FEBRUARY 3, 1989

TO: SENATOR DOLE

FROM: KATHY ORMISTON
CAROLYN SEELY

SUBJECT: MERRILL LYNCH SEMINAR TAPING

Last night Merrill Lynch submitted questions which may be asked during the 2:30 p.m. taped interview. We have prepared some possible responses.

QUESTIONS FOR MERRILL LYNCH INTERVIEW

1) What is the likelihood of our meeting the Gramm-Rudman targets for FY 1990?

THE PRESIDENT APPEARS TO BE VERY COMMITTED TO WORKING WITH CONGRESS AND PRODUCING A BUDGET AGREEMENT EARLY ON IN THE ADMINISTRATION. HIS FIRST MEETING WITH CONGRESSIONAL LEADERS WHICH I ATTENDED WAS A TWO HOUR BIPARTISAN SESSION ON THE DEFICIT. BOTH THE CONGRESS AND THE PRESIDENT WANT TO AVOID THE TURMOIL A SEQUESTER WOULD CAUSE.

PRESIDENT BUSH WILL, I AM SURE, PRESENT US WITH A BUDGET THAT MEETS THE GRAMM-RUDMAN-HOLLINGS TARGETS -- WE SHOULD DO NO LESS. I THINK OUR CHANCES OF MEETING THE TARGETS ARE QUITE GOOD IF THE CONGRESS IS SERIOUS ABOUT SPENDING REDUCTION.

2) What do you expect will be the differences in the Bush Administration's approach to the budget compared to the Reagan Administration's approach?

I THINK FROM THE STATEMENTS THE PRESIDENT MADE DURING AND AFTER THE CAMPAIGN WE CAN EXPECT TO SEE MORE SPENDING FOR PEOPLE PROGRAMS, ESPECIALLY EDUCATION, MEDICAID, THE HOMELESS, AND CHILD CARE. IT IS ALSO LIKELY THAT PRESIDENT BUSH'S BUDGET MAY REDUCE THE GROWTH IN DEFENSE SLIGHTLY TO PAY FOR THESE NEW EXPENDITURES.

THE BIGGEST SURPRISE MAY NOT BE THE DIFFERENCES IN THE REAGAN AND BUSH BUDGETS, BUT THE SIMILARITIES. A LOT OF THOSE PEOPLE, WHO GAVE THE REAGAN BUDGET ITS LAST RITES ARE GOING TO VERY SURPRISED INDEED.

3) What do you feel are the likely areas that we can achieve spending cuts this year?

I WOULD PREFER TO SEE PRESIDENT BUSH'S BUDGET CHANGES ON FEBRUARY 9 BEFORE I COMMENT ON THAT. I THINK WE OUGHT TO GIVE THE PRESIDENT A CHANCE TO PROPOSE HIS OWN PLAN.

4) What can we do to achieve long term solutions to our budget deficit problems?

ONE OF THE MOST IMPORTANT THINGS WE NEED TO DO IS MAKE SOME SIGNIFICANT REFORMS IN THE BUDGET PROCESS. IT'S A MESS AND MOST AMERICANS KNOW IT.

ON THE FIRST LEGISLATIVE DAY OF THE SENATE, I INTRODUCED TWO PIECES OF LEGISLATION TO ADDRESS BUDGET REFORM: A CONSTITUTIONAL AMENDMENT TO BALANCE THE BUDGET AND A BILL TO GIVE THE PRESIDENT ENHANCED RESCISSION AUTHORITY.

IN ADDITION, I HAVE COME TO BELIEVE THAT THE CONSTITUTION IN ARTICLE 1, SECTION 7, CLAUSE 8 ALREADY GIVES THE PRESIDENT THE LINE ITEM VETO. I HAVE ENCOURAGED PRESIDENT BUSH TO TEST HIS LINE ITEM VETO POWER AND ALLOW THE COURTS TO DECIDE WHETHER IT IS CONSTITUTIONAL.

5) What is you assessment of the overall economic outlook for the country?

I AM VERY POSITIVE ABOUT THE ECONOMIC OUTLOOK FOR THE COUNTRY. THE MARKETS HAVE RECOVERED STRONGLY FROM THE 1987 "CRASH". UNEMPLOYMENT HAS REACHED RECORD LOWS, AND AFTER SEVERAL YEARS OF STRONG ECONOMIC GROWTH, INFLATION IS STILL AT TOLERABLE LEVELS.

