CLINTONOMICS
A Report Card

JONATHAN KIM/TONY STONE

By Timothy Taylor

Whether you love William Jefferson Clinton or hate him, whether you think he should be anointed Emperor or tossed in the clink, it is inescapably true that as he enters his final year as President, the economy is in fine fettle.

In February 2000, the upswing that began in March 1991 reached 107 months. This breaks the previous record for the longest period of sustained growth in a century – a record previously held by great boom of the 1960's (February 1961 to December 1969).

When judging Clinton, grade on a curve

But the extraordinary length of the upswing is not the most surprising news. Just a decade ago, most economists were convinced that unemployment could not fall below 6 percent without igniting inflation. Yet joblessness has been below 5 percent since May 1997, even as inflation has hovered around 2 percent. Unemployment, now about 4 percent, has not been this low since the late 1960's, and inflation hasn't been this tame since the early 1960's.

You want more good news? The stock market has been on a roll since the 1980's, with the Dow Jones industrial average tripling since 1992. As recently as 1996, the budget deficit was in the $200 billion range and the White House was forecasting deficits as far as the eye could see. Yet by 1998, the budget was in surplus and the green-eyeshade crew was predicting that this happy state could last into the second decade of the 21st century.

Most delightful of all, the late 1990's have witnessed a surge in productivity. According to recently released figures, productivity growth averaged 1 percent annually from 1973 to 1982, rose to 1.7 percent a year from 1982 to about 1995 and then rose again to 2.5 percent a year from 1995 to 1998.

Productivity is the most powerful determinant of trends in living standards. If per capita gross domestic product rises at 1 percent annually, the standard of living doubles over a 72-year lifetime. However, if income per person grows at 2.5 percent, the standard of living rises sixfold over that same life span. If this recent productivity performance can be sustained, the American experience will change in remarkable ways during the 21st century.

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The President plays a remote second fiddle to the Federal Reserve on monetary policy.

HOW MUCH ARE PRESIDENTS RESPONSIBLE FOR THE ECONOMY?

The Clinton Presidency has certainly benefited politically from this boatload of good news. But how much credit can Bill Clinton fairly claim?

As the elected leader of the world's most powerful nation, the President is always in the limelight. But the United States economy is highly decentralized: although the White House can draft a trade treaty or send the Marines to Haiti, it cannot set wages at General Motors or tell the company when to roll out a new line of Chevy Blazers. Even in macroeconomics, the President rarely has much control over policy. He shares spending and tax decisions with Congress and plays a remote second fiddle to the Federal Reserve on monetary policy. By the same token, no President takes office with a clean slate. For better or worse, each must make do with a work perpetually in progress.

The serious moving and shaking in the United States economy happens in the private sector. The economy has about 5.5 million private companies, with about 800,000 new ones started each year. They operate within a web of regulation that both empowers them – for example, by making contracts enforceable

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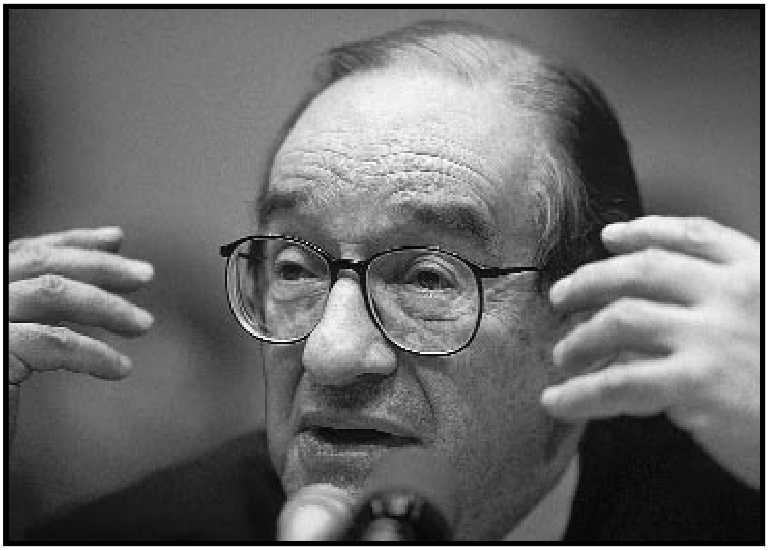
– and constrains them. But most business choices – those involving suppliers, production, marketing, accounting, hiring, compensation, sales, R&D, new products and more – are only marginally affected by Washington.

