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Economic Pack

Committee on Political Education, AFL-CIO
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AMERICAN FEDERATION OF LABOR & CONGRESS OF INDUSTRIAL ORGANIZATIONS
AFL-CIO

political memo from COPE

GEORGE MEANY, Chairman WM. F. SCHNITZLER, Secretary-Treasurer AL BARKAN, National Director

NO. 11—64 JUNE 1, 1964

LBJ's First Six Months . . .

His Brand Is On The Office

Lyndon Johnson, in his first six months as President, has imprinted his brand unmistakably upon the office, the government and the nation.

He has been an activist President, so active that Washington reporters are making a career of tabulating his speeches, press conferences, trips, White House Rose Garden statements, and handshakes. He has made more than 200 speeches, conducted scores of press conferences, and has shaken more hands than reporters can count. They are awestruck by his energy.

But more important than the quantity of activity is its quality. To weigh this, the Memo below prints Johnson quotes on specific issues, and the deeds that have backed up his words.

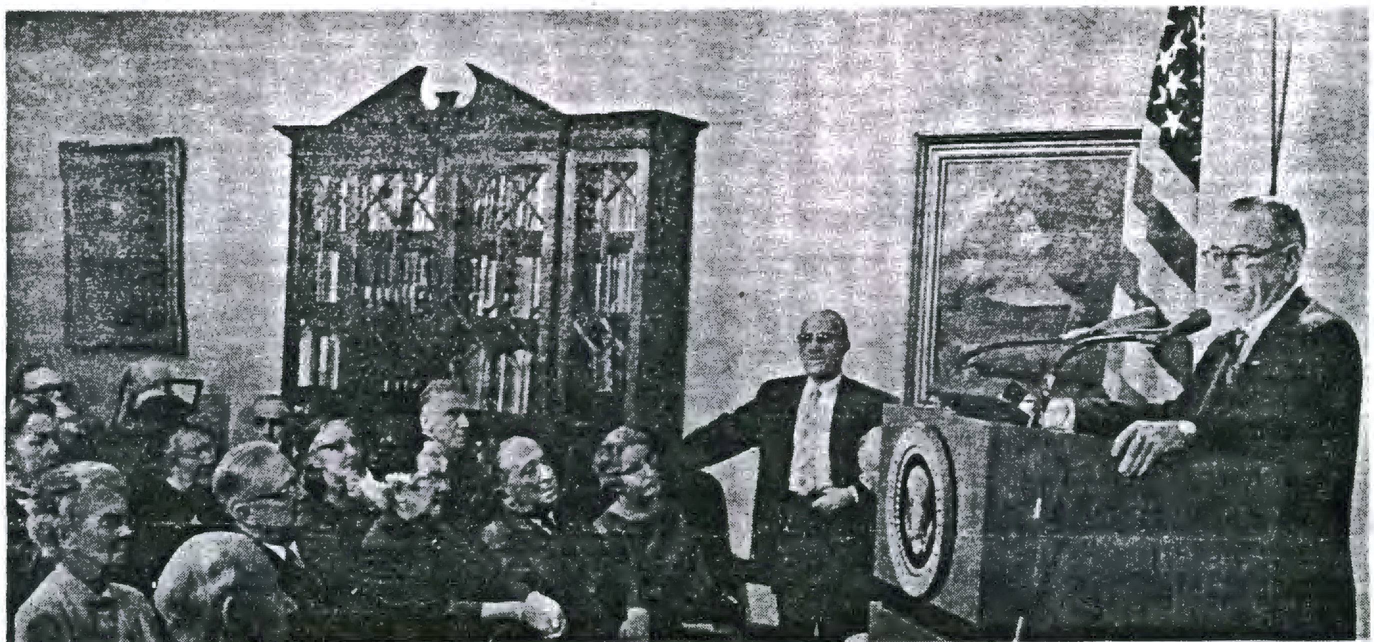
CIVIL RIGHTS

"Today, Americans of all races stand side by side in Berlin and in Viet Nam. They died side by side in Korea. Surely, they can work and eat and travel side by side in their own country."—State of the Union message, Jan. 8, 1964.

"We have talked long enough in this country about equal rights. We have talked for 100 years or more.

(Continued on page 2)

GREETING AFL-CIO EXECUTIVE COUNCIL MEMBERS—A promise to spur the economy to new heights. "I don't intend to sit idly by while this problem of unemployment swells and coarsens."



ADDRESSING SENIOR CITIZENS REPRESENTATIVES—A strong bid for health care under social security. "It is practical. It is sensible. It is fair. It is just."

(Continued from page 1)

It is time now to write the next chapter and to write it in the books of law."—First address to Congress as President, Nov. 27, 1963.

The President has made clear he considers full equality for all Americans a paramount goal of his administration. He has made a personal crusade for civil rights. He injects the issue into his speeches, statements, press conferences, off-the-cuff remarks in the White House Rose Garden. No President before him has addressed a southern audience with an impassioned appeal to bury the "dead issues" of the past and to get on with the business of the present unencumbered by prejudice. Johnson did just this in a recent speech in Atlanta before a group that included members of the Georgia State Legislature.

Prodded by the President, the House of Representatives acted quickly on the civil rights bill soon after Johnson took office. With bipartisan support and leadership, the bill was approved, 290-130.

Dixiecrats in the Senate, however, now have filibustered for more than two months in an attempt to block or seriously weaken the House bill. The President has brought to bear all the pressure and persuasion of his office in support of the bill. But in the end, only cloture—shutting off filibuster by vote of two-thirds of senators present and voting—or the threat of cloture, seems likely to achieve the results the President so persistently has fought for.

POVERTY

"This administration today, here and now, declares unconditional war on poverty in America."—State of the Union message, Jan. 8, 1964.

"Unfortunately, many Americans live on the outskirts of hope, some because of their poverty, some because of their color, and all too many because of both. Our task is to help replace their despair with opportunity."—State of the Union message.

"Our chief weapons (in the war on poverty) will be better schools, better health, better homes, better training and better job opportunities to help more Americans—especially young Americans—escape from squalor and misery."—State of the Union message.

One-fifth of our citizens—35 million persons in 9.3 million families—live at or below the $3,000 per year poverty level family income. Another fifth live perilously close, according to government statistics. Hardest hit are Negroes, the aged, the unskilled and unschooled, families living in areas of vanishing industry, and those in the mountainous 10-state Appalachia region running from western Pennsylvania south to Alabama and Georgia.

For many families, poverty has become a legacy, handed down from one generation to another. The child of a poverty-ridden family is unable to remain in school as long as his contemporaries. Missing an education, he is cheated of the opportunities the future holds for others.

President Johnson has exposed this skeleton in the American closet to full view, the first national leader in decades to do so, and millions of Americans have been shaken by the knowledge, long ignored, that in the midst of plenty, poverty remains widespread and entrenched.

(Continued on page 3)

(Continued from page 2)

The President has proposed a billion-dollar beginning in his war to eradicate poverty. Neither he, nor its other advocates, pretend this is enough—but it is a starting point, and the war needs a start.

To focus national attention on the plight of the poor, President Johnson twice has traveled through the Appalachia region, an area of unrelieved deprivation.

He has appointed Sargent Shriver, effective as director of the Peace Corps, to organize and wage the war on poverty.

The anti-poverty program has its detractors. Some Republicans and southern Democrats have peppered the proposal in hearings before a House committee. They assert war on poverty is useless—"there will always be poor among us."

Others feel it is inadequate, but concede a small start is better than no start at all.

The President is seeking general acceptance of the need for the program. If he wins, he will have achieved a significant gain. (The proposal last week cleared the House Education and Labor Committee. See accompanying story.)

MEDICAL CARE FOR THE ELDERLY

"We have so much to be proud of in this country, so much to be thankful for, so much to preserve and so much to protect, but nothing that we want to protect more than those who have reached their later years and want the privilege of, in dignity, providing for themselves."—Remarks to Senior Citizens, Jan. 15, 1964.

"The social security health insurance plan which President Kennedy worked so hard to enact is the American way. It is practical. It is sensible. It is fair. It is just."—Remarks to Senior Citizens, Jan. 15, 1964.

President Johnson has argued persistently and convincingly for a medical care program for the elderly under the social security system, as President Kennedy did before him.

He has repeatedly stated it is a priority goal of his administration, and despite sometimes pessimistic forecasts of the bill's chances this year, he has stuck to his guns.

TAXES

"The tax cut is our modern weapon today against unemployment, which breeds poverty and ignorance, the inconsiderate allies of apathy and neglect. I don't intend to sit idly by while this problem of unemployment swells and coarsens. This tax bill must pass."—Remarks to AFL-CIO Executive Council, Dec. 4, 1963.

The tax cut emerged as one of the first major legislative accomplishments of the Johnson administration. It had been a key proposal of President Kennedy, and President Johnson made it a matter for immediate action.

Passage of the bill meant the equivalent of a 7½ cent an hour take-home pay increase for the average American, and gave a needed shot in the arm to the economy. Though President Johnson does not attempt to pass off the tax cut as a cure-all for the nation's economic problems, he does view it as a key chemical in the fuel mixture he hopes will boost the economy into an orbit of long-term growth and expansion.

On other key issues, Johnson as President has made his mark. Shortly after he took office, Congress passed a series of important education bills. A farm bill that had been given little chance of passage was enacted to bolster farm income. The President has urged an investigation into supermarket food prices. He has backed key consumer protection bills.

He promised early in his tenure that women would play an important role in his administration and backed this up with dozens of significant appointments, among them the appointment of Mrs. Esther Peterson as the first Special Assistant to the President for Consumer Affairs. Mrs. Peterson once was legislative representative of the AFL-CIO Industrial Union Department.

Of overriding importance, Johnson has said, is the problem of jobs. He told the AFL-CIO Executive Council in December the goal of his administration is 75 million jobs. The tax cut, the war on poverty, other key proposals—all are aimed at helping to create more jobs and to reduce unemployment.

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Lyndon Johnson assumed office six months ago in the midst of tragedy, and he established a sense of continuity that reassured a stricken nation. He embraced the programs of his predecessor, John F. Kennedy, and he has proposed programs of his own.

In a major address at the University of Michigan on May 22, exactly six months after he took the oath of office, he unfolded his vision of the "Great Society," one in which the vast wealth of this nation would be used "to enrich and elevate our national life—and to advance the quality of American civilization." It would be a society, he said, of "abundance and liberty for all," a society of wholesome cities, uncluttered countryside, unpolluted air and water, excellence in education, equal opportunity for everyone.

The President did not pretend that creation of the "Great Society" would be an easy matter, or a quick one. But he called on Americans to begin the building of it.

Their response to his call will be known five months hence, on Election Day

Poverty Bill Clears First Hurdle, 19-12

President Johnson has won the first skirmish in the war on poverty. His anti-poverty program cleared the House Education and Labor Committee last week on a strict 19-12 party-line vote. Nineteen committee Democrats voted for the bill, 12 Republicans voted against. Next stop: the House Rules Committee which must give the go sign on the bill for floor action.

As reported by the Education and Labor Committee, the bill authorizes funds for only one year, $962.5 million. Added in committee were two programs not proposed in the original administration bill. One would provide federal money for adult basic education classes. The other is aimed at aiding migrant farm workers by providing housing, sanitation, educational and child care assistance.

Stress on education and training in skills for young people is the hallmark of the program.

Some $412.5 million would be channeled into three youth opportunities programs:

- A 40,000-member Job Corps for needy boys and girls age 16-21, who would be enrolled in conservation camps or rural and urban residential training centers. They would be provided basic education and job training.

- Work-training for another 200,000 young people which would permit them to earn while continuing or resuming their education.

- Work-study programs to provide part-time jobs for still another 140,000 college students who otherwise could not pursue their college training.

Another $430 million is earmarked for helping communities to improve educational, job training, health and housing opportunities for low-income families.

The Johnson program, if finally approved, will be a beginning in the attack on poverty which afflicts some 35 million Americans, one-fifth of our population. Living at the poverty level income of $3,000 a year and under are 9.3 million of the 47 million families in the country.

Of these, five million families live in cities; 4.3 million live in the south; six million have a family head with less than ninth grade education; two million are non-white; 2.3 million have a woman as head of the family; 3.2 million have a family head 65 years old or older.

The problem is national in scope, affecting all major urban areas, and countless rural areas. It even strikes in Westchester County, N. Y., one of the richest counties in the nation. Commuter-land, Westchester records an average family income of $11,695. Yet, one of 12 families in the county lives in abject poverty.

House Public Works Hears Special Appalachia Plans

The anti-poverty bill reported favorably by the House Education and Labor Committee should not be confused with the special legislation aimed at lifting the hard-hit Appalachia region up from poverty. The region stretches from Pittsburgh, Pa., in a 10-state area south to parts of Alabama and Georgia.

