



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 2, 1997

To: The Secretary
The Deputy Secretary

From: Jon Gruber *JG*

Re: Economic Policy Weekly Report

Work on Presidential Initiatives

Climate Change: A planned series of cabinet-level discussions will continue over the next several weeks, to prepare the cabinet and President for a decision in October on a possible new U.S. commitment on climate change. The Assistant Secretaries' group continues to prepare option papers to support this decision. We are working with EPA in drafting a paper on domestic emissions trading. We are also preparing a stand along piece laying out our view of the likely role of technology in helping to meet any emissions targets we might sign on to, and the proper role of government in helping foster the development of new technology. On the latter issue, our views differ sharply from those of others in the Administration. We are also working with CEA on estimating the relative costs of attaining different emissions targets, and the implications of meeting any given target according to different timetables.

Electricity Restructuring: There will be an NEC Deputies meeting on September 5 to discuss 1) a new Federal tax on electricity sales with the receipts earmarked for a public benefits fund (PBF), and 2) a renewable portfolio standard that would require electricity generators to produce a certain percentage of their output with energy sources other than nuclear-, hydro-, or carbon-based systems. Since the last NEC Deputies meeting on August 8, Treasury, OMB, CEA, and Commerce staff have been negotiating with DoE and EPA staff to develop an alternative to the PBF that is politically saleable and more efficient. We hope to have this alternative worked out by the September 5 meeting.

Child Care: We have been attending initial meetings of the interagency process on child care policy with the White House, Labor, HHS, CEA, and the First Lady's office. We will work with Tax Policy to evaluate alternative policy instruments to increase the affordability of child care. We are also working to remind other agencies of the tradeoffs between mandates to increase child care quality and the affordability of market child care for low income families.

Children's Health: The recently enacted children's health package involves a complicated set of implementation issues, and the states are looking to the administration for guidance. We will work with HHS to provide this guidance, in particular focusing on

1) mechanisms to limit the substitution of public insurance for employer-provided coverage, and 2) a proper evaluation structure for these important changes in state insurance policy.

Medicare: We will be working closely with Tax Policy on the implementation of the Medical Savings Account demonstration that was mandated by the recent budget bill. We are also beginning discussions with other agencies, including the White House and HHS, about reintroducing the concept of means-tested Part B premiums after the idea was tabled at the end of the budget debate.

Higher Education Financial Aid: As noted previously, the Department of Education has chosen to reduce the taxation of assets under its financial aid formula. We support this effort. As anticipated, they have run into strong opposition from the financial aid community over this proposal. We are working with ED to develop analyses that support their position. We will be drafting a memo for the Deputy Secretary to send to Mike Smith, offering our support and providing evidence that the distributional impacts of their proposal will be minimal.

Personal Bankruptcy Reform: We have been tasked by the NEC with producing the options paper for personal bankruptcy reform by next week. We plan to disagree with the forthcoming recommendations of the (non-binding) Bankruptcy Reform Commission in several areas. In general, the recommendations of this commission will be much too pro-debtor, in an environment where personal bankruptcy is growing out of control (more than 1.2 million expected this year). We plan to propose an alternative which 1) includes substantially lower uniform national asset exemption levels for those filing bankruptcy, and 2) introduces a need-based system which leads to income-based repayments for those high income filers requesting bankruptcy protection. We are consulting with Legislative Affairs to assess the political forces involved in this debate and to help guide our policy development in this area.

District of Columbia: Staff is preparing background materials for several upcoming community meetings to discuss tax and other provisions of recent legislation which restructured the relationship between the District of Columbia and the federal government. Staff continues to meet with local civic leaders to explore alternatives to the economic development corporation which was not included in recent legislation for the District of Columbia.

Encryption: An NSC interagency working group will meet on September 5 to identify countries with effective anti money-laundering laws. Under proposed export regulations, US exporters would be able to receive general export licenses to sell very strong encryption products without key recovery capability to banks and financial institutions in those countries. Applications to export such products to banks and financial institutions in all other countries would be reviewed on a case-by-case basis.

Tobacco: Economic Policy continues to work on issues related to the proposed Tobacco

level in July after rising by 3.2 percent in June. Sales of new single-family homes jumped by 5.2 percent in June and edged up further in July, while resales of existing homes increased by 2.2 percent in July. Real residential investment rose at a strong 7.1 percent annual pace in the second quarter.

Industrial production increased by 0.2 percent in July, held down by a decline in auto output. Excluding the auto sector, production increased 0.3 percent. The capacity utilization rate declined in July to 83.1 percent from 83.3 percent in June.

While new orders for durable goods edged down by 0.6 percent in July, underlying strength in the durable goods sector was impressive. July orders were held back by a large drop in the volatile aircraft component. Orders for nondefense capital goods excluding aircraft, in contrast, jumped by 5.3 percent, and shipments of these goods imply continued growth in capital equipment investment in Q-III.

The first look at the manufacturing sector in August shows some moderation in growth. The **National Association of Purchasing Management Index** dipped to 56.8 percent in August from 58.6 percent in July, with growth in both production and new orders slowing slightly. Indicators of price and capacity pressures, such as the NAPM price index and the suppliers' delivery index, edged up slightly.

Indicators Scheduled for Next Week (Through September 9)

- Leading Economic Indicators, July (September 3)
- Construction Expenditures, July (September 3)
- Manufacturers' Orders and Inventories, July (September 4)
- New Car and Light Truck Sales, August (September 4)
- Employment Report, August (September 5)
- Consumer Installment Credit, July (September 8)
- Productivity and Labor Costs, Revised Q-II (September 9)
- Wholesale Trade Inventories, July (September 9)

EP Schedule (Robert Gillingham and Jon Gruber)

Tuesday, September 2

- Weekly Health Strategy Meeting (@OEOB)

Wednesday, September 3

- Meeting on Income Related Premium and Medical Savings Accounts (@OEOB)

Thursday, September 4

- No external meetings scheduled

Friday, September 5

- Meeting on Voluntary Purchase Cooperative for small business health insurance purchases (@OEOB)

The Week Ahead:

Monday, September 8

- No external meetings scheduled

Tuesday, September 9

- Weekly Health Strategy Meeting (@OEOB)

Wednesday, September 10

- Child Health Care Meeting (@HHS)

Thursday, September 11

- No external meetings scheduled

Friday, September 12

- No external meetings scheduled