EVEN LIBERAL ECONOMISTS NOW AGREE THAT THE LONG PREDICTED RECESSION IS LOOKING LESS AND LESS LIKELY. AND IF WE CONTINUE CLOSING THE DEFICIT GAP, I THINK WE CAN EXPECT THE ECONOMY TO REMAIN IN GOOD SHAPE FOR YEARS TO COME.

Economic Headaches

President Bush may be able to avoid a recession, economists say, though it won't be easy. But can he free his economic agenda from Reagan's unfinished business?

BY JONATHAN RAUCH

In a complicated world, it is refreshing to discover that President Bush's economic agenda consists of only two items:

No. 1. Keep out of a recession.

No. 2. Everything else.

Of the six Republican presidential terms in the postwar period, five began with recessions: both of President Eisenhower's terms, both of President Nixon's and one of President Reagan's. Typically, inflationary pressures had built up, and recessions soon after the election tamped (or, in 1981, pounded) them back down. President Carter haplessly managed to run the Republican cycle in reverse, ending his term with a recession. Today, mindful of the regular pattern and of what happened to Carter when he defied it, some in Washington have quietly wondered whether Bush might be well advised to go ahead and get his recession over with early.

The answer: forget it.

Contrary to popular belief, the evidence is ambiguous on the question of whether high debt levels in the economy would make the next recession more serious than usual. But there is less doubt that a recession could be punishing for Bush, in economic as well as political terms. In a no-growth climate, bailing out savings and loans institutions would be a lot more expensive, the Third World debt situation might get out of hand, corporate bankruptcies could create all kinds of costly federal headaches. And Bush's prospects for growing out of the budget deficit would be ruined.

"If there were a recession in '89," Lawrence A. Kudlow, the chief economist of Bear, Stearns & Co. Inc. in New York City, said recently, "it would completely disrupt any deficit reduction plans, put everything on hold, and Congress would simply walk away from the Gramm-Rudman [1985 Balanced Budget Act] targets. This fiscal problem makes Bush's first year quite unlike other first years, from a macroeconomic standpoint. I don't think for Bush there's a first-year recession option."

At least as important from a Washington viewpoint is that Bush has made a political commitment to keeping growth going—perhaps a stronger and more explicit such commitment than made by any of his recent Republican predecessors. In September, Bush told *The Wall Street Journal* that the biggest economic issue is not to reduce the deficit but "to keep the recovery going. And I think it's to create more jobs." During the second presidential debate in October, he declared: "What I want to do is keep this expansion going. I don't want to kill it off by a tax increase."

The Bush staff has filled a thick volume with the new President's campaign proposals and promises, but only one, as of now, amounts to a clear economic policy mandate. As a member of the Bush transition staff put it, "Bush got elected with a mandate, first and foremost, to keep the economic recovery going." If there is one thing a new President does not want to do, it's to bungle his mandate.

Second on the Bush agenda is—you were going to say the budget deficit? Wrong. The deficit has become the Nicaragua of economic policy: a preoccupation that has tended to blot everything else out. Undoubtedly, the deficit is an important problem—probably the most important problem that the federal government, acting alone, has the power to solve. For Bush, the deficit is a political test of manhood. "I think of the deficit as the threshold he's got to get over to do these other things," Sen. Phil Gramm, R-Texas, said in a recent interview. "The economic credibility of the government is going to be measured by what we do on the budget deficit this year." *(See this issue, p. 121.)*

Even so, at an estimated 3 per cent of the gross national product

Richard A. Bloom

Sen. Phil Gramm, R-Texas
Bush needs a "vision that goes far beyond" Reagan's.

in the current fiscal year, the deficit is now viewed by most economists as being more like a festering (but slowly healing) sore than an acute illness. The priority at the top of the "everything else" part of the agenda is instead to hold inflation down, if only because the response to rapid inflation would probably be a tight-money policy, inducing a recession.

To avoid a recession, three things have to go right. First, there must be no crippling outside shock—no drought, oil crisis or whatever. Second, Bush has to avoid making any big mistakes—say, a descent into a protectionist maelstrom, an S&L-driven crisis in the financial industry or a perceived failure on the deficit. Third, the Federal Reserve Board has to stay ahead of inflation, and it has to be perceived as doing so.

