REMARKS OF SENATOR DOLE

CONGRESSIONAL LEADERSHIP SEMINAR

Friday, January 25, 1985--8:00 a.m.

Mayflower Hotel, Chinese Room, Washington, D.C.

1. The 99th Congress

o The 99th Congress is gearing up to face major challenges right away, ranging from spending cuts to reduce the budget deficit to the MX missile, from tax reform to aid to the contras in Nicaragua. I believe we can meet all of these challenges if we forge a strong working relationship, based on mutual respect, with President Reagan. We have an obligation to do that, because dealing with these problems is in everyone's interest--particularly the public interest.

o We should not pretend that everything will be easy going, but I believe the new leadership in both the Senate and the House know and respect one another, and are prepared to go to work. We will have our differences, and there are bound to be winners and losers. But all members of Congress know that President Reagan's overwhelming election victory sends a strong message about what the people expect us to do. President Reagan knows that I already am at work on his agenda for Congress. Success will depend a lot on keeping all channels of communication open at all times, and on mutual recognition that Pennsylvania Avenue is a two-way street.

o Our top priority is to cut spending to reduce the budget deficit. That is why Senator Domenici and I introduced S. 1, which commits us to getting the deficit down to $100 billion or less by 1988. The vital issue of tax reform should proceed on a separate track to allow us to sort out the options and see if we can build a consensus without losing momentum on the urgent problem of the deficit. Other issues that require attention in 1985--a new farm bill, Superfund, national defense, and arms control--will not be neglected. But unless we can keep the recovery going at a steady pace and act decisively on the deficit, we will not be fulfilling our responsibility to the voters.

2. Our Economic Progress

o Economic recovery remains on track and is moderating to a pace that can be sustained in the years ahead. Real GNP grew 6.1% in 1983, and continued at 6.8% in 1984, peaking at a 10.1% rate in the first quarter last year. That is the highest real growth rate since 1951. This remains one of our strongest recoveries.

o With national unemployment down to 7.2%, this recovery has created over 6.5 million jobs. More people are working than ever before. Factories are operating at the highest capacity levels in 4 years, close to 82%. Housing starts in 1984 reached 1.74 million, the best since 1979.

o The best news about this recovery is that inflation is staying low. Producer prices in 1983 showed the smallest increase since 1964. The 1983 CPI increase was just 3.8%, indicating we can sustain strong growth with low inflation. Prices rose by only 3.7% in 1984, and most economists expect inflation to stay low.

o Growth, lower inflation, and major tax relief have translated into real income gains for all Americans. Real personal income has risen by over $116 billion since the low point of the recession (August 1982). Real after-tax incomes grew 6.8% in 1984--the biggest increase in over a decade.

o Trends in the economy still look good. The prime rate--which rose from 6.5% to 21.5% under Carter-Mondale--stands at 10-1/2%. The misery index, which peaked at 24.5% in March of 1980, is around 11%. Right not it is imperative that the Federal Reserve allow this nominflationary recovery to proceed at a healthy pace. With the recent drop in the discount rate and other signs of Fed easing, it looks like the Fed agrees.

3. The Budget And The Deficit

Nature Of The Deficit Problem

o After several years of budget deficits that approached the $200 billion mark, some people seem to be getting complacent about the problem. Since the economy has continued to do well, with low inflation and strong growth, why worry about the deficit?

o The answer is that everything we have achieved for the economy in the last several years is put at risk unless we deal with the deficit. And part of the problem is that the public can't get very excited about the deficit dilemma. It seems we need to have a crisis on our hands, or some kind of visible faltering in the economy, to convince people of the urgency of reducing the budget deficit.

The Real Point

o Everyone is to blame for the deficit problem, because all of us together have put more demands on the government than we are willing to finance through taxes. Unless we lower some of our expectations for government involvement--meaning reduced Federal spending--deficits will persist.

o Sustained deficits in the $200 billion range are a real threat to continued recovery. Unless deficits decline we will either have to offset Federal borrowing with higher inflation, or accept slow growth and rising unemployment as the Federal government absorbs the bulk of available credit. Without assurance that inflation will remain under control and credit available at acceptable rates of interest, business will not expand through new investment, and jobs will not be available for our sons and daughters when they are ready to enter the workforce.

Risks Ahead

o Time is of the essence, because we are at the point where economic expansion will either continue, competing against heavy Treasury borrowing, or the recovery will slow and possibly slip into recession. That is why Senate Republicans have set the goal of working out a budget plan by February 1. The risk is that the deficit problem will compound itself: each year that we add $200 billion in new Federal debt adds about $15 billion to the next year's interest costs. The exploding cost of servicing the Federal debt will make controlling spending that much more difficult each year.

