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WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

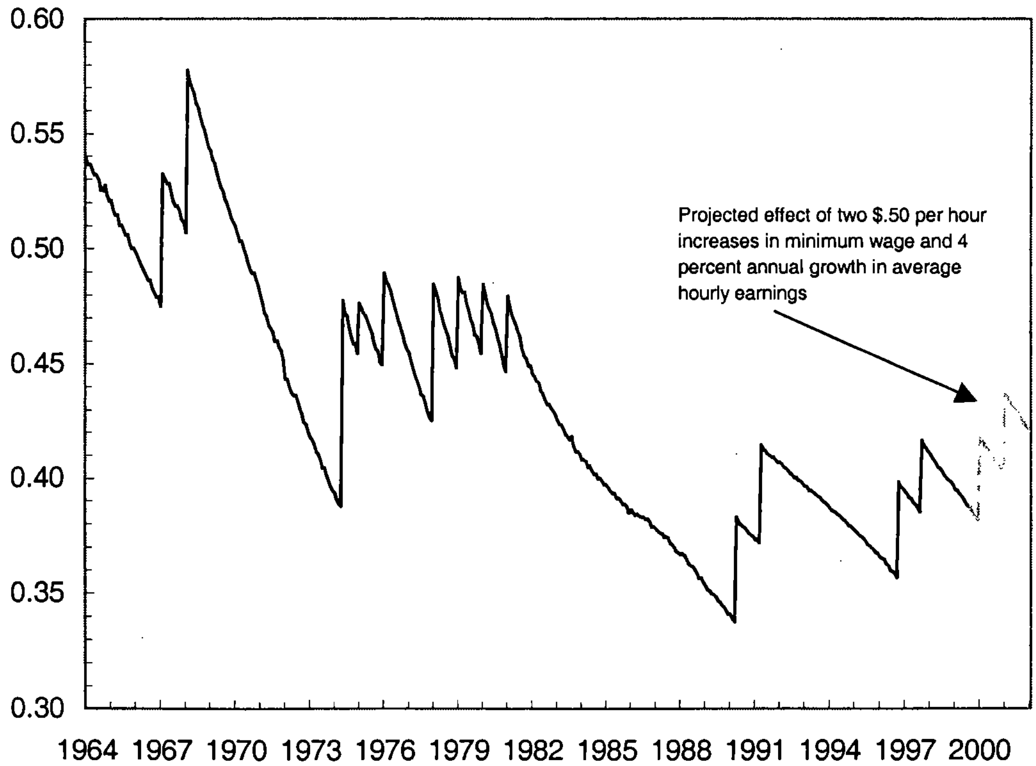
Prepared by the Council of Economic Advisers
with the assistance of the Office of the Vice President

September 24, 1999

copied entire report: Baily/Podesta
pg 6: Sperling/Podesta

CHART OF THE WEEK

Ratio of the Minimum Wage to Average Hourly Earnings



Between the late 1960s and the late 1980s, the minimum wage fell from over 55 percent of average hourly earnings to less than 35 percent of average hourly earnings. Increases in the minimum wage in the 1990s twice pushed this ratio to about 40. The chart shows that two $.50 per hour increases in 2000 and 2001 (along with 4 percent annual growth in average hourly earnings) could push the ratio above recent peaks—though it would start to decline again with continued growth in average hourly earnings.