The Fed is not unaware of its critical role. "If we do our job well, a recession is not necessarily inevitable," Manuel H. Johnson, the Fed's vice chairman, said. "Barring those outside shocks or policy mistakes, I think it's pretty much up to us."

If Bush can live up to his anti-recessionary campaign rhetoric, he will have the money and the opportunity to get a start on his kinder and gentler initiatives—if, that is, he can also bring his domestic priorities into sharp enough focus to take control of the agenda, a task that remains ahead of him.

Two questions are thus central for the new President. Can he realistically hope to avoid a recession? And, given that there is more to life than balancing the budget, can he define a positive economic program?

EVITABILITY

Until recently, most people probably took it for granted that every so often—about every four or five years—the economy would stall into a recession. But as the current expansion has stretched on into its seventh year, becoming the second-longest of the postwar era, a certain amount of rethinking has been going on. No one is saying that there will never be another recession. But few economists are saying these days that recessions are either inevitable or regularly periodic.

"Business cycles occur because of two things: One is a policy mistake, or two is an external shock to the economy," David H. Resler, the chief economist for Nomura Securities International Inc. in New York City, said in an interview. "I totally reject the inevitability of recessions. It's only inevitable if excesses in the economy can't be contained." At Georgia State University's Economic Forecasting Center, Donald Ratajczak said, "An expansion doesn't end because of old age; it ends because of economic imbalances."

That view, or some close variant on it, has become more or less predominant. And the view that markets themselves generate regular imbalances, and thus are inherently unstable, falls increasingly out of vogue as the expansion continues. Instead, imbalances are seen as generally caused by outside forces—in particular, shocks to the system such as the oil-price jumps of the 1970s—or by a serious policy mistake, such as the easy-money policy many economists blame for creating the inflationary spiral of the 1970s.


Susan M. Muniak

Brookings Institution economist Robert E. Litan
"I'd say it's a better-than-even bet that [Bush will] skate through for four years."

The first question for Bush, then, is whether imbalances are building up within the economy. The consensus answer is that such imbalances are not now in evidence, but that there is not necessarily a lot of room for maneuvering. "This economy is clearly in that area where we can't grow easily without stimulating inflation," Ratajczak said. In particular, manufacturing capacity utilization, a number that economists watch closely for clues as to how much room for growth remains in the economy before inflationary shortages set in, is at nearly 85 per cent. That's not as high as in the high-inflation late 1970s, but it is still high enough to make many economists nervous.

Nonetheless, that's only a small part of the story. "On my computer, I could avoid a recession with the right mix of policies," Ratajczak said, "and maybe it's worth a try."

What economists are hoping will happen is this. Earlier in the expansion, strong demand and rapid growth in the United States pulled along foreign economies, which prospered by shipping their goods here for Americans' consumption. More recently, U.S. domestic demand has slowed somewhat, while demand has picked up abroad. If all goes as the experts hope, that pattern will continue—especially if a lower U.S. budget deficit helps dampen demand and free up capacity at home. Strong demand overseas would make room for U.S. exports, so that the U.S. trade deficit would come down. In effect, America and the rest of the developed world would change places. Meanwhile, continued but not overexuberant capital spending in the United States and elsewhere would keep the economy's productive capacity growing, relieving inflationary pressures.

That is quite a bit to hope for; but so far, so good. "I don't see that there's any reason to expect the economy to go into a recession," W. Lee Hoskins, the president of the Federal Reserve Bank of Cleveland, said. Recessions have generally been caused by policy mistakes, he said. "As I look at it now, I don't see anything that's baked in the cake that would cause policy shocks."

Recently, the numbers have been especially hard to read. *(See box, p. 119.)* They can be reasonably regarded as warning of overheating or as signaling the hoped-for moderation of U.S. growth. Milton W. Hudson, the senior economic adviser at Morgan Guaranty Trust Co. in New York City, views 1989 as a close call between the expansion's spilling over "into an untidy end-phase of the cycle" and a shift to slower growth. If it's the latter, he said, he sees no reason why the recovery couldn't go on for quite a long time.

