

"VICTORY '90" CAMPAIGN

I will serve as a member of Governor Hayden's
1990 re-election committee.

NAME _____

ADDRESS _____

CITY / STATE _____ ZIP _____

HOME PHONE _____ OFFICE _____

MEMORANDUM FOR SENATOR DOLE

FROM: MIKE GLASSNER
SUBJ: MISC. FOLLOWUP
DATE: JUNE 6, 1990

I AM WORKING ON THE FOLLOWING ITEMS AS A RESULT OF YOUR
RECENT CAMPAIGN TRIPS:

* ✓ BILL SCHUETTE REQUESTED YOUR HELP WITH CHRYSLER CORP.
AND THE DAIRY P.A.C. I HAVE PASSED THIS INFORMATION
ALONG TO JO-ANNE.

* ✓ RICK HAWKS IS OUR CANDIDATE FOR CONGRESS IN INDIANA-
4. YOU REQUESTED CAMPAIGN AMERICA TO SEND \$ 1000.
TO HIS CAMPAIGN. I HAVE GIVEN JO-ANNE HIS ADDRESS.

* ✓ ALLY MILDER REQUESTED YOU CONTACT ED ROLLINS AT THE
CONGRESSIONAL COMMITTEE TO ENCOURAGE HIM TO "TARGET"
HER RACE. I BELIEVE JO-ANNE IS WRITING A LETTER.

* ✓ GOVERNOR ORR ASKED YOU TO WRITE A LETTER TO PRESIDENT
REAGAN REQUESTING AN APPEARANCE FOR HER THIS SUMMER.
I WILL DRAFT A LETTER FOR YOUR APPROVAL AND COORDINATE
THIS WITH RICK SMITH OF THE EISENHOWER CENTER, WHO HAS
A SIMILAR REQUEST. *✓ by
LJ*

* ✓ KEN GNADT OF GRAND ISLAND, NEBRASKA REQUESTED THAT YOU
PUT HIM IN TOUCH WITH MORGAN WILLIAMS. I HAVE A CALL
INTO MORGAN TODAY.

* ✓ KEN WAGNON OF WICHITA DONATED \$ 1000 TO DOLE FOR
SENATE '92. I HAVE PASSED IT ON TO JO-ANNE.

* ✓ PATRICIA McCAMPBELL OF WICHITA HAS A HOME IN HAWAII
AND IS INTERESTED IN HOSTING AN EVENT FOR PAT SAIKI.
I HAVE PASSED HER ADDRESS AND PHONE NUMBER ON TO JO-
ANNE. *✓ by
LJ*

* ✓ DR. ROBERT MASTERS OF FORT HAYS STATE IS INTERESTED IN
BEING CONSIDERED FOR THE DIRECTORSHIP OF THE EISENHOWER
CENTER. I HAVE FORWARDED THIS INFORMATION TO MARCIE.

* ✓ BILL AMSTEIN, JR. OF KANSAS STATE UNIVERSITY HAS AN
INTEREST IN BEING APPOINTED TO A POSITION AT U.S.D.A.
I HAVE FORWARDED HIS INFORMATION TO MARCIE.

(CONTINUED)

SENATOR DOLE FOLLOWUP
JUNE 6, 1990
PAGE 2

* BILL PEARSON OF KOCH INDUSTRIES CALLED TO THANK YOU FOR YOUR PARTICIPATION. HE SAID THAT CHARLES KOCH WILL FOLLOW UP WITH JIM WHOLEY ON YOUR MEETING.

* SAM COHEN REQUESTED A PHONE CALL FROM WAYNE ANGELL. I HAVE A CALL INTO ANGELL'S OFFICE TODAY AND WILL BRIEF HIM ON SAM'S INTEREST.

* HANK SALISBURY OF KANSAS CITY REQUESTED INFORMATION ABOUT YOUR TREADMILL. JOYCE HAS ORDERED BROCHURES FROM THE MANUFACTURER, AND I WILL FORWARD THEM TO HANK ALONG WITH A LETTER WHEN THEY ARRIVE.

* JOYCE HAS THE PHONE NUMBERS FOR KANSAS HOUSE RECRUITMENTS CALLS. I WILL STAY IN TOUCH WITH THE CANDIDATES AND WITH THE PARTY ON THESE.

* W.O. BROWN OF SALINA HAS CELEBRATED HIS 90TH BIRTHDAY. I UNDERSTAND FROM JUDY BIVIANO THAT SHE IS DRAFTING A LETTER FOR YOUR SIGNATURE.

* NEXT TRIP: I WILL WORK WITH JO-ANNE, JUDY KAY, AND RITA RILEY TO COORDINATE FUTURE EVENTS IN JOHNSON COUNTY AND SOUTHEAST KANSAS.

* THANK YOU NOTES: I WILL PREPARE AND SEND TO YOU A.S.A.P.

CC: JO-ANNE
JIM W.

sent by June 6

June 1, 1990

TO: SENATOR DOLE
FROM: DAVE SPEARS
SUBJECT: STATUS REPORT: AG WORKING GROUP

SOME PROGRESS WAS MADE ON THE STAFF LEVEL BUT THE TWO MAJOR ISSUES REMAIN UNRESOLVED. THESE ARE TARGET PRICES AND LOAN RATES. THE DEMOCRATS CONTINUE TO WANT BOTH HIGHER TARGET PRICES AND LOAN RATES. IN ADDITION, THEY WANT A MARKETING LOAN FOR WHEAT AND FEED GRAINS.

WE (REPUBLICANS) HAVE HELD THE LINE ON TARGET PRICES AND HAVE CONTINUED TO STATE THAT A FREEZE IS THE MAXIMUM AND WE WILL LIKELY BE FACED WITH ADDITIONAL CUTS WITH THE BUDGET SUMMIT RESULTS.

THE BUDGET MAY TAKE CARE OF THE TARGET PRICE ISSUE, BUT THE LOAN RATE ISSUE IS A DIFFERENT MATTER. IT IS A MAJOR POLICY DECISION. LUGAR HAS OFFERED A COMPROMISE OF A FREEZE AT CURRENT LEVELS WITH A MARKETING LOAN BENEATH. THIS WOULD HAVE LITTLE EFFECT AND SHOULD NOT HURT OUR COMPETITIVENESS.

LEAHY IS ESSENTIALLY IN A BOX RIGHT NOW. HE HAS EITHER THE CHOICE TO SIDE WITH THE REPUBLICANS AND FISCALLY RESPONSIBLE DEMOCRATS OR THE HIGH PLAINS DEMOCRATS. IF HE SIDES WITH THE HIGH PLAINS DEMOCRATS, THEN A 10-9 VOTE IS VERY LIKELY AND AS A RESULT THE BILL WILL FALL APART ON THE FLOOR. THEREFORE, TIME IS ON OUR SIDE.

ON ISSUE FARMERS HAVE WANTED IS FLEXIBILITY. THERE IS ONLY MARGINAL FLEXIBILITY IN THE PACKAGE. THIS IS COMBINED WITH A MINIMUM OILSEED MARKETING LOAN.

THEREFORE, IF THE TRADE-OFF IS HIGHER TARGET PRICES AND LOAN RATES FOR MINIMUM FLEXIBILITY, THEN IT MAY NOT BE WORTH IT. IF THAT IS THE CASE, THEN AN EXTENSION OF THE 1985 FARM BILL WITH MINOR FINE-TUNING MAY BE THE BEST OPTION.

ONCE AGAIN, I BELIEVE TIME IS AN ALLY IN BOTH NEGOTIATIONS AND ANY PRESSURE FOR AN EXTENSION OF THE 1985 FARM BILL.

Address by:
The Honorable Michio Watanabe
Former Japanese Minister of Finance, Former Minister of MITI, and
Former Chairman of the Policy Board of the LDP

Hong Kong to 1997 and Beyond: A Business Assessment
The Asia Society
May 21, 1990

HONG KONG AND THE REGION: A JAPANESE PERSPECTIVE

Ladies and Gentlemen:

It is a great pleasure for me to be given this opportunity today to make some brief remarks about Hong Kong, which I visited only a few weeks ago.

That particular trip actually started in early May in China, where I met with General Secretary Jiang Zemin, Premier Li Peng, and Vice Premier Wu Xueqian. In the meetings, I exchanged views with the Chinese side on the question of how it intends to deal with Hong Kong after July, 1997, in addition to Sino-U.S., Sino-Vietnamese and Sino-Soviet relations. I believe that whether before or after 1997, the prosperity and stability of Hong Kong has important bearing upon the prosperity and stability of the entire Asia-Pacific region. On the basis of that, I sought out the Chinese view.

Their response, in short, was that they would faithfully implement the China-U.K. Joint Declaration and that they did not intend to impose levies on Hong Kong, as

they did on Shanghai. They said that the "one country, two systems" approach, which allows a capitalist society in the Hong Kong Special Administrative Region, remained unchanged even after the Tiananmen incident, and that they wished Hong Kong to remain a major financial trading center after reversion. The stability and prosperity of Hong Kong benefits investors of China, the U.K. and Hong Kong, they said.

Whether this will be so depends on whether the people of Hong Kong and investors around the world trust the words of today's Chinese leaders.

The more that China perceives that the major countries investing in Hong Kong will continue to have interest there, and the more China feels that preserving Hong Kong as a free port will contribute to its own economic reform and development, the better chance that China will observe the Joint Declaration. It follows that the role of Japan and the United States in supporting Hong Kong's prosperity and stability is an extremely important one.

Also important in sustaining Hong Kong prosperity is rebuilding the confidence of the Hong Kong people in their own future -- the confidence that was lost as a result of the Tiananmen incident. For that to happen, the best way is to deepen, even further, the close working relationship that exists between the Hong Kong and Chinese economies. For the people of Hong Kong, who tend to give precedence to short-term gains, measures that hurt Hong Kong in the immediate future will never convince those

people to take permanent residence there, even if those measures are regarded in the west as being the right thing to do over the medium-to long-run. Hong Kong people would probably better appreciate benefits two months or six months down the road, than being told that five to ten years ahead they may be making profits. The United States imposing economic sanctions on China under the totally good intention of promoting democracy in that country is no source of reassurance as far as the Hong Kong people are concerned. The Chinese economy going down the drain does not help development of Hong Kong trade -- it only results in contraction and economic losses.

Rather than applying economic pressure on China in pursuit of rapid democratization, I believe that the west can do better service to a more natural consolidation of liberal-democratic tendencies in China by helping China promote its policies of economic reform and openness.

I understand the deadline for a decision on the return of China to most-favored-nation state will come in early June. I also hear that there are some extreme voices in this country saying that if China does not respond to all the demands of Congress, it should be deprived of this privilege. Should that happen, it will seriously impede Chinese exports to the United States and deal a heavy blow to China's policy of promoting an open economy through the expansion of trade. And Hong Kong's economy, which is heavily dependent on U.S.-China trade, will suffer on a devastating magnitude. I have seen various estimates, one of which even claims that Hong Kong

will lose 9 billion U.S. dollars out of its 24 billion dollar trade with the United States, and that it will suffer a loss of 100,000 jobs.

Such a situation means the destruction of the system where goods are produced in southern China by factories built by investment via Hong Kong and then exported, again, via Hong Kong, to the United States. The economic route that links Hong Kong to China and China to Hong Kong will be constrained, and economic activity severely contracted. Such a measure will, thus, not only aggravate U.S.-China relations, it will also have a chilling effect upon U.S.-Hong Kong relations.

In order to be able to say to the people of Hong Kong, "Please rest assured," we must avoid deterioration in U.S.-China or U.K.-China relations. If it seems likely that those relations will further deteriorate, Hong Kong people with foreign passports will leave Hong Kong before 1997, and, at the same time, western investment in Hong Kong will decline.

Let me turn to the value of Hong Kong as I see it.

First, Hong Kong Harbor, with an average depth of 12 meters and the deepest point being 27 meters, is, in and of itself, an excellent port. Given that it enjoys the smallest range of tide in China, and that it is operational 24 hours a day, Hong Kong cannot be matched by any other port in China which wants to promote an open

economic system and to expand trade with the outside world.

Today's Hong Kong enjoys freedom of economic activity, extremely low tax rates, and freedom in foreign exchange operations; English has full currency; and it boasts well-established communications, transportation and accommodation facilities. Coupled with a well-trained work-force, these make Hong Kong an excellent base for economic activities and a full-fledged international business center.

In order to develop Hong Kong even further, the Hong Kong Government has plans for the construction of a new airport and other large-scale public works projects, such as the expansion of the harbor terminal. These projects will best be undertaken when well explained to the Chinese side so that China can deepen its understanding of the financial feasibility and profitability of the projects.

Hong Kong's appeal in an even larger context will be its relations with hinterland Guangzhou and the entire Pearl River delta area. Under the "one country, two systems" framework, a capitalist, liberal Hong Kong will mingle with that part of China, and it will invest there, building factories and employing workers from the abundant labor-force. The increase in employment and the rising living standards will demonstrate, in concrete terms, the benefits of a free economy -- an avenue much more constructive in shaping democratic tendencies in China than applying economic pressure. Fortunately, China still welcomes foreign capital, and states that the policy of introducing market

principles remains unchanged.

China is a nation of one billion one hundred million people, an enormous population to govern. My sense is that the majority of those people wish, for the time being, to have political stability and improvement in living standards first, rather than attempting to jump to equality of the individual, as we know it in the seven Summit nations of the west.