Tax policy affects these decisions, of course, as do the rate and composition of Government spending. But this is like pointing out that you can guide a Flexible Flyer careering downhill: in the end, gravity has more to do with where you end up than does your steering. Similarly, billions of daily business judgments have more to do with the shape and direction of the economy than do the incentives created by Government.



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Economic results not only bubble up from the decisions of managers and workers, but are shaped by international forces. Globalization gets the most attention when it is disruptive – as in the rise of Japanese competition in the 1970's, or in the Asian financial meltdown in 1998. But unseen trends and obscure events can also have great impact.

Consider international trade and financial flows. In the 1960's, the United States ran moderate trade surpluses every year. At the end of the decade, imports and exports each equaled about 6.5 percent of GDP. In the 1990's, by contrast, trade was more like 15 percent of GDP, and the United States economy ran a "current account" surplus only in 1991, when the United States recession slowed imports. In 1998 the current account deficit hit an all-time high of $220 billion and may have touched $300 billion in 1999.

Indeed, because of the large and growing trade deficits, the United States economy has become heavily – and seemingly permanently – dependent on inflows of foreign capital. Yet no President chose to make this seismic shift, and it's far from clear that even a determined President could have done much to resist it.

Similarly, it's hard for the White House to bear much responsibility for the policy-making power of the Fed. Jimmy Carter can claim some credit for appointing Paul Volcker to head the Fed in 1979, as can Ronald Reagan for nominating Alan Greenspan in 1987. But the most that the Clinton Administration can claim is to have stayed out of the Fed's way.

Finally, there is the question of what a President inherits – and what he bequeaths. The table on page 53 offers some comparisons of the economic reality inherited by the last four United States Presidents. Clinton took office with an unemployment rate similar to that inherited by Carter and Reagan, while all three faced unemployment rates worse than the one inherited by George Bush. Clinton inherited the lowest inflation rate of the four and Reagan by far the highest.

Of the four, Reagan clearly inherited the worst economic situation: high unemployment, towering inflation and the economy on a roller-coaster ride between recessions. Bush inherited an economy that appeared in strong shape, with low unemployment and a long boom well under way.

However, Bush had the misfortune to take office just as the Fed made a lunge against inflation. The benchmark interest rate that banks charge each other for overnight loans rose from 6.1 percent in February 1987, 23 months before Bush entered the White House, to 9.8 percent by March 1989, two months after. Thus, Bush inherited an economy that looked good – yet one in which the Fed was stomping on the brakes.

Carter and Clinton each inherited economic upswings that had been under way for 22 months. In political terms, this may be an ideal time frame for taking credit for a recovery. Indeed, in some ways Bill Clinton was bequeathed the ideal situation. Unemployment was high in January 1993 but was already falling. The unemployment rate dropped to 6.5 percent by December 1993, before Clinton's economic policies could have any real impact. Since inflation was already under control in 1993, there was no immediate danger that the Fed would rain on this President's parade.

The flip side of the economic reality a President inherits is the one he leaves behind. Even if a new President manages to get legislation enacted with all due dispatch – a minimum of six months – major policy shifts rarely have much impact in less than a year.

Thus, in appraising Carter's economic legacy, it's worth remembering that a mere six months after he left office, the economy went into a nasty 16-month tailspin. On the other hand, Bush presided over the first 22 months of what has turned out to be the longest recorded economic upswing in United States history. As for Clinton, the book won't close the day he leaves office. If a recession arrives during 2001 – or, for that matter, in 2002 – it will, in part, be a Clinton recession.