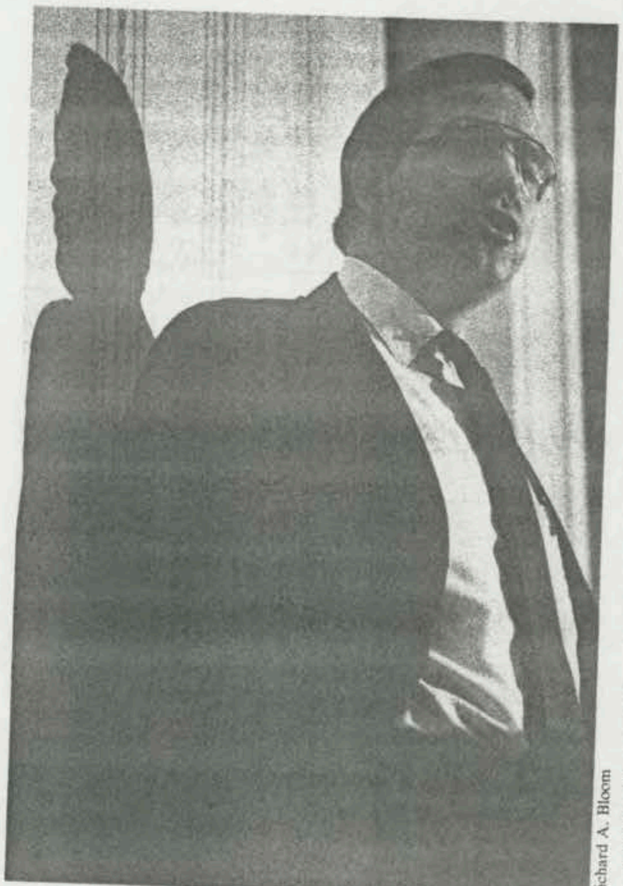
No one thinks that that is overwhelmingly likely. Still, the number of economists taking seriously the proposition that Bush might get through his whole first term without a recession—achieving a 10-year expansion—comes as something of a surprise. At the Brookings Institution in Washington, economist Robert E. Litan today says what he can't imagine himself saying even two years ago: "I'd say it's a better-than-even bet that he'll skate through for four years."

Partly, this sense that a Bush recession is not inevitable stems from the unexpected durability of the Reagan expansion. But there are grounds to wonder, too, whether the economy may be more recession-resistant than in the past. To an extent never seen before, a single international capital market, through which huge sums move at lightning speeds, has replaced separate national ones. Moreover, deregulated interest rates, as Kudlow pointed out, respond to changing events with a shorter lag than before. Arguably, therefore, anything that any one country or industry does is absorbed by a much larger market, and is more quickly counteracted by financial flows, than in the past. The economy is better able to adjust to surprises before self-feeding cycles of overreaction get started and turn into a broad downturn.

Most U.S. economists, for example, expected the large budget deficits of the early 1980s to drive up interest rates to levels that would choke off growth; the reason this didn't happen was that foreign funds came pouring in. The dollar and the trade deficit roared upward, punching U.S. farmers and manufacturers in the gut. None of that was pleasant, but it was better than a general recession. It is also possible that what would ordinarily have been the next recession has already taken place, but in the form of a steady stream of smaller, painful but nonrecessionary adjustments in agriculture, manufacturing, energy and other sectors.

"I think if policies are stable, you're going to have these rolling industry recessions," the Fed's Johnson said, "but there's no reason for them to develop into something general."

HOW HARD A FALL?



Richard A. Bloom

Fed vice chairman Manuel H. Johnson
If the Fed does its job, a recession isn't inevitable.

At Brookings, Litan said, "It's probably true that in the absence of major OPEC-like shocks, we may be in the middle of a new era that's recession-free." It will take a few decades, of course, to find out whether he is right. And no one is betting large sums of money on the business cycle's demise. "I guess when we think the business cycle is dead is when it's going to come back and bite us from behind," said M. Kathryn Eickhoff, a New York City economic consultant and former Reagan Administration economist.

Suppose there is a recession. Would it be disastrous, as some have warned? Many of the people issuing these warnings have been using the threat of a recession as a bogeyman with which to lobby for preferred policies. Conservatives (and Bush) say that a tax increase would start a recession, and liberals argue that spending reductions would start one. Actually, it isn't at all clear that a recession would be easy to create or that if one were created, it would be unusually severe. Yes, the budget deficit would go up, but that would not make the recession itself any worse.

