

cc to Gus F.



The Secretary of the Treasury

October 15, 1997

NOTE FOR JON GRUBER

FROM: BOB RUBIN

Page 1 -- Climate Change

You may well be right.

Child Care

Good -- I gather you prevailed.

Page 2 -- Affirmative Action in Federal...

In what respect?

Attachment



October 7, 1997

INFORMAL

To: The Secretary
The Deputy Secretary
From: Jon Gruber JG
Re: Economic Policy Weekly Report

to: Jon Gruber

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Work on Presidential Initiatives

Climate Change: The NEC options memo was submitted to the President on October 5, and we are awaiting his guidance on the issue. Treasury and the other economic agencies supported a least-cost gradual approach to reducing emissions, while the NEC and CEQ supported a more aggressive approach, with a "safety valve" that would limit costs. We have expressed concerns that this safety valve may be lost in the process, leaving us only with the more aggressive, and costly, emissions limits. We will be meeting this week to discuss issues related to the international negotiation of this type of commitment.

you may well be right.

Child Care: At an October 1 interagency meeting on the Administration's child care initiative, chaired by the DPC and the First Lady's Office, Treasury highlighted its opposition to using the tax system to assist low-income families in paying for child care. Of particular concern to us is the fact that it would be difficult to increase the number of families receiving tax-based subsidies without making the credit refundable, which would be very difficult politically. HHS presented options on how an expanded direct subsidy program could reach more low-income families, a concept we strongly support. The interagency group will be focusing its efforts, in the near-term, on the President's child care conference on October 23.

Good - I get the you prevailed

Electricity Restructuring: The NEC would like to include one aspect of our electricity restructuring legislation, the Renewable Portfolio Standard (which mandates that a certain share of generation be from renewable energy sources), in the rollout of our climate change plan. There is general consensus on this issue, so long as (from the perspective of the economic agencies) it includes a cap on the increases that it might impose on electricity prices. For example, we have proposed that the RPS would only bind so long as the cost of purchasing renewable generation is less than one cent per KW-hour more than non-renewable; once the price differential grows to one cent, the government would cap this requirement. We are working out the details of this approach with the Energy department. There may be a Principals meeting on this issue in the near future.

EXECUTIVE SECRETARIAT

Tobacco: Economic Policy continues to examine issues related to the proposed Tobacco Settlement, including: measuring the effect on underage smoking from the non-price aspects of a settlement (e.g. marketing and retail restrictions); examining the likely size of the price increase that would be passed through from industry payments; and understanding related anti-trust issues.

Disaster Insurance: Economic Policy is working with Domestic Finance to structure a proposal for a limited government role in private capital markets for disaster insurance. In this role the government would support the developing private market securitization of catastrophe reinsurance by addressing identified market failures and by validating the emerging standardization of bond contracts and the risk modeling. We are meeting with Domestic Finance and Legislative Affairs to consider merits of this option relative to other possibilities, with the aim of providing a proposed policy to the Deputy Secretary soon.

Affirmative Action in Federal Contracting: We are working with the Commerce Department to develop measures of federal utilization of minority-owned businesses in particular industries, as well as the capacities of such firms. This effort is in response to a 1995 Supreme Court decision limiting the ability of the federal government to use contract set-asides. We expect the results of this project will generate considerable controversy when Commerce presents them, most likely at the end of October.

Children and Environmental Health and Safety Risks: On October 8, Economic Policy will be attending the first meeting of an interagency working group on children's health and safety and the environment, chaired by the EPA. This effort is in response to an Executive Order President Clinton issued in April, requesting that federal agencies identify and assess environmental health and safety risks that affect children.

FASB Draft Standards: Economic Policy is working with Domestic Finance to review a Financial Accounting Standards Board draft standard on accounting for derivative and derivative-like instruments and hedging. From our perspective, the most objectionable aspect of the proposed standard is that it would force businesses to apply different methods in accounting for inflation-indexed securities than are used for conventional securities. We are preparing a letter to FASB from the Deputy Secretary expressing this and possibly other concerns related to the proposed standard.

Interest on Reserves: We are also working with Domestic Finance to evaluate whether the Federal Reserve should be allowed to pay interest on reserves, and whether banks should be allowed to pay interest on demand deposits. Both the Federal Reserve and commercial banks favor the idea.

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Major Economic Indicators in the Past Week (Through October 7)

The **unemployment rate** remained unchanged at 4.9 percent in September. **Payroll employment** rose by 215,000, after an increase of only 40,000 in August and an outsized 384,000 advance in July. August was depressed by the UPS strike and September was boosted when strikers returned to work. September results were also affected by a large 78,000 drop in government employment, stemming mainly from seasonal adjustment problems. After sorting out some of these distortions, the latest results suggest the possibility of moderation. Private industry employment on a strike-adjusted basis was up by 127,000 in September, little different from the August pace, but down from 304,000 in July and gains averaging 212,000 during the first half of the year. **Average hourly earnings** edged up by only 0.3 percent in September despite the 8.4 percent hike in the minimum wage. Over the past 12 months, earnings are up a moderate 3.6 percent in nominal terms but 1-1/2 percent in real terms.

Unit sales of new cars and light trucks declined by 3-1/2 percent in September to a 15.0 million unit seasonally adjusted annual rate from the strong 15.5 million pace of each of the previous two months. The September result nonetheless matches the sales figure for the year-to-date, as well as for all of 1996. Sales for the entire third quarter strengthened considerably, rising to a 15.3 million unit annual rate from the soft 14.5 million pace of the second quarter.

Bolstered by a jump in orders for durable goods, **manufacturers' new orders** rose by 1.3 percent, about double the rate of monthly gain averaged so far this year. Orders and shipments of nondefense capital goods excluding aircraft (an indicator of current investment) fell but earlier gains point to another good increase in capital equipment spending in the third quarter.

Inventories held by manufacturers rose by 0.4 percent in August, in line with recent growth. The inventory-shipments ratio rose because of a drop in shipments, but remains at a very low level.

Construction expenditures dipped 0.3 percent in real terms in August, following a 1.5 percent advance in September. Through the first two months of the third quarter, real construction spending is up at a 3-1/2 percent annual rate, about the same pace as in the second quarter.

The **National Association of Purchasing Management's index** of industrial activity declined in September to 54.2 percent from 56.8 percent in August. The decline indicates only a slowdown in industrial activity for the month, but any reading above 50 percent suggests continued expansion and the index has been above 50 for sixteen straight months.

The **composite index of leading economic indicators** rose by 0.2 percent in August, in line with average growth over the past six months. The index points to continued moderate economic expansion.

Indicators Scheduled for Next Week (Through October 14)

Consumer Credit, August (October 7)

Wholesale Trade, August (October 8)

Producer Price Index, September (October 10)

EP Schedule (Robert Gillingham and Jon Gruber)

Tuesday, October 7

- Kids Health Implementation Meeting (@OEOB)
- Weekly Health Strategy Meeting with Chris Jennings (@OEOB)

Wednesday, October 8

- No external meetings scheduled

Thursday, October 9

- No external meetings scheduled

Friday, October 10

- No external meetings scheduled

The Week Ahead:

Monday, October 13

- No external meetings scheduled

Tuesday, October 14

- Kids Health Implementation Meeting (@OEOB)
- Weekly Health Strategy Meeting with Chris Jennings (@OEOB)

Wednesday, October 15

- Poverty and Children's Well-being Conference (sponsored by HHS)

Thursday, October 16

- No external meetings scheduled

Friday, October 17

- No external meetings scheduled