With these reservations duly noted, a President's economic policies still matter. Even one with limited power has more ability to affect the economy than any other public official in the world – save the chairman of the Federal Reserve.

HOW DOES CLINTONOMICS STACK UP?

If ever a Presidency begged to be evaluated on its economic performance, it is this one. After all, the unofficial slogan of the 1992 Clinton campaign was, "It's the economy, stupid."

However, it should be clear by now that a President's economic legacy can't be measured by crude aggregates like the unemployment and growth rates. That would be like comparing the current performances of the chairmen of IBM and Apple Computer solely on this year's profits. Circumstances, history and judgment matter, too.

A more useful approach is to examine actual policy choices. Looking back, I count five moments at which the Administration can fairly claim substantive initiatives.

The first was the 1993 budget, a deficit reduction package that included spending caps and higher taxes on the affluent. It was clearly Clinton's budget, passing Congress without a single Republican vote. But it did not strangle the economy, as its more strident opponents had predicted. Instead, it created the spending discipline that pushed the budget into surplus later in the decade and gave the Fed the discretion to keep interest rates low in the teeth of the economic boom.

A second important Clinton decision was to support the institutions of free trade, notably through the passage of the North American Free Trade Agreement and the creation of the World Trade Organization. For ardent free-traders (like me) the President's advocacy often seemed frustratingly half-hearted – as does his current reluctance to embrace reforms of anti-dumping rules. But when push came to shove, Clinton made common cause with Republicans in Congress (and against many in his own party) to drive these deals through.

A third economic initiative for which Clinton deserves credit is really a package of policies, all intended to strengthen the work ethic among low-skilled workers. The best-known is the 1996 Welfare Reform Act, which ended the entitlement status of welfare and imposed work requirements. Clinton had promised during his 1992 campaign "to end welfare as we know it." Even though the package that emerged from the Republican-controlled Congress in 1996 offended his liberal supporters, he bit the bullet.

The Administration supported other steps to raise the living standards of the working poor: the expansion of the earned-income tax credit wage subsidy, expansions of Medicaid to cover the families of the working poor and a higher minimum wage. I'm a bigger fan of the EITC and Medicaid changes than of the minimum wage increase. But recent research suggests that modest increases in the minimum wage do little harm – and may do some good.

The fourth Clinton economic policy of note can be measured by its degree of self-restraint: the White House has not second-guessed the Federal Reserve. A cynic might say that there hasn't been much to criticize. But the Fed did carry out a controversial "preemptive strike" against inflation by doubling short-term interest rates, from 3 percent in 1994 to 6 percent in February 1995.

Some Democrats railed against this increase, fearing that Greenspan had a secret agenda to bring on a recession and drive Clinton from office in 1996. But to its credit, the Clinton Administration said little, acknowledging that the first priority was to keep inflation low – thus buttressing the Fed's credibility.

THE PRESIDENTS' ECONOMIC LEGACIES

	UNEMPLOYMENT	INFLATION	HOW LONG UPSWING?	HOW LONG UNTIL RECESSION?
JIMMY CARTER (January 1977)	7.5%	5.2%	22 months	36 months
RONALD REAGAN (January 1981)	7.5%	11.8%	6 months	6 months
GEORGE BUSH (January 1989)	5.4%	4.7%	74 months	18 months
BILL CLINTON (January 1993)	7.3%	3.2%	22 months	——

Giving Clinton credit for a fifth initiative, the repeal of the Depression-era Glass-Steagall Act that kept banks from merging with other financial institutions, is a bit of a stretch. Repeal was hardly the Administration's highest priority. But the bill did pass with White House help, and this limited bank deregulation will open the door to substantial efficiency gains in America's financial-services industry over the next few years.

Others might wish to add to this list of achievements. For example, some would credit the Administration with a resurgence in antitrust activism in light of the Justice Department's much-heralded attack on Microsoft. But whatever one's views on the merits of the Microsoft case, it's hard to discern a clear policy emerging. An administration that has overseen record levels of mergers and acquisitions – including a marriage of the oil behemoths Mobil and Exxon – can hardly claim credit for a crusade against corporate size and power.