The Appalachia proposal now is subject of hearings before the House Public Works Committee.

While nationally one of five families lives at or below the $3,000 a year poverty-level income, in Appalachia the figure is one of three. Per capita income there is $1,400 against the national per capita income of $1,900. Employment dropped 1.5 percent in Appalachia in the 1950-60 decade while it was rising 15 percent nationally.

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TALKING POINTS

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file Economic package

The Gramm-Latta budget resolution was passed in the House of Representatives by a wide, 77 vote margin on April 7. The Senate overwhelmingly approved the budget resolution by a vote of 78-20 five days later. President Reagan's words after the announcement of the House vote emphasized that the nation was behind the movement: "For years, the American people have been asking the federal government to put its house in order. Today the people have been heard."

If the passing of the Gramm-Latta budget resolution is the administration's first big victory, then the Reagan tax cut will have to be the second. President Reagan is as committed as ever to the 30 percent across-the-board reduction in marginal income tax rates. It is absolutely essential that the tax cut portion gets passed along with the rest of the Program for Economic Recovery.

While 63 House Democrats and 28 Senate Democrats sided with the President on the budget vote, Democratic leaders will be exerting massive pressure on them to vote against the President's tax cut program, even though it is part of a comprehensive policy. The following are several opposition attacks on the tax cut and some suggested responses.

Attack:

A large tax cut at this time would only aggravate the problem of inflation.

Response:

1. The previous administration believed that the answer to inflation lay in curbing economic growth (creating recessions). This caused the economy to see-saw between inflation and recession. The Reagan administration knows that the only way to get off this see-saw is to get America back on the road to real growth, which is exactly what the tax cut will do. The Program for Economic Recovery will give us real growth (between 4 and 5 percent) without inflation (the inflation rate will drop from 10 percent this year to 7.2 percent in 1982 and 5.6 percent by 1986).

2. The government has the choice of financing the deficit by printing more dollars, which causes inflation, or by using existing financial resources. While some say that using existing financial resources would in turn take money away from the private sector, this ignores that the tax cut will do much to encourage savings. The savings rate will rise from 5.5 percent to 7.5 percent, providing $42 billion more for needed investment funds. The tax cut will allow the government to finance its deficit and will also allow private business to invest in America's growth.

Prepared by the RNC Communications Division · Mark Tapscott, Director

3. It is not more inflationary to let the American people spend their own money than it is for the federal government to spend it for them. As long as the effects of tax rate reduction on receipts are balanced by reductions in outlays, the demand for goods and services will remain the same. Since the House and Senate have already passed the Reagan plan for budget cuts with flying colors, tax reductions will be balanced by budget reductions.

Attack:

The tax cut will benefit the rich, while penalizing the poor and the middle class.

Response:

1. Savings, investment, and spending decisions by Middle Americans create jobs and business opportunities for everybody. The surest way to combat poverty is to create new wealth. The middle class are the Americans most likely to respond favorably to a tax cut.

2. The Reagan tax cut strongly favors Middle Americans because they are the most willing and able to invest in America's future. The percent of taxes paid by Middle Americans is 67.2 percent. Their percentage of the Reagan tax cut is 69.9 percent. Thus the group who pays the most in taxes--the middle class--gets the most tax relief.

3. Reductions in tax rates are expected to increase tax compliance and reduce tax shelters. By reducing tax rates on high income earners, the federal government will actually collect more tax revenues from this group. With more revenues from the higher income groups, the burden of supporting necessary government expenditures will fall less on the middle class and the poor and more on the rich. By all means, tax the rich--but do it in a way so that growth is encouraged, not suppressed. The Kennedy tax cut of 1964 is an excellent example of how lowering tax rates on marginal income will actually bring in more revenues. Not only did revenues increase under the Kennedy tax cut--the deficit shrank as well.

4. How the tax cut will affect different regions of the nation is a question linked to the "fairness" debate. As a matter of fact, regional per capita distributions of the tax cut (as well as the budget cuts) are about as fair and equitable as they could be.

	Increase in Disposable Personal Income from Tax Cuts	Distributable Outlay Reductions (from Budget cuts)
U.S. Total	$1161	$166
Northeast	$1211	$170
Midwest	$1246	$155
South	$1063	$169
West	$1168	$168

The figures illustrate that the distribution of the tax and budget cuts is equal among regions in the United States and that the tax cut will put all regions ahead by a big margin.

Attack:

Cutting taxes now is the wrong approach. Congress should raise taxes to collect more revenue so they can balance the budget. Only when the budget is balanced can there be talk of a tax cut.

Response:

1. Tax burdens have been rising for 15 years straight, yet the budget deficit has continued to widen. This is evidence that raising taxes is part of the problem, not the solution.

2. Rising tax burdens inhibit all forms of economic growth and boost unemployment. Every 1 percent increase in unemployment raises budget outlays by about $9 billion and lowers tax receipts by about $20 billion. This represents a worsening of the budget deficit by about $29 billion. Rising tax burdens can be directly traced to bigger deficits.

3. Since 1973, real GNP has grown by only 2.4 percent a year. From 1950 to 1970, real growth averaged 3.7 percent a year. Much of the difference can be attributed to rising inflation and rising tax rates. In the past decade, tax rates rose over 168 percent. For two years now, inflation has been running at 12 percent. The pernicious effects of this duo are well-known, if not well-understood in Congress: simultaneous stagnation, unemployment, and sky-rocketing prices.

4. Inflation and steeply progressive tax rates have caused the federal government to claim a larger share of the nation's GNP--from 18.3 percent of GNP in 1976 to 21.4 percent in 1980. If the Reagan tax cut is enacted, the federal government's share of GNP will shrink from a high of 23 percent in 1981 to 21.8 in 1982 and eventually down to around 19 percent in 1984. Every dollar spent by the government is a dollar not spent by the American people.

The tax cut bill drafted by the House Ways and Means Committee Chairman Dan Rostenkowski (D-Ill.) is not really a cut at all--it will mean large tax increases for all Americans over the next four years. Here is a closer glance at the Rostenkowski tax bill:

1. Chairman Rostenkowski provides for a one-year cut of only $20.8 billion in FY82--that's $20 billion less than the Reagan tax cut for that year, and there are no assurances that taxes will be cut further (as compared to the Reagan plan, which reduces taxes over a three-year period).

2. Consider the programmed increases in income taxes that will take place over the next four years to see how much relief each tax cut proposal will really provide. First there are the scheduled social security tax increases ($22 billion in 1982 and $27 billion in 1984). Then there is the inflation tax, which pushes people into higher marginal income tax rates ($30 billion in 1982 and $85 billion in 1984). The extra taxes from the inflation tax, or "bracket creep." alone amount to two and one half times the total budget deficit scheduled for 1982.

3. The net effect of the tax "cut" proposed by Chairman Rostenkowski is a real tax increase for all Americans of $31.2 billion in 1982 and $75.6 billion in 1984.

4. Only with the Reagan tax cut will Americans feel real relief from the tax steamroller that is scheduled to gear up over the next four years. President Reagan's plan would provide $1.4 billion in tax relief for 1983 and $8.4 billion for 1984.

5. It is clear that Chairman Rostenkowski is using the old trick of producing smaller deficits by "balancing the budget on the backs of the taxpayers," rather than slashing wasteful and ineffective social programs to bring the budget in line with reality.

6. An ill effect of Chairman Rostenkowski's smaller tax bill is that it will provide "breathing room" for some of his more incorrigible Democratic free-spenders who want to restore some of the social programs that President Reagan eliminated. In a helpful tone of voice, they would query, "Since the Reagan budget has already been voted in with such a large deficit, why can't we have a smaller tax cut and keep some of our programs?" May's budget victory could be stolen easily in late summer with arguments of this kind. The problem with this wrangling is that it ignores productivity increases that the Reagan tax cut will give to the American economy, and that spending did indeed have to be cut.

Parting Shots:

Our true choice is not between tax reduction on the one hand and the avoidance of large federal deficits on the other... An economy (stifled) by restrictive tax rates will never produce enough revenue to balance the budget--just as it will never produce enough jobs or enough profits.

President John F. Kennedy

Marching in lockstep with the whole program for reductions in spending is the equally important program of reduced tax rates. Both are essential if we are to have economic recovery. It is time to create new jobs, build and rebuild industry, and give the American people room to do what they do best.

President Ronald W. Reagan

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HOUSTON OUTLOOK '82

MURRAY L. WEIDENBAUM
NATIONAL ECONOMIC OUTLOOK

file

HYATT REGENCY HOUSTON
JANUARY 14, 1982

Recovery

ECONOMIC POLICY FOR 1982

Let me give you my fearless forecast for 1982 in a nutshell:

(1) The old proverb still holds: It is always darkest before the dawn.

(2) Unlike another old adage, 1982 will come in like a lamb but roar out like a lion.

(3) A year from today, the American economy will be enjoying both more prosperity and less inflation.

Yes, I am forecasting that, as 1982 moves along, we will see the tangible evidence that the Reagan economic program is working. Yes, tax cuts, expenditure cuts, regulatory relief, and monetary restraint -- those four points in concert -- are the correct medicine to restore the health of the American economy. And yes, the task of fundamentally turning around the economy will be neither quick nor easy, but that essential task is being done.

Introduction

Let me begin by explaining the basic framework in which economic policy in the Reagan Administration is made. We start with a fundamental and deeply felt view of the role of government. That view is based on the notion that the people who make up the economy -- workers, managers, savers, investors, buyers, and sellers -- do not need government to make their decisions for them on how to run their own lives. As we see it, the most appropriate role for government economic policy is to provide a stable framework in which private individuals and business firms can plan confidently and make appropriate decisions.

This fundamental notion of economic freedom is widely and deeply shared by all of us who are involved daily in economic policy-making, beginning with Ronald Reagan. In other words, we start each day with a firm and common philosophical framework about the proper relationship of government to the economy. The same cannot be said for all past administrations.

Our widespread skepticism about the supposed blessings of government intervention is relatively new. In many past administrations, fascination with fine tuning was a major and generally fruitless preoccupation. While there obviously are ways in which government policies can contribute to easing both short- and long-term economic problems, they generally involve doing less -- not more. We have tried to learn from the mistakes of the past. To turn on its head one old and familiar phrase: "We have seen the past. And it doesn't work."

A critical feature of our approach to economic policy-making is that it is oriented to the long run. Thus, we are highly skeptical of "fine tuning," whether of the fiscal or the monetary variety, which assumes extraordinary forecasting ability and a degree of expertise that only the ignorant or the overly-educated presume to possess.

Reducing the Burden of Government

Another fundamental theme of our program is the compelling need to reduce the burden of government on the private sector of the economy. That reduction must involve all of the many dimensions of government intervention -- expenditures, taxes, credit allocation, and regulation. That, in turn, will enable the United States to reemphasize, once again, the private sector as the primary engine of economic growth and progress.

This attitude toward government finds its most apparent expression in the President's four-part program for economic recovery. Each of those four elements is based on a view that less, not more, government is the preferred approach to reinvigorating our economy: less, not more, regulation; less, not more, monetary expansion and volatility; less, not more, expansion in government spending; lower, not higher, tax rates. Our approach is, so to speak, a concept of minimizing, not maximizing, government's relationship to the economy.

But our view of the role of government must be carefully defined. Let there be no misunderstanding of the true meaning of our policies. They do not mean being simple-mindedly pro-business. I don't mean a "partnership" between government and business, or subsidies for failing industries, or "incomes" policies and government planning to control economic developments. Promoting limited government means that no favored treatment is to be given to any specific interest group or industry. It means restraining any tendency to shift resources from those who are entitled to them by virtue of their own economic activity to those who receive them by political decision.

Furthermore, our concern for the principles of economic freedom cannot stop at the water's edge. Freer worldwide flows of trade and investment -- a free enterprise system writ large -- offer greater economic welfare to the peoples of the world. The same specialization of labor and individual creativity that we see among the people of our society also can be encouraged beyond our borders.

The economic case for more limited government is not just philosophical. It is vital that we free up the resources and potential of the American business system so that it can deliver to the public the rising living standard which had been the hallmark of the American economy -- and which, sadly, has not been achieved during the past decade.

From Recession to Prosperity

With this backdrop about the fundamentals of the Reagan economic program, let us turn to the current business situation and the current recessionary situation -- and let me answer that frequently asked question, "What are you going to do about the recession?" In past administrations, the tendency at this time has been to push the proverbial panic button. We all know the traditional responses: increase government spending; enact quickie, consumption-oriented tax cuts; and encourage the Federal Reserve to shift to an easy money policy.

