 1992, America spent $880 billion on health care.

- According to the Congressional Budget Office, federal health expenditures will comprise 30% of total federal spending by 1995.

Altman will also probe into the reasons for rising health care expenditures -- examining the elements of private health insurance premiums.

The U.S. spends at least 25% more of its GNP on health care than any other industrialized nation -- almost twice as much as many nations.

2. **Health Care Costs and U.S. Competitiveness**

Harold Poling, the C.E.O. of Ford -- who joined the company as a cost analyst in the Steel Division and has repeatedly identified health care as one of Ford's most compelling problems -- will use the case of the U.S. auto industry to illustrate the direct impact rising health care costs have on U.S. competitiveness and employment. The goal of this session is to show that aside from the obvious consequences of exorbitant health care costs (the health of the American people, the budget deficit), there are other less apparent but equally damaging effects.

Our inability to control health care costs adds significantly to American business costs, making our final products less competitive at a time when weakened world demand has dampened export markets for the U.S. A direct causal relationship between the soaring costs of health care and declining U.S. employment will be established. The health care cost per automobile -- or the portion of an auto's total cost that was used to provide employee health care -- is nearly twice as much in the U.S. as in Japan. Over $900 of the cost of each U.S. car goes to health care, compared to $514 in Japan.

ADDITIONAL POINTS TO NOTE:

- Altman will probably note the CBO projection that, without reform, health care costs will continue to soar -- consuming 18 percent of GDP by the year 2000, or almost $1.7 **trillion** dollars. Ask him: What would implications be for the U.S. economy in the year 2000 if these projections are indeed realized?

  [Altman will probably respond that: The Congressional Budget Office notes that if federal spending on health care (Medicare and Medicaid) could be held to its 1991 share of GDP, the nation's growth in the year 2000 would be 2.2 percent higher than CBO currently predicts it to be. [CBO, October 1992] **If he does not mention this point, it is a good one to bring up or around which to frame a question.**]

- As I believe your international comparison chart illustrates, health care spending in Germany has consistently held at around 9%. I know that Germany has a system of universal coverage under which all citizens receive quality, affordable health care. How has Germany been able to do this? What lessons can we draw from their experience?

BACKGROUND:

A. Economic Implications of Rising Health Care Costs
Congressional Budget Office, October 1992

The U.S. spent about 12 percent of the nation's GDP on health care in 1990 -- more than twice the amount spent on national defense and nearly twice the amount spent on education. CBO expects health care spending to grow to 18 percent or more of GDP by the year 2000 -- an increase as large as that between 1965 and 1991. Much of this will result from advances in medicine, but misallocation of resources will grow as well.

Special Characteristics of the Health Care Market:
There is a weak relationship between what U.S. consumers pay for health care and the value they place on health care, because of health insurance and the delegation of treatment authority to providers. Compared with other industrialized countries, the U.S. spends a much greater proportion of GDP on health but does not have a substantially healthier population.

Three characteristics make cost control difficult. First, the system of financing health care is fragmented, raising administrative costs and making piecemeal reform unlikely to succeed, as costs can be shifted from one area to another. Second, this fragmentation gives consumers little bargaining power to negotiate lower prices. Third, the market exercises only loose control over the acquisition of new capacity in the health care system. Additional capacity leads to higher costs.

Why Are Health Costs Rising So Rapidly?
Demographic change, defensive medicine, and the spread of AIDS do not account for much of the increase. Most of the growth is simply from the upward trend in per capita spending for services. Medical technology advances are a major cost factor which faces little market discipline, with no assurance that their costs will be justified by their benefits.

How Rising Costs for Private Health Insurance Affect the Economy:
The sharp rise in health costs, together with slower growth in productivity and total compensation, are the main reasons for the weak growth in workers' real wages and salaries over the past 20 years. Allowing employees to buy health insurance with pretax income encourages them to buy more insurance than they otherwise would. Employer-paid costs tend to be shifted to employees in the form of lower wages or nonmedical benefits. For this reason, rising health costs have little direct effect on the international competitiveness of U.S. firms.

The subsidy borne by the tax system is ultimately paid for by higher taxes, reduced public services, or by future generations in the form of a larger federal debt. An increase in the subsidy (because of higher insurance costs) would probably increase the size of the federal budget deficit under current policy because there is no automatic mechanism to offset such revenue losses with either spending cuts or tax increases.