It's interesting to compare Clinton's list of substantive economic policy steps to those of his immediate predecessors. George Bush cut his own deal to reduce the budget deficit in 1990, with his own set of spending caps and tax increases. The impact on the deficit was delayed because the recession of 1990-1991 led to lower tax payments and higher spending on the social safety net. But the long-term impact of Bush's 1990 deal on the budget deficit was actually larger than the 1993 Clinton package.

Bush provided a solid economic framework. Clinton reaped the rewards.

The Bush Administration negotiated NAFTA and initiated the talks that led to the WTO. Bush also encouraged the first welfare-to-work initiatives, which were mandated under the Family Support Act of 1988. The Bush Administration dealt aggressively with the collapse of the savings and loan industry. It first pushed for passage of the Financial Institutions Reform, Recovery and Enforcement Act of 1989, which reorganized deposit insurance for the S&Ls and provided $150 billion to pay off depositors. Then, it followed up with the FDIC Improvement Act of 1991, which reorganized banking regulation. Indeed, this latter law made the repeal of Glass-Steagall politically thinkable.

In many ways, the Bush and Clinton economic initiatives were on the same track. The Bush legacy is very similar to Clinton's.

Yes, Bush presided over a recession induced by a combination of higher interest rates and a spike in oil prices during the Gulf War. But I find it hard to blame his Administration for interest rate increases that happened before he took office, or for the imperial ambitions of Saddam Hussein. Bush provided a solid economic framework. Clinton built on that framework and reaped the rewards.

How does the Clinton legacy stack up against Ronald Reagan's? Each led the economy through a long period of growth and stable prices. As noted earlier, productivity growth increased in the 1980's and increased still more in the last few years. But in both cases, the good news had far more to do with private trends, especially the remarkable developments in information and communications technology, than with Presidential leadership.

Reagan does deserve credit for reducing high marginal tax rates and for passing the loophole-closing Tax Reform Act of 1986 in his second term. He also stalwartly backed the Fed's efforts to reduce inflation, even when tight money led to a deep recession early in his first term. The 1988 welfare-to-work legislation passed on his watch. However, Reagan left behind a huge Government debt and chronic budget deficits. Also, even though the Reagan Administration did support the earned-income tax credit, it did little else for low-skilled workers.

All told, comparing the Clinton Administration's economic legacy with the Reagan Administration's comes down to how one weighs the benefits of tax reform and lower marginal tax rates against the lower Government debt and greater advocacy for the working poor. It's a closer call than partisans on either side like to admit.

CLINTON'S SINS OF OMISSION

Clinton's greatest economic liabilities are tied not to what he did but to what he hasn't done. For example, it was widely recognized in the early 1990's that Social Security and Medicare could not be sustained indefinitely at the legally mandated levels of taxation and benefits. However, the Clinton Administration has never stood behind a clear vision for reform. Indeed, it has done its share to poison public discussion of the issues.

Back in 1995, the Republican-led Congress proposed sweeping changes to slow growth in Medicare spending. Hard though it is to remember, the auguries for passage of a compromise were favorable. Then came the 1996 election season and, led enthusiastically by Clinton, the Democrats used Medicare as a club to beat the Gingrich crew. It made for good politics but destroyed all vestiges of bipartisanship on this delicate issue. Since then, the Republicans have refused to take the lead on either Medicare or Social Security.

Subsequent discussions of the big entitlement transfers have been dominated by split recommendations from bipartisan commissions. An advisory council was appointed to look at Social Security. But its 1996 report only emphasized the members' deep differences: some wanted to preserve the present system, some wanted to privatize pensions and some wanted to create a hybrid system. The Bipartisan Commission on the Future of Medicare, popularly known as the Breaux Commission, presented an equally divided report in March 1999.

In neither case did the Clinton Administration take a strong position or push for a compromise. Far from it: the President's empty stance as the great defender of Social Security and Medicare has reduced the prospect of reforms anytime soon.