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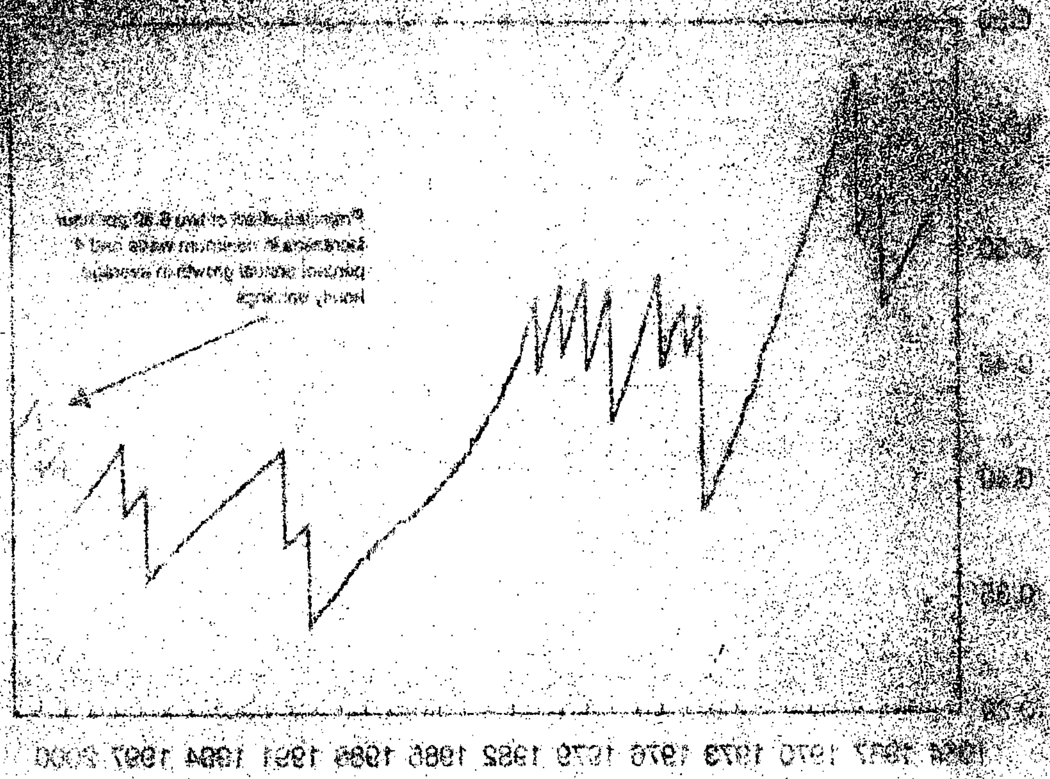
Ratio of Minimum Wage to Average Hourly Earnings



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CONTENTS

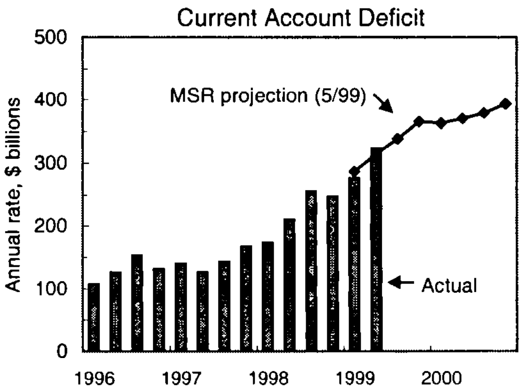
"Gentlemen, it's time we gave some serious thought to the effects of global warming."

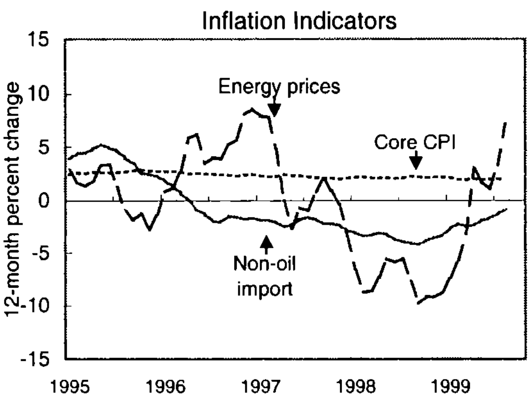
MACROECONOMIC UPDATE

Third Quarter Should Be Strong

Labor market and consumption indicators point to an acceleration of GDP in the third quarter.

Output and demand. Production-worker hours appear to be growing at a 3½ percent annual rate in the third quarter, enough to support about 4 percent real GDP growth. Consumption, which constitutes two-thirds of GDP, appears to be growing at about a 4 percent rate. In addition, orders for capital goods appear strong, and stockbuilding probably will boost third-quarter demand.





Leakage abroad. Some of this robust demand is being met with imports. Over the past year, nominal imports have increased substantially more than exports, a consequence of stronger growth here than among our trading partners and a legacy of a rising dollar from 1995 to 1998. The second-quarter erosion of the current-account deficit had been anticipated in the unpublished detail underlying the Mid-Session Review projection, and the deficit is expected to widen further over the next year-and-a-half (see upper chart).

Inflation. The rate of core consumer price inflation has been well contained at only 1.9 percent for the 12 months through August—down from 2.2 percent during the year-earlier period (adjusted for consistent methodology). However, two of the factors holding down inflation over the past year (falling energy and non-oil import prices) are no longer playing that role (see lower chart). Energy prices have skyrocketed since February, while import prices stopped falling in April. Although rising energy prices may get passed through to prices of other core items, surveys of inflation expectations have remained stable.

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SPECIAL ANALYSIS

Hot Economy, Cool Emissions?

Historically, U.S. carbon dioxide (CO_2) emissions have grown about ¾ percent for every 1 percent increase in real GDP. In 1998, however, CO_2 emission increased only 0.4 percent while GDP grew 3.9 percent. CEA analysis suggests that this slow emissions growth in 1998 can be explained by the strong contribution to growth of high-tech (low emissions) industries and a warm winter. Improvements in technology do not appear to have been unusually large.