The Rising Number of Uninsured Workers
In 1990, 33 million people under the age of 65 did not have insurance coverage. By the year 2000, CBO expects that number to grow to almost 40 million. One reason for uninsured workers is the voluntary nature of the system. Low-income workers may prefer higher cash wages, or simply cannot afford insurance. A second explanation is the increased use by insurance companies of experience rating and policies that exclude high-risk people.

The Effects on the Shape and Structure of the Labor Market
Rising health care costs may distort the labor market, as employers move low-wage workers to part-time status with no insurance or eliminate the lowest-paid positions and hire independent contractors. This reduces the flexibility of the labor market.

How Do the Costs of Government Health Programs Affect Government Budgets and the Economy? Medicare and Medicaid are the fastest-growing portions of the federal budget -- from 1 percent of GDP in 1970 to 3 percent in 1991, to an expected 6.1 percent of GDP by the year 2002. The growth alone will cost the government an additional $313 billion in the year 2002. If these cost increases are financed through a larger budget deficit, they will raise the interest costs on the federal debt by $91 billion in 2002.

States spent $100 million on health care in 1991. CBO projects spending will rise to $244 billion by 2000 -- an average increase of more than 10 percent each year. Rising costs are likely to crowd out other state priorities.

Effects on the Federal Budget Deficit
CBO projects that under current policy the federal deficit will swell to more than $500 billion by the year 2002, largely as a result of increased spending for Medicare and Medicaid. CBO calculations suggest that if federal spending on these programs could be held to its 1991 share of GDP, output (real GDP) would be about 2.2 percent higher that the CBO baseline by the year 2002. Incomes (as measured by real gross national product) could rise even more -- by about 2.4 percent -- because servicing costs on debt to foreigners would be reduced. In addition, a reduction in federal borrowing would improve the competitiveness of U.S. industry, as a decline in the real value of the dollar lowers the prices of U.S. tradable products.

B. "Putting People First" on Health Care

1. **National Health Budget:**

   A board of consumers. health providers, business and labor leaders will establish a national budget to contain growing health care costs.

2. **Managed Competition:**

   Managed Competition will make the budget work and maintain quality. Managed competition pools consumers and businesses in large regional groups to increase their bargaining power; and makes health care networks compete by submitting bids, consistent with their budget to provide consumers with a comprehensive plan. In many areas, managed care networks will take some time to develop. During that time, traditional insurance plans will pay doctors and hospitals according to a schedule of fees ensuring that budgets are met.

3. **Insurance Company Regulation:**

   Under the new plan, insurers will be required to compete on fair terms ensuring that recipients receive the highest quality care at the lowest price.

4. **The Plan does the following:**

   - Bans Exclusions for "pre-existing" conditions.
   - Requires "community rates."
   - Ends the "fine print" by requiring policies to cover a core package of benefits including preventive and primary care, illness care, prescription drugs and basic mental health services.

4. **Additional Major Cost Control Steps:**

We will reform medical malpractice laws; eliminate drug price gouging and cut red tape by streamlining billing systems.