I want to assure you that such counterproductive measures are not part of this administration's economic policy. Those misguided responses of the past are precisely the types of action that lie at the root of today's deep-seated, long-run economic problems. The stop-and-go policies of the past will not be repeated. And, as I'll show in a moment, they would be both unnecessary and counterproductive. But first let's take a look at current business conditions.

By postwar standards, the current recession is likely to be of about average length and depth. How did we get here? And, far more important, how are we to move to prosperity?

This downturn is closely related to the extended period of high interest rates that prevailed from the latter part of 1980 through the first half of 1981. Those painfully high rates produced an ever-widening circle of weakness, especially in homebuilding and motor vehicle production, the two industries most affected by interest rates. As we saw last year, falling demand for housing and autos gradually had an impact on an increasing number of other industries, ranging from forest products to steel and rubber to appliances and home furnishings. The high interest rates also squeezed farm incomes and hit those other industries and services closely tied to agriculture.

About those high interest rates: let us review some not-so-ancient history to see how we got there. In mid-1980, short-term interest rates were generally under 10%. In July 1980, for example, three-month Treasury bills averaged 8%. Long-term rates were in the vicinity of 10%-11%. Then, in the second half of 1980, we witnessed the fastest rate of money growth for a six-month period that has ever been recorded, a 13% annual rate. At roughly the same time, federal expenditures were increasing rapidly -- at an 18% annual rate.

By the end of 1980, not surprisingly, interest rates had advanced to new peaks: in the final week of December, the Federal funds rate averaged close to 20%, the prime rate reached 21.5%, and three-month Treasury bills had nearly doubled in yield from their mid-year lows. Long-term rates had risen in some cases by as much as three full percentage points. Until late last summer, with the exception of a brief short-lived decline in the spring, short-term rates remained in the vicinity of their year-end 1980 highs. Long-term rates, on the other hand, advanced by another two percentage points before joining the declining trend very late this past summer.

I think it is a fair characterization of this period to say that excessive monetary and fiscal stimulation in the latter half of 1980 drove interest rates to near-record highs. Rates were maintained at those levels for the next six months or so by a variety of factors, including the initial but temporary impact of a shift to monetary restraint. Interest rates then fell because of the monetary restraint that has been the hallmark of Federal Reserve policy since the beginning of last year. But as we have learned over many years, interest rates rarely move in a straight line for any extended period. The present is no exception.

In retrospect, those high interest rates were clearly a major factor in precipitating the current downturn. Just as clear, however, is the fact that those high rates were part of the legacy of the past, a legacy of excessively rapid growth in government spending, taxing, regulation, and credit creation that we are determined to put behind us.

Let me emphasize a key point: interest rates have been coming down not because policy shifted to ease, but because restraint was maintained -- restraint that is succeeding in squeezing out the inflation that became embedded in those high interest rates. In some cases, such as for Treasury bills, rates have fallen rapidly from their earlier highs, from nearly 17% in May to about 12% in recent days. The prime rate recently has fallen from 20.5% to 15.75%. Long-term rates, including those on residential mortgages, are now beginning to follow the lead set by short-term rates.

As we know, the decline in the economy has been unusually uneven. To confuse matters, the first three months of 1981 showed an upward spurt at an unsustainable rate. That, of course, was the legacy of that burst of monetary and fiscal ease during late 1980. The second quarter, reacting to all that, declined a bit, but the third quarter recovered briefly. It was like a fighter who dropped to the count of five, got up only to be socked again, and then really hit the canvas. That, of course, was just what happened in the last three months of 1981, when the economy really reached bottom.

The Outlook

Where do we go from here? I do anticipate that a few more months of poor economic statistics are in front of us. But there are powerful forces already at work to reverse the downturn, and in a timely fashion. I am referring to the tax cuts, lower interest rates, and rising defense production. Not surprisingly, I expect that the sectors of the economy that were hardest hit by the high interest rates will be among the first to feel the beneficial effects of the lower interest rates that we are now experiencing -- autos, homebuilding, and their supplying and supporting industries. As the expansion progresses, I anticipate that capital spending will accelerate. It usually is the last major part of the economy to respond to the forces of recovery. In the current cycle, the recently-enacted tax cuts should accentuate the normal upturn in business investment.

The absence of speculative activity before the recession is a plus in the recovery ahead of us. For example, continued population growth remains a major source of unsatisfied demand for new housing. The pace of new construction has been running well below that demand for a long time. The pipeline of materials and supplies for the industry is quite low. Considerable increases in production are needed just to refill it to normal levels.

Similarly, the average age of cars on the road has lengthened considerably in the past year or so, suggesting that replacement demand will be a stronger-than-normal factor in auto sales as 1982 develops. Finally, although some industries may be holding higher inventories than they would like, I do not see industry having to go through a prolonged period of inventory liquidation.

Let me summarize briefly this evaluation of the outlook for the American economy. There is little doubt in my mind that we are on our way to a vigorous recovery in 1982. But for the year as a whole, the statistics for 1982 may not look like much of a winner. Real growth is likely to average only 1% or less over 1981. But that will obscure the fundamentally favorable development -- the acceleration in activity as the year progresses.

I anticipate that signs of the upturn will become visible in the next few months. Indeed, there are already some potential straws in the wind, such as modest upturns in home sales, housing starts, and auto sales. The second quarter -- in my crystal ball -- will witness the beginning of recovery, with the second half of 1982 experiencing real growth rising at more than a 5% annual rate. Furthermore, 1983 -- when the full force of both the business and personal tax cuts will take hold -- should be a very vigorous and less inflationary period of economic growth.

The outlook for inflation is also encouraging. The increase in the Consumer Price Index in 1981 was approximately 9.5%. That was a significant improvement from the 12.5% recorded in 1980. Given the maintenance of current policies, I think that a CPI increase this year of between 7% and 8% appears likely. The lessened inflation will bring further relief to consumers and play an important role in moderating cost pressures in business during a year with a full calender of wage negotiations.

We should note that this relatively upbeat evaluation of the prospects for the American economy is not significantly different from the prevailing forecasts of experienced private economists. They generally share my view of a turnaround some time in the first half of this year, followed by a strong recovery in the second half of the year, simultaneous with continued progress on the inflation front.

Reducing Those Budget Deficits

At this point, a few words are in order about the federal budget for the fiscal year beginning October 1, 1983, which we are in the midst of preparing. As you are aware, we have postponed our 1984 target date for a balanced budget. But this does not imply that the goal of a balanced budget has been abandoned. Indeed, between now and 1984 we will be striving, with the assistance of the Congress, to make very substantial and credible progress toward that goal.

It is especially important to reduce the deficit financing of the federal government in fiscal year 1983, a period in which we expect the private sector -- and its financing requirements -- to be expanding significantly. During a time of recession, such as the present, the deficit that I anticipate, although much larger than I would like to see, is not likely to be "crowding out" the rather modest funding needs of business and consumers. But in fiscal 1983 and beyond, when we expect a period of rapid growth in the economy, substantial reductions in the budget deficit -- and in off-budget financing -- will be very much needed.

We cannot view substantial budget deficits with indifference. Apparently, the folks who invented deficit spending are now, rather late in life, developing concerns about the government's red ink. Surely we long-time fiscal conservatives welcome their belated support. Let me assure them that deficits do matter.

Financing those deficits decreases the amount of private saving and foreign capital that is available to the private sector, and that reduces the economy's long-term growth prospects. Financing those deficits makes the Federal Reserve's job of monetary restraint more difficult. But we must not forget that in order for the inflationary potential of deficits to be realized, they must be monetized by the Federal Reserve. And I have every confidence that such a development simply is not in the cards. I believe that the Federal Reserve System is determined to maintain the policy of gradually reducing the growth in the supply of money and credit.

The heart of budget-making, of course, is the choice of expenditure priorities. In this administration we are all hawks in the continued battle to restrain the growth of government. It is on the outlay side of the budget where that battle is now being waged.

In that regard, I find the continuing concern about the budget deficits of the federal government a very constructive factor. The desire to reduce the large deficits in the budget is an extremely important counterweight to the always present pressures for additional growth in governmental outlays that do not have to meet the continuing test of the marketplace.

The effort to reduce deficit financing and slow down the growth of government should properly be viewed in a larger dimension -- as part of a fundamental attempt to shift the focus of economic decision-making in our society from the public sector back to the private sector. For it is in the private sector that products are created, markets are developed, factories are built, productive jobs are generated, and economic progress is truly advanced.

Thus, the battle of the budget is more than a fiscal matter -- important as that is. Our budgetary concerns reflect the Reagan Administration's determination to enhance economic welfare by defining more modestly the role of the federal government in the American economy -- a role that covers the tax power, the expenditure power, the credit power, and the regulatory power. But the battle is more than a matter of thinking small in the public sector -- it is also a matter of thinking big when it comes to enhancing individual opportunities in the private sector.

A New Sense of Realism

I suggest that the Administration's policies already have made for a new sense of realism in economic decision-making, both in the public and in the private sectors. Companies are becoming more cost-conscious and are learning the advantages of being competitive in an economy in which the federal government does not assuredly come to "bail out" the losers in the marketplace. Employees are learning that their wages, salaries, and fringe benefits are vitally dependent on the success of their company. Many workers appear to be increasingly willing to accept adjustments in work rules and job practices to ensure their company's success. Taxpayers are seeing that reductions in government program outlays, no matter how painful or unpopular, go hand in hand with reductions in tax rates, which are always more welcome. Business and consumers alike are experiencing the benefits of lower inflation rates that result from maintaining a determined policy of restraining the growth of the supply of money and credit.

Citizens generally are learning that the benefits of long-run economic growth and stability are not achieved instantaneously; rather, they entail undergoing a period of adjustment as we all learn to adapt to a new and surely more enlightened sense of economic realism.

In conclusion, even through we currently are going through a period of adjustment, I am profoundly encouraged by what I believe are the first significant steps toward decisively reversing the debilitating trends of the recent past. Private attitudes and expectations, as well as public policies, are undergoing far-reaching shifts. Vigorous, sustained, noninflationary growth is within our reach -- if we continue to resist the temptation for a return to the stop-and-go policies of the past. I assure you that this administration is determined to stay the course.

THE PRESIDENT'S FEDERALISM INITIATIVE: BASIC FRAMEWORK

JANUARY 26, 1982
EMBARGOED FOR RELEASE 9:00 P.M.

INTRODUCTION

THE PRESIDENT IS OUTLINING A FRAMEWORK FOR A MAJOR FEDERALISM INITIATIVE. HE PLANS TO SEND ENABLING LEGISLATION TO CONGRESS IN A FEW WEEKS. BEGINNING TOMORROW, HE WILL WORK WITH STATE AND LOCAL OFFICIALS AND CONGRESS TO DEVELOP THE NECESSARY PROGRAM DESIGNS.

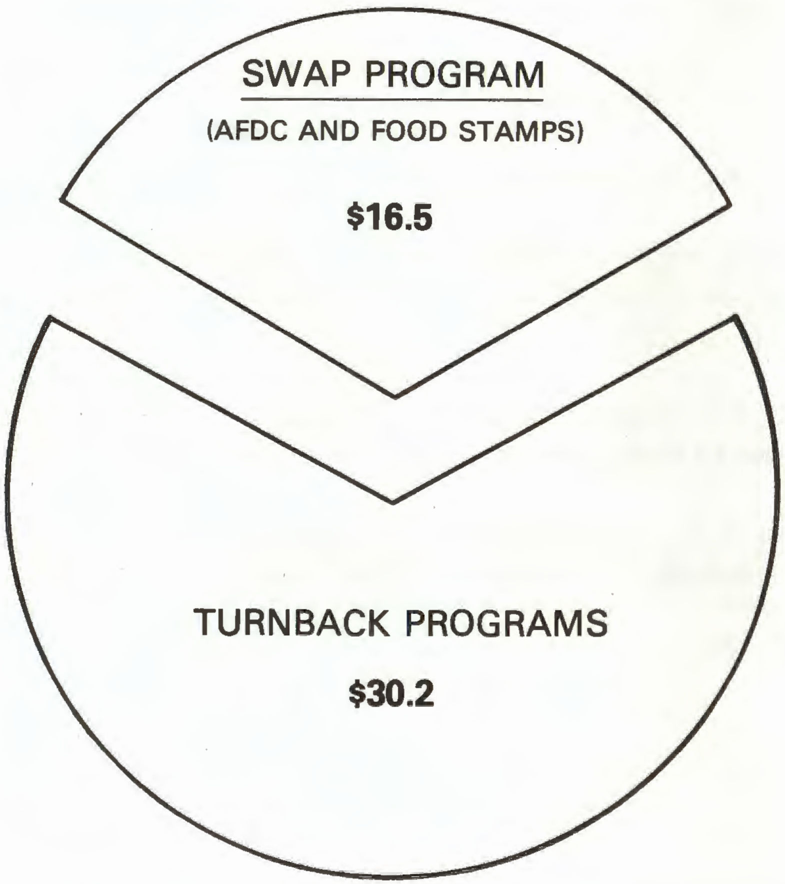
I. BASIC FEATURES

- $50 BILLION TRANSFER OF FEDERAL PROGRAMS TO STATES OVER 8-YEAR PHASED TRANSITION—WITH EQUIVALENT REVENUE SOURCES. TWO MAJOR COMPONENTS INCLUDE:
  - SWAP COMPONENT—FEDERAL TAKE-OVER OF MEDICAID IN SWAP FOR STATE TAKE-OVER OF FOOD STAMPS AND AFDC—A $20 BILLION EXCHANGE;
  - TURNBACK COMPONENT—MORE THAN 40 FEDERAL EDUCATION, TRANSPORTATION, COMMUNITY DEVELOPMENT AND SOCIAL SERVICE PROGRAMS TURNED BACK TO STATES—WITH $28 BILLION FEDERALISM TRUST FUND TO FINANCE THEM.