Factors influencing emissions. In general, a variety of factors besides growth in aggregate output can affect carbon dioxide emissions, notably the following:

- Structural change. The U.S. economy continues to experience a shift in output away from traditionally energy-intensive manufacturing sectors towards service and high-tech industries.

- Weather. Colder winters increase the demand for heating fuels and hotter summers increase the demand of electricity for cooling. Because heating on a cold day is more energy-intensive than cooling on a hot day, on balance, a warmer year tends to reduce energy use.

- Energy prices. Sharp energy price increases stimulate energy efficiency and reduce CO_2 emissions while sharp energy price decreases can result in higher energy consumption and CO_2 emissions.

- Technological change. Technological improvements can result in reducing the energy consumption necessary to generate a unit of output. Higher energy prices can accelerate the diffusion of more energy-efficient technologies, and government programs aimed at promoting energy efficiency may also facilitate technology diffusion.

What happened in 1998. Output in non-high-tech industries grew just 2.2 percent in 1998—less than the 3.9 percent increase in aggregate GDP and less than the 3.0 percent per year long-term trend rate of growth for this group of industries. This slow growth reflected not only the longer-term shift toward a more high-tech and service economy but also the weakness of several energy-intensive industries, such as steel. Weather, too, played a role in moderating energy use. The 1998 winter was 11 percent warmer than the previous winter. The 1998 summer was also warmer than the previous year's, but the increased emissions from more summer cooling were less than the reduced emissions from less winter heating. Finally, residential energy prices changed little between 1997 and 1998.

In CEA's statistical model of how structural change, weather conditions, and energy prices influenced U.S. CO_2 emissions over the 1962-1998 period, predicted levels of CO_2 emissions were on average within 1 percent of actual emissions. The level of 1998 emissions predicted by the model was very close to (0.1 percent lower than) actual 1998 emissions. This suggests that omitted variables such as short-term technological change were not important determinants of the 1998 decline in emissions.

Conclusion. The continuing transition towards a less energy-intensive high-tech economy and a mild winter resulted in slow CO_2 emissions growth in 1998. Short-term technological improvements did not appear to have a significant effect.

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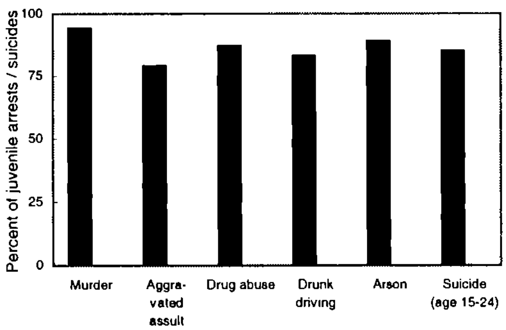
ARTICLE

"Reviving Laertes:" Recent Studies of Boys' Development

After a decade of influential studies on the development of girls, including the 1992 report *How Schools Shortchange Girls* and the 1994 book *Reviving Ophelia*, several recent studies have focused on boys. One important reason not to neglect the development of Ophelia's brother is that socially costly problems of crime and violence remain overwhelmingly problems of boys and men.

Boys' Share of Juvenile Arrests & Suicides, 1997



Crime and suicide. Juveniles arrested for property and violent crimes are overwhelmingly boys (see chart). Male students are substantially more apt to fight at school or to carry a weapon than female students in high school. And the suicide rate of young men aged 15 to 24 is more than five times that of young women that age.

The economic costs of crime and violence arise not only from the financial costs to victims but also from the loss of productive work arising from time spent in criminal activity and premature death. For example, the Justice Department's 1999 national report on juvenile offenders and victims estimates that the cost of a youth's dropping out of high school for a life of crime and drug abuse is between $1.7 and $2.3 million (in present value terms). This figure includes drug treatment and rehabilitation costs, medical costs, criminal justice costs, and victim costs, as well as the value of lost wages and output.

Insights from beyond the dismal science. One sociological insight into boys' greater involvement in crime and violence comes from *Raising Cain*, a recent book co-authored by a professor of public health at Harvard and a child psychologist. The book concludes that above and beyond the role of biology, differences between boys and girls are amplified by a culture that supports emotional development for girls and discourages it for boys. In particular, stereotypical notions of masculine toughness limit boys development of a full range of emotional resources, mitigating an "emotional literacy" needed to read and understand their emotions and those of others. The result, it argues, is that many boys are left to manage conflict, adversity, and change with a limited emotional repertoire, in turn leading to a higher propensity toward conflict and violence.