5. **Universal Coverage: Privately-Provided, Publicly-Guaranteed**

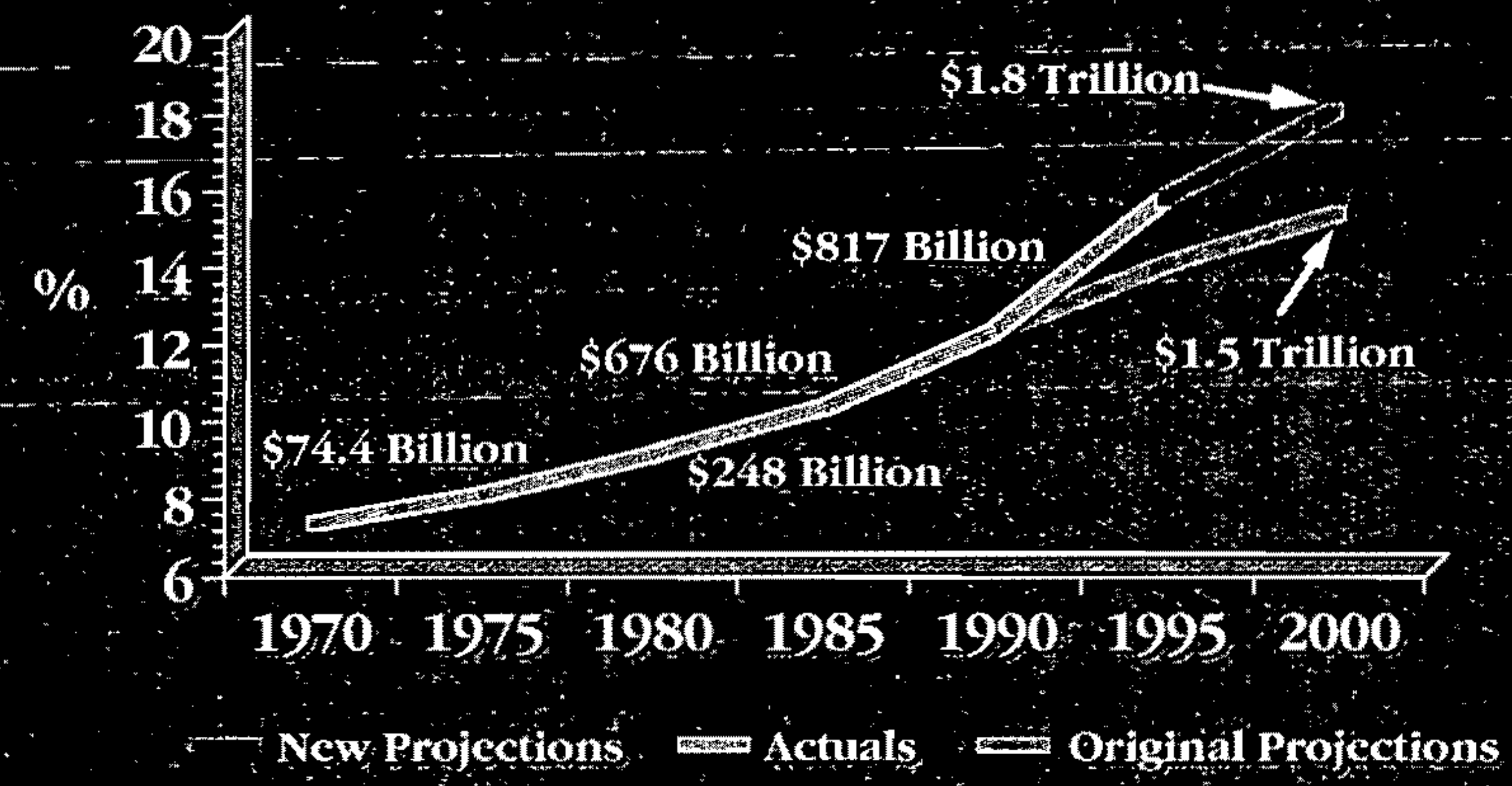
The plan requires employers to insure workers, with tax credits to help build businesses meet their obligations. Businesses can join a purchasing group for cheaper rates and more choices for employers, and the smallest businesses will be phased in last. There is no payroll tax. The plan guarantees that the unemployed will receive private coverage through the purchasing groups based on ability to pay and phases in universal coverage as cost control measures generate savings. Expands long-term care for the elderly and disabled. Increase access to health care providers through expanded school-based, rural and inner-city clinics.

