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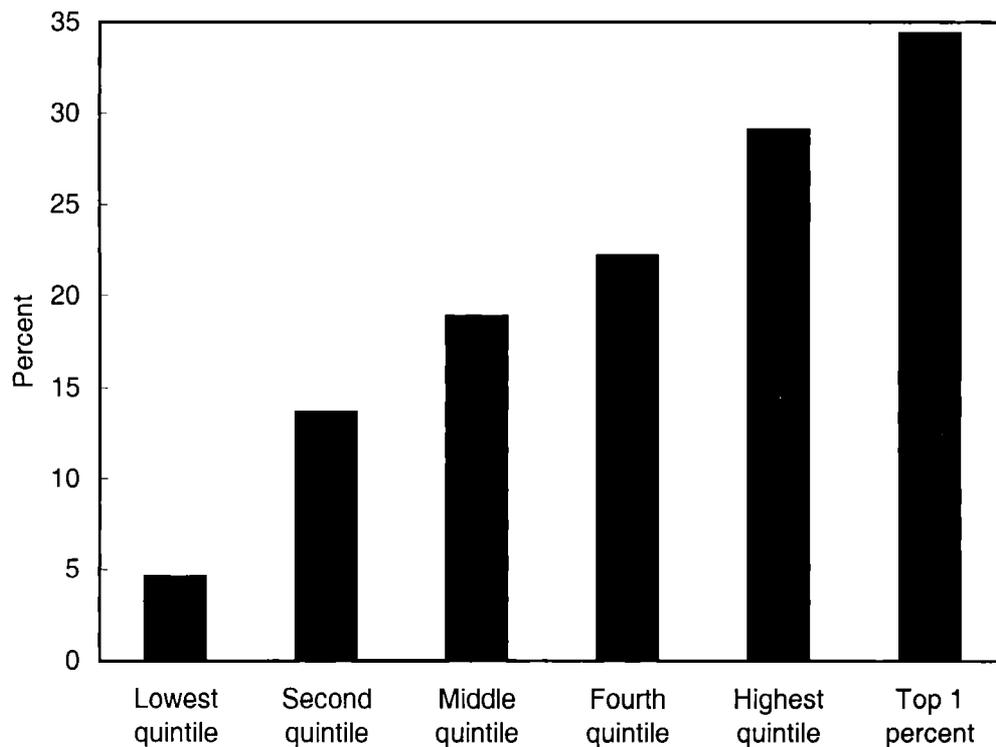
WEEKLY ECONOMIC BRIEFING OF THE PRESIDENT OF THE UNITED STATES

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

April 21, 2000

CHART OF THE WEEK

Effective Federal Tax Rates by Income



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

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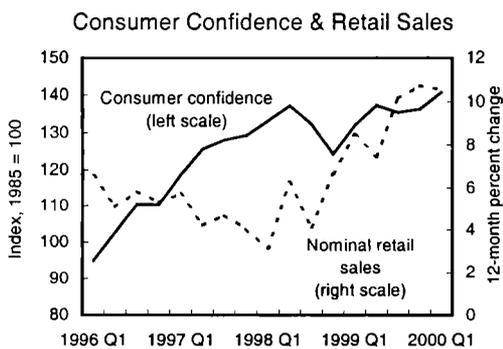
"Uh-oh. The so-called marriage penalty."

MACROECONOMIC UPDATE

First Quarter Looks Strong

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

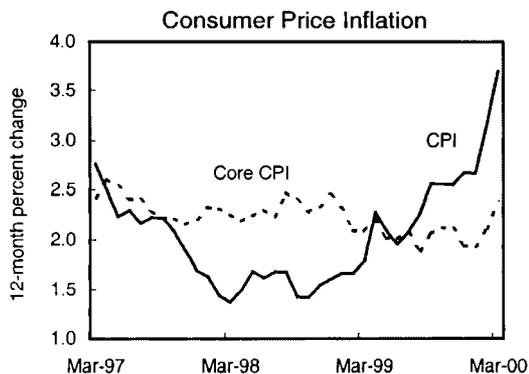
Continued strong demand. The strong economy and a stock market up 3.5 percent over the first



quarter propelled consumer confidence to an all-time high (see upper chart). Retail sales surged in the first quarter, with motor vehicles selling at a record 18.1 million unit annual pace. Real personal consumption is now projected to increase about 8 percent at an annual rate in the first quarter. Residential investment seems to have been strong, but forward-looking housing indicators point to a decline in the second quarter.