Clinton's efforts also fell short in health care. Today, the number of uninsured Americans and the annual rate of increase in health-care costs look very much as they did when Clinton first took office.

Perhaps the problems of America's health-care system are too deeply rooted for a President to make much difference. But the ham-handed way in which Clinton approached reform in 1994, handing it over to his untested spouse and her old college chum while shutting out both centrist economists and Republicans, was hardly a practical approach.

A third fundamental issue is investment in productivity. When Clinton was elected in 1992, productivity growth had been falling short since the early 1970's. The pace has picked up since the 1980's, thanks to the new developments in information technology. But the Clinton Administration has done relatively little to nourish the renaissance.

This assessment may seem harsh: Clinton can point to the 1993 Deficit Reduction Act, which ultimately took the Government out of the competition for private savings. However, the investment surge of the 1990's has been largely financed with capital from abroad, which implies that a good chunk of the returns will go to foreign investors. America's R&D spending rose from 2.2 percent of GDP in the 1970's to 2.6 percent of GDP in the 1980's, but has stayed at that level since. Finally, while Clinton has talked a lot about improving public education, his impact on schools has been modest at best.

A fourth test of the economic dimension of the Clinton Presidency is less tangible: did he make the public more amenable to globalization? Earlier, I gave the Clinton Administration credit for its support of NAFTA and the WTO. But with time running out in Clinton's second term, Americans are probably more hostile to trade than they were in 1992. In a poll in late 1998, protectionists outnumbered free-traders by 56 percent to 37 percent.

The protectionist cause has attracted strange bedfellows in recent years, from labor on the left to isolationists on the right to environmentalists and populists from across the political spectrum. The battle of Seattle in December, when the World Trade Organization failed even to set an agenda for further talks, showed that many Americans have come to believe that trade is a foreign plot. Consequently, there has been a crying need for a President who would explain the importance of free trade and stand by it.

Instead, the White House has practiced brinkmanship, threatening allies with sanctions in the name of looking tough, while backing away from actual trade wars. This lent credence to those who believe that "unfair" trade is deeply injurious to America's economy, while further convincing them that nothing will be done about it.

A final test of the Clinton Administration has been its impact on social mobility. Yes, the White House has supported policies to help the working poor. But it is hard to argue that members of the underclass and their children have a markedly better chance to succeed in America's competitive economy than they did back in 1993.

The problems that Bill Clinton failed to ameliorate all predated his Administration, and so it may seem inappropriate to place them on his account. But Bill Clinton entered office without the double-digit inflation and looming recession that Ronald Reagan faced, and without the rising interest rates, recession and S&L meltdown that George Bush confronted. Clinton has benefited from unbroken prosperity, which should have bought him some political space to leave a more important mark on the commonweal.

GOOD FORTUNE AND COMPETENCE

Historians will look back on Clinton as a President who was dealt a great economic hand. He entered office in January 1993 just as the economic recovery was shifting into high gear. He had the good fortune to inherit Alan Greenspan. He inherited a framework for deficit reduction, trade liberalization, welfare reform and banking deregulation that he could build upon.

This good fortune extends to the world arena. On his watch, Japan became a paper tiger and Europe was too preoccupied with its own economic and monetary union to stir the global economic pot. Energy prices, untouched by conflict in the Middle East, have remained relatively stable.

Perhaps Clinton's greatest good fortune has been to reap the fruits of the revolution in information and communications technology. That revolution has not only raised productivity but driven the stock market to levels unimaginable in 1993. And tax revenues from the whopping capital gains of the late 1990's helped balance the budget in double-quick time.

The Clinton Administration has played the economic game competently, and competence should never be belittled. But competence must also not be confused with the situational advantage. Bush was about as competent as Clinton, but confronted harsh challenges. Clinton's economic policy, by contrast, allowed and assisted a good situation to continue – but that is no reason to cast the President as a genius. Nothing in Clinton's economic record reaches beyond competence, which is why it should go down in history as only a notch or two better than ordinary.