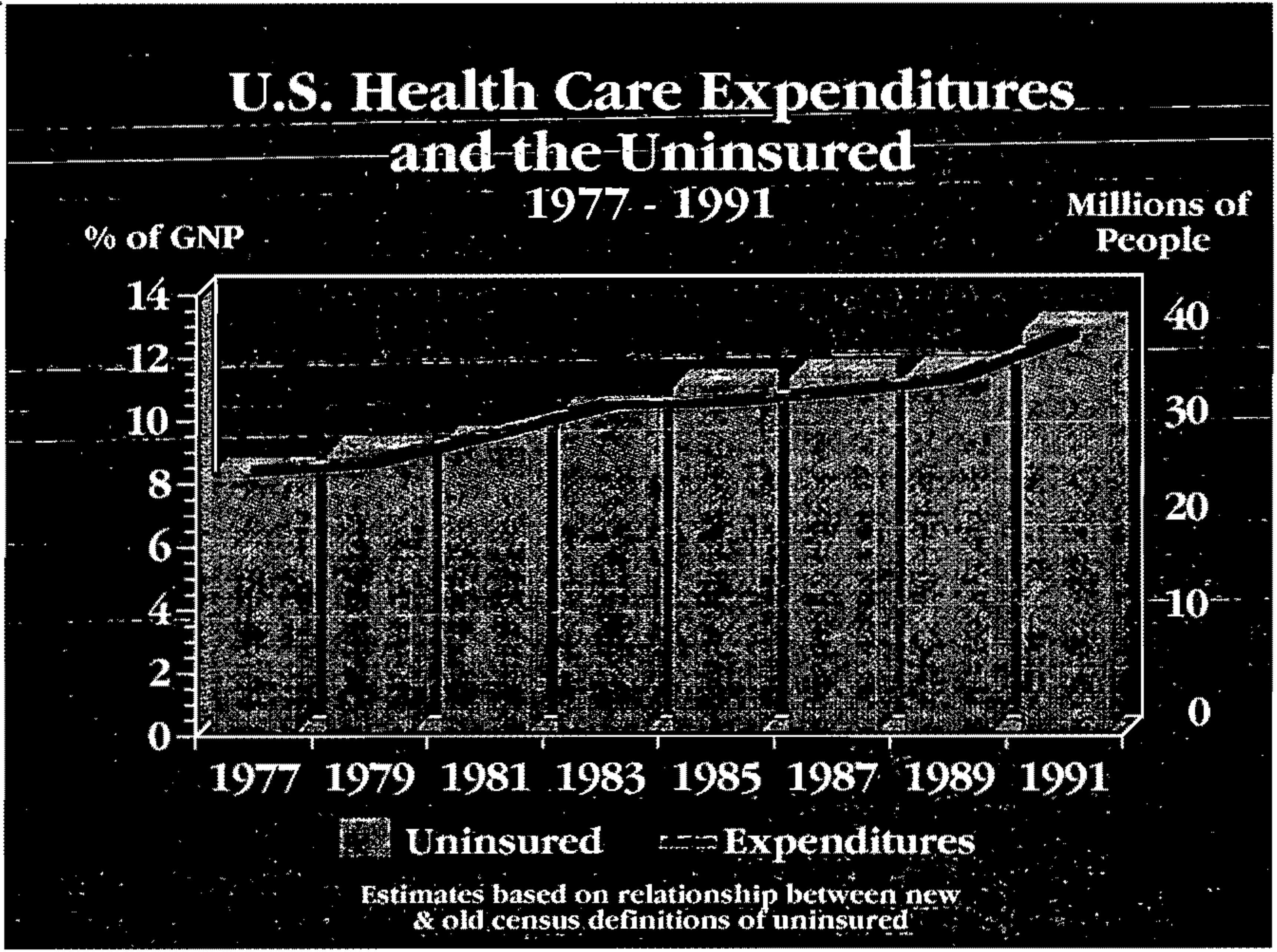
POSSIBLE POINTS OF CONTENTION:

- You may be asked to specify whether, in an attempt to reduce federal expenditures on health care, you would cut Medicare and Medicaid and the extent of these cuts.
- Small business owners are also concerned that health care reforms could impose additional costs on them that they can ill afford.

National Health Expenditures as a % of the Gross National Product

(1995 - 2000 Projected)





U.S. Health Care Expenditures and the Uninsured
1977 - 1991
% of GNP
Millions of People
14
12
10
8
6
4
2
0
40
30
20
10
0
1977 1979 1981 1983 1985 1987 1989 1991
Uninsured
Expenditures
Estimates based on relationship between new & old census definitions of uninsured