FEDERALISM PROGRAM — FY '84 LEVEL

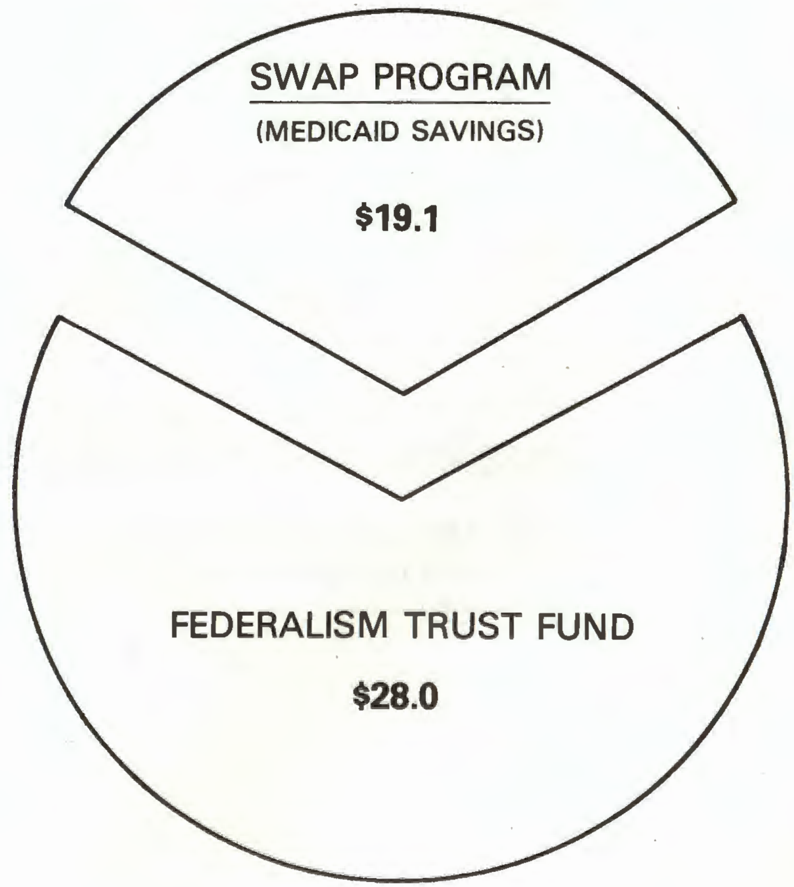
(BILLIONS OF DOLLARS)

STATE/LOCAL PROGRAMS AND COSTS ABSORBED. . .



TOTAL: $46.7

REVENUE SOURCES TO FINANCE THEM

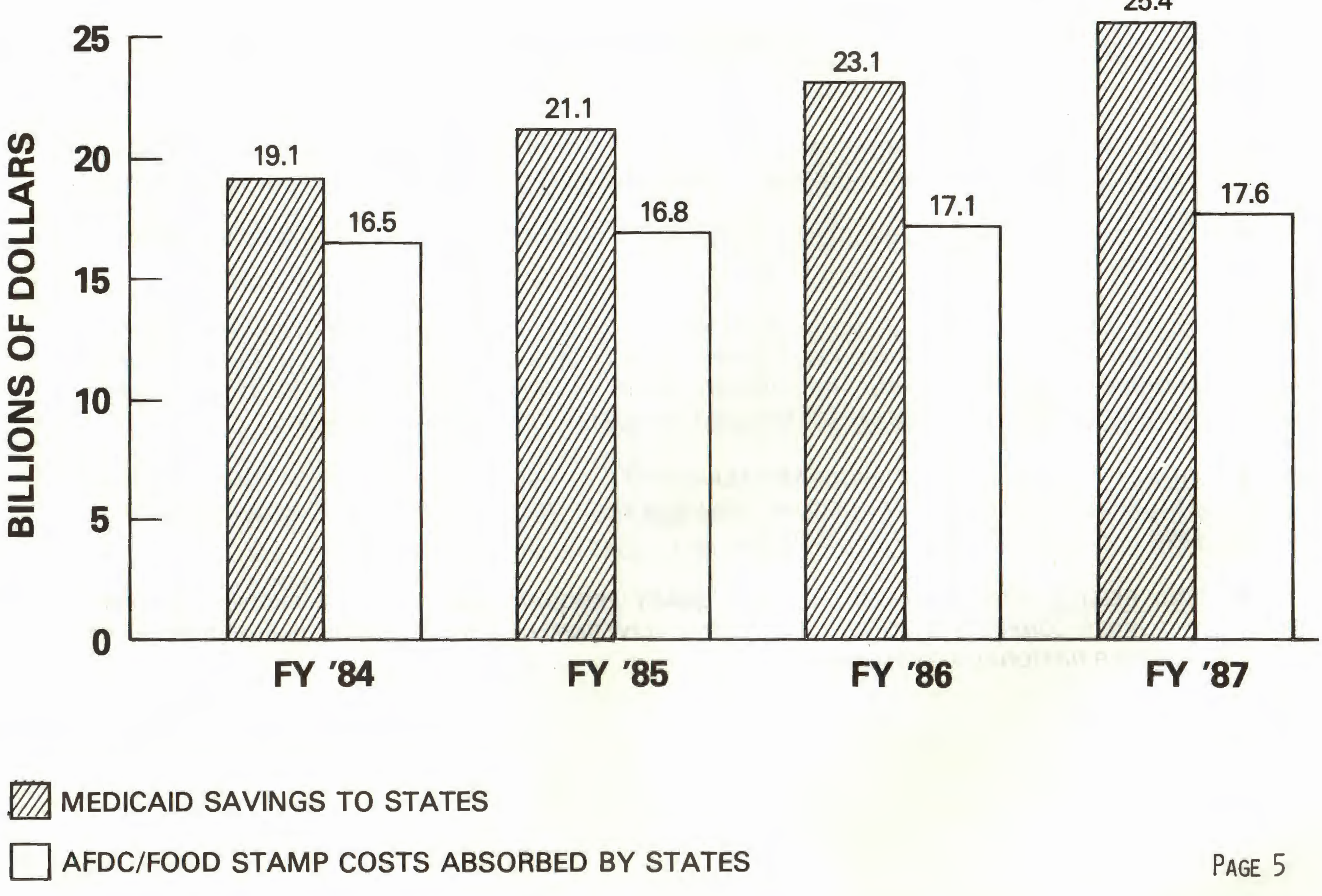


TOTAL: $47.1

II. MEDICAID/PUBLIC ASSISTANCE SWAP

- $20 BILLION EXCHANGE OF PROGRAM RESPONSIBILITIES:
  - FEDERAL GOVERNMENT ASSUMES MEDICAL ASSISTANCE FUNCTION;
  - STATE GOVERNMENTS ASSUME INCOME ASSISTANCE FUNCTION FOR NON-ELDERLY.
- MEDICAID FULLY FEDERALIZED IN FY '84. WILL BE RESTRUCTURED AS PART OF INTEGRATED FEDERAL COST CONTAINMENT INITIATIVE TO LIMIT SKYROCKETING GROWTH OF MEDICARE AND MEDICAID PROGRAMS.
- STATES ASSUME FULL RESPONSIBILITY FOR AFDC AND FOOD STAMPS IN FY '84—WITH FLEXIBLE MAINTENANCE OF BENEFITS REQUIREMENT FOR NEW STATE CASH ASSISTANCE PROGRAM.
- STATE MEDICAID SAVINGS GROW FROM $19 BILLION IN FY '84 TO $25 BILLION BY FY '87—EXCEEDING THE COSTS OF AFDC/FOOD STAMPS AND THEREBY FREEING-UP INCREASING PORTION OF THEIR OWN TAX BASES.

SWAP COMPONENT OF FEDERALISM INITIATIVE



III. TURNBACK PROGRAMS

- MORE THAN 40 CATEGORICAL AND BLOCK GRANT PROGRAMS TURNED BACK TO STATES ON VOLUNTARY BASIS IN PHASE I (FY'84-87) AND ON PERMANENT BASIS BEGINNING IN FY'88 (PHASE II).
- $28 BILLION ANNUAL FEDERALISM TRUST FUND PROVIDES NEARLY DOLLAR-FOR-DOLLAR FINANCING IN PHASE I.
- PHASE I: FY'84-87. TRUST FUND ALLOCATIONS TO STATES BASED ON HISTORIC PROGRAM SHARES (FY'79-81) MODIFIED BY GAIN OR LOSS ON SWAP. STATE FUNDS MAY BE APPLIED TO FEDERAL GRANT PROGRAMS WHICH CONTINUE IN CURRENT FORM THROUGH FY'87—OR AS NO-STRINGS SUPER REVENUE-SHARING PAYMENT IF STATES OPT OUT OF FEDERAL PROGRAMS EARLY.
- PHASE II: FY'88-91. GRANT PROGRAMS TERMINATED AT FEDERAL LEVEL. TRUST FUND PAYMENTS AND FEDERAL EXCISE TAXES DECLINE 25% EACH YEAR—WITH STATES FREE TO SUBSTITUTE THEIR OWN TAXES OR REDUCE PROGRAM COSTS.
- END RESULT. MORE THAN 40 FEDERAL GRANT PROGRAMS AND EXISTING EXCISE TAX BASES RETURNED COMPLETELY TO STATES. FEDERAL GOVERNMENT FREE TO FOCUS ON FEWER ISSUES OF GREATER NATIONAL SIGNIFICANCE.

IV. FEDERAL GRANT PROGRAMS INCLUDED IN TURNBACK

- TURNBACK CONSISTS OF FEDERAL CATEGORICAL AND BLOCK GRANT PROGRAMS ORIENTED TOWARD LOCAL COMMUNITY NEED AND INDIVIDUAL SERVICE DELIVERY—ACTIVITIES BEST SUITED FOR STATE/LOCAL MANAGEMENT DISCRETION. PROPOSED MAJOR PROGRAMS WOULD INCLUDE:

  - NON-INTERSTATE HIGHWAYS, AIRPORTS AND LOCAL MASS TRANSIT;
  - SEWER TREATMENT GRANTS, UDAG, CDBG, AND RURAL WATER/SEWER AND FACILITIES GRANTS;
  - VOCATIONAL REHABILITATION AND EDUCATION, TRAINING AND EMPLOYMENT GRANTS AND STATE EDUCATION BLOCK GRANT;
  - HEALTH, SOCIAL SERVICES AND COMMUNITY SERVICES BLOCK GRANT, CHILD NUTRITION, LOW INCOME ENERGY ASSISTANCE, AND NUMEROUS CATEGORICAL SOCIAL WELFARE PROGRAMS;
  - REVENUE SHARING.