More worrisome is that heavily indebted corporations might start going bankrupt in unprecedented numbers. In the 1988 Brookings Institution book *American Living Standards: Threats and Challenges*, Litan writes, "The [computer] simulations suggest that another recession comparable to that of 1981-82 could easily double the current number of corporate bankruptcies."

But what people often forget, Litan said in an interview, is that "just because [more] corporations go bankrupt does not mean you have a deeper recession." Bankrupt corporations are restructured while their creditors are put on hold, Litan said, but they don't disappear. Moreover, he said, the next recession would presumably start at lower rates of inflation than in 1981, and so the Fed could come to the rescue earlier with monetary stimulus.

Still, there is no doubt that a recession would be costly—particularly so for Bush. The public forgave Reagan his recession because it turned out to have been an inflation-killer; a Bush recession would just be a recession. Also, Bush ran against the Democrats with a warning that if they were elected, they would upset the steady prosperity of the Reagan years. So a recession would not do his political credibility much good.

And then there is the fact that some of the economy's most dangerous trouble spots relate to debt: the savings and loan problem, the Third World debt crisis and the budget deficit, to name the three most prominent. As a class, debt problems are easier and less costly to deal with in prosperous times than when incomes get socked, which is what happens during a recession. If a recession led to the souring of significant amounts of debt, the Bush Administration could have a lot more cleaning up and bailing out to do than if growth gradually alleviated debt burdens. Furthermore, an early recession could afflict Bush with a reinvigorated deficit crisis, preoccupying everybody and reducing his ability to take charge of the domestic agenda.

Bush can buy himself some recession insurance by getting the deficit down, and thus (most economists expect) freeing more space in the economy for noninflationary growth. Besides, some observers say, he has to show that he is doing more than just crossing his fingers and hoping for the best. Persuading the world that he is in charge means being perceived as doing something about the deficit.

"In the short run, it has to be clear that George Bush has a workable program to reduce the deficit, meet the Gramm-

Rudman targets and continue the economic recovery," Gramm said. "I think the plan has to be presented pretty quickly, and I think the President has to put a tremendous amount of political capital into the economic debate"—something that Reagan, Gramm noted, didn't do after the first year or so.

One other thing: Bush and other policy makers, some analysts say, have to be careful not to insist on pushing the economy too hard. "The Fed knows this, and I think the Bush economic team knows this as well," Kudlow said. "You don't hear what I call the extreme supply-side view" that the sky is the limit. This time eight years ago, the Reagan team based its first budget plan on assumed real economic growth of about 5 per cent in 1982 and 1983. All such wildly optimistic talk has disappeared; the final Reagan budget calls for growth of about 3.5 per cent, and the Bush people show no signs of reverting to go-go rhetoric.

In all of this, the Fed's role is crucial. "In effect," Litan said, "George Bush is relying on the Fed to fine-tune him [around] the next recession—and so far, the Fed has been terrific." Gradually but steadily, the Fed has been tightening the money supply and raising interest rates. The federal funds rate, an interest rate that the Fed can directly control, has moved up a full percentage point since August, and 2 points since May. "We've done it slowly and smoothly, but consistently," Johnson said.

Confusing Economic Numbers

Economic numbers are hard to read under the best of circumstances. But in the past few months, if you were trying to figure out whether the economy is headed toward overheating or cooling off, you'd have especially good reason to be puzzled.

"The source of the confusion is that the economy is giving conflicting signals on a month-to-month basis," said Gail D. Fosler, the economist for the Senate Budget Committee's minority staff. Here's a sampling of what forecasters are up against:

- The index of leading indicators, which is supposed to warn of coming economic downturns, has been behaving like a yo-yo. It fell in May, rose in June, fell in July, rose in August, fell in September, rose in October and fell in November. The rule of thumb says three consecutive drops warn of a recession. But, recently, the index hasn't done anything consecutively.
- October brought the news that in the third quarter of 1988, the economy grew at its slowest rate since 1986, a possible sign of slowdown. But close on the heels of that news came the announcement of a fall in civilian unemployment to 5.3 per cent, matching June 1988 for the lowest rate since 1974. December repeated that performance.
- New orders for capital goods, which are a barometer of manufacturing strength and which boomed in 1987 and much of 1988, have weakened in recent months. But a recent survey of purchasing agents for industrial companies found a rapid surge in activity in December, and the industrial production index has been strong.
- Manufacturing employment fell in August and September, as though to presage a slackening, but then rebounded. And nonfarm employment, a broader measure, has soared recently, with a million jobs added from August to November.