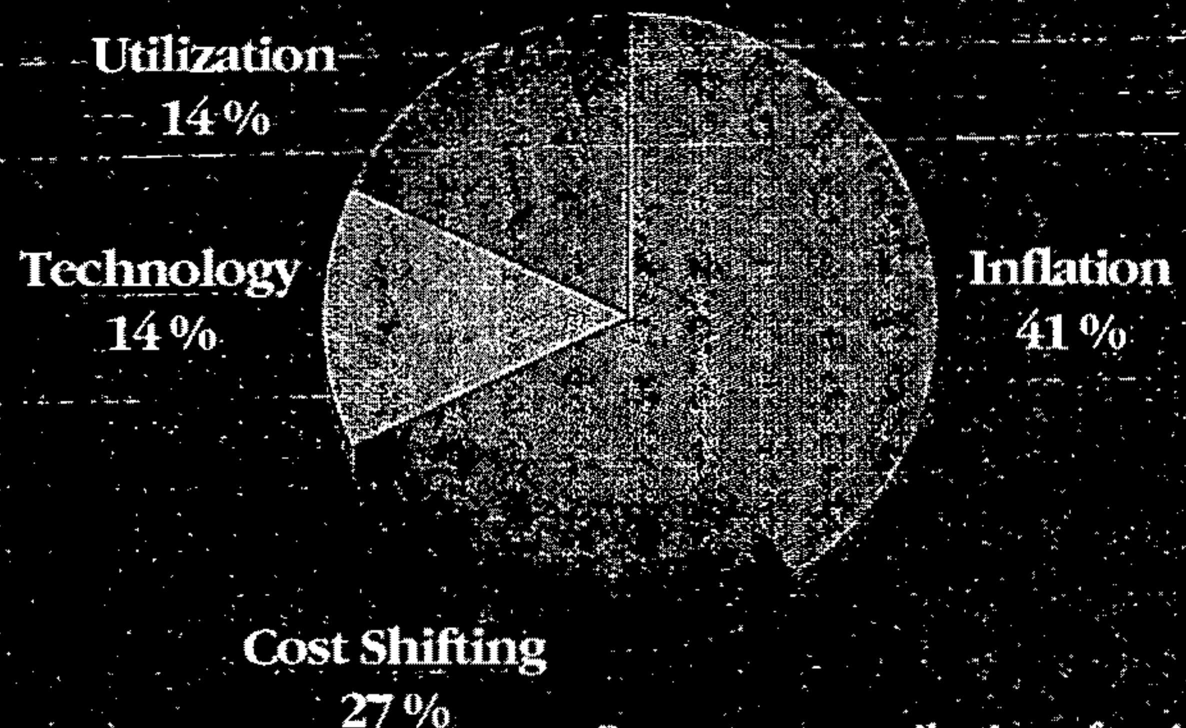
Payments for Hospital Care by Payer Group in 1990

Payer Group	Payment to Cost Ratio	Payment Under or Over Costs (Billions)
Below-cost Payments		
Medicare	89.6%	($8.2)
Medicaid	80.1%	($4.6)
Uncompensated Care	21.0%	($9.6)
Total		($22.4)
Above-cost Payments		
Private Insurers	127.6%	$22.5
Other Govt. Payers	106.4%	$0.2
Total		($22.7)