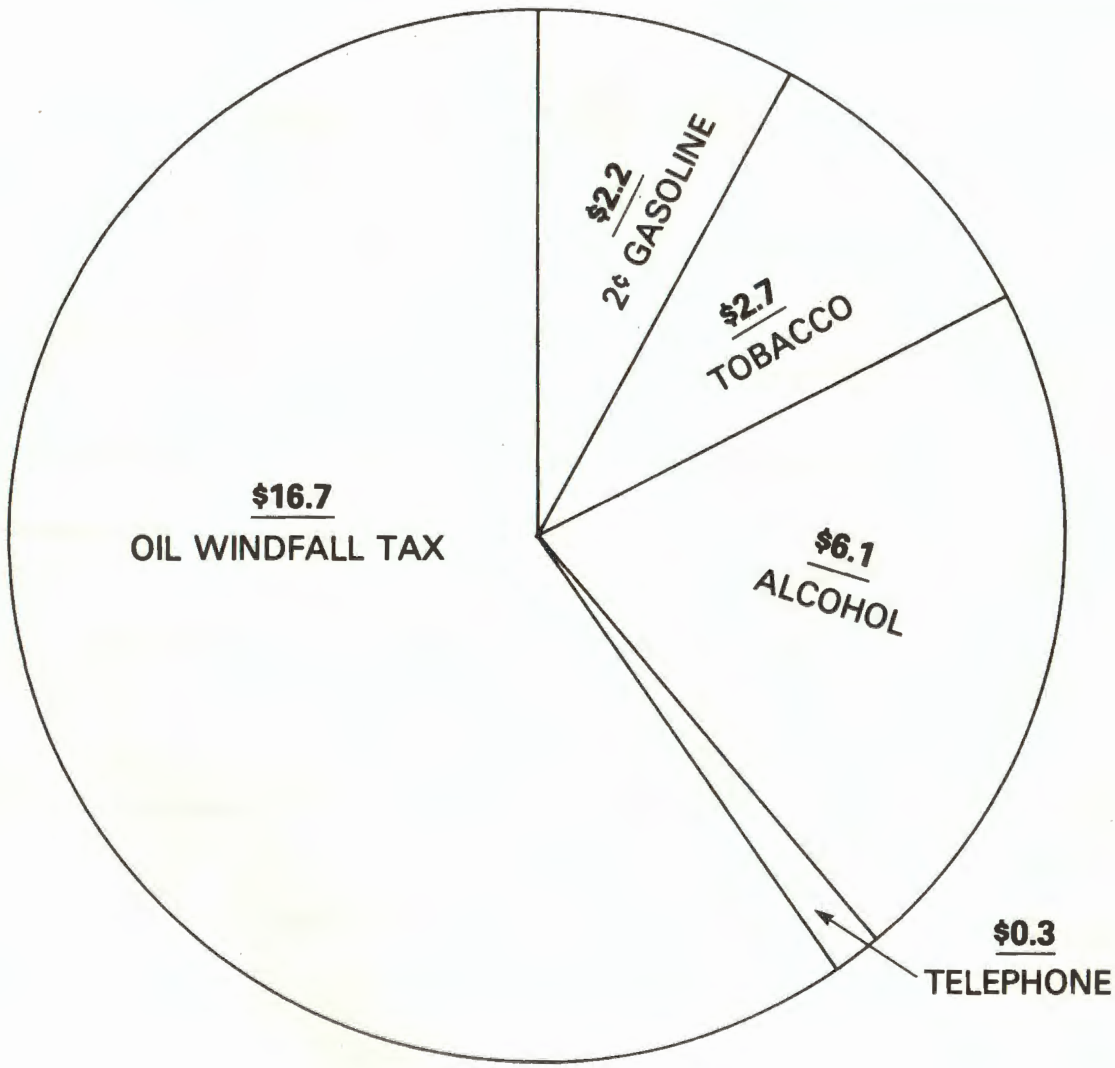
TURNBACK PROGRAM COMPOSITION
FY '84 LEVEL

TOTAL: $30.2 BILLION

V. FEDERALISM TRUST FUND

- USED FOR TWO MAJOR PURPOSES DURING PHASE I:
  - FINANCING SOURCE FOR MORE THAN 40 TURNBACK PROGRAMS OR SUPER REVENUE-SHARING AT STATE OPTION;
  - EQUALIZE GAINS AND LOSSES AMONG STATES ON MEDICAID/PUBLIC ASSISTANCE SWAP.
- ALLOCATED AMONG STATES ON BASIS OF HISTORIC SHARES (FY'79-81) OF TURNBACK PROGRAM COSTS—MODIFIED BY GAIN OR LOSS ON SWAP;
- FINANCED FROM EXISTING FEDERAL ALCOHOL, TOBACCO AND TELEPHONE, MOTOR FUEL (2 CENTS ONLY) AND PART OF OIL WINDFALL TAX;
- $28 BILLION PER YEAR THROUGH FY'87, THEN DECLINES BY 25% ($7 BILLION/PER YEAR) THROUGH FY'91—AS FEDERAL EXCISE TAXES PHASE-DOWN (OIL WINDFALL TAX PHASES OUT UNDER CURRENT LAW SCHEDULE);
- FINAL RESULT: FEDERAL EXCISE TAXES RETURNED FULLY TO STATE JURISDICTION.

FEDERALISM TRUST FUND — DEDICATED RECEIPTS
FY '84 —'87 LEVEL



TOTAL: $28 BILLION

VI. STATE OPT-OUT MECHANISM — PHASE I

- FEDERAL PROGRAMS OPERATED AND MANAGED AT FEDERAL LEVEL THROUGH FY'87—TO GIVE STATES AMPLE TIME TO DEVELOP POLICY AND ADMINISTRATIVE CAPACITIES;

- STATES MAY ELECT TO WITHDRAW FROM SOME OR ALL FEDERAL GRANT PROGRAMS BEFORE FY '87—IF APPROVED BY LEGISLATURE AND GOVERNOR AFTER CONSULTATION WITH AFFECTED INTERESTS. ONE-YEAR NOTICE TO FEDERAL GOVERNMENT FOR VOLUNTARY WITHDRAWAL.

- IF STATES WITHDRAW FROM FEDERAL GRANT PROGRAMS, RESULTING TRUST FUND SURPLUS TREATED AS SUPER REVENUE-SHARING PAYMENT, AND MAY BE USED FOR ANY PURPOSE.

- SOME OF SUPER REVENUE-SHARING PAYMENT MUST BE PASSED-THROUGH TO LOCAL UNITS.

- IF STATES REMAIN IN FEDERAL GRANT PROGRAMS DURING PHASE I (FY'84-87), MUST REIMBURSE FEDERAL AGENCIES FOR PROGRAM EXPENSES FROM TRUST FUND, AND ABIDE BY FEDERAL CONDITIONS AND RULES.

- ALL FEDERAL GRANT PROGRAMS TERMINATED IN PHASE II (FY'88-91). ENTIRE DECLINING STATE TRUST FUND BALANCE TREATED AS SUPER REVENUE-SHARING.

VII. <u>SUPER REVENUE-SHARING PASS-THROUGH</u>

- TO INSURE FULL LOCAL PARTICIPATION IN THE FEDERALISM PROGRAM AND FAIR TREATMENT DURING THE TRANSITION, SUPER REVENUE-SHARING PAYMENTS SUBJECT TO THREE PASS-THROUGH CONDITIONS:
  - IF STATES OPT-OUT OF <u>DIRECT FEDERAL-LOCAL</u> GRANT PROGRAMS (E.G. UDAG, MASS TRANSIT)—100 PERCENT PASS-THROUGH TO LOCAL UNITS;
  - IF STATES OPT-OUT OF OTHER FEDERAL PROGRAMS—<u>15 PERCENT</u> PASS-THROUGH TO LOCAL UNITS BASED ON GENERAL REVENUE SHARING FORMULA.
  - <u>NO PASS-THROUGH OF EDUCATION MONIES</u>—AS THESE PROGRAMS GENERALLY NOT IN JURISDICTION OF GENERAL UNITS OF LOCAL GOVERNMENT.

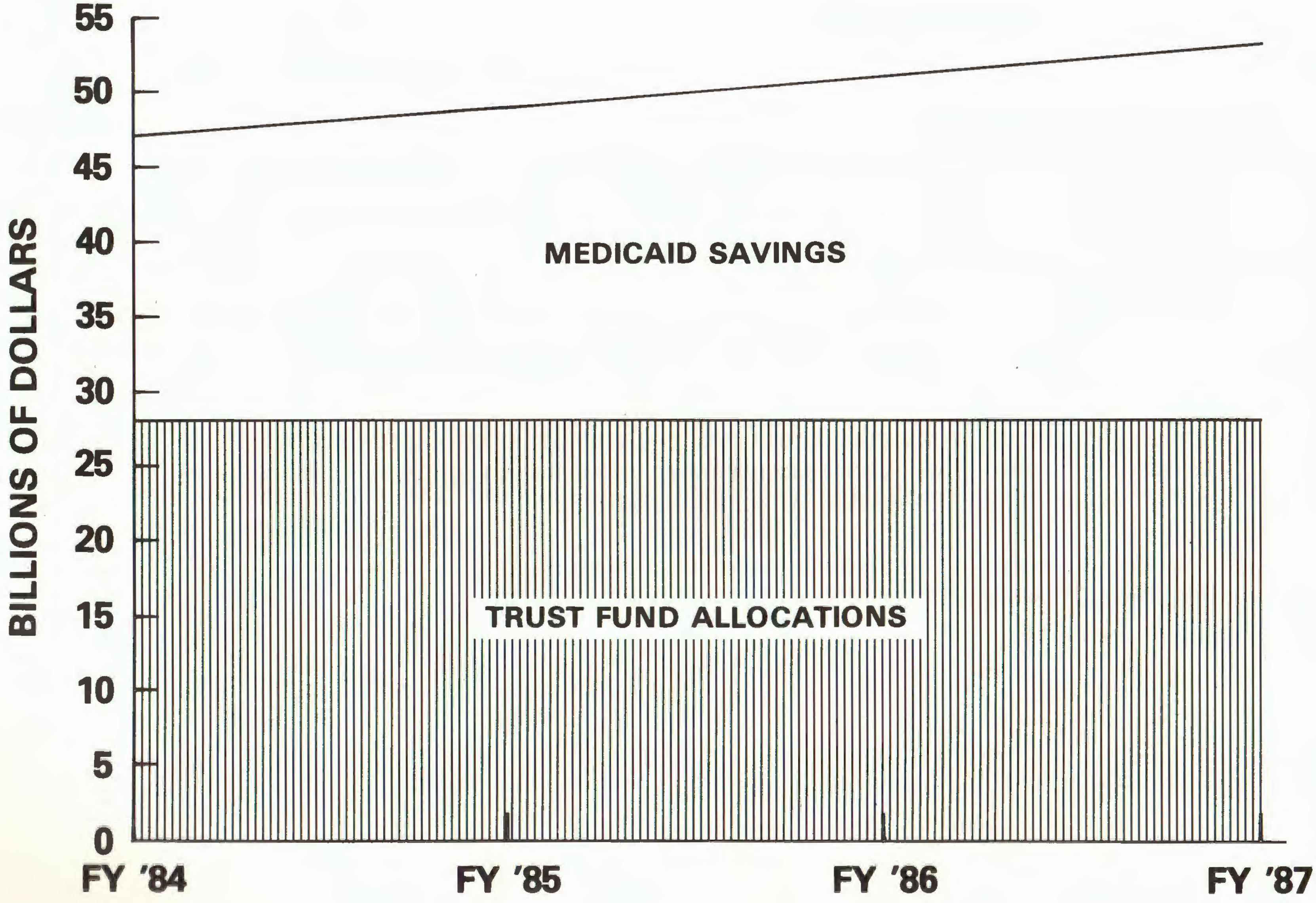
VIII. STATE AND LOCAL FISCAL IMPACT

- $28 BILLION FEDERALISM TRUST FUND AND GROWING SAVINGS FROM MEDICAID FEDERALIZATION OVER FY '84-87 PROVIDE INCREASING REVENUE SOURCES TO FINANCE NEW STATE PROGRAM RESPONSIBILITIES. REMOVES FEDERAL FUNDING UNCERTAINTY FOR REST OF DECADE.