The largest foreign investor in Hong Kong manufacturing is the United States, accounting for 34%, and Japan is second with a 27% share. These two countries alone exceed 60% when combined. The largest trading partners with Hong Kong are China, the United States and Japan, in that order. This shows how important it is for Japan and the United States, together with the United Kingdom, to continue keeping their interest in Hong Kong and to further expanding their investment there. That, I believe, will reassure the Hong Kong people to stay on, enable Hong Kong to sustain and expand its prosperity, and prevent China from turning inward toward isolationism. Above all, it will help maintain peace and prosperity in the region and the world.

Before I conclude, let me also say how deep a concern the Indochinese boat people question is for Hong Kong. The numbers exploded between June, 1988 and February, 1989 by a staggering 48,000. The number of those still in Hong Kong reached 55,000 by the end of March this year. Last year, Japan contributed eleven

million dollars through the United Nations High Commissioner for Refugees for such purposes as expansion of the refugee camps. Japan will continue the earmarked contribution this year through the UNHCR. We are also contemplating financial assistance to the UNHCR plan for vocational training in Vietnam. This is intended as a means to help those who returned to Vietnam voluntarily and to reduce the incentive to leave the country in the first place. Modest as these efforts may be, I think they are another way Japan intends to help Hong Kong. Thank you.

#

| APRIL | | | | | | | MAY | | | | | | | JULY | | | | | | | AUGUST | | | | | | |
|-------|-----|------|-----|------|-----|-----|-----|-----|------|-----|------|-----|-----|------|-----|------|-----|------|-----|-----|--------|-----|------|-----|------|-----|-----|
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| 15 | 16 | 17 | 18 | 19 | 20 | 21 | 13 | 14 | 15 | 16 | 17 | 18 | 19 | 15 | 16 | 17 | 18 | 19 | 20 | 21 | 12 | 13 | 14 | 15 | 16 | 17 | 18 |
| 22 | 23 | 24 | 25 | 26 | 27 | 28 | 20 | 21 | 22 | 23 | 24 | 25 | 26 | 22 | 23 | 24 | 25 | 26 | 27 | 28 | 19 | 20 | 21 | 22 | 23 | 24 | 25 |
| 29 | 30 | | | | | | 27 | 28 | 29 | 30 | 31 | | | 29 | 30 | 31 | | | | | 26 | 27 | 28 | 29 | 30 | 31 | |

JUNE 1990

| sun | mon | tues | wed | thurs | fri | sat |
|---|--|--|--|---|---|-----|
| | | | | | 1 Iowa return to DC | 2 |
| 3 3:00 hr. D.C. evening: Gorkovets leaves | 4 Salina - Econ Develp Conf 9:30 ar Nat'l | 5 8:00-11:00 AM Affiliates Convention W.H. Kelly J.W. Marriott | 6 | 7 | 8 | 9 |
| 10 | 11 | 12 8:00-11:00 AM Ragbun Had. Pico Dennis 11-12:00 AM Ragbun Had. Pico for Pico. Kimmer-S. 2:30 President's Dinner | 13 6:00-8:00 PM Dole Fdn. Recs Women's Art Museum approx 9:00 SPEAK - FRAC Wark. Helton | 14 FLAG DAY 12-2 SPEAK DEF's Sixth Women in Development Award | 15 10:30-11:30 AM SPEAK - Pige Awards Ceremony | 16 |
| 17 FATHER'S DAY | 18 | 19 9:30 SPEAK Pres Classroom for Young Americans | 20 2 Lunches F/Min of Mining & Ind. of Colorado 5:30 SPEAK - Milk Industry Foundation | 21 | 22 | 23 |
| 24 | 25 hold St. Jo. Anne | 26 hold St. Jo. Anne | 27 9:00- Grand Hyatt SPEAK - Am Trucking Assoc. | 28 | 29 | 30 |

May 7, 1990

M E M O R A N D U M

TO: SENATOR DOLE

FROM: DENNIS SHEA

SUBJECT: SUMMARY OF DEMOCRAT CAMPAIGN FINANCE REFORM BILL

The following is a brief summary of the Democrat campaign finance reform bill. Although a "head-count" of co-sponsors is not yet available, I have been told that "more than half" of the Senate Democrats have signed on as co-sponsors.

Spending Limits. Would establish a system of voluntary "flexible" spending limits, based on state voting age population, ranging from \$950,000 to \$5,500,000 for Senate general election campaigns. The general election spending limit for Kansas would be \$956,000.

The Flexible Component: The spending limit could be increased by up to 25%, to the extent that a candidate receives \$100 contributions from individuals residing in the candidate's home state.

Public Financing. A candidate would be eligible for 90% public financing (70% through direct funding and 20% through broadcast vouchers), if the candidate raises 10% of the spending-limit amount in individual contributions of \$250 or less. 50% of these contributions must be from in-state individuals.

Pretty confusing. Sounds like a "lawyer's full-employment act."

Practical Effect for Kansas Senatorial Candidates. The Kansas spending limit is approximately \$1 million. In order to be eligible for public financing, a candidate would have to raise 10% of this amount (\$100,000) in individual donations of \$250 or less. 50% of this \$100,000 -- or \$50,000 -- must come from in-state individuals.

A Kansas Senatorial candidate would be eligible for the full \$900,000 in public funds if he 1) received \$50,000 in out-of-state contributions, and 2) lined up 200 Kansans for \$250 donations.

This doesn't make sense, and it discourages participation by the people who ought to count -- a candidate's own constituents.

Soft Money -- Tax-Exempt Organizations. The Democrat bill contains restrictions on tax-exempt organizations that fall far short of the restrictions contained in the Republican bill.

The Republican bill would prohibit all 501(c) organizations from engaging in political activity on behalf of a specific candidate for federal office. The Democrat bill, on the other hand, contains no comparable provision.

Broadcasting Provisions. The Democrat bill provides that candidates who accept spending limits and public financing would be entitled to purchase non-preemptible time at the lowest unit rate for pre-emptible time during the entire general election period. (Senator Danforth is opposed to linking the broadcast discount to acceptance of public financing and spending limits.) The Republican bill also contains the lowest unit rate provision, but obviously does not link the availability of the lowest unit rate to acceptance of public financing and spending limits.

The Democrat bill provides that all candidates would be required to appear at the end of their television advertisement conveying the message that the advertisement was paid for by the candidate. (An obvious sop to Senator Danforth.)

Personal Funds

The Democrat bill provides that candidates agreeing to spending limits would be prohibited from spending more than \$250,000 of their own funds for election to the Senate. The Republican bill would require Congressional candidates to declare upon filing their intention to spend over \$250,000 in personal funds and would raise the individual contribution limit to \$5,000 per election for all opponents of a candidate who declares such an intention (the Domenici provision).

Loopholes.

1. The Democrat bill does absolutely nothing to curb labor union soft-money abuses. The Republican bill would codify the Supreme Court's Beck decision, which states that union members may object to the use of union dues for political activities. The Republican bill would also prohibit unions and corporations from engaging in get-out-the-vote campaigns aimed at their members and stockholders, respectively.

2. The Democrat bill purports to ban PAC contributions to Senate candidates. Unlike the Republican bill, the Democrat bill does not ban PAC contributions to House candidates, the national and state parties, and the Senatorial and Congressional Committees.

May 11, 1990

M E M O R A N D U M

TO: SENATOR DOLE
FROM: DENNIS SHEA
SUBJECT: CAMPAIGN FINANCE REFORM -- DEMOCRAT BILL

As of today, the Democrat campaign finance reform bill has 42 co-sponsors.

To my knowledge, the following 12 Democrats have not signed on as co-sponsors: Baucus, Breaux, Bryan, Burdick, Dixon, Harkin, Heflin, Hollings, Johnston, Levin, Rockefeller, and Shelby. The Democrat bill has no Republican co-sponsors.

PAC Loophole

Although the Democrats claim that their bill would ban PAC contributions to Senate candidates, the Democrat bill would still allow Senate candidates to receive PAC contributions under certain circumstances.

The Democrat bill would also still permit PACS to contribute to House candidates, to the national and state parties, and to the Senatorial and Congressional Committees.

Exception for Senate Candidates. As a general matter, the ban on PAC contributions to Senate candidates is effective on the date of the Democrat bill's enactment. However, a Senate candidate may still receive PAC contributions after the effective date to make up for any difference between PAC contributions received before the effective date by the candidate and his opponent.

For example: If Candidate A received \$150,000, and Candidate B received \$200,000, in PAC contributions before the effective date of the Democrat bill, then Candidate A would still be permitted to collect \$50,000 in additional PAC contributions after the effective date.

National and State Parties. Under current law, each PAC may annually contribute \$15,000 in the aggregate to the national and state parties. The Democrat bill would not change current law.

Aggregate PAC Receipts of the National Party Committees. The Democrat bill would prohibit the national party committees from receiving PAC contributions in excess of 2 cents per voter during any two-year election cycle.

In 1988, the U.S. voting age population was approximately 174,550,000. Using the 1988 voting age population figure, the national parties would be permitted to receive approximately \$3.5 million in PAC contributions (.02 times 174,550,000) during the two-year election cycle.

Senatorial Committees. The Democrat bill would prohibit the Senatorial Committees from receiving PAC contributions in excess of 30% of the 441a(d) limit (a limit imposed by Section 441a(d) of the Federal Election Campaign Act) during any two-year election cycle. According to Bill Canfield, the 1988 441a(d) limit for each of the two Senatorial Committees was approximately \$12,800,000.

It appears that the Democrat bill would allow each of the two Senatorial Committees to receive PAC contributions totalling approximately \$3,840,000 (.30 times 12,800,000) during a two-year election cycle.

The 441a(d) limits vary somewhat from election cycle-to-election cycle, depending upon the states in which there are contested seats.

U.S. Senate Republican Policy Committee

William L. Armstrong, *Chairman*

April 26, 1990

A REVIEW OF THE BUDGET 1970 - 1990

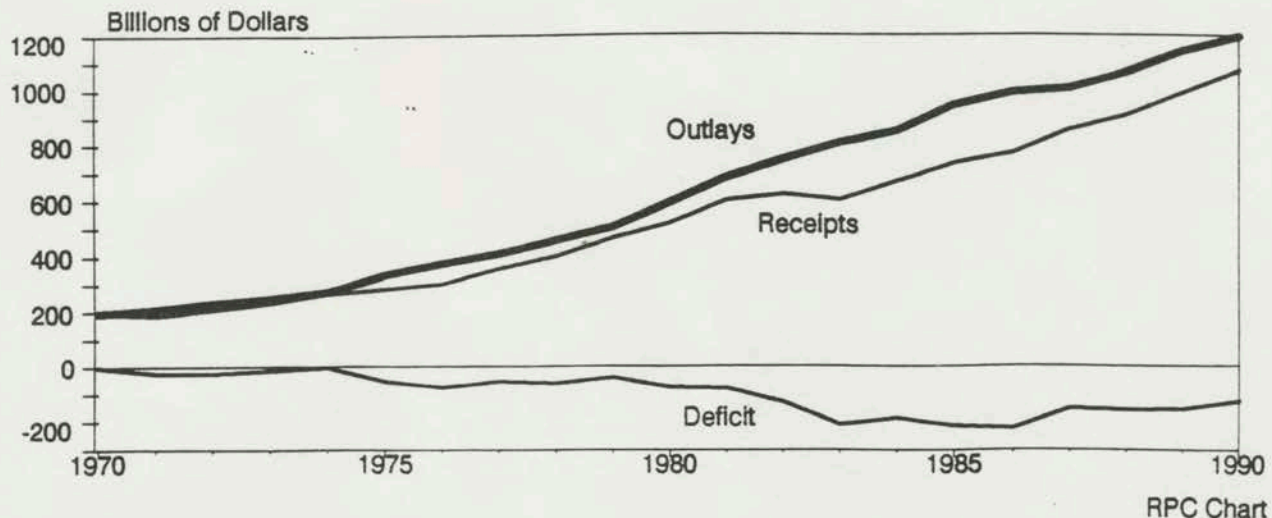
The Federal budget is an enormous document. The President's Fiscal Year 1991 proposal alone is 1569 pages. Who knows how many numbers it contains. Add to that the publications of the Congressional Budget Office and the House and Senate Budget committees, and you're really swimming in numbers. Fortunately, a picture is worth a thousand words. This paper is a collection of charts tracking the Federal budget from 1970 to 1990.

As the deliberations on the FY91 budget proceed, the following charts and talking points may be useful. This presentation of the budget looks at spending and revenues in nominal and inflation-adjusted dollar amounts, as percentages of spending and revenues, and as percentages of GNP. These summary observations provide information on fiscal trends and developments over the past 20 years.

Several points recur from chart to chart, including:

- The budget deficit is the result of runaway spending, and not due to a lack of taxes.
- The lion's share of funding increases have gone to entitlements and mandatory spending over the past 20 years.
- Considerable progress has been made on deficit reduction, in terms of both inflation-adjusted dollar amounts, and as a percent of GNP. Further progress should come from spending restraint.
- Republican fiscal policy in the future should include the goal of continued reduction of the Federal sector's share of the whole economy, thereby promoting greater opportunity and prosperity for all through the primary source of economic growth — *the private sector*.
- The fiscal discipline resulting from Gramm-Rudman does make a difference.