[1] Operating subsidies from state & local govt. included as payments

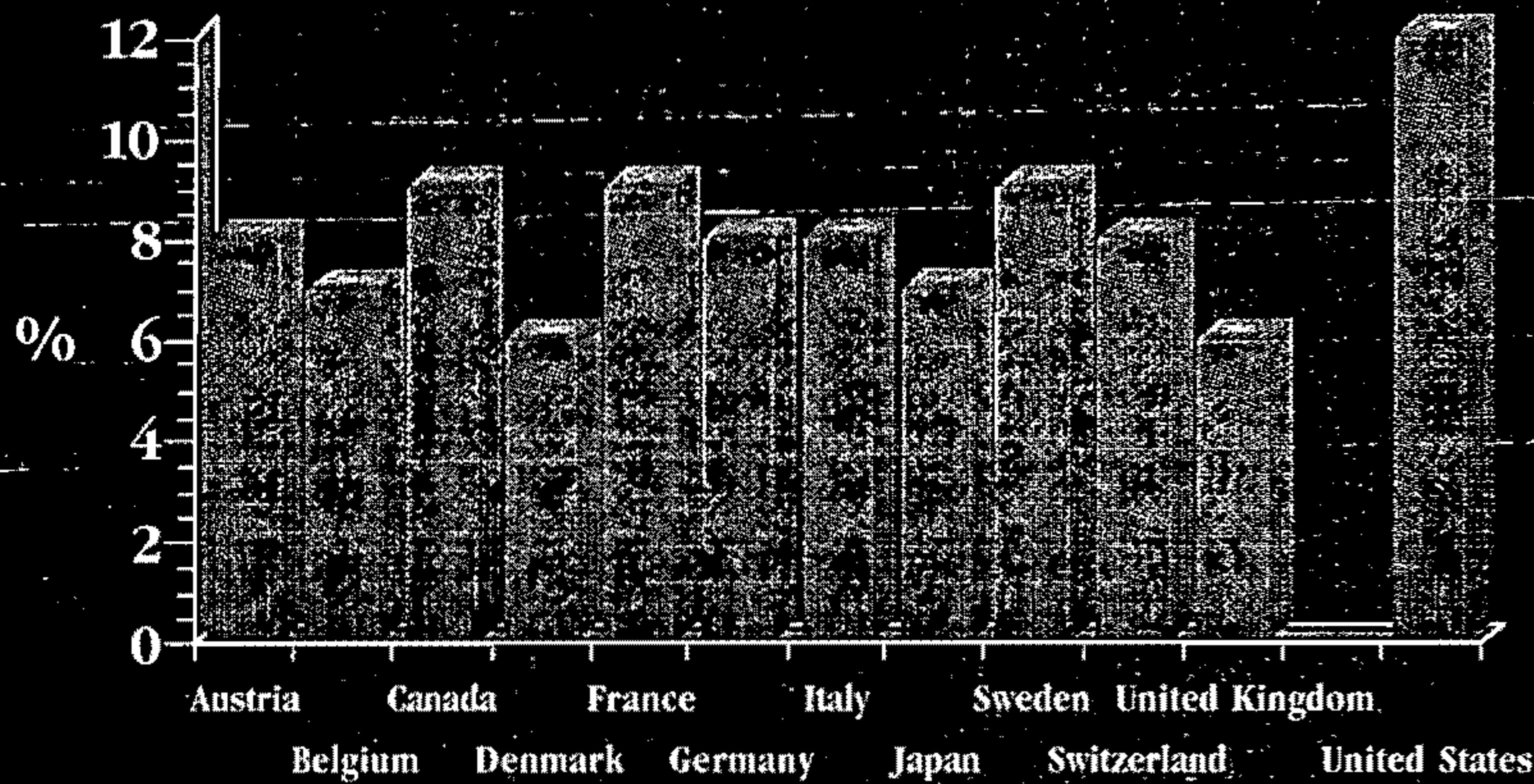
Note: Includes all inpatient & outpatient services

Why Private Health Insurance Premiums Increased

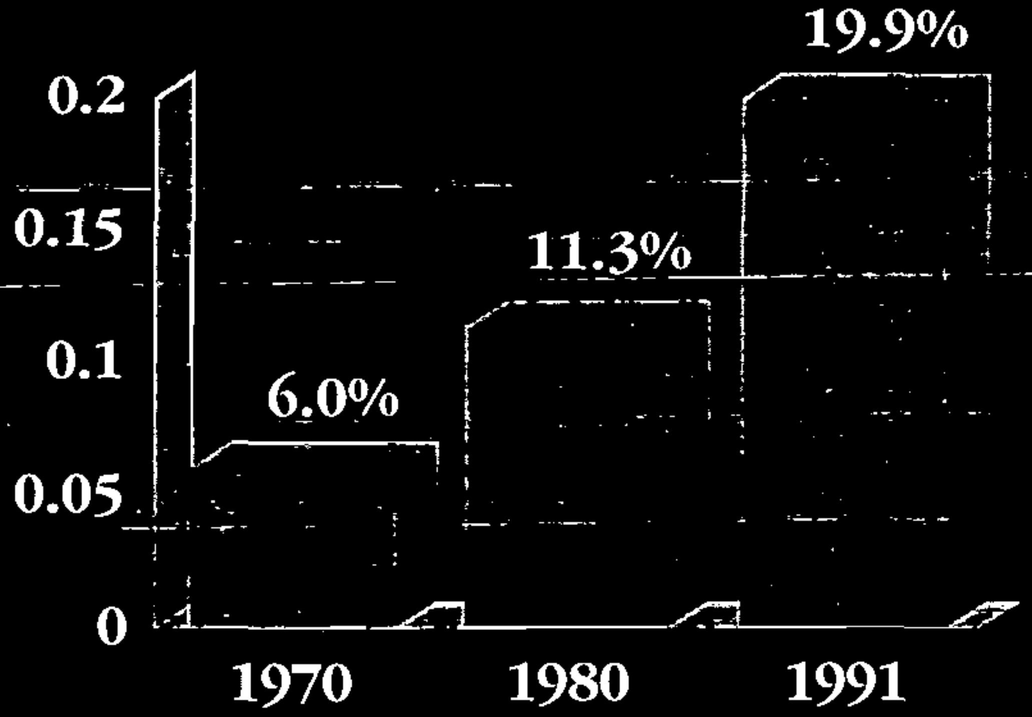


Percentage contribution of various factors to increased indemnity insurance costs in 1990