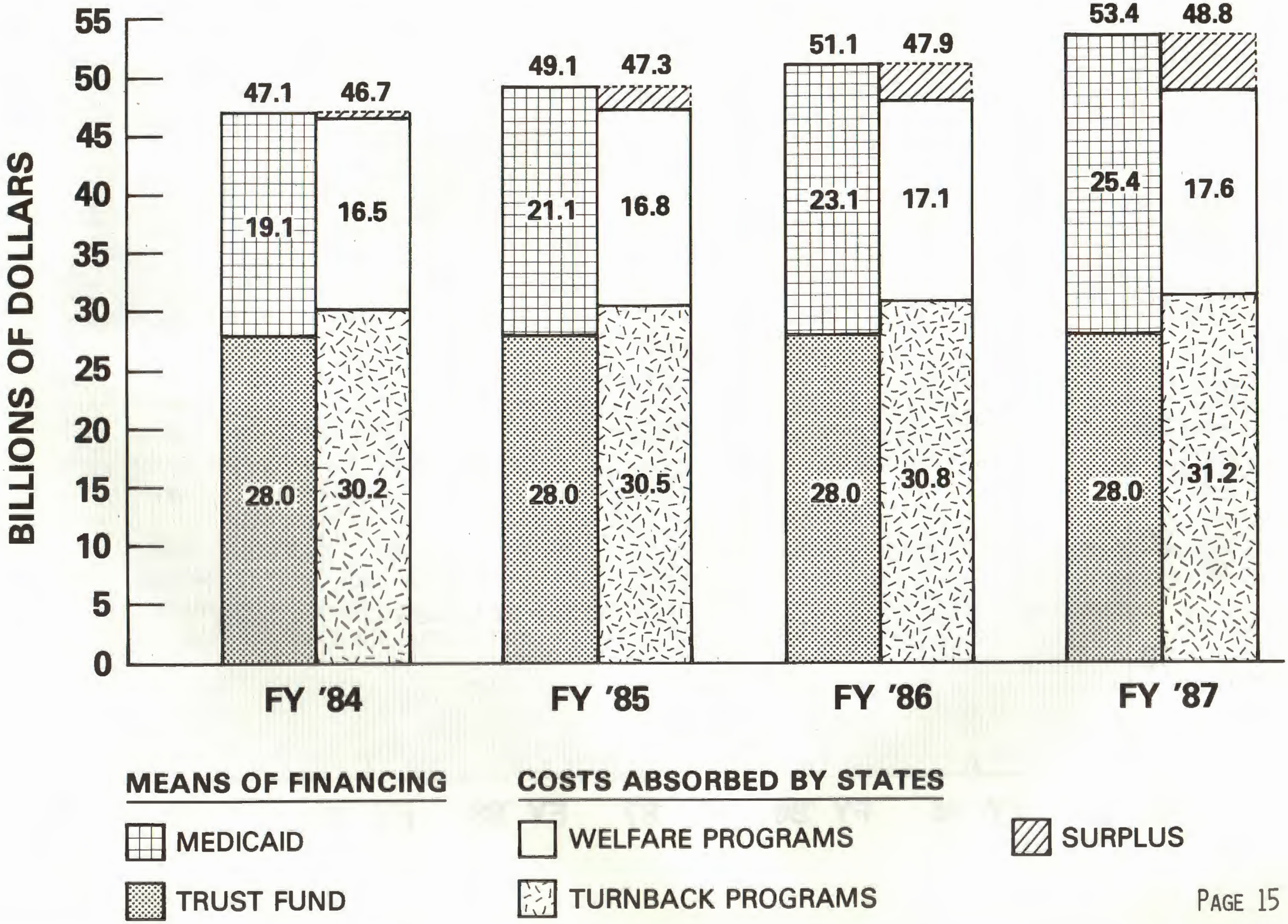
- SWAP AND TRUST FUND/TURNBACK COMPONENTS NOT-SEPARABLE. TOGETHER THEY ASSURE STATES AS A WHOLE AN EVEN FISCAL TRADE, AND THAT NO INDIVIDUAL STATE GAINS OR LOSES MORE THAN A SMALL PERCENT IN TOTAL REALIGNMENT.

- STATES HAVE SIX YEARS TO DETERMINE BEST MIX OF PROGRAM SAVINGS AND TAX INCREASES BEFORE FEDERALISM TRUST FUND BEGINS TO PHASE OUT IN FY'88.

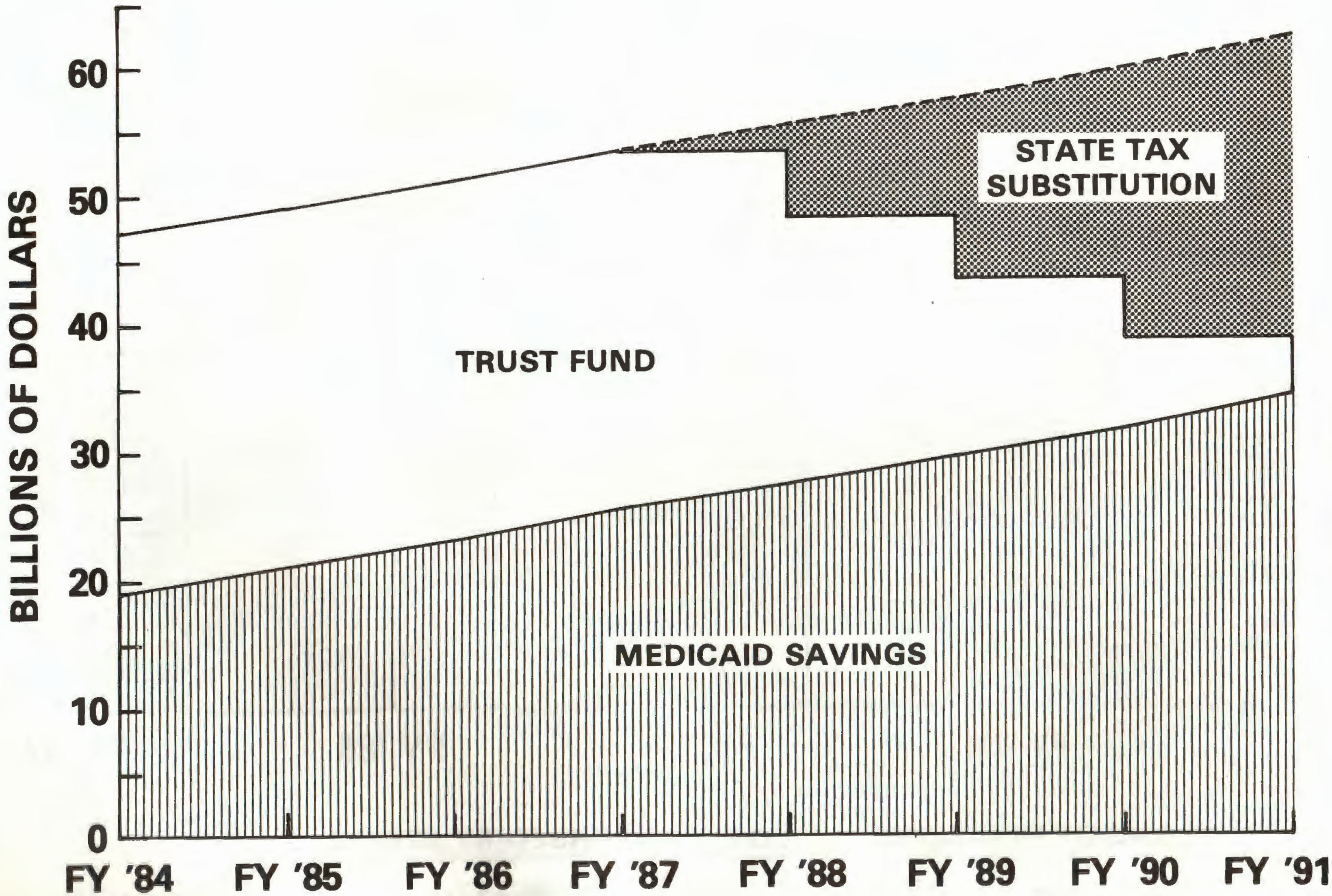
REVENUE SOURCES AVAILABLE TO STATES



NET FISCAL IMPACT



STATE FINANCING SOURCES FY '84—'91



IX. RATIONALE AND JUSTIFICATION

- DESIGNED TO RESTORE BALANCE OF RESPONSIBILITIES WITHIN FEDERAL SYSTEM AND TO REDUCE DECISION, MANAGEMENT AND FISCAL OVERLOAD ON FEDERAL GOVERNMENT;
- PROVIDES CLEAN SEPARATION OF DOMESTIC WELFARE RESPONSIBILITIES BETWEEN FEDERAL AND STATE/LOCAL SECTORS;
- LARGELY ABOLISHES OVER 8 YEARS THE EXISTING, UNWORKABLE FEDERAL/STATE GRANT-IN-AID SYSTEM WHICH TENDS TO TRANSFORM NON-FEDERAL UNITS INTO SUBORDINATE MIDDLE-MANAGEMENT EXTENSIONS OF THE WASHINGTON BUREAUCRACY. AFTER TRANSITION, INTER-GOVERNMENTAL RELATIONSHIP BASED ON INDEPENDENT PROGRAM RESPONSIBILITIES, INDEPENDENT FINANCES, AND FULL AND MUTUAL SOVEREIGNTY;
- PREMISED ON FACT THAT OVER PAST 30 YEARS—REAPPORTIONMENT, GOVERNMENTAL REFORM AND MODERNIZATION, AND EXTENSIVE OPERATIONAL RESPONSIBILITIES FOR DOMESTIC WELFARE PROGRAMS—HAVE DRAMATICALLY STRENGTHENED STATE AND LOCAL CAPACITIES FOR FULL AND RESPONSIBLE PARTNERSHIP IN THE AMERICAN GOVERNMENTAL SYSTEM.

CLEAN SEPARATION OF DOMESTIC WELFARE RESPONSIBILITIES

FEDERAL GOVERNMENT

- SOCIAL INSURANCE SYSTEM. SOCIAL SECURITY RETIREMENT, DISABILITY AND MEDICARE.
- TRANSFER AID TO NEEDY ELDERLY. SSI, MEDICAID, HOUSING, SENIOR SERVICE PROGRAMS.
- HEALTH INSURANCE AND MEDICAL ASSISTANCE. MEDICARE, MEDICAID, AND TAX INCENTIVES FOR PRIVATE INSURANCE.
- PROJECTS OF NATIONAL SIGNIFICANCE/PRIORITY. COMPENSATORY EDUCATION AND HEAD START, HIGHER EDUCATION SUPPORT, HANDICAPPED EDUCATION, INTERSTATE HIGHWAYS, AND REGULATORY PROTECTIONS WITH INTERSTATE IMPACT.

STATE AND LOCAL SECTOR

- LOCAL TRANSPORTATION. BRIDGES, STREETS, STATE/LOCAL HIGHWAYS, MASS TRANSIT.
- COMMUNITY DEVELOPMENT AND LOCAL CAPITAL INVESTMENT. SEWER TREATMENT PLANTS, NEIGHBORHOOD RENEWAL, DOWNTOWN REVITALIZATION.
- GENERAL EDUCATION. ALL CURRENT FEDERAL PROGRAMS OTHER THAN HANDICAPPED AND COMPENSATORY.
- SOCIAL, HEALTH AND NUTRITION SERVICE DELIVERY. DAY CARE, REHABILITATION, COMMUNITY HEALTH CENTERS, DRUG/ALCOHOL TREATMENT, NUTRITION AND HEALTH SERVICES TO LOW-INCOME FAMILIES, SOCIAL WORK AND PROTECTIVE SERVICES.
- CASH ASSISTANCE TO NON-ELDERLY NEEDY. SUCCESSOR PROGRAMS OF STATE/LOCAL DESIGN FOR FOOD STAMPS/AFDC.

THE WHITE HOUSE

Office of the Press Secretary

For Release at 9:00 p.m. EST
Tuesday, January 26, 1982

FACT SHEET

THE PRESIDENT'S STATE OF THE UNION ADDRESS

Summary

I. In his first State of the Union message to the nation, President Reagan outlined a comprehensive program to address the nation's domestic concerns:

A. Continued adherence to the economic recovery program

-- New restraints in federal spending growth while preserving the social safety net;

-- No tax increases this year and "no retreat from the basic program of tax relief."

-- Continued commitment to regulatory relief and slow, steady monetary growth.

B. A major new partnership with states and local communities

-- A gradual return of over 40 Federal programs to State and local governments accompanied by the means to finance them;

-- An equal "swap" of the Medicaid program to the Federal government and the AFDC and food stamp programs to state and local authorities.

-- Close consultation with State, local officials and Congress prior to submission of the legislation.

C. Enterprise Zones

-- Proposed the creation of enterprise zones as an experimental free-market program for improving the economic conditions of urban areas.

-More-

II. Other Domestic Commitments

During his address, the President also briefly touched upon several other domestic concerns:

- -- He called for a responsible Clean Air Act that would create jobs while continuing to improve the quality of air; he also welcomed the bipartisan initiative in the House of Representatives and said he looked forward to working closely with the Senate and House toward prompt enactment of legislation in 1982.

- -- He called for the private sector to mobilize its resources to assist in efforts to combat social ills.

- -- He vowed that the nation's "long journey towards civil rights for all our citizens" will continue and he restated his commitment to an extension of the Voting Rights Act.

- -- He emphasized that the nation must continue its efforts to secure equal rights for women; and,

- -- He said that we must transform our legal system in order to cope with the problem of crime.

III. Foreign Affairs: Toward the end of his address, the President reviewed the state of affairs in other parts of the world. His address briefly discussed conditions in Poland, relations with the Soviet Union, his hopes for reducing arms, America's alliances, the Middle East, China, and the President's plan for a Caribbean Basin Initiative. The President said he would address foreign policy and defense issues in greater detail at a subsequent time.