As of now, the most common reading is that growth will continue, but at a somewhat reduced pace. To that, the data say clearly: maybe, maybe not. "We are clearly in experimental territory," Fosler said, "in terms of the length of the cycle and the vehicles we have used to keep it going."


Susan M. Muniak

Economic consultant M. Kathryn Eickhoff
The business cycle is far from dead.

As of now, the financial markets seem satisfied that the Fed has inflation well in hand. If that confidence evaporates, the Fed's job, and thus Bush's, will get substantially harder.

BEYOND THE DEFICIT

The prescription for Bush, then, is this: His best hope of living up to his continued-growth mandate—and he has some real prospect of doing that—is to be perceived as being on top of the the deficit, to avoid committing any big blunders and to cross his fingers. The trouble with that economic prescription is that it is not an agenda for positive governance. And as Bush prepared to take office, it was not clear just what such an agenda might be.

In September 1980, candidate Reagan set out the basics of his economic program in a speech in Chicago: constrain the rate of growth in government spending, cut taxes 30 per cent over three years, review and overhaul regulations and run a tighter ("stable and sound," Reagan called it) monetary policy. After the election, Office of Management and Budget (OMB) director-designate Dave Stockman and members of Reagan's policy staff worked frantically to prepare a set of economic proposals with which to storm the congressional barricades. Whatever one may think of the resulting policies, the Administration's approach put Reagan on the offensive and gave shape and direction to his economic policy making for four years.

No comparable effort seems to have been mounted by the Bush team. "There's really nothing going on, as far as I can tell," a member of the Reagan Administration said. "Personnel is there, and still nothing seems to be happening. . . . The impression I get is that there's a general sense of downgrading of the White House policy process."

Actually, there are some good reasons for Bush not to take a storm-the-barricades approach. In 1980, Reagan was elected having promised to take whatever steps were necessary to get the economy straightened out, and he had just thrown out a Democratic President. Bush, by contrast, was elected with a mandate to change things, but not very much. Besides, as a Bush staff member noted, Reagan's approach would not necessarily be appropriate for Bush. "Reagan's style was high drama," the staff member said. "I think Bush is going to be the kind of guy who says [to House Ways and Means Committee chairman Dan Rostenkowski, D-Ill.], 'Look, Danny, you and I served on Ways and Means together, we're pals—let's do this.' "

This approach has made for much comity and friendly talk between Bush and the congressional leadership, but it is not without risks—chief among them that Bush may lose control of the domestic policy agenda to Congress and to the budget deficit, the S&L mess, the nuclear materials crisis and whatever other fires need to be put out. Reagan was able to prevent such matters from seizing the agenda, often by blithely ignoring them; Bush might not be able to get away with a stay-aloof strategy even if he were inclined to try, which he probably isn't.

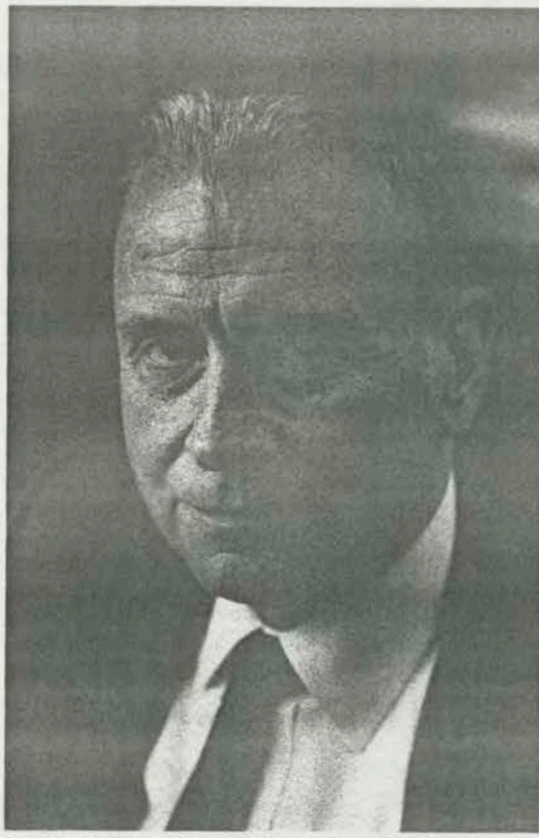
"He will not have the mandate that Reagan had in 1981," said Rep. Lee H. Hamilton, D-Ind., the new chairman of the congressional Joint Economic Committee. "What impresses me is how little I know about George Bush's economic policy. He has said amazingly little about that."