Health Care Spending as a Share of GDP



Ford Health Care Costs as a Percent of Payroll

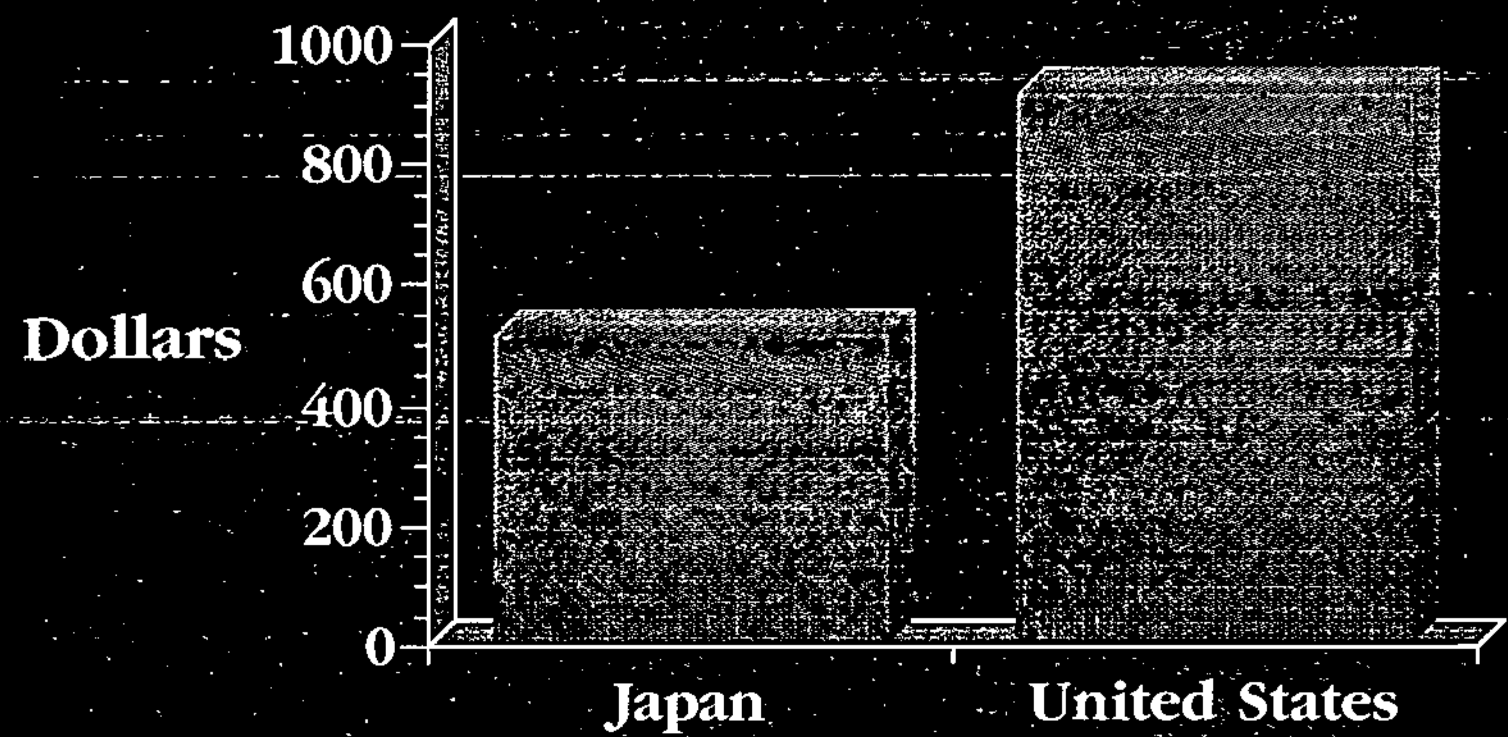


Memo: Costs (Mils)	$144	$552	$1,257

U.S. Health Care Costs Compared With Other Countries

Memo: Ford Cost Index

Health Care Costs per Vehicle



Source: Economic Strategy Institute

Principles For Reform

- Universal Coverage
- Quality Assurance
- Administrative Simplicity
- Cost Containment
- Equitable Financing