A more complete examination of the President's statements on domestic economic issues follows. A separate summary of the President's federalism initiative is also available to the press and public.

A. CONTINUED ADHERENCE TO THE ECONOMIC RECOVERY PROGRAM

President Reagan reaffirmed the four-part Economic Recovery Program put in place last year and pledged there would be no change of course despite temporary recession conditions. The Economic Recovery Program includes:

-- Supply-side tax rate cuts for individuals and business to increase incentives for savings, investment and job-creation -- a program fully implemented in the historic 1981 Economic Recovery Tax Act set to spur the economy into recovery during the years ahead;

-- Continued slow-down in the growth rate of Federal spending and in government's share of GNP by reforming entitlements, reducing discretionary programs and eliminating excess bureaucratic overhead and waste, fraud and abuse -- efforts which have already cut the Federal spending growth rate nearly in half;

-- Reduction of unnecessary Federal regulations and market intervention -- which has already reduced the number of new pages in the Federal Register by one-third and new regulations by one-half.

-- A steady restraint in money supply growth to reduce inflation.

1.) No Tax Increase to Solve Budget Problems

President Reagan made it clear that larger than anticipated deficits -- due to the recession and the decline in projected inflation and in the growth of governmental receipts -- will not be solved by resorting to raising tax rates. Specifically, he will propose no new increases in existing tax rates in the FY 1983 budget to be released February 8.

2.) Elimination of Unnecessary and Obsolete Tax Code Provisions

The only tax changes planned are of the type announced last fall: efforts to close loopholes. The President renewed his September proposals for tax code revision and announced that the FY 1983 budget will include a proposal to strengthen the minimum corporate tax to ensure that all larger, economically profitable corporations pay a minimum fair share of Federal taxes.

Other major tax code revisions will include the repeal of energy tax credits for business, limitations of tax-exempt industrial bonds, changes in code provisions relating to contract progress payments and construction period interest and taxes, and all health insurance.

-More-

With broad based tax rate reductions, new savings and investment incentives and a generous business depreciation system now in place, these special tax code provisions are no longer needed. Their elimination will increase Federal receipts by an estimated $24 billion in the 2-year period of FY 1983 and 1984.

3.) Federal Outlay Reductions

President Reagan indicated there will be no retreat from the overriding fiscal policy imperative of reducing the growth rate of Federal spending. The FY 1983 budget will include $63 billion in new entitlement reforms over the next four years and substantial reductions in discretionary programs. Also, the President will propose tens of billions in additional savings through management initiatives over the next three years -- including improved debt collection, surplus property sales, accelerated sales of off-shore oil and gas leases, and strengthened fraud, waste and abuse prevention efforts.

Overall, the growth rate of Federal spending will decline from an average of 17 percent a year from FY 1979 to FY 1981, to 9 percent in the recession budget of FY 1982, to about 5 percent in the FY 1983-84 budget.

4.) Reduction of the Federal Deficit

The President repeated his commitment to reducing Federal deficits and borrowing by means of renewed economic growth, continued budget reductions, and elimination of tax abuses and obsolete provisions.

The FY 1982 deficit will be under $100 billion. Its size is largely due to the current recession and consequent reduction in tax receipts and increased unemployment-related payments. The FY 1982 deficit is too large but, nevertheless, as a share of GNP it is smaller than the recession deficit of FY 1976.

The deficit will decline each year after the 1982 recession peak, as the economic recovery takes hold and budget savings measures are implemented. Full details on additional budget savings proposals will be transmitted with the President's Budget for Fiscal Year 1983 on February 8.

-More-

B. <u>A MAJOR NEW PARTNERSHIP WITH STATES AND LOCAL COMMUNITIES</u>

President Reagan has proposed a major reshaping of the fiscal relationship between the Federal government and the states. The program, involving some $47 billion in Federal grants-in-aid, is intended to sort out the responsibilities properly assigned to each governmental level, return to the states both those responsibilities better handled by the states and the revenue sources needed to fund them, and achieve economies for the states and the Federal government.

The plan has two major components:

- A "swap" of Medicaid to the Federal government for full funding in return for which the states would assume responsibility for the food stamp and AFDC welfare programs.

- A "turnback" of responsibility to the states for over 40 Federal programs in education, community development, transportation and social services along with funds from a $28 billion Federal trust fund to be financed by existing Federal excise taxes. The turnback will be voluntary through FY '87, permanent after that.

The program will be phased in over 8 years, starting in FY 1984. By 1991, state and local authorities will have assumed responsibility for over 40 programs now administered by the Federal government. The state and local governments will also have received equivalent revenue resources through the elimination of major federal excise taxes (alcohol, tobacco, telephone and motor fuel except for a 2¢ tax per gallon retained by the Federal government) and the phase-out of the federal windfall profit tax on decontrolled oil.

The program contemplates no net financial gain or loss to the states and includes protections in such areas as pass-through of funds to local governments, civil rights and adequate welfare standards.

The President plans to submit enabling legislation to the Congress this Spring. He will immediately begin consultations with state and local officials and Congress to develop the necessary program designs.

<u>For further detail</u>, see attachment: The President's Federalism Initiative: Basic Framework

C. ENTERPRISE ZONES

President Reagan has proposed a plan for creation of enterprise zones as an experimental free-market program for dealing with some aspects of urban problems. The purpose of the experiment is to explore new ways:

-- to create jobs in the nation's depressed areas, particularly jobs for disadvantaged workers;

-- to redevelop and revitalize the geographic zone areas themselves.

The underlying concept of enterprise zones is to create a wide-open, free-market environment in depressed areas through relief from taxes, regulations and other government burdens; privatization of some municipal services; and involvement of private, neighborhood organizations. Because the program is based on the concept of removing government burdens rather than providing government subsidies, it should involve no appropriations, at least at the Federal level.

The incentives and natural market forces thus unleashed should stimulate economic activity within the zones and accomplish the program's objectives.

The program is intended to:

-- stimulate new economic activity within the zones, not relocation of businesses from elsewhere;

-- allow the market to decide which sort of businesses may be established in the zones, not stimulate any particular kinds of enterprises;

-- include a relatively balanced set of economic incentives for a wide-range of business activity though the Federal tax incentives will encourage labor intensive businesses.

The President intends to submit his plan for enterprise zones to the Congress in the next several weeks.

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'83 budget

Facts belie '83 budget agonizing

WASHINGTON — Critics of President Reagan's budget for 1983 seem to be voicing two principal complaints — first, that further cuts in social programs are unbearable, and second, that the prospective deficit is intolerable. Neither complaint has merit.

To listen to the agonized cries from the liberal left, one might suppose

JAMES J. KILPATRICK

that the president had no purpose in mind but to grind the faces of the poor — that he advocates starvation, illiteracy, rotting teeth and the mass eviction of elderly couples from their humble abodes.

Mr. Reagan is being depicted as a cruel and heartless monster who delights in slashing, destroying, undermining and hitting hard. A contributor to the editorial page of *The Wall Street Journal* charges that the president's budget "makes it clear that the needs of our poorest people are his least concern."

Suppose we look at the figures.

The food stamp program provides a useful example. The program got off the ground in 1965 with an outlay of $35.6 million. By 1970 the outlay was $577 million. As recently as 1975, which was not so very long ago, food stamps cost the taxpayers $4.7 billion. In 1980, just two fiscal years ago, the program topped $9 billion. For 1983, Mr. Reagan proposes $10.3 billion.

Some of this mind-boggling increase of course is owing to inflation. In constant dollars, the growth is not quite so alarming. But when that factor has been fully discounted, a program of phenomenal dimensions still remains. More than 19 million persons will be receiving food stamps under the president's "slashed" and "heartless" recommendation.

Housing subsidies provide another example.

In 1977, just five fiscal years ago, federal outlays for housing assistance came to $3 billion. For 1983 Mr. Reagan proposes housing assistance of $8.9 billion. If this is cruelty, it is cruelty of a curious kind.

Are the elderly being tossed to the wolves?

In 1978, just four fiscal years ago, Social Security, Medicare and other programs amounted to $103.9 billion. For 1983 these same benefits would amount to $209.6 billion. On down the road, in 1987, the benefits are fixed at $283.3 billion.

The Office of Management and Budget asserts that the average elderly couple, retiring next year, stands to receive $15,700 in tax-free benefits. Would the president's critics provide vastly more?

Look. The most dismaying aspect of this criticism is in what it tells us about ourselves. We have drifted a long way from the old moorings — from self-reliance, local responsibility, the virtues of can-do and make-do.

Whole generations of middle-income Americans used to get their higher education without guaranteed loans and Pell grants. There was a time, and it wasn't so long ago, when our people survived without 95 million subsidized meals every day.

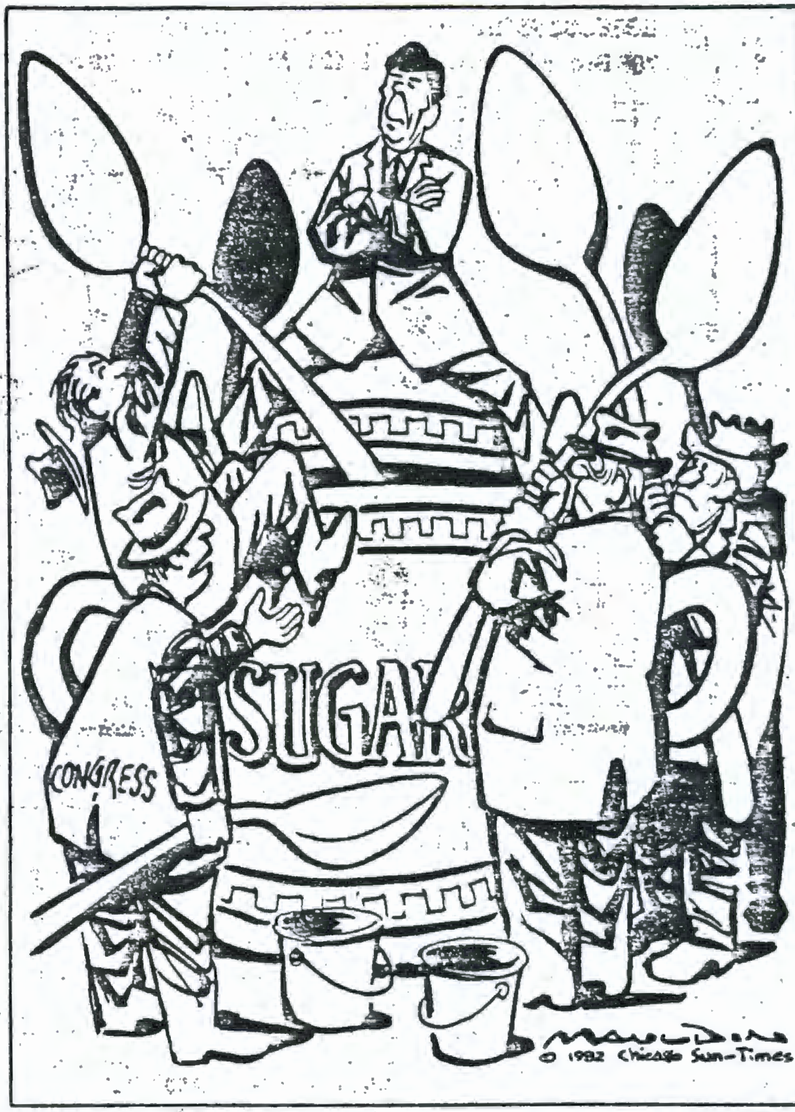
To the extent that Mr. Reagan's budget nudges us back toward the old initiatives, the budget ought to be praised and not condemned.

The 1983 deficit is estimated at $92 billion. It will probably be higher. Congress has a high obligation to reduce the figure by selective tax increases and by further cuts in spending — including defense spending.

But to cry that a $92 billion deficit is "intolerable" is to lose a sense of perspective. The sum represents about 3.1 percent of our gross national product, not greatly beyond the 2.9 percent of 1977 and 1980 and much lower than the 4.5 percent of 1976. As a percentage of total federal spending, the prospective deficit is less than we somehow tolerated in 1975 and 1976.

None of this is to say that Mr. Reagan's budget is cast in stone. It is arguable that in some areas, he is attempting to cut too much too soon for local government and the private sector to adjust to the changes. No one is happy about a $92 billion deficit. But neither should we accept the calamity-howling as if catastrophe truly lies ahead.

This budget moves in sound directions. Subject to minor course corrections, it ought to be adopted.



". . . But man, this is an *election* year!"