Conclusion and implications. Recently, researchers have shown an interest in the problems of boys. Besides crime and violence, these include school performance and, to some extent, self-esteem (see box on next page). In the future, the new research, combined with more standard economic analysis of the role of factors like family income and poverty status, might help in the design of

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policies to address problems such as the higher average crime rates and lower average educational attainment of African American boys relative to other boys.

Addressing the problems of boys is also one way to improve the future outcomes of men. With respect to fatherhood, for example, preliminary evidence finds that "emotionally illiterate" boys are more likely to become uninvolved fathers when they are adults. In addition, results from the 1999 National Survey of American Attitudes on Substance Abuse suggest the importance of healthy father-son relationships. It finds in two-parent families that a teenager whose relationship with the father is fair or poor is 68 percent more likely to smoke, drink, and use drugs than one whose relationship is average.

Developmental Differences between Boys and Girls

Besides findings on criminal and violent behavior, recent research has re-examined two other aspects of possible differences in boys' and girls' development that were raised in the earlier research on girls.

- School performance. Boys are more than twice as likely as girls to have a learning disability and two to three times more likely to have an attention deficit problem. From grade school to graduate school, females earn higher grades, on average—even in mathematics and sciences. In high school, girls now equal or outnumber boys in science classes, on average, except for physics. Differences in standardized test scores are small, with females scoring higher in writing ability and reading achievement and males scoring higher in science and mathematics (a gap that is shrinking). Men are a minority of college students (45 percent in 1995) and earn less than half of bachelor's and master's degrees.

- Self-esteem. *Raising Ophelia* argued that girls suffer a severe drop in self-esteem at adolescence, while boys gain in self-assurance as they age. Subsequent, more comprehensive research has revealed a less dramatic gap in self-esteem between genders. For example, a 1997 report found that girls had the advantage over boys in terms of future plans, teachers' expectations, and everyday experiences in school and in the classroom, with minority boys the most likely to feel discouraged about the future and the least interested in getting a good education. A recent study of self-esteem summarizes over 150 previous findings and concludes that males score higher on standard measures of self-esteem than females, but that the differences are small.

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BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

Beige Book Reports Continued Overall Strength. All Federal Reserve district economies continue to exhibit overall strength, with most experiencing moderate-to-brisk rates of growth, according to the Fed's latest summary of commentary on current economic conditions. Retail sales are generally up in most districts, with back-to-school sales meeting or exceeding retailers' expectations in many cases. Vehicle sales remain robust, with some dealers unable to meet demand for popular models. Industrial activity is on the rise in most parts of the country, with orders and production both up. In some cases, resurgent Asian demand is contributing to this rise in activity. Although commentary from most district reports continues to highlight widespread labor shortages, several districts have noted a slackening in the demand for labor. There are few reports of acceleration in nominal wages and salaries, although some districts note a substantial upswing in the cost of health-care benefits. While price pressures at the consumer level remain mostly calm, numerous districts report significant increases in some materials prices. Home sales and construction remain elevated, but many districts have begun to notice a slowdown. The recent drought has worsened crop and livestock conditions in the East and parts of the Midwest.

Many Workers Know Little about Their Pensions. A recent study found that a large percentage of Americans are unaware of basic details concerning their pensions. Only half of the study's respondents correctly identified their pension type. Fewer than half (43 percent) knew, within a year, the eligible date for their early retirement and only 40 percent knew, within a year, the date for normal retirement. According to company data, two-thirds of the respondents will be able to take early retirement by age 55, yet less than half of them think they will be able to do so. Respondents were also confused about the value of their pensions. The researchers expressed concern that many respondents approaching retirement may not be reacting to the correct information, and may be making their decisions based on a faulty understanding of their retirement programs.

Gene —
Summarize
to Sperling
about this

Is the Stock Market Undervalued? The authors of the new book *Dow 36,000* argue that the stock market is currently *undervalued* and that the Dow will rise to 36,000 within 3 to 5 years (compared with today's level of less than 10,500). They cite a study showing that over periods of 20 or more years, a well-diversified equity portfolio is no riskier than an investment in bonds. In their view, investors are catching on fast and will continue to bid up stock prices until the "equity premium"—the excess of stock returns over bond returns—disappears. Although the large size of the equity premium historically (an average of 6.6 percent from 1926-1997, by one estimate) has been a puzzle to most economists, the authors' argument that it will fall to zero has been greeted with skepticism. To the extent that many investors are concerned about short-term fluctuations in stock prices, they may rationally demand some risk premium to compensate for the risk they are taking.