Asked just what Bush's agenda would look like, staff members point to a 347-page collection of his campaign speeches and policy proposals. Included is everything from "George Bush will ban all ocean dumping of sewage sludge by 1991" to a call for investment in the prevention of heart attacks. The book is full of ideas; to an outsider, however, it looks more like a menu than an agenda.

Stockman's current counterpart, OMB director-designate Richard G. Darman, has been busying himself with the deficit problem. At least one Bush insider hinted that Darman takes an ambitious view of OMB's role and may well emerge as the leading force behind domestic policy thinking. But if Darman has formulated an economic agenda beyond getting the deficit down, it is still in his head.

At the Treasury Department, Secretary Nicholas F. Brady is known to think that the Third World debt problem and the S&L crisis, particularly the latter, ought to be grappled with early on. Treasury has been studying strategies for dealing with both, according to a department spokesman, and Brady hopes to get moving quickly with corrective action on the S&L front. *(See NJ, 1/14/89, p. 60.)* Treasury, meanwhile, has convened a study group to develop policies encouraging investors and managers to focus more on long-term goals and less on the next quarter's bottom line.

"This is something that [Brady] has a great deal of interest in," the Treasury spokesman said. But, he added, the result is not likely to be a splashy package of first-year legislative proposals so much as a continuous effort to consider policy improvements. "This is a long-run thing,"



Richard A. Bloom

Economic Committee chairman Lee H. Hamilton
Bush won't have the mandate" Reagan had.

he said. "It may take the full four years of the Bush Administration."

Judging from what several members of Bush's transition staff said, the likeliest place to look for agenda-shaping initiatives from Bush is on the new President's kinder and gentler side. They say that Bush is absolutely serious about reforms dealing with education, the environment and poverty. "His own personal commitment to these things is very strong," an aide said.

In that commitment, Bush is following, as much as leading, Republican opinion. Housing and Urban Development Secretary-designate Jack F. Kemp has been preaching for years that Republicans need to reach out to the less privileged: "You're never, as a conservative, going to appeal to a black constituency in America if you say that government is the enemy," Kemp said in a 1987 interview.

Somewhat less expected, though, is the suggestion from Sen. Pete V. Domenici, R-N.M., that tackling inner-city problems represents "a rare opportunity for Republicans." In an interview last year, he said: "I think Republicans ought to go after them [the inner-city poor]. We ought to put the best thinkers and bona fide concerned people to work on it." The federal government needs to do more to solve the problems of drugs, the underclass and undereducation among the poor and minorities, he said: "I think those are very, very dangerous things for our economic productivity. They're not just social issues."

Domenici is the sort of moderately conservative, business-oriented politician who was synonymous with "mainstream Republican" in the days before the Reagan wing took charge of the GOP. For that matter, so is Bush. Republicans who talk of taking on issues traditionally viewed as belonging to the Democrats are largely reflecting sentiment within their business constituency. Business has become active in calling for improvements in education; a recent Opinion Research Corp. survey found two-thirds of business executives saying that the U.S. educational system is inferior to its European and Japanese counterparts at preparing young people to enter the work force.

Meanwhile, as zealous an opponent of pork-barreling as Gramm asked an interviewer to imagine how many jobs the economy could create "if government was actually building infrastructure again." A century ago, Republicans and their business supporters, in the name of advancing commerce, used federal muscle and tariff receipts to build railroads and bridges. If Bush seeks to mobilize government to solve social problems and build public goods, he may find a strong base of support in the post-Reagan GOP.

But all of that remains ahead. First, the new President has to deal with the deficit. That is likely to be hard enough. What may be still harder for him will be to look beyond the deficit so as to free his presidency from Reagan's unfinished business.

"If it becomes clear that you have a vision that goes far beyond the Reagan vision," Gramm said, "you can create an optimism that feeds on itself."

There's that "vision thing" again. The question remains, as it was before the election, whether Bush can gather his domestic policy proposals from all points of the compass and fashion a course that establishes a clear direction, a governing philosophy, for his presidency. □