The Federal Budget: Outlays, Receipts, and Deficits



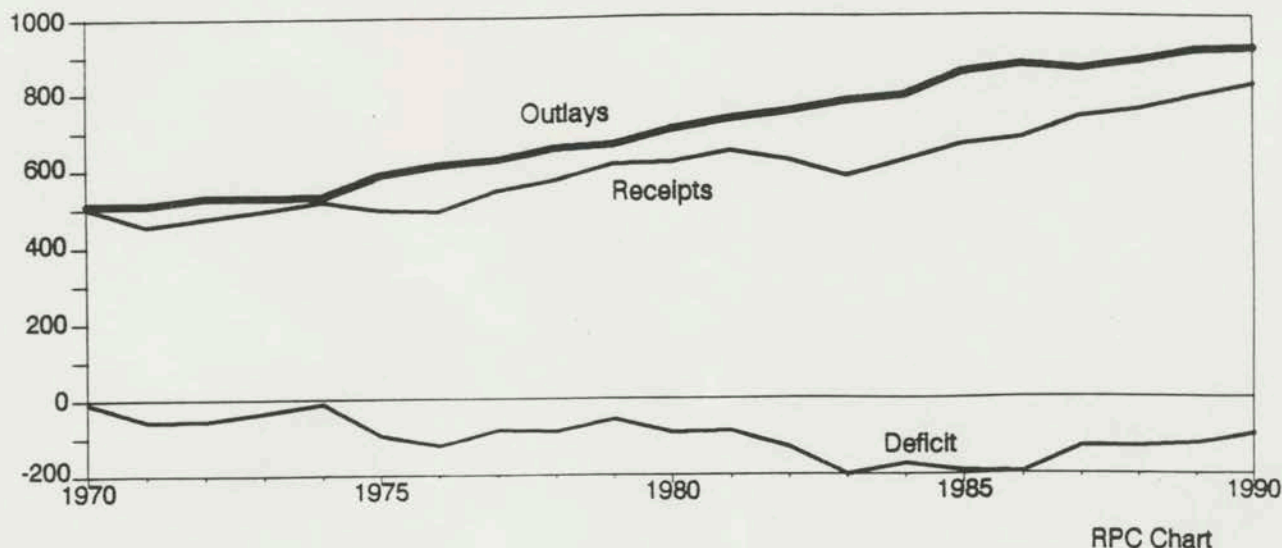
- Despite growing revenues, the Federal Government has run a deficit in every year since 1969.
- Revenues fell 2.8% between 1982 and 1983 due to the recession ending in 1982. Critics claim the Reagan-era tax cuts caused revenues to fall. But the tax rate cuts weren't fully implemented until 1984. The fact is, revenues have grown rapidly on the strong economic growth caused by Republican policies.
- Revenues have grown an average of 8.6% per year since 1983, yet opponents of Republican economic policy continue to blame the deficit on not enough tax revenue.
- The deficit problem lies squarely on runaway spending. Between 1975 and 1980, outlays grew 78%. From 1980 through 1985, outlays grew another 60%. Spending restraint was given a boost because of the discipline of the Gramm-Rudman-Hollings balanced budget act. Between 1985 and 1990, spending has grown 46%, far slower than the 10 years prior to 1985.
- Much progress has been made on the budget deficit, which peaked in 1986. Our fiscal goal for further deficit reduction should be continued spending restraint.

FEDERAL OUTLAYS, RECEIPTS, AND DEFICITS Billions of Current Dollars

| Fiscal Year | Outlays | Receipts | Deficit |
|-------------|---------|----------|---------|
| 1970 | \$195.6 | \$192.8 | -\$2.8 |
| 1975 | 332.3 | 279.1 | -53.2 |
| 1980 | 590.9 | 517.1 | -73.8 |
| 1981 | 678.2 | 599.3 | -78.9 |
| 1982 | 745.7 | 617.8 | -127.9 |
| 1983 | 808.3 | 600.6 | -207.8 |
| 1984 | 851.8 | 666.5 | -185.3 |
| 1985 | 946.3 | 734.1 | -212.3 |
| 1986 | 990.3 | 769.1 | -221.2 |
| 1987 | 1003.8 | 854.1 | -149.7 |
| 1988 | 1064.0 | 909.0 | -155.1 |
| 1989 | 1142.6 | 990.7 | -152.0 |
| 1990* | 1197.2 | 1073.5 | -123.8 |

Source: OMB. * 1990 is January estimate. The deficit is expected to be \$8-20 billion higher. CBO predicts a deficit of \$138 billion
 Note: All tables subject to rounding.

The Federal Budget Adjusted for Inflation



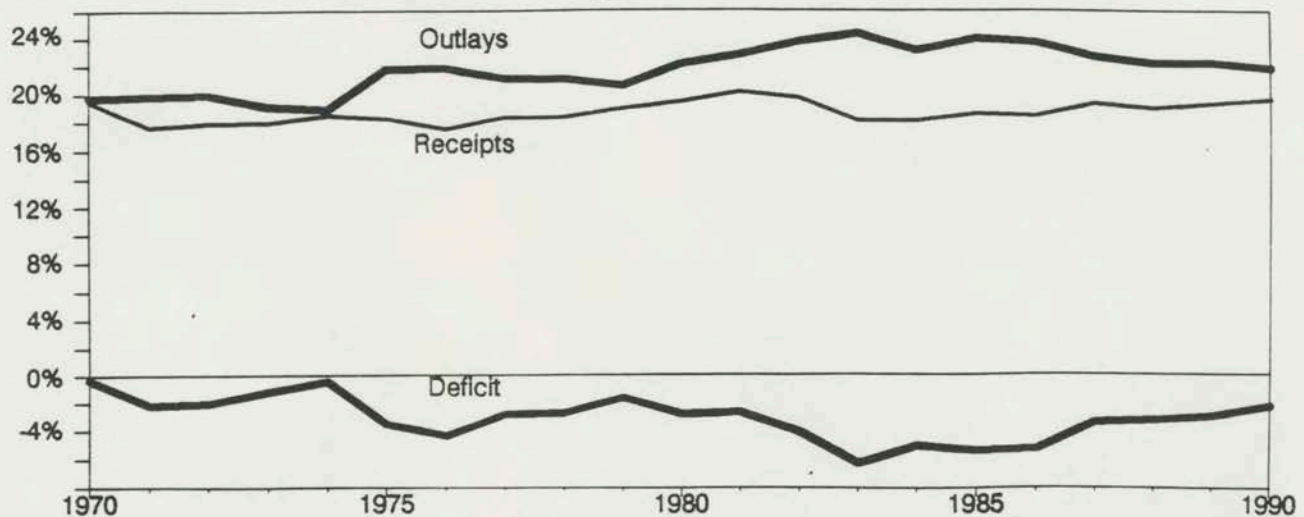
- Growth in government is not just inflation — *far from it*. Real outlays grew 19% between 1975 and 1980; 22% between 1980 and 1985; and 7% between 1985 and 1990. The slowdown in growth reflects progress made from Gramm-Rudman.
- During the same five-year intervals, inflation-adjusted revenues grew at different rates. Between 1975 and 1980, when inflation was clouding economic judgment and “bracket creep” was clobbering taxpayers, revenues advanced 24%. But the price of inflation was stagflation and recession. As a result, real receipts fell 10% between 1981 and 1983. They rebounded a strong 14% between 1983 and 1985. With an economy running full-steam-ahead, real revenues grew another 24% between 1985 and 1990.
- The inflation-adjusted deficit peaked at \$199.2 billion (1982 dollars) in 1983, a figure nearly reached again in 1986, which was the year of the largest nominal deficit.

FEDERAL OUTLAYS, RECEIPTS, AND DEFICITS Billions of Constant (1982) Dollars

| Fiscal Year | Outlays | Receipts | Deficit |
|-------------|---------|----------|---------|
| 1970 | \$509.4 | \$502.0 | -\$7.4 |
| 1975 | 586.0 | 492.1 | -91.9 |
| 1980 | 699.1 | 611.7 | -87.3 |
| 1981 | 726.5 | 642.0 | -84.6 |
| 1982 | 745.7 | 617.8 | -127.9 |
| 1983 | 775.0 | 575.8 | -199.2 |
| 1984 | 788.1 | 616.6 | -171.5 |
| 1985 | 849.6 | 659.1 | -190.6 |
| 1986 | 868.0 | 674.2 | -193.9 |
| 1987 | 858.0 | 730.1 | -127.9 |
| 1988 | 879.6 | 751.4 | -128.2 |
| 1989 | 907.1 | 786.5 | -120.6 |
| 1990* | 912.2 | 817.9 | -94.3 |

Source: OMB. *1990 estimate subject to revision.

The Federal Budget as a Percent of GNP



RPC Chart

The budget is often shown as a percent of Gross National Product. This is a useful way to depict how much of the economy is controlled by the Federal sector. It also is useful to put the effect of the budget deficit in a larger perspective. However, showing government as a share of GNP should not be used to mask the fact that government continues to be a growing influence in our business and private lives, not only in taxes and spending, but also in its intervention in our economic choices as consumers, savers, investors, and workers.

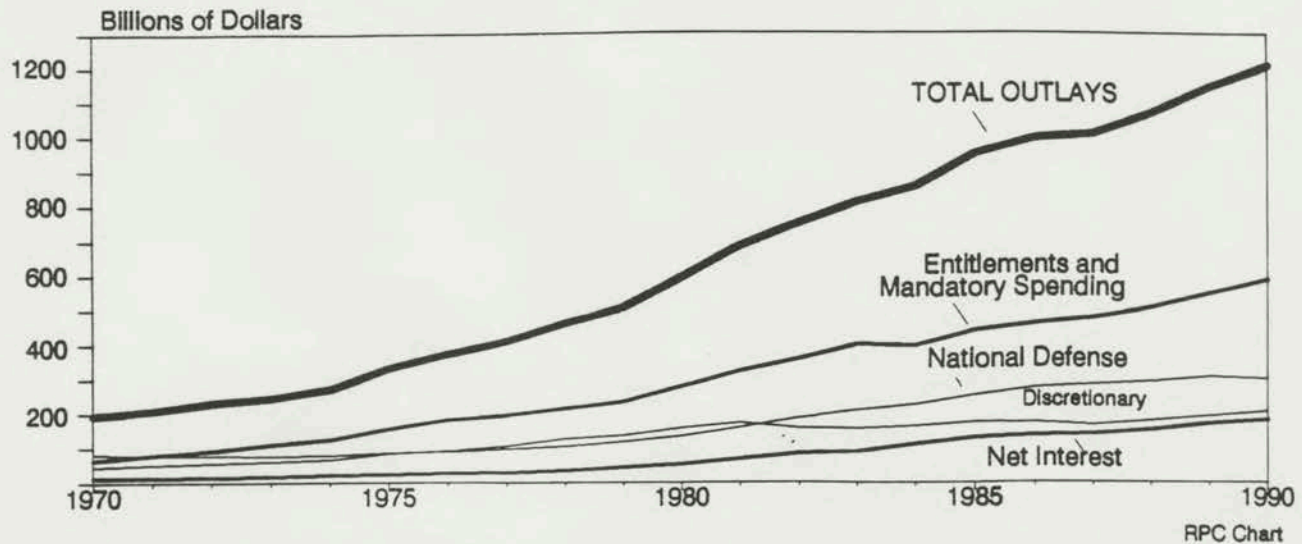
- Since 1960, outlays have averaged about 21% of GNP. In every year since 1974, outlays have exceeded 21%. Since 1960, revenues have averaged about 18.5% of GNP. For eight of the past 11 years, revenues have exceeded that average. *Clearly, this shows that excessive spending is the cause of the deficit.*
- The deficit as a percent of GNP peaked in 1983, at 6.3%. It has diminished steadily since then, reaching 2.9% in 1989. It will likely fall below 2.5% in 1990.
- Republican economic policy in the 1980s created a record-breaking economic expansion, now in its 8th year. Strong economic growth permitted a growing Federal sector even though the Federal government's size relative to the whole economy has diminished in recent years. However, government's share of GNP is still larger than the post-1960 average.

FEDERAL OUTLAYS, RECEIPTS, AND DEFICITS As a Percent of Gross National Product

| Fiscal Year | Outlays | Receipts | Deficit |
|-------------|---------|----------|---------|
| 1970 | 19.8% | 19.5% | -0.3% |
| 1975 | 21.8 | 18.3 | -3.5 |
| 1980 | 22.1 | 19.4 | -2.8 |
| 1981 | 22.7 | 20.1 | -2.6 |
| 1982 | 23.8 | 19.7 | -4.1 |
| 1983 | 24.3 | 18.1 | -6.3 |
| 1984 | 23.1 | 18.1 | -5.0 |
| 1985 | 23.9 | 18.6 | -5.4 |
| 1986 | 23.7 | 18.4 | -5.3 |
| 1987 | 22.7 | 19.3 | -3.4 |
| 1988 | 22.2 | 19.0 | -3.2 |
| 1989 | 22.2 | 19.2 | -2.9 |
| 1990* | 21.8 | 19.6 | -2.3 |

Source: OMB. *1990 estimate subject to revision.

Federal Spending by Category



The budget committees divide the budget into four major categories. Two are self-explanatory — national defense and net interest. The other two require explanation. Entitlements and mandatory spending, by far the largest category, contains programs that are funded more-or-less “automatically.” Their appropriations are controlled indirectly through devices like eligibility requirements or benefit rules. Included here are Social Security, Medicare, farm price supports, deposit insurance, and other commitments. Nondefense discretionary includes 11 appropriations bills, whose programs cover international affairs, transportation, space, science, environment, law enforcement, and environmental protection — to name a few. One-third of discretionary is grants to state and local governments. Another fifth goes to nondefense government employees’ pay and benefits.