INTERNATIONAL ROUNDUP

Bank of Japan Asserts Its Independence. The Bank of Japan announced on Tuesday that, despite the recent strengthening of the yen, it would not increase Japan's money supply. The announcement, which came immediately after the latest Monetary Policy Meeting, emphasized the central bank's independence and that its policies were never determined in consultation with outside bodies. This announcement was widely seen as rebuking the Ministry of Finance, which reportedly was urging actions to prevent the yen from climbing. An implication of the Bank's announcement is that any intervention in the foreign exchange market would be "sterilized," so that any change in the supply of yen due to the intervention would be offset by other operations in order to keep the money supply unchanged. Foreign exchange interventions are generally more effective if the central bank allows the supply of currency to change. The Ministry of Finance has reportedly been seeking support from other countries for a coordinated intervention in the foreign exchange market. The Bank's announcement appears to make such intervention more difficult. It also seems to have been the cause of an immediate sharp rise in the yen and a sharp drop in the Japanese stock market when it opened the next day.

China Considers Liberalizing Trade in Grains. In a paper for a recent OECD workshop on agriculture, the Vice Director-General of the Chinese State Development Planning Commission urged China to modify its long-held policies supporting a high level of self-sufficiency in grain supply. The paper cites a number of problems associated with that policy, including ecological damage; high costs, which reduce benefits to farmers and increase costs to the government and consumers; and adverse consequences for trade relations, as current self-sufficiency policies oblige the government to impose high protective tariffs that violate WTO rules. The paper recommends that China's grain self-sufficiency decline to 90 percent within the next 30 years and advocates a number of adjustments to current Chinese protective trade policies, including lowering import tariffs and eliminating the state monopoly on grain imports and exports.

OECD Assesses Implementation of Jobs Strategy. Countries that have taken substantial steps to implement the OECD's Jobs Strategy have seen employment gains, according to a new OECD assessment. The report finds, however, that youth, older workers, and the low-skilled still face poor employment prospects and a low quality of available jobs in most OECD countries. It finds that countries that have been more successful in achieving a smooth transition from school to work for those with poor qualifications focus on providing them with recognized vocational qualifications and reinsertion programs for school drop-outs. ~~The report also~~ notes several adverse consequences of policies that had tended to increase incentives for early retirement in many countries. While recent pension reforms have typically addressed these incentives by strengthening the link between lifetime contributions and pension benefits, most OECD countries still have other programs, such as unemployment insurance or disability benefits, with adverse employment incentives.

RELEASES THIS WEEK

U.S. International Trade in Goods and Services

The goods and services trade deficit rose to $25.2 billion in July from $24.6 billion in June.

MAJOR RELEASES NEXT WEEK

Consumer Confidence—Conference Board (Tuesday)
Advance Durable Shipments and Orders (Wednesday)
Gross Domestic Product (Thursday)
NAPM Report on Business (Friday)

U.S. ECONOMIC STATISTICS

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

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

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

FINANCIAL STATISTICS

	1997	1998	July 1999	August 1999	Sept. 23, 1999
Dow-Jones Industrial Average	7441	8626	11052	10935	10319
Interest Rates (percent per annum)					
3-month T-bill	5.06	4.78	4.55	4.72	4.69
10-year T-bond	6.35	5.26	5.79	5.94	5.87
Mortgage rate, 30-year fixed	7.60	6.94	7.63	7.94	7.76
Prime rate	8.44	8.35	8.00	8.06	8.25

INTERNATIONAL STATISTICS

Exchange Rates	**Current level September 23, 1999**	**Percent Change from**	
		Week ago	**Year ago**
Euro (in U.S. dollars)	1.042	-0.0	N.A.
Yen (per U.S. dollar)	104.2	-0.9	-23.6
Major currencies index (Mar. 1973=100) (trade-weighted value of the U.S. $)	92.79	-0.3	-4.6

International Comparisons [1/]	**Real GDP growth** (percent change last 4 quarters)	**Unemployment rate** (percent)	**CPI inflation** (percent change in index last 12 months)
United States	3.9 (Q2)	4.2 (Aug)	2.3 (Aug)
Canada	3.7 (Q2)	7.7 (Jul)	2.1 (Aug)
Japan	1.1 (Q2)	4.9 (Jul)	-0.1 (Jul)
France	2.1 (Q2)	11.3 (Jun)	0.3 (Jun)
Germany	0.6 (Q2)	7.1 (Jul)[2/]	0.6 (Jul)
Italy	0.8 (Q2)	12.1 (Apr)	1.7 (Aug)
United Kingdom	1.4 (Q2)	6.1 (May)	1.1 (Aug)

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

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