Document No. ________________

WHITE HOUSE STAFFING MEMORANDUM

FEB 24 1982

DATE: 2/24/82 ACTION/CONCURRENCE/COMMENT DUE BY: ________________

SUBJECT: DOMENICI PLAN -- AND GUIDANCE

	ACTION	FYI		ACTION	FYI
VICE PRESIDENT	☐	☑	GERGEN	☐	☑
MEESE	☐	☑	HARPER	☐	☑
BAKER	☐	☑	JAMES	☐	☑
DEAVER	☐	☑	JENKINS	☐	☑
STOCKMAN	☐	☑	MURPHY	☐	☑
ANDERSON	☐	☑	ROLLINS	☐	☑
CANZERI	☐	☐	WILLIAMSON	☐	☑
CLARK	☐	☑	WEIDENBAUM	☐	☑
DARMAN	☐P	☑SS	BRADY/SPEAKES	☐	☑
DOLE	☐	☑	ROGERS	☐	☑
DUBERSTEIN	☐	☑	________	☐	☐
FIELDING	☐	☑	________	☐	☐
FULLER	☐	☑	________	☐	☐

Remarks:

Attached are a Domenici press release on the Domenici Budget Plan and a Stockman summary memo on the relationship of Domenici's plan to ours.

Agreed guidance (for now) on the subject is as follows:

> "The plan is comprehensive and represents a good faith effort that merits our careful examination. But we do have some obvious concerns about the Domenici proposal:
>
> * Specifics of how he would raise the revenues and the impact upon economic recovery;
> * Impact of his defense plans upon our national security;
> * Whether there would be any unintended adverse impact of his proposed spending freeze."

Richard G. Darman
Assistant to the President
and
Deputy to the Chief of Staff
(x-2702)

NEWS

United States Senate

Committee on the Budget

FOR RELEASE
6 p.m., EST
February 23, 1982

CONTACT: Nancy Moore
(202) 224-4129

NEW YORK -- U.S. Senator Pete V. Domenici (R-NM), Chairman of the Senate Budget Committee, told a meeting of the Conference Board here Tuesday night that he will push a budget plan for the next three years that will save more than $320 billion from the projected federal deficits.

Domenici said that the plan was an expanded version of the one he had developed last September. That plan, however, was opposed by the administration and defeated by Domenici's committee on a 12-10 vote.

"The President's plan will not pass Congress in its present form," Domenici said. "My concern with the President's budget is that it fails to do enough to cut spending and accepts almost benignly what are malignant deficits."

Domenici said that he believes his plan occupies "middle ground" between the budget proposed by the President and recent plans that have been offered by both Republicans and Democrats in the Senate.

"I believe that the Senate can develop a bi-partisan consensus and I intend to work toward that, starting with Senator Hollings and others on my committee," Domenici said.

"A real mood for compromise with the President exists and I believe that the compromise will keep faith with the basic goals of the President's overall economic strategy, which I strongly support."

"The President is more on target on what needs to be done to the federal budget and the economy than any President in this century," Domenici said, "but, in an economy as fragile as ours, and with the free world facing serious economic stress, deficits of the size projected would be disastrous."

Domenici said that he would urge the President to work with the Congress to develop a bi-partisan plan that would yield deficits as low as $50 billion by 1985.

The Domenici Plan is as follows:

--reduce the President's defense outlay path by $20-25 billion during the FY 1983-85 period, by imposing a 5 percent real growth

--freeze federal pay raises in FY 1983 and limit these to 5 percen in FY 1984-85, saving $25 billion in the three years;

--limit other domestic discretionary spending by freezing such accounts at the 1982 levels for three years, thus saving $34 billi

more

--freeze indexed entitlements for 1983, saving $60 billion during the 1983-85 timeframe;

--limit Medicare and Medicaid increases in 1983 to the rise in the Consumer Price Index, saving $22 billion over three years;

--enact tax changes that would yield $18 billion in new revenues in FY 1983, $49 billion in FY 1984, and $55 billion in FY 1985, preferably by closing existing tax loopholes.

These actions would reduce the projected deficits sufficiently to save $53 billion in interest payments on the public debt during the three years according the Congressional Budget Office.

# # # #

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

February 24, 1982

MEMORANDUM FOR THE PRESIDENT

FROM: DAVID A. STOCKMAN

I. The following elements of the Domenici plan parallel or go beyond your FY 83 budget in areas outside of Defense and taxes:

A) Federal pay freeze in FY 83 and 5% thereafter

	FY 83-85
Domenici savings............	$25.0
FY 83 budget savings........	9.0

B) Medical Entitlement Reforms

	FY 83-85
Domenici savings............	$22.0
FY 83 budget savings........	24.0

C) Freeze domestic appropriated programs at FY 82 levels for three years.

	FY 83-85
Domenici savings............	$34.0
FY 83 budget savings........	76.0

D) One-year freeze on all Federal cost of living adjustments.

	FY 83-85
Domenici savings............	$60.0
BY 83 budget................	No comparable savings

II. Proposed Changes in Defense and Taxes

A) $20-25 billion Defense reduction over 3 years.

	FY 83-85
President's budget level...	$748 billion
Domenici cut...............	25 billion
Percent reduction..........	3 percent

B) Additional Revenues over FY 83-85 - "Preferably by closing existing tax loopholes," but actual tax change left vague.

	FY 83	FY 84	FY 85
Revenue increases in President's FY 83 budget..............	13	19	23
Domenici proposal....	18	49	55
Domenici increase....	+5	+30	+32

III. Comparison of Total Deficit Reduction Measures

	FY 83-85
FY 83 budget total savings...	$239
Domenici plan - toal savings.	$320

THE WHITE HOUSE

WASHINGTON

March 9, 1982

MEMORANDUM FOR ELIZABETH H. DOLE

THRU: DIANA LOZANO

FROM: MORTON BLACKWELL MB

SUBJECT: Constituent Group Support for and Opposition to President's Economic Program

This is a summary of the views of groups in the limited government, conservative religious, and veterans communities.

All of these groups were supportive of the President's election in 1980 and worked actively in behalf of the major legislative initiatives of the Administration in 1981.

I. The limited government groups are all in total opposition to any tax increases this year and support the President's strong anti-tax position.

These groups are militantly opposed to the projected budget deficits. They find them totally unacceptable. They insist that not enough attention has been paid to cutting social programs.

No one in the conservative and limited government groups is prepared to defend this budget.

Terry Dolan has undertaken to lead a large coalition in developing a complete alternate budget. He has put staff on this project and is working closely with a wide variety of groups. Approximately mid-March this conservative coalition will unveil its detailed proposals.

II. In the veterans and service organization community there is lots of concern over the size of the deficits. This group would be prepared to vigorously support cuts, particularly in entitlement programs, in the range of $ 20 - 25 billion.

Interestingly, the coalition of activist groups in this area, the Ad Hoc Committee, discussed these matters at their March 9th meeting. They would be opposed to anything other than token ($2-5 billion) cut in the proposed defense budget.

They discussed the possibility of some reduction in an area very sensitive to them, military retirement pay. One participant reported that there was no "tearing of hair or pounding on the table about this prospect." In other words, they could accomodate some cuts in military retirement entitlements as long as major cuts were made in social spending entitlements.

III. The conservative religious community is "scared to death of deficits."

They want the President to succeed, but they are near despair because the President shows "no signs of getting spending under control." They would vigorously support deep additional cuts in social spending.

A decidedly secondary but recurring theme from the conservative religious community is that the rise in defense spending has gone too far too fast. They are not locked in concrete on the issue, however. A couple of strong briefings on national defense could have a major impact on these groups.

In the absence of deeper spending cuts, we can expect no activist role from this community analogous to last year's heavy support. Neither would there be any major rebellion from this basically supportive quarter.

Their mood is one of despair at what they perceive as lack of focus.

Of course, the liberal religious leaders are opposed to every aspect of the President's budget proposal.

This seems to be an appropriate occasion to make the following observations:

1. It seems clear to me that the 1983 budget was an attempt to construct the best budget which would have a reasonable chance of passing in this Congress. It is clearly only a further step in the direction the President would like to take. It is not the budget the President thinks we ought to have but a product of a judgment of the best that could be had.

   Perhaps we are too enamored of our record of virtually complete legislative success last year. We seem to fear fighting battles which we might lose. In the long run, this may be very shortsighted.

If conservatives had taken this attitude on the Panama Canal treaty, we would have unilaterally disarmed ourselves for the political battles of 1978 and 1980 in which we took out of the Senate most of the supporters of that "winning" treaty. Sometimes fighting losing battles is essential to invigorate our grass-roots support. Surely, the Canal treaty was a Pyrrhic victory for the liberals.

It might be instructive to consider Harry Truman's experience. He fought many losing battles with Congress in the 1940's, but the public credited him with leadership and sticking by his guns. His Democratic party turned those legislative defeats into election victories.

2. Caught as we are, proposing a deficit which demoralizes our strongest supporters, we have one good way out. The President, who is a notorious foe of deficits, could almost totally reclaim the initiative by committing all the political resources of the Administration in support of the balanced budget, tax limitation constitutional amendment which now has 52 Senate co-sponsors.

   At one stroke, we would restore the fighting vigor of our core supporters and steal from our opponents the major issue on which they are making headway against us. Liberal Democrats who have been decrying the deficits would face an insoluble problem. Most of the pain of the 1983 deficit would ease. The market would surely rally. The effect on long term interest rates would probably be dramatic.

   Vigorous Administration support would almost assure the needed 2/3 vote in both Houses, particularly if urged by the President in a nationwide televised address.

   Ratification by 3/4 of the states would likely be some time down the road, thus buying us time to cope with the bulge in social spending that we inherited from previous administrations.

   Most important, though, would be the impact of this move on the 1982 elections. It would restore intact in 1982 the 1980 Reagan winning coalition.

file Economic Program

April 21, 1982

RECENT GOOD NEWS ITEMS CONCERNING CURRENT U.S. ECONOMIC CONDITIONS

1. The entire first quarter decline in Gross National Product was attributable to inventory liquidation. Final sales were up at a 1.8 percent annual rate (in 1972 dollars) in the first quarter. This suggests a need to rebuild inventories, thereby raising production and income in the second quarter.

2. Durable goods orders in March increased for the second consecutive month and have now risen by 5 1/2 percent since January. Orders for machinery were up 3 1/2 percent for the month indicating an improving outlook for capital investment spending. (Source: U.S. Department of Commerce, April 21, 1982).

3. Short and long term interest rates are again falling. The prime rate is now four percent below the September high of 20 1/2 percent.

4. Investment spending in this recession has declined about one percent from its peak, compared to a four percent decline during the first two quarters following the peak in the previous seven recessions.

5. Retail sales in February were up 2.6 percent and up 0.3 percent in March from February after taking into account declining gasoline station sales. Retailers reporting higher sales in March included department stores (up 2.1 percent), automotive dealers (up 3.2 percent), and furniture stores (up 1.8 percent), from February levels. (Source: U.S. Department of Commerce, April 12, 1982).

6. Housing starts bottomed at an 854,000 annual rate in October and recovered to a 947,000 annual rate in March. Housing starts were nearly 11 percent above the recession low in October. (Source: U.S. Bureau of Census, April 16, 1982).

7. Building permits for privately owned housing units bottomed at 722,000 in October. The rate in March was 870,000, up 20 percent from the October low. This indicates that further increases in housing starts are on the way. (Source: U.S. Bureau of Census, April 16, 1982).

8. The percent of industries in which employment increased was 31.4 percent in March. Nearly one-third of American industries increased employment during March. (Source: U.S. Bureau of Labor Statistics April 2, 1982).

9. During the 3 months through February, the compound annual rate of inflation as measured by the Consumer Price Index was 3.7 percent. (Source: U.S. Bureau of Labor Statistics March 23, 1982). The GNP implicit price deflator was up at a 3.6 percent annual rate in the first quarter of 1982.

10. The Federal budget deficit for the first five months of fiscal year 1982 was $2 billion less than for the same period in fiscal 1981. Individual income tax receipts for the first five months were over 10 percent greater than in the same period in 1981. Corporate tax receipts were up 11 percent. (Source: Treasury Statement of Receipts and Outlays of the U.S. Government, March 23, 1982).

11. The "coincident indicators index" was up .75 percent in February, the first increase since July 1981. In February this index included employment, real personal income less transfer payments, and industrial production. The composite index of four coincident indicators is a monthly approximation of aggregate economic activity. (Source: Bureau of Economic Analysis, U.S. Department of Commerce, March 30, 1982).

12. The "misery index", the combined total of the inflation rate, as measured by consumer prices, and the unemployment rate, fell to 11.4 percent in February from January's 12.4 percent. The index was at 19.3 percent in February of 1981.