- Entitlements and mandatory spending has grown the most in dollar amount, rising over \$200 billion in the 1970s, and rising another \$300 billion in the 1980s. By contrast, defense grew about \$60 billion in the 1970s and another \$170 billion in the 1980s. Entitlements and mandatory programs today are almost twice the size as defense. In 1970, entitlements were about four-fifths the size of defense.
- Increases in entitlements and mandatory spending exceeded increases in defense spending in every year but two of the Reagan defense build-up years.
- Financing deficits has caused interest payments to soar. Interest payments tripled in the 1980s.
- Nondefense discretionary spending more than tripled in the 1970s, but grew just 11.7% from 1981 to 1989.

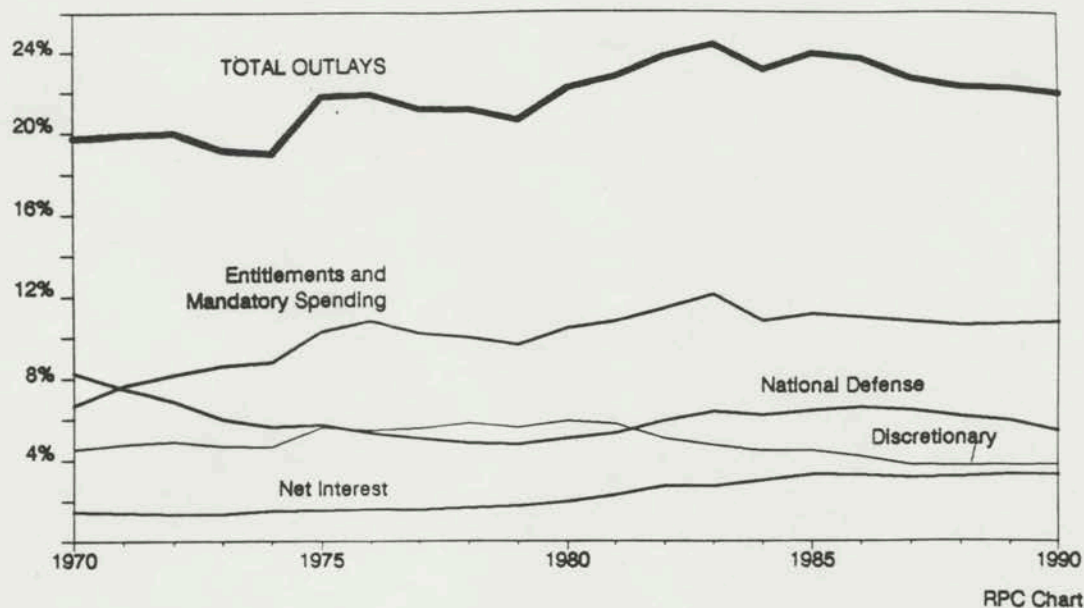
FEDERAL OUTLAYS BY MAJOR CATEGORY

Billions of Dollars

| Fiscal Year | Total Outlays | Entitlements & Mandatory Spending | National Defense | Nondefense Discretionary | Net Interest | Offsetting Receipts |
|-------------|---------------|-----------------------------------|------------------|--------------------------|--------------|---------------------|
| 1970 | \$195.6 | \$66.2 | \$81.7 | \$45.0 | \$14.4 | -\$11.6 |
| 1975 | 332.3 | 156.4 | 86.5 | 84.7 | 23.2 | -18.5 |
| 1980 | 590.9 | 277.2 | 134.0 | 157.6 | 52.5 | -30.3 |
| 1981 | 678.2 | 320.4 | 157.5 | 170.8 | 68.7 | -39.2 |
| 1982 | 745.7 | 356.0 | 185.3 | 156.6 | 85.0 | -37.2 |
| 1983 | 808.3 | 398.8 | 209.9 | 156.0 | 89.8 | -46.1 |
| 1984 | 851.8 | 394.7 | 227.4 | 163.9 | 111.1 | -45.3 |
| 1985 | 946.3 | 437.3 | 252.7 | 174.9 | 129.4 | -48.0 |
| 1986 | 990.3 | 454.8 | 273.4 | 173.2 | 136.0 | -47.0 |
| 1987 | 1003.8 | 472.4 | 282.0 | 165.1 | 138.6 | -54.2 |
| 1988 | 1064.0 | 502.7 | 290.4 | 177.2 | 151.7 | -58.0 |
| 1989 | 1142.9 | 543.6 | 303.5 | 191.0 | 168.9 | -64.2 |
| 1990* | 1205 | 584 | 297 | 205 | 180 | -60 |

Source: CBO. *1990 is the budget baseline estimate.

Federal Spending as a Percent of GNP



Due to a growing economy, three of the four major categories of Federal spending have decreased in size relative to Gross National Product, compared to levels of the early 1980s.

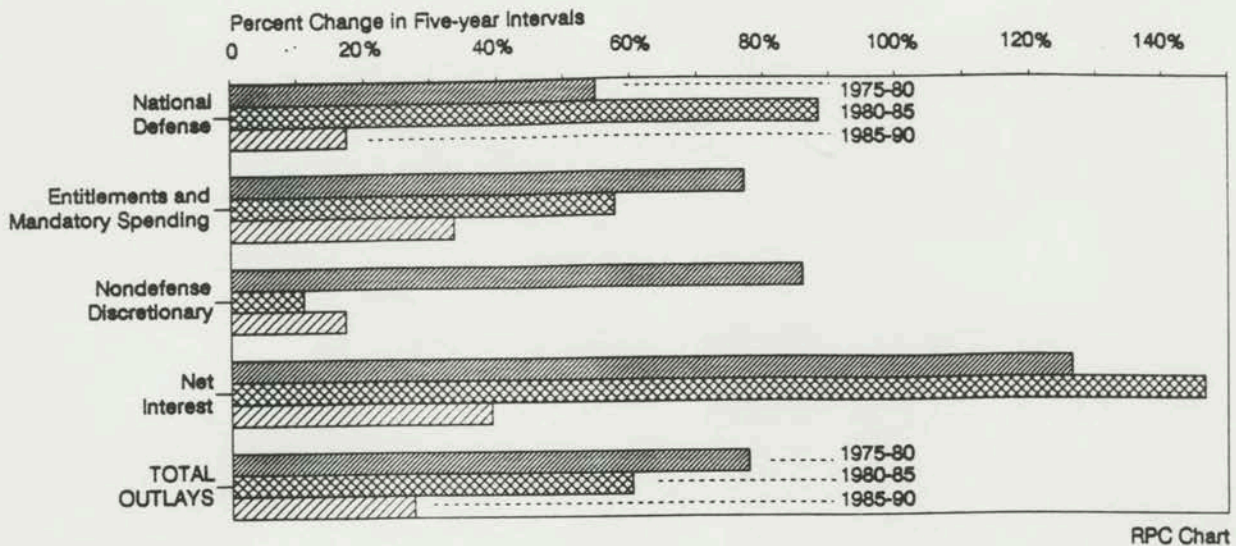
- Total outlays peaked at 24.3% of GNP in 1983, and have fallen to an estimated 22.1% in 1990.
- Entitlements and mandatory spending peaked at 12.0% in 1983, and have held fairly steady in the 10.5% to 10.7% range over the past four years.
- National defense peaked at 6.5% of GNP in 1986, but levels much higher than that prevailed in the years prior to the mid-1970s.
- Net interest is the only category to have steadily increased as a share of GNP during the 1980s.

FEDERAL OUTLAYS BY MAJOR CATEGORY As a Percent of Gross National Product

| Fiscal Year | Total Outlays | Entitlements & Mandatory Spending | National Defense | Nondefense Discretionary | Net Interest | Offsetting Receipts |
|-------------|---------------|-----------------------------------|------------------|--------------------------|--------------|---------------------|
| 1970 | 19.8% | 6.7% | 8.3% | 4.5% | 1.5% | -1.2% |
| 1975 | 21.8 | 10.3 | 5.7 | 5.6 | 1.5 | -1.2 |
| 1980 | 22.1 | 10.4 | 5.0 | 5.9 | 2.0 | -1.1 |
| 1981 | 22.7 | 10.7 | 5.3 | 5.7 | 2.3 | -1.3 |
| 1982 | 23.8 | 11.3 | 5.9 | 5.0 | 2.7 | -1.2 |
| 1983 | 24.3 | 12.0 | 6.3 | 4.7 | 2.7 | -1.4 |
| 1984 | 23.1 | 10.7 | 6.2 | 4.4 | 3.0 | -1.2 |
| 1985 | 23.9 | 11.1 | 6.4 | 4.4 | 3.3 | -1.2 |
| 1986 | 23.7 | 10.9 | 6.5 | 4.1 | 3.3 | -1.1 |
| 1987 | 22.7 | 10.7 | 6.4 | 3.7 | 3.1 | -1.2 |
| 1988 | 22.2 | 10.5 | 6.1 | 3.7 | 3.2 | -1.2 |
| 1989 | 22.2 | 10.6 | 5.9 | 3.7 | 3.3 | -1.2 |
| 1990* | 22.1 | 10.7 | 5.4 | 3.7 | 3.3 | -1.1 |

Source: CBO. *1990 is baseline estimate.

Growth in Federal Spending



- Growth in government has not been uniform among the categories over the years.
- Net interest outlays have grown the fastest in each of the past three 5-year time intervals. Fortunately, that rate of growth slowed in the late 1980s, thanks to lower interest rates and smaller deficits.
- Contrary to critics' complaints of the dominance of defense, growth in defense outlays exceeded entitlement outlays in only the 1980-85 interval.
- In the last 15 years, entitlements and mandatory spending grew 273% compared to 243% for defense.
- Nondefense discretionary spending skyrocketed during the Carter years and nearly halted in the early 1980s. In the late 1980s, it was the only category to have its growth rate increase. However, discretionary growth remained the lowest of all categories.

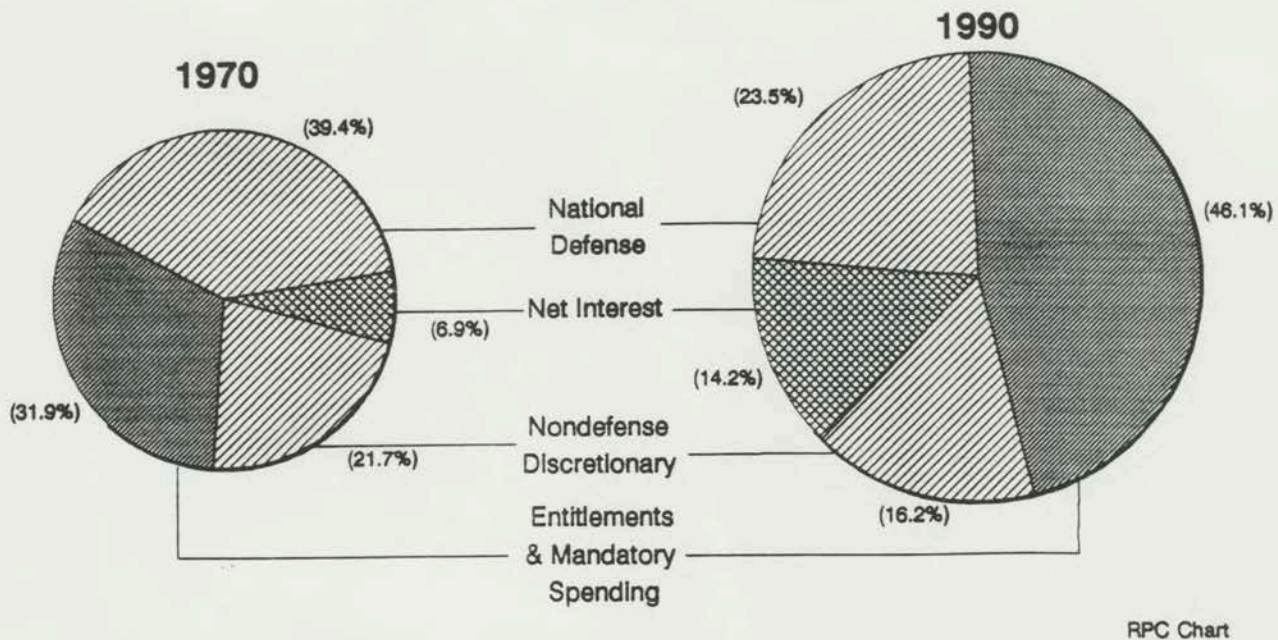
GROWTH IN FEDERAL SPENDING BY MAJOR CATEGORY

Percentage Increases for 5-year Intervals, 1975-1990

| Interval | Total Outlays | Entitlements & Mandatory Spending | National Defense | Nondefense Discretionary | Net Interest |
|-------------|---------------|-----------------------------------|------------------|--------------------------|--------------|
| 1975 - 1980 | 77.8% | 77.2% | 54.9% | 86.1% | 126.1% |
| 1980 - 1985 | 60.2 | 57.8 | 88.6 | 11.0 | 146.5 |
| 1985 - 1990 | 27.3 | 33.6 | 17.5 | 17.2 | 39.1 |
| 1975 - 1990 | 262.6% | 273.4% | 243.4% | 142.0 | 675.9% |

Source: CBO. Note: 1990 baseline estimate is used.

Changing Budget Priorities



Budget categories have experienced shifting shares over the years. These pie charts show how the priorities have shifted. The relative sizes of the pies show the budget has almost doubled in inflation-adjusted terms between 1970 and 1990.