It is worth noting that recent stock market declines should have little immediate effect on spending.

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



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

SPECIAL ANALYSIS

Why Isn't Japan a New Economy Too?

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

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

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

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

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

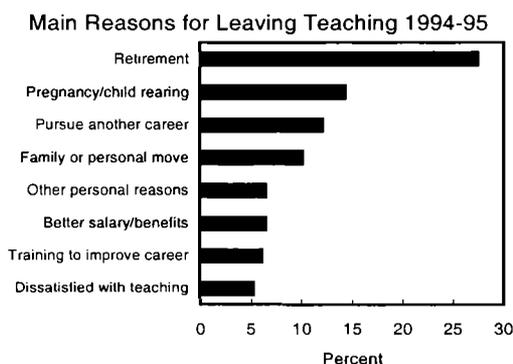
improve the outlook for Japan's economy. First, it is important for Japan to use coordinated monetary and fiscal policy to stimulate demand and improve consumer and business confidence. Second, structural reforms including deregulation of product markets and reform of financial markets are needed to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

ARTICLE

Encouraging Teachers to Stay

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

Reasons for leaving. About 6 percent of public school teachers leave their profession each year. Retirement and family decisions are among the leading reasons why teachers left the profession in 1994-95, according to national survey



data (see chart). Other reasons, however, are more likely related to working conditions and compensation, including “to pursue another career,” “for better pay or benefits,” and “dissatisfaction with teaching as a career.”

Satisfaction not guaranteed. For the 20 percent of respondents who cited “dissatisfaction with teaching as a career” as one of their *three* main

reasons for leaving the profession, the survey asked respondents to identify their main area of dissatisfaction. Many of the answers relate to working conditions. The most frequently cited areas were a lack of recognition or support from the school administration (29 percent), student discipline problems (18 percent), poor student motivation to learn (18 percent), and poor salary (11 percent). A different study on what matters for job satisfaction among current teachers finds a similar ranking. In addition, it concludes that factors difficult to change, such as school size, minority enrollment, teacher race or gender, or years of teaching experience are only weakly related to job satisfaction. The statistical analysis also suggests that compensation makes only a small contribution to job satisfaction.

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

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

Are Teacher Salaries Competitive?

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

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

BUSINESS, CONSUMER, AND REGIONAL ROUNDUP

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

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

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

INTERNATIONAL ROUNDUP

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

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

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

RELEASES THIS WEEK

U.S. International Trade in Goods and Services

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

Housing Starts

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

MAJOR RELEASES NEXT WEEK

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

U.S. ECONOMIC STATISTICS

	1970- 1993	1999	1999:2	1999:3	1999:4
Percent growth (annual rate)					
Real GDP (chain-type)	2.9	4.6	1.9	5.7	7.3
GDP chain-type price index	5.2	1.6	1.3	1.1	2.0
<u>Nonfarm business (NFB) sector:</u>					
Productivity (chain-type)	1.7	3.6	0.6	5.0	6.4
Real compensation per hour:					
Using CPI	1.0	1.7	1.4	2.1	0.8
Using NFB deflator	1.5	3.0	2.9	4.0	2.1
Shares of Nominal GDP (percent)					
Business fixed investment	11.4	12.6	12.6	12.7	12.5
Residential investment	4.5	4.4	4.5	4.4	4.4
Exports	8.2	10.8	10.7	10.8	10.9
Imports	9.2	13.5	13.4	13.8	14.0
Personal saving	6.6	1.7	1.8	1.5	1.3
Federal surplus	-2.8	1.2	1.3	1.4	1.2
<hr/>					
	1970- 1993	1999	January 2000	February 2000	March 2000
Unemployment Rate (percent)	6.7**	4.2**	4.0	4.1	4.1
Payroll employment (thousands)					
increase per month			394	7	416
increase since Jan. 1993					21213
Inflation (percent per period)					
CPI	5.8	2.7	0.2	0.5	0.7
PPI-Finished goods	5.0	3.0	0.0	1.0	1.0

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

FINANCIAL STATISTICS

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

INTERNATIONAL STATISTICS

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

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

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

2/ Data from OECD standardized unemployment rates.