What Needs To Be Done

o We have to agree at the outset that the sacred cow is a thing of the past: everything in the budget has to be on the table, and everything has to be scrutinized for possible cost-savings. It is not acceptable to say that we have done all we can to reduce Federal spending when the budget represents nearly 25% of the gross national product.

Freeze Option

o 1985 is fast becoming the year of the budget freeze. There is great interest in Congress and the White House in some type of freeze or 'freeze plus' on spending for FY 1986. A 'freeze plus' would couple a freeze on most programs with reform of others and termination of some. We need to cut spending by $50 billion or more in FY 1986 to reach our goal.

Attack Spending First

o Spending is our first line of attack in reducing the deficit. All government spending must be financed by either taxes or borrowing, and either method of finance takes resources away from the private sector. Distinguished experts such as Alan Greenspan, Charles Schultze, and Paul Volcker tell us that cutting spending by $50 billion or more in 1986 will reduce interest rates, keep inflation down, and make the economy more secure.

All Aboard

o Everyone must share in the effort to close the deficit gap. We want a strong economy with stable prices, rising productivity, more jobs and more challenging, future-oriented jobs. We are on the verge of achieving that goal, thanks to President Reagan, and we will achieve it if we build public support for deficit reduction. People will accept a limited, short-term sacrifice for the cause of fiscal restraint if they understand that it is the best investment they can possibly make for their own, and their families', economic future. That is what is at stake in the deficit debate, and that is why I am confident we will join together in a bipartisan effort to do the job.

Procedural Changes

o There is a lot to critize in the was we prepare a budget, and it may be necessary to impose some external controls on Congress. The President has asked for a line-item veto, which I support and which could be effective. There is still strong support for some kind of balanced budget or fiscal restraint amendment in the constitution that would help restore a more balanced fiscal posture in the years ahead.

o Still, nothing will work unless Congress and the President have the will to make it work. Unless we forge a consensus in favor of deficit reduction, no budget procedure will do the job.

4. Major Tax Reform

o The Treasury Department proposed an innovative, constructive new plan for reforming our tax system. Some of the proposal will be highly controversial, and the President no doubt will modify some things--but clearly he is committed to tax simplification. The Treasury initiative provides an excellent starting point for the 1985 tax reform debate.

o Under the Treasury plan, there would be just three tax rates: 15, 25 and 35 percent. The personal exemption would double, to $2,000. Rate brackets, the zero bracket, and the personal exemption would continue to be indexed. For corporations, there would be a single rate of 33 percent.

o Major tax breaks that would be dropped include the deduction for State and local taxes, the marriage penalty offset, the investment tax credit, the capital gains exclusion, the tax exemption for private purpose bonds, and the exemptions for employer-provided fringe benefits.

o Tax provisions that would be modified include mortgage interest deductions for second homes (disallowed); the charitable deduction (limited to amounts in excess of 2 percent of adjusted gross income); business expense deductions (limited); and taxation of dividends (a partial dividends-paid deduction).

o Indexing would be extended to capital gains; interest income and expense; depreciation deductions; and the earned income tax credit.

o It is important to build a consensus for any far-reaching changes, drawing on the Treasury plan, Bradley-Gephardt, Kemp-Kasten, and other plans. It may be necessary to move gradually, and reform will not be possible without strong Presidential leadership. And the people will have to let us know if they think the kinds of trade-offs being proposed are worthwhile.

5. International Trade

o Another major challenge is to keep international markets as free and open as possible in an era of record U.S. trade deficits. Reducing the budget deficit will be a tremendous help, because it will help moderate interest rates and the value of the dollar.

o So far we have done well in keeping avenues of trade open. It is especially significant that last year's trade bill extended for 8 1/2 years, the Generalized System of Preferences, which provides duty-free treatment for certain imports from the underdeveloped world.

o In a similar trade liberalizing vein, the bill authorizes the negotiation of free-trade zones, specifically with Israel, and the reciprocal reduction of tariffs on semiconductors.

o It is hoped that the authority to negotiate bilateral free trade arrangements may induce other countries to join in trade liberalization.

o The trade bill recognized, for the first time, the importance of trade in services (including banking); The President is directed to negotiate reduction in barriers to trade in services (a sector in which the U.S. has the competitive advantage and which represents a major portion of our GNP.)