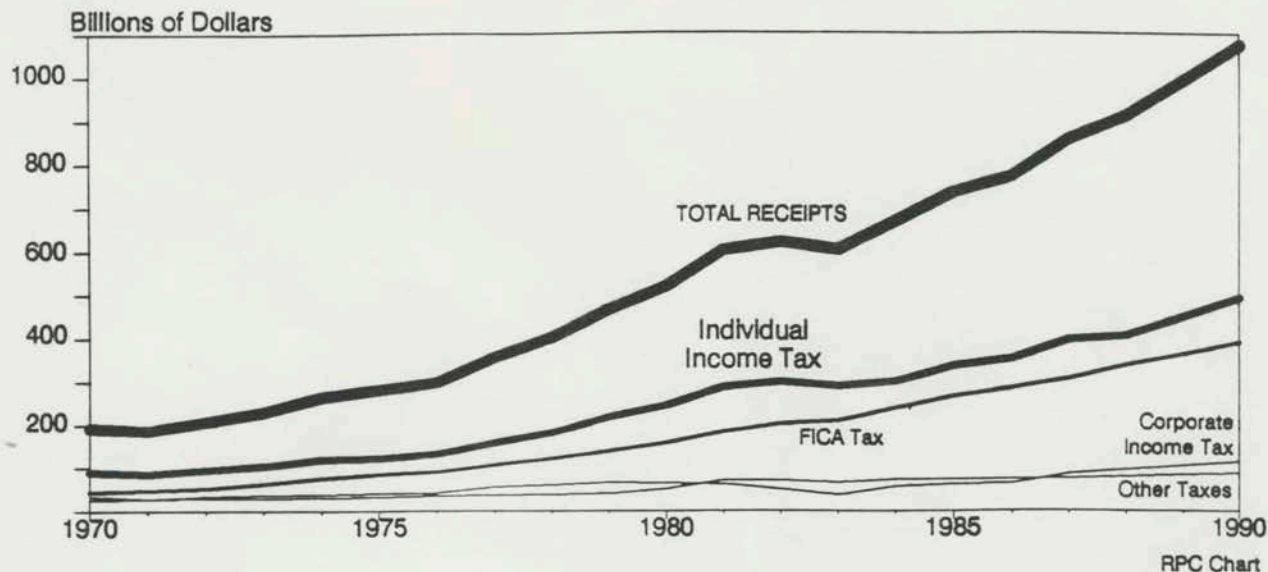
- Interest payments doubled their share of the budget between 1970 and 1990.
- Nondefense discretionary spending increased its share of the budget in the 1970s, and then lost ground in the 1980s.
- Defense's share of the budget fell to 21.6% in 1980, then rose with the Reagan buildup, peaking at 26.7% in 1987. Since then, its share has fallen to an estimated 23.5% in 1990.
- Entitlements and mandatory spending increased its share by 14.2 percentage points between 1970 and 1990, and accounts for just under half the budget in 1990.

MAJOR CATEGORY SPENDING As a Percent of Total Outlays

| Fiscal Year | Entitlements & Mandatory Spending | National Defense | Nondefense Discretionary | Net Interest |
|-------------|-----------------------------------|------------------|--------------------------|--------------|
| 1970 | 31.9% | 39.4% | 21.7% | 6.9% |
| 1975 | 44.6 | 24.7 | 24.1 | 6.6 |
| 1980 | 44.6 | *21.6 | 25.4 | 8.5 |
| 1981 | 44.7 | 22.0 | 23.8 | 9.6 |
| 1982 | 45.5 | 23.7 | 20.0 | 10.9 |
| 1983 | 46.7 | 24.6 | 18.3 | 10.5 |
| 1984 | 44.0 | 25.3 | 18.3 | 12.4 |
| 1985 | 44.0 | 25.4 | 17.6 | 13.0 |
| 1986 | 43.8 | 26.4 | 16.7 | 13.1 |
| 1987 | 44.6 | 26.7 | 15.6 | 13.1 |
| 1988 | 44.8 | 25.9 | 15.8 | 13.5 |
| 1989 | 45.0 | 25.1 | 15.8 | 14.0 |
| 1990* | 46.1 | 23.5 | 16.2 | 14.2 |

Source: Based on CBO data. *1990 is baseline estimate. Note: percentages do not include offsetting receipts.

Federal Receipts



Federal revenues have risen rapidly over the past 15 years, but not all for "good" reasons. The rapid increase of the late 1970s was driven by inflation and "bracket creep." These problems gave rise to stagflation and frustration, which in turn led to recession and caused revenues to fall. With the correct economic policies adopted in the 1980s, revenues rose because an expanding economy generated more income, wealth, and opportunity for all Americans.

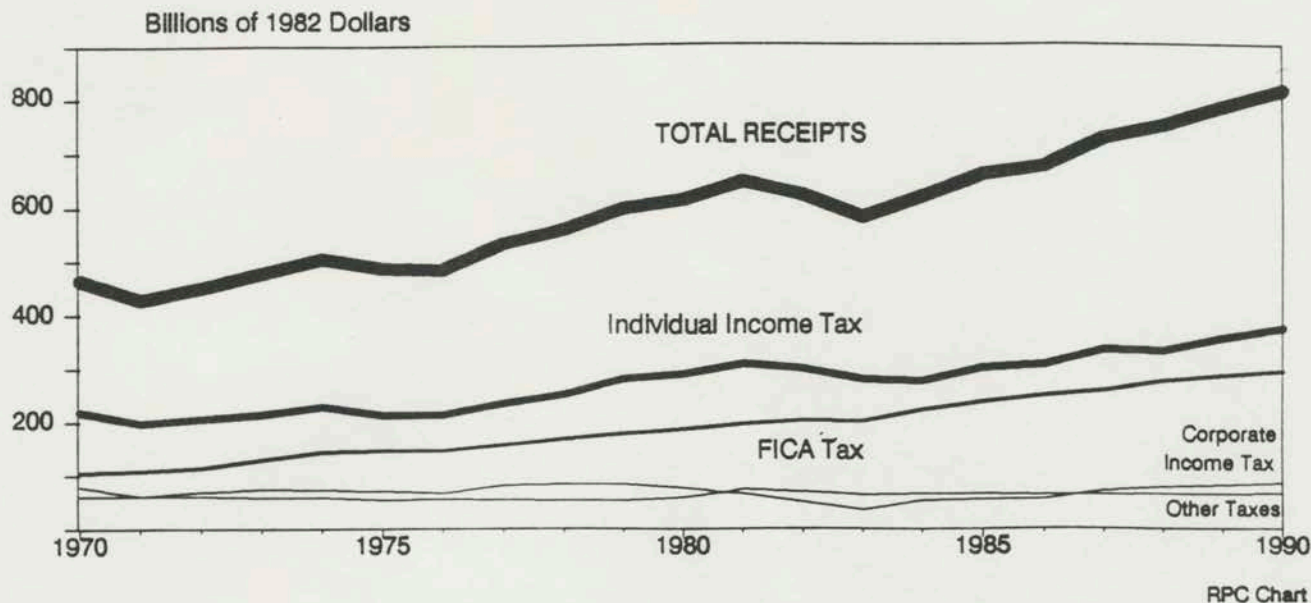
- Total receipts doubled in the 1980s.
- A growing economy that created over 18 million jobs and raised personal income over 65% since 1982 naturally elevated Federal revenues.
- Corporate and individual income tax revenues declined between 1982 and 1983 due to a recession, not because of tax rate cuts.
- Since 1983, individual income taxes have risen \$200 billion. Social Security payroll taxes have risen \$175 billion.
- Excise tax revenue has not changed much in the 1980s.

FEDERAL RECEIPTS Billions of Dollars

| Fiscal Year | Individual Income Tax | Corporate Income Tax | FICA Tax (Social Security) | Excise Taxes | Other Taxes | TOTAL RECEIPTS |
|-------------|-----------------------|----------------------|----------------------------|--------------|-------------|----------------|
| 1970 | \$90.4 | \$32.8 | \$44.3 | \$15.7 | \$9.5 | \$192.8 |
| 1975 | 122.4 | 40.6 | 84.5 | 16.6 | 15.0 | 279.1 |
| 1980 | 244.1 | 64.6 | 157.8 | 24.3 | 26.3 | 517.1 |
| 1981 | 285.9 | 61.1 | 182.7 | 40.8 | 28.7 | 599.3 |
| 1982 | 297.7 | 49.2 | 201.5 | 36.3 | 33.0 | 617.8 |
| 1983 | 288.9 | 37.0 | 209.0 | 35.3 | 30.3 | 600.6 |
| 1984 | 298.4 | 56.9 | 239.4 | 37.4 | 34.4 | 666.5 |
| 1985 | 334.5 | 61.3 | 265.2 | 36.0 | 37.0 | 734.1 |
| 1986 | 349.0 | 63.1 | 283.9 | 32.9 | 40.2 | 769.1 |
| 1987 | 392.6 | 83.9 | 303.3 | 32.5 | 41.9 | 854.1 |
| 1988 | 401.2 | 94.5 | 334.3 | 35.2 | 43.7 | 909.0 |
| 1989 | 445.7 | 103.6 | 359.4 | 34.1 | 47.9 | 990.7 |
| 1990* | 489.4 | 112.0 | 385.4 | 36.2 | 50.5 | 1073.5 |

Source: OMB. *1990 estimate subject to revision.

Federal Receipts Adjusted for Inflation



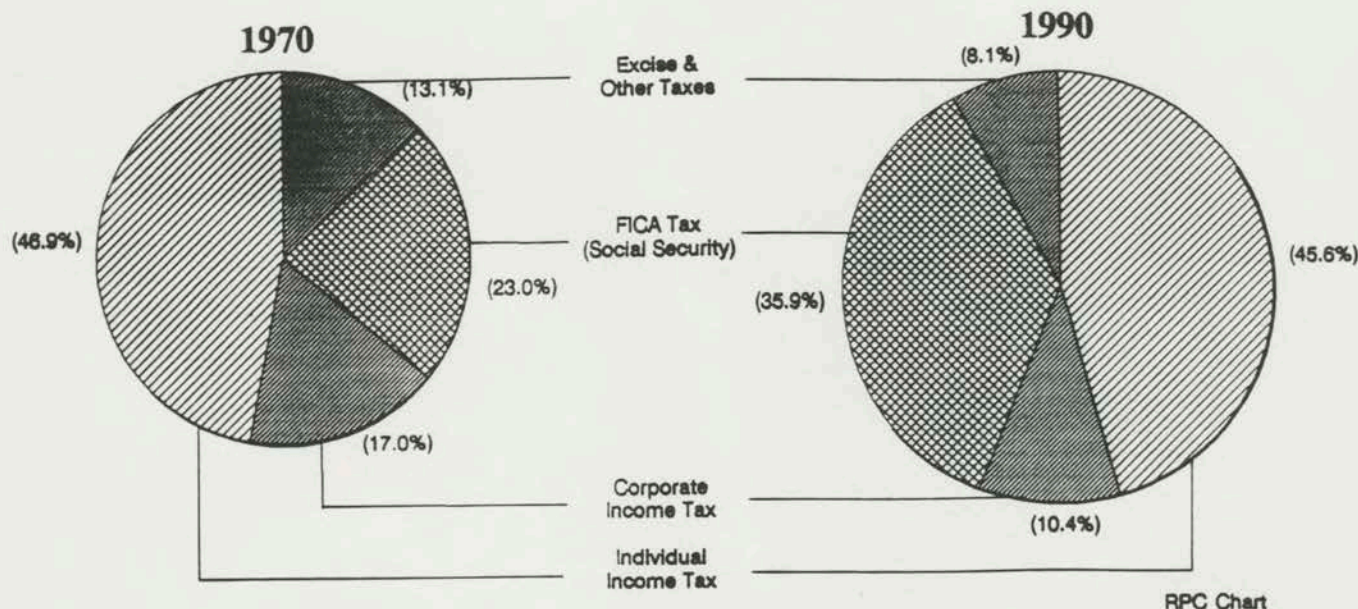
- From 1983 to 1990, total receipts have grown 41.3% after inflation.
- From 1980 to 1990, total receipts have grown 33.4% after inflation.
- Real total receipts during the 1975-80 expansion years grew 4.7% per year. In the post-1982 expansion, receipts have grown 5.1% *with lower tax rates in effect*. This shows that sound economic policies have contributed positively to our fiscal affairs.

FEDERAL RECEIPTS Billions of Constant (1982) Dollars

| Fiscal Year | Individual Income Tax | Corporate Income Tax | FICA Tax (Social Security) | Excise Taxes | Other Taxes | TOTAL RECEIPTS |
|-------------|-----------------------|----------------------|----------------------------|--------------|-------------|----------------|
| 1970 | \$217.9 | \$79.1 | \$106.9 | \$37.8 | \$22.9 | \$464.6 |
| 1975 | 212.5 | 70.5 | 146.8 | 28.7 | 26.0 | 484.5 |
| 1980 | 288.2 | 76.3 | 186.3 | 28.7 | 31.1 | 610.5 |
| 1981 | 307.1 | 65.7 | 196.3 | 43.9 | 30.8 | 643.7 |
| 1982 | 297.7 | 49.2 | 201.5 | 36.3 | 33.0 | 617.8 |
| 1983 | 277.3 | 35.5 | 200.6 | 33.9 | 29.1 | 576.4 |
| 1984 | 275.8 | 52.6 | 221/2 | 34.5 | 31.8 | 615.9 |
| 1985 | 300.0 | 55.0 | 237.8 | 32.3 | 33.2 | 658.3 |
| 1986 | 304.8 | 55.1 | 247.9 | 28.8 | 35.1 | 671.7 |
| 1987 | 332.7 | 71.1 | 257.0 | 27.5 | 35.5 | 723.8 |
| 1988 | 329.9 | 77.7 | 274.9 | 29.0 | 35.9 | 747.5 |
| 1989 | 315.8 | 81.8 | 283.7 | 26.9 | 37.8 | 781.9 |
| 1990* | 371.4 | 85.0 | 292.5 | 27.4 | 38.3 | 814.7 |

Source: OMB. Inflation adjustment used implicit GNP deflator; numbers will vary somewhat from other sources.*1990 subject to revision.

Receipts shown as a Percentage of Total Receipts



The many sources of revenue for the Federal Government have shifted in relative size as well as dollar amounts over the years. The sizes of the pies reflect the increase in real revenues over the past twenty years.

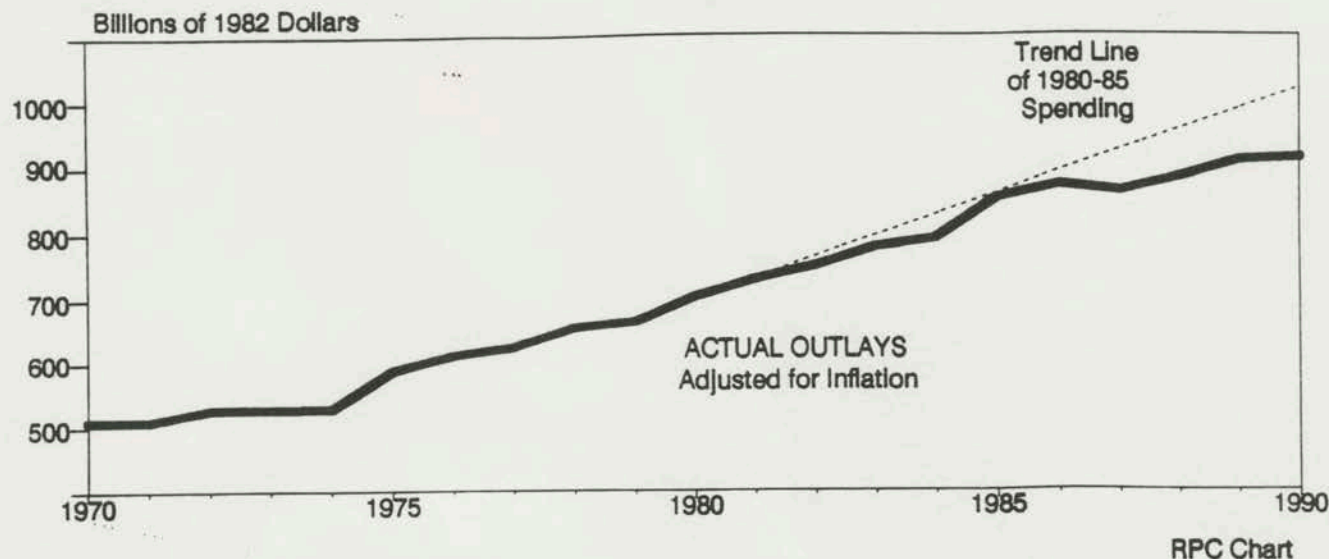
- Between 1970 and 1980, the share of receipts coming from Social Security taxes increased 7-1/2 percentage points, and another 5-1/2 points between 1980 and 1990.
- The rapid rise in Social Security caused the relative size of other sources of revenue to fall. For example, excise and other taxes as a share of all receipts plummeted from 13.1% in 1970 to 8.1% in 1990, even though inflation-adjusted revenues increased \$5 billion during those 20 years.
- Individual income tax revenue has remained in the 45% to 48% range over the past 20 years, even though it grew 70%, or over \$150 billion in real terms, during that time.
- Corporate receipts in 1990 will be higher than either 1980 or 1970, even though its share has fallen from 17.0% to 10.4%.

SOURCES OF REVENUE AS A PERCENTAGE OF TOTAL RECEIPTS

| Fiscal Year | Individual Income Tax | Corporate Income Tax | FICA Tax (Social Security) | Excise Taxes | Other Taxes | TOTAL RECEIPTS |
|-------------|-----------------------|----------------------|----------------------------|--------------|-------------|----------------|
| 1970 | 46.9% | 17.0% | 23.0% | 8.1% | 4.9% | 100.0% |
| 1975 | 43.9 | 14.6 | 30.3 | 5.9 | 5.4 | 100.0 |
| 1980 | 47.2 | 12.5 | 30.5 | 4.7 | 5.1 | 100.0 |
| 1981 | 47.7 | 10.2 | 30.5 | 6.8 | 4.8 | 100.0 |
| 1982 | 48.2 | 8.0 | 32.6 | 5.9 | 5.3 | 100.0 |
| 1983 | 48.1 | 6.2 | 34.8 | 5.9 | 5.0 | 100.0 |
| 1984 | 44.8 | 8.5 | 35.9 | 5.6 | 5.2 | 100.0 |
| 1985 | 45.6 | 8.4 | 36.1 | 4.9 | 5.0 | 100.0 |
| 1986 | 45.4 | 8.2 | 36.9 | 4.3 | 5.2 | 100.0 |
| 1987 | 46.0 | 9.8 | 35.5 | 3.8 | 4.9 | 100.0 |
| 1988 | 44.1 | 10.4 | 36.8 | 3.9 | 4.8 | 100.0 |
| 1989 | 45.0 | 10.5 | 36.3 | 3.4 | 4.8 | 100.0 |
| 1990* | 45.6 | 10.4 | 35.9 | 3.4 | 4.7 | 100.0 |

Source: OMB. *1990 estimate subject to revision.

Have we made any progress on the Budget?



Even though Gramm-Rudman deficit targets have never been reached, significant progress has been made on deficit reduction. The most important accomplishment in fiscal policy in the past five years is the slowdown in Federal spending.

- Between 1980 and 1985, inflation-adjusted Federal outlays grew at a 5.0% annual rate. Between 1985 and 1990, inflation-adjusted outlays grew just 1.4% per year.
- In nominal dollars, outlays grew an average of 9.9% per year from 1980 to 1985. Between 1985 and 1990, that annual growth rate was halved (4.8%).
- The slowdown in Federal spending has been accompanied by a steady rise in revenues due to economic growth. This combination creates a "glide path" to a balanced budget *without any need for tax increases*.
- If outlays after 1985 had grown at the same rate as the 1980-85 period, 1990 outlays would be about \$1,517 billion, instead of the projected \$1,197 billion — a difference of \$320 billion! In inflation-adjusted terms, 1990 outlays would have been about \$1,033 billion, instead of \$912 billion (1982 dollars). In this light, the discipline encouraged under Gramm-Rudman has made a remarkable contribution to our fiscal affairs.

| Fiscal Year | Nominal Outlays | Percent Change from previous year | Nominal Outlays at 9.9 percent growth | Real Outlays (billion) | Percent Change from previous year | Real Outlays at 4 percent growth |
|---------------------------------------|-----------------|-----------------------------------|---------------------------------------|------------------------|-----------------------------------|----------------------------------|
| 1980 | \$590.9 | — | | \$699.1 | — | |
| 1981 | 678.2 | 14.8% | | 726.5 | 3.9% | |
| 1982 | 745.7 | 10.0 | | 745.7 | 2.6 | |
| 1983 | 808.3 | 8.4 | | 775.0 | 3.9 | |
| 1984 | 851.8 | 5.4 | | 788.1 | 1.7 | |
| 1985 | 946.3 | 11.1 | | 849.6 | 7.8 | |
| 1986 | 990.3 | 4.6 | \$1040.0 | 867.6 | 2.1 | \$883.6 |
| 1987 | 1003.8 | 1.4 | 1142.9 | 857.8 | -1.1 | 918.3 |
| 1988 | 1064.0 | 6.0 | 1256.1 | 879.6 | 2.5 | 955.7 |
| 1989 | 1142.6 | 7.4 | 1380.4 | 907.1 | 3.1 | 993.9 |
| 1990* | 1197.2 | 4.8 | 1517.1 | 912.2 | 0.6 | 1033.7 |
| 1980-85 Average Spending Growth: 9.9% | | | | | 4.0% | |
| 1986-90 Average Spending Growth: 4.8% | | | | | 1.4% | |

Source: OMB. Inflation adjustment is in 1982 dollars. *1990 estimate subject to revision.

ECONOMIC TALKING POINTS

Republican Policy Committee

May 8, 1990

The U.S. economy, now in its 90th month of growth, continues to perform better than forecasters have predicted.

- **Real GNP** grew 2.1% in the first quarter of 1990 (advance report, seasonally adjusted annual rate). The Blue Chip consensus forecast was just 1.2%. The larger-than-expected growth is welcome news following the slowdown at the end of 1989. The Administration has forecast 2.4% growth for this year, compared to Blue Chip's 1.9%. The economy measured improvement along a broad base: consumer spending (up 2.5%), business investment (up 7.6%) and net exports (up 3.7%) (all annual rates). [Commerce Dept.]
- **Employment growth** slowed in April, with the net gain of 64,000 new jobs (establishment data). The unemployment rate ticked upward to 5.4%. The manufacturing sector reported 22,000 fewer factory jobs. Construction employment also fell by 99,000 jobs. These losses were more than offset by increases in services. The job "tote board" is piling up big numbers: 2.5 million jobs were created in the past 12 months, and a total of almost 21 million jobs since the recession ended 7-1/2 years ago (establishment data). [Labor Dept.]
- **Personal income** was up a strong 0.8% in March, marking the third month of steady growth. Total personal income now stands at 4.67 trillion (seasonally adjusted annual rate). [Commerce Dept.]
- **Consumer spending** in March registered a 0.4% gain. Because income grew more than this amount, the personal saving rate increased. Americans are now saving 5.8% of their personal income, up from 1989's 5.4% rate. Most observers view the trend of increased saving as very favorable. [Commerce Dept.]
- **The inflation outlook** has analysts cautious. The consumer price index for urban consumers (CPI-U) rose 0.5% in March. The 12-month period ending in March had a 5.2% rate. However, the annual rate recorded in the first three months of 1990 for the CPI was 8.5%. [Labor Dept.]
- Fortunately, the **producer price index (PPI)** fell 0.2% in March. Producer prices have leveled off since January's 1.8% surge, a one-month record increase. [Labor Dept.]
- **The index of leading economic indicators** jumped a strong 0.9% in March, the largest increase in nearly 2 years. Among the signs of strength were plant and equipment orders, consumer goods orders, and higher stock prices. The largest negative was a decline in building permits. [Commerce Dept.]
- **Industrial production** rose 0.7% in March on strength in the auto and utilities sectors. This report begins the use of an index using 1987 as the base year. The index now stands at 108.8, with 1987 = 100.0. This measure means that U.S. industries are currently producing 8.8% more output than they did in 1987. The gain follows the 0.8% increase in February. Capacity utilization rose 0.4% in March to 83.3% of "full capacity." [Federal Reserve]

- **Productivity** -- the measure of output per hour worked -- fell a disappointing 1.0% (annual rate) in the first quarter of 1990 for the nonfarm business sector. The lackluster performance of service industries more than offset an impressive 4.1% increase in productivity in the manufacturing sector. [Labor Dept.]
- **Orders for durable goods** shot up 6.7% in March -- the biggest monthly gain in over a year. Total orders rose \$8.1 billion to \$128.8 billion (seasonally adjusted). The transportation sector (auto and aircraft in particular) accounts for most of the big gain. [Commerce Dept.]
- **Business Inventories** slipped 0.4% in February, to \$794.6 billion. This drop, the biggest in over three years, follows an inventory buildup of 0.3% in January and continues the pattern of caution and adjustment caused by the consumer spending slowdown. [Commerce Dept.]
- **Businesses plan to increase spending on plant and equipment by 7.8% in 1990. These capital outlays** are expected to reach a record level of \$512.9 billion. Observers are delighted with this estimate, because low corporate profits in 1989 were expected to lead to meager investment in 1990. On this news alone, many forecasters are revising upward their GNP estimates for 1990. [Commerce Dept.]
- **Construction spending** fell 1.4% to \$432.5 billion in March (seasonally adjusted annual rate). This adjustment is on the heels of February's big growth of 3.2% (revised upward) and January's 2.4% gain. This investment, along with the growth of plant and equipment outlays, bodes well for future economic growth. [Commerce Dept.]
- **Housing starts** fell 9% in March, to 1.321 million (seasonally adjusted annual rate). The large decrease was caused in part by the surge of housing activity in January and February. [Commerce Dept.]
- **Orders for manufactured goods** rose 3.8% in March -- an increase of \$8.8 billion to \$240 billion (seasonally adjusted). This is the largest monthly gain in over a year. Durable goods orders rose 6.6% in March. [Commerce Dept.]
- **Retail Sales** fell 0.6% in March, to \$148.5 billion (seasonally adjusted). This decline follows a February decline of 0.3%; however, the February figure initially was estimated to be a much worse decline of 0.9%. [Commerce Dept.]
- **Interest rates** remain stubbornly high in late April. The jump in inflation in early 1990 has caused short term rates to increase, and long term rates have been climbing in part due to a heavy issuance of long term bonds. Three-month treasury bills were earning about 7.8%, and 30-year treasury bonds were yielding about 9% in late April. Lower rates are expected as inflation cools, but not as low as forecasters predicted earlier this year. [Federal Reserve and Treasury Dept.]
- **The merchandise trade deficit** plummeted 29.4% in February, to \$6.5 billion -- the lowest monthly figure since December 1983. This improvement came from falling imports, principally oil. U.S. exports slipped a modest 0.9% to \$31.6 billion -- but this is still the second-highest monthly export value ever. The trade gap between Japan and the U.S. in the first two months of 1990 has shrunk 27% from the same period of 1989. [Commerce Dept.]

April 13, 1990

MEMORANDUM FROM JOHN TAYLOR J. H. T.

As you may know, for medical reasons RN had to postpone an address to the World Affairs Council on April 12th. I thought you might be interested in seeing a copy of the speech as prepared for delivery.

You will note that his blunt conclusions are contrary to the current line of most of the liberal pundits inside the Beltway:

--"The Soviets have lost the Cold War, but the West has not yet won it."

--"Gorbachev must choose between Lithuania and the United States. If he uses force or threats of force to deny independence to Lithuania, there is no way that the Senate would approve any agreement from the Bush-Gorbachev summit."

--"To say that we must choose between independence for Lithuania and a summit misses the mark. It is possible to have both."

--"We hear reports that Gorbachev is trying to influence his Third World clients to adopt less aggressive policies. There is one sure way he can influence them. He can quit subsidizing them."

ADDRESS BY FORMER PRESIDENT NIXON BEFORE THE
BOSTON WORLD AFFAIRS COUNCIL

April 12, 1990
(as prepared for delivery)

The Real Gorbachev

In addressing this distinguished audience of foreign policy observers, I want to tell you up front what my approach will be.

Virtually all of the foreign policy experts these days are singing the same tune. Editorial writers, columnists, think tanks, and television commentators tell us:

The Cold War is over.

The West has won.

The Soviet Union no longer poses a significant threat to our interests.

A State Department expert observes that we are witnessing what he calls the end of history. We no longer need to devote our attention to the great issues that have divided us during the Cold War, but can now devote our efforts to issues which unite us like global warming.

I believe profound changes have taken place, but I see the world from a different perspective from those who reside in the Washington Beltway, the modern version of Plato's cave.

I believe the Soviets have lost the Cold War, but that the West has not yet won it.

I believe that we are witnessing the defeat of communism, but that this alone does not assure the victory of freedom.

I believe that while the Soviet threat has receded, we face challenges all over the world which will test us to the limit of our capabilities and our will.

Finally, I also profoundly believe that if we meet our leadership responsibilities, the twentieth century, which was the bloodiest in world history, will be succeeded in the year 2000 by a century of peace.

Nineteen-eighty-nine was the year of the century for the forces of freedom in the world. We saw the Berlin Wall come down and communist leaders in Poland, Hungary, Romania, Bulgaria, Czechoslovakia, and East Germany driven from power by the people in those countries. The year was capped by the stunning defeat in a free election of another communist leader, Daniel Ortega in Nicaragua.

We now face a new challenge. Winning an election or a

revolution is difficult. But far more difficult is running a government after you win. Now that the people of these countries have ridded themselves of the evils of communism, we must help them find a way to enjoy the blessings of freedom.

Democracy alone is not the answer. Democracy means government by elected leaders and elected leaders can provide bad economic policies as well as good ones.

Democratic socialism is not the answer. For seventy years we have opposed totalitarian communism because it is evil. Today we must oppose democratic socialism because it won't work. The trouble with the socialists is that they promise the golden egg and then kill the goose that lays it.

As Czechoslovakia's brilliant finance minister recently observed, partial economic reforms won't work. There is no halfway house between communism and freedom.

There is only one way to progress for these nations which have rejected communism. They should adopt the free market policies which have produced economic miracles in the United States, Western Europe, and Japan. Those like Poland who go through the agony to move that way deserve our full support.

The newly free nations of Eastern Europe and Nicaragua rejected communism because it didn't work. Our challenge is to assist them in ways that will make certain that freedom does not suffer the same fate. Rather than sending them political experts on how to run a campaign, we should send them economic and technological experts on how to run a free economy.

In his inaugural address on January 20, 1949, President Harry Truman announced what he called a "bold new program for making the benefits of our scientific and industrial progress available for the improvement and growth of undeveloped areas." Unfortunately, while this visionary Part Four program, as it was called, was never fully implemented in the 1950s, it provides a useful example in the 1990s of how we should approach the problems of the new democracies in Eastern Europe and Nicaragua and the less developed countries of the Third World. What we need today is an International Freedom Corps sponsored by the United States, Western Europe, and Japan which would have the responsibility to provide expert economic advice to those nations who chose freedom on how to develop and implement free market policies. For example, in the United States, retired chief executive officers of major corporations who are still in the prime of life could be of invaluable assistance in such a program.

The bottom line is that we should not blithely assume that if we can just "export democracy" these countries will find an answer to their desperate need for economic progress. Far more than our money to subsidize half-baked policies that are bound to

fail, these countries need the benefit of our experience in dealing with the infinite complexities of free market economic systems.

Let us now take a close look at the most remarkable statesman of our time -- Mikhail Gorbachev.

Gorbachev is a troika, a three dimensional personality. The fact that he does not have a single-minded vision, as was the case with his predecessors, should not be considered a liability. Unfortunately, history tells us that leaders with vision, more often than not, produce nightmares.

Despite what you may hear that he could be a closet democrat or even a closet Christian because he treats the Pope respectfully, Gorbachev is in fact a true believing communist. His goal is not to abandon communism, but to save it.

He is a patriotic Russian nationalist. His goal is not to dismantle the Soviet empire, but to preserve it, as demonstrated by the hard-line he is taking on Lithuanian independence.

But the most dominant facet of his complex personality is that he is a consummate pragmatic politician who likes power, knows how to use it, and will do what is necessary to keep it. It is this characteristic which has primarily influenced his decisions to adopt his revolutionary political, economic, and foreign policy reforms.

Rather than trying to psychoanalyze him, let us see what he has done.

His political reforms do not meet out standards. But compared with what the Russian people had before, they are breathtaking. Where there was no freedom of the press, there is now some. Where there was no freedom to criticize party leaders, there is now some. Where there were no free elections, there are now some. After having had their voices stilled for over seventy years, the great silent majority of the Russian people are finally being heard.

On the other hand, his economic reforms have been a dismal failure. For example, in the ten years of Deng Xiaoping's reforms in China between 1979 and 1989, the per capita income of the Chinese people doubled. In the five years Gorbachev has been in power, the per capita income of the Russian people has gone down.

His foreign policy reforms, however, have exceeded all expectations. He has withdrawn the Red Army from Afghanistan. He has announced reductions in his Warsaw Pact forces and in his defense budget. Most important, he has not used the Red Army to keep his East European clients in power, as did Khrushchev in Budapest in 1956 and Brezhnev in Prague in 1968.

We must keep this last point in context, however. The conventional Beltway wisdom is that it was Gorbachev who inspired and encouraged the anti-communist revolts in Eastern Europe. The truth is that it was Western values contrasted with the failure of communist policies, which brought millions into the streets of the great cities of Eastern Europe. Gorbachev deserves credit for not sending in the Red Army. But the revolutions in Eastern Europe were not pro-Gorbachev. There were pro-freedom and anti-communist.

The most significant question to address is why Gorbachev changed previous Soviet policies. Here we see the pragmatic politician taking over from the ideological communist and the Russian nationalist. Look at what he confronted when he came to power five years ago. Everywhere he looked, communism was suffering from terminal illness.

All of the Soviet Union's Third World conquests were losers, costing the Soviet Union \$15 billion a year in subsidies.

Dissent and outright rebellion were boiling beneath the surface in the captive nations of Eastern Europe.

Most ominous, the Soviet economy was a basket case plagued by shortages, crime, and corruption.

Abroad he saw that his major potential adversary, the United States, had recovered from the malaise of the late 1970s and the recession of the early 1980s, had a booming economy, a stronger military, and a new initiative, SDI, which would cost him billions of dollars he did not have to be competitive.

In 1985, shortly after Gorbachev came to power, I asked China's General Secretary Hu Yaobang if he thought Gorbachev would adopt economic reforms as Deng Xiaoping had. He replied, "If he doesn't, the Soviet Union will disappear as a great power in the twenty-first century." He was right and Gorbachev knows it. He had no choice but to reform at home and to retrench abroad.

There is no question that Gorbachev has changed since the time he totally supported Brezhnev's policies. But it is a change of the head, not the heart. At a time he is using his head, we should not lose ours.

Let us see what he has not changed.

In implementing his political reforms, some communist officials have lost their positions. But Gorbachev has strengthened his. He is the most powerful Soviet leader since Stalin.

Despite cuts in his defense budget, he still spends twenty percent of his GNP on defense, compared with six percent in the United States. He has modernized all three legs of his nuclear

triad, as well as his conventional land, sea, and air forces. The Soviet military is leaner, but stronger than when he came to power five years ago.

He has withdrawn the Red Army from Afghanistan, but spends \$4 billion a year to keep the same communist government in power. Except for Nicaragua, all of the Soviet Union's Third World clients are still in power, subsidized to the tune of \$15 billion a year in arms and economic aid from the Kremlin. The Cold War may be ended in Eastern Europe, but it is still being waged in the Third World.

Why did Gorbachev act as he did in Eastern Europe? He did what he did not to help us but to help himself. If he had used the Red Army to keep his unpopular clients in power in Eastern Europe, he would have aborted his brilliant diplomatic blitzkrieg to psychologically disarm Western Europe. He had to choose between Eastern Europe and Western Europe. He made the right choice. He chose Western Europe.

He faces a similar choice today. He must choose between Lithuania and the United States. If he uses force or threats of force to deny independence to Lithuania, there is no way that the Senate of the United States would approve any arms control, trade, or other agreement at the upcoming Bush-Gorbachev summit. Those who cynically say that having a Bush-Gorbachev summit must take priority over our concern for the independence of Lithuania are profoundly wrong morally. They are also wrong politically. The tough-minded, pragmatic politician who did nothing to keep his subservient client in power in strategically important East Germany will not risk his relationship with Western Europe and the United States to keep tiny Lithuania under Soviet control. The Ukraine, maybe; Lithuania, never.

To say that we must choose between independence for Lithuania and a Bush-Gorbachev summit misses the mark. It is possible to have both. Gorbachev will go to the brink, but he will stop short of action which would irreparable damage his new relationship with Western Europe and the United States, who in the final analysis he knows are going to have to bankroll perestroika.

Gorbachev's decision not to use force in Eastern Europe has been a brilliant success from his point of view. He has removed the fear -- the glue that holds the NATO alliance together. Even more important, his benign image as a man of peace has increased his chances to get the credits and technology he needs for his sick economy.

Should we help Gorbachev? The answer is yes if it serves our interests as well as his.

It does not serve his interests or ours unless his reforms go far enough to work. His current reforms do not meet that test. As Andrei Sakharov observed shortly before his death, "In

the absence of radical reforms, credits and technological aid would only prop up an ailing economy and delay the advent of democracy."

Even if his economic reforms go far enough to work, it does not serve our interests to help Gorbachev if as a result we will be facing an economically stronger Soviet Union with the same aggressive foreign policy.

As we applaud Gorbachev's new thinking in Eastern Europe, we should take a hard look at some of his old thinking in the Third World. In nation after nation he is supporting anti-American regimes in Asia, Africa, and Latin America.

He provides \$6 billion a year in arms and other aid to Castro, \$2.5 to Vietnam, \$4 billion to Afghanistan, \$1 billion to North Korea, \$1.5 billion to Syria, \$1 billion to Angola, \$1 billion to Libya.

We hear reports that he is trying to influence his Third World clients to adopt less aggressive policies. There is one sure way he can influence them. He can quit subsidizing them.

Now that the people of Eastern Europe have ended the Cold War in Eastern Europe, the time has come for Gorbachev to end the Cold War in the Third World.

But isn't this asking him to give up too much? Let us examine this question in historical perspective. In 1945, Winston Churchill sent a message to the new President of the United States, Harry Truman: "It is vital that we reach an understanding with Russia now before we mortally reduce our armed forces and withdraw to our zones of occupation." In effect, Churchill was saying, "Make a deal now when Stalin needs one because of our strength rather than waiting until later when he will not need one because of our weakness." His advice was rejected, and as a result a hundred million people in Eastern Europe were forced to endure 40 years of Soviet domination and repression.

We are at another great watershed of history. Gorbachev needs our help for his terminally sick economy. We should make a deal now which serves our interests rather than waiting until later when as a result of our help, he may no longer need one. We should link our decisions on items he wants like trade, credits, and technology to his actions on items we want like eliminating his support of our potential enemies in the Third World.

We should totally reject the fatuous advice of those who suggest that we should help finance perestroika. It is in our interest and in Gorbachev's as well for him to finance perestroika by cutting back on his Third World foreign aid programs and his huge defense budget.

Let us assume the best -- that we will be entering a new era in which the Cold War is over, not just in Eastern Europe, but in the Third World as well. What are the challenges we will face?

First, there is the Soviet Union. Even without Eastern Europe, the Baltics, and its Third World outposts, the Soviet Union will not be an international pussycat. It will still have 30,000 nuclear warheads, the world's largest conventional army, and a modern, blue-water navy. And it will have a long history of pervasive Russian expansionism which began centuries before the Bolshevik Revolution. Those who fear a united Democratic Federal Republic of Germany because of Germany's history should take a hard look at the totalitarian Soviet Union in light of Russian history.

There is China -- a nuclear power with one and one-tenth billion potentially capable people which in spite of not because of communism will be a military and economic superpower in the next century. Whether China will play a peaceful or destructive role in the world, whether it will repress or respect human rights, depends on whether the United States is able to again develop a constructive relationship with China. No other Pacific power can play that role. Does anyone seriously believe that the Japanese, let alone the Russians, would export democracy to China?

There is Japan, an economic superpower. It is fashionable and politically profitable to bash Japan these days. And as last week's issue of Newsweek indicated, it has now become fashionable in Japan to bash the United States. We must insist that we have fair trade as well as free trade with Japan. But we must recognize that as the two most advanced free world economies we are destined to be vigorous and at times even fierce competitors. But we must keep that competition in perspective. Those who contend that Japan has now replaced the Soviet Union as our major adversary in the world are grossly exaggerating the problem. The Dutch own more of America than do the Japanese. Even if all trade barriers between the United States and Japan were removed, our trade deficit with Japan of \$45 billion a year would be reduced by only \$5 to \$7 billion. As we consider the causes of our economic problems, rather than always looking out the window toward Japan, we should look in the mirror. Above all, we must never lose sight of the fact that without a constructive, strategic relationship between the United States and Japan, peace will not survive in the Pacific.

There is Western Europe, which after 1992 will challenge the United States as the world's major economic superpower. Before blithely dismantling NATO, we must remember that we need it for two reasons: As insurance against a renewed Soviet threat, and as reassurance for those who rightly or wrongly fear the power of a united Germany. Let's look at Europe without NATO. For forty years, the goal of Soviet foreign policy has been to de-nuclearize Europe, get the United States out of Europe, neutralize Germany, and dismantle NATO. Such a Europe would

leave the Soviet Union as the only nuclear superpower and as the dominant conventional power in Europe. How long could the German economic powerhouse tolerate that situation?

There is the Third World. By the end of the century, four billion people will be living in the less developed nations of Latin America, Africa, and Asia. They will have a per capita income of \$800 a year, as compared with \$18,000 a year in the United States, Western Europe, and Japan. That disparity is a recipe for revolution in a part of the world in which there have been over 100 wars since World War II in which more people have been killed than in World War I.

The people of these countries have enormous problems. In the past, the communists at least have talked about the problems. Too often, we only talk about the communists. Now with the communist threat receding, we should address those problems honestly and creatively.

I could go on, but as you can see, apart from the Soviet threat which has monopolized our attention for over forty years, we face awesome challenges. But they are also inspiring because they are the challenges of peace, not of war. Can America meet those challenges? It is ironic that at the very moment we are at the brink of victory in the Cold War, a wave of isolationism is sweeping across the country. From the left we hear that the United States is a declining power and that we are no longer able or even worthy to carry the burden of free world leadership. From the right, we hear that the United States has carried that burden long enough and that the time has come for those we helped after World War II, particularly the Japanese and the Germans, to assume that responsibility.

There is no question that the Germans and Japanese should do far more. But that does not mean that the United States should do nothing.

We are not as powerful as we were after World War II, relative to the rest of the world. But the United States is still the world's only true superpower. The Soviet Union is a military superpower. The Japanese and Germans are economic superpowers. Only the United States is a military, economic, and geo-political superpower.

As Herb Stein recently pointed out, the United States is a very rich country. We are not rich enough to do anything, but we are rich enough to do everything important.

In speaking of the power of the United States in his Iron Curtain speech, Churchill said, "This is a solemn moment for the American Democracy. For with primacy in power is joined an awe-inspiring accountability for the future." That statement is as true today as it was when he spoke those words forty-four years ago. Leadership that only the United States can provide in both Europe and Asia is indispensable if peace and freedom are to

survive in the world.

We should provide that leadership not just for others but for ourselves. America cannot be at peace in a world of wars. When freedom is lost anyplace, it is lost in America. We cannot have a healthy American economy in a sick world economy. For example, while there was significant progress politically in many Latin American countries in the 1980s, economically, the eighties were a lost decade. Only Colombia showed growth -- and that for very unhealthy reasons. As the poor of Latin America escape from poverty, we in North America will find our lives enriched.

Let me put the challenge we face in historical perspective. In 1947, two freshman congressmen, Jack Kennedy and I, had offices near each other on the fifth floor of the old House Office Building. I vividly recall our first major foreign policy vote, exactly forty-three years ago. In a dramatic joint session of Congress, President Truman asked for military and economic aid for Greece and Turkey to meet the communist threat to those countries. It was a tough vote for both of us. It was tough for him because the liberal Democrats in his Massachusetts district opposed any military foreign aid. It was tough for me because the conservative Republicans in my California district opposed all foreign aid.

We both voted for it and helped to launch the great bipartisan initiative which deterred Soviet aggression in Western Europe for the past forty years.

We were young then. And with the enthusiasm of youth, we were highly motivated by the belief that we were serving a great cause -- the defeat of communism.

You, the present and future leaders of America, have a greater cause -- the victory of freedom. If you meet your challenge as we met ours, your legacy will be not just that you saved the world from communism, but that you helped make the world safe for freedom.

FACT SHEET ON CONTINUATION OF MFN FOR CHINA

-- China Meets the Emigration Requirements of Jackson-Vanik. Approximately 17,000 Chinese nationals received U.S. immigration visas to travel from the mainland in 1989. Chinese immigration continues to meet U.S.-imposed limits. Other visa levels are about the same as the previous year's, with privately sponsored students up sharply and government sponsored students down.

-- U.S. Business Would Be Hurt. Investments of \$4 billion in China would be put at risk, as would U.S. exports to China which totaled nearly \$6 billion in 1989. The Chinese would retaliate for loss of MFN with higher duties, particularly on products where the U.S. has serious competition. Major exports at stake are:

- Wheat. \$1.1 billion (20% of US exports)
- Aircraft/Aerospace Equipment. (Current prospects of \$1 billion per year with big contracts pending)
- Fertilizer. \$487 million.
- Cotton. \$259 million.
- Timber/paper. \$262 million (10-20% of US log exports)
- Computers/machinery. \$342 million.
- Acids. \$162 million.

-- U.S. Consumers Would Be Hurt. China supplies about one-third of US toy consumption, 9% of footwear, 13% of imported apparel, and a rapidly increasing volume of electronic products. Non-MFN duties would raise landed costs an average of 40%.

-- Hong Kong Would Be Hurt. Already shaken by the events in China, MFN loss would damage the colony by costing as many as 20,000 jobs and as much as 2.5% of GNP growth.

-- Denial of MFN Will Harm Reformers and Strengthen Hardliners. In China, the advocates of political and economic reform and of greater human rights depend on outside contacts and support. Cutting them off will weaken them while giving hardliners a nationalistic scapegoat for their failing policies.

-- Sanctions Remain in Place. US pressure for reform is contained in the sanctions already enacted. The Administration will continue to press for progress on our human rights and other concerns. MFN status is not a concession; it is the basis of everyday trade. Our competitors will not follow us in denying MFN.

-- Engagement Pays Off in the Long Run. Western involvement in China has helped produce the major social and economic changes behind the Tiananmen demonstrations. Despite the past year's repression, greater interaction will lead ultimately to greater influence.

US-CHINA TRADE DATA AND MFN/NON-MFN DUTY RATES

US-China Trade
 (Billions)

| | <u>1979*</u> | <u>1980</u> | <u>%Chg</u> | <u>1988</u> | <u>1989</u> | <u>%Chg</u> | <u>%Chg 79-89</u> |
|----------------------|--------------|-------------|-------------|-------------|-------------|-------------|-------------------|
| <u>Total Trade</u> | 2.3 | 4.8 | 109 | 13.5 | 17.8 | 32 | 674 |
| <u>US Exports</u> | 1.7 | 3.7 | 118 | 5.0 | 5.8 | 16 | 241 |
| <u>US Imports</u> | .6 | 1.0 | 67 | 9.3 | 12.0 | 29 | 1900 |
| <u>Trade Balance</u> | 1.1 | 2.7 | 145 | (3.5) | (6.2) | (77) | (664) |

Leading US Exports to China in 1989
 (FAS Value)

Wheat -- \$1.1 billion
 Fertilizer -- \$487 million
 Aircraft, spacecraft, launch vehicles -- \$366 million
 Cotton -- \$259 million
 Rough wood -- \$ 175 million
 Parts of aircraft, spacecraft -- \$170 million
 Polycarboxylic acids, etc. -- \$162 million
 Automatic data processing machines -- \$126 million
 Turbojets, turbopropellers, turbines -- \$116 million
 Machinery parts -- \$112 million
 Various machines -- \$104 million
 Kraft paper and paperboard -- \$87 million

Selected PRC Import Tariffs

| <u>Commodity</u> | <u>MFN Tariff(%)</u> | <u>Non-MFN Tariff(%)</u> |
|-----------------------|----------------------|--------------------------|
| Wheat | 0 | 0 |
| Aircraft & Pts | 6 | 11 |
| Fertilizers | 30 | 40 |
| Cotton | 30 | 40 |
| Rough Wood | 3 | 8 |
| Polycarboxylic Acids | 15 | 20 |
| Specialized Machinery | 20 | 30 |

* Last year before US granted MFN status to China

Leading Chinese Exports to the US in 1989
 (Customs Value)

Baby carriages, toys, games, sporting goods -- \$1.76 billion
 Articles of apparel NES -- \$1.03 billion
 Womens/girls coats, non-knit -- \$88 million
 Footwear -- \$721 million
 Trunks/suitcases -- \$555 million
 Mens/boys coats, non-knit -- \$485 million
 Radiobroadcast receivers -- \$476 million
 Crude Oil -- \$460 million

Selected US Import Tariffs

| <u>Commodity Category</u> | <u>MFN Duty(%)</u> | <u>Non-MFN Tariff(%)</u> |
|---------------------------|--------------------|--------------------------|
| Manufactured Articles | 0-32 | 0-110 |
| Apparel, clothing items | 0-34.6 | 25-90 |
| Telecommunications, Sound | 2.4-8.5 | 35 |
| Footwear | 0-48 | 10-84 |
| Travel goods/handbags | 4.6-20 | 35-90 |
| Petroleum, oils | \$.105/bbl | \$.21/bbl |

People's Republic of China

Emigration and Student, Business and Other Travel

Emigration

- o The Chinese Government has continued to permit its nationals to emigrate to the United States. New Chinese travel regulations appear to be aimed at regulating non-emigrant travel and not emigration.
- o In FY 1989, the number of US immigrant visas issued in China increased 9.5 percent to 16,920. The annual numerical limit for Chinese immigrants to the United States was fully met. In the first five months of FY 1990, US officials issued 7,932 immigrant visas, which is about the same number issued during the period one year earlier.
- o US immigration law restricts the number of immigrants from China, as from other countries, (aside from parents, children and spouses of US citizens) allowed to enter the United States. There has recently been a marked increase in the number of parents of US citizens who have received immigrant visas.

Business, Student and Other Travel

- o The total number of US visa applications of all categories other than emigration has remained about the same although the composition of applicants has changed in the last year.
- o Applications for private travel, which includes tourists, have increased significantly. For example, in Beijing applications for private travel increased 94 percent to 3,226 in the October 1989-March 1990 period, compared with 1,662 in October 1988-March 1989.
- o Applications for privately sponsored student visas and their dependents have also risen sharply. Beijing recorded increases of 86 and 110 percent respectively in these two categories in the period October 1989-March 1990, compared with October 1988-March 1989. Student applications increased to 3,398 from 1,828. Their dependents' applications increased to 1,409 from 671.
- o Since late 1988, Beijing visa applications of government officials and state enterprise personnel traveling for business have declined by 30 percent from 12,364 in October 1988-March 1989 to 8,651 in October 1989-March 1990. We believe this decline is due mainly to the government's economic retrenchment policy and cutbacks in travel funds rather political restrictions on travel.

CHINA SANCTIONS

- In the years prior to Tiananmen, there were frequent, regular exchanges of high-level visits, involving White House/State Department banquets, major speeches, meetings with senior U.S. businessmen and the press, with travel around the U.S. For example, President Yang Shangkun in '87, Vice Premiers Wu Xueqian and Tian Jiyun in '88, Politburo member Wan Li in '89, George Shultz to the PRC in '87 and '88, President Bush to China in February '89. With the exception of the Scowcroft-Eagleburger special missions, which I will discuss later, this process has been halted.
- There were regular visits annually to and from China by the Director of ACDA, State Department's Under Secretary for Political Affairs, Assistant Secretary for EAP, PM Director, equivalents from other agencies. These have halted.
- The JEC and JCCT, headed by Treasury and Commerce Secretaries, were annual events. They are now halted.
- We had four ongoing FMS programs. Deliveries on them have been halted.
- We were discussing future FMS programs in other areas. Those discussions have been halted.
- There were commercial sales of weapons to China, and sales of items such as helicopters made by Sikorsky (and plans for Boeings) to the PLA. Since June, there have been no commercial sales of weapons to China, and no sales to the PLA or Chinese security forces.
- China was proceeding apace toward accession to the GATT. That process has now effectively stalled.
- China was recipient of major assistance from the World Bank. About \$1 billion in loans were frozen last June. Only basic human needs loans have been authorized since January, consistent with the letter and spirit of U.S. statute. Other loans remain frozen.
- China has been the beneficiary of a succession of liberalizations by COCOM since 1984. A major liberalization was under discussion for 1989. It was shelved.
- Chinese naval ships visited U.S. ports in early 1989. There have been no visits since, and none is under discussion or contemplated.
- The Science & Technology Agreement is due for a five-year extension, which was to be done at a meeting of a joint commission at the ministerial level last year. That

commission meeting was postponed, and the Agreement has not been renewed, though it has been extended on an interim basis. S&T exchanges continue on a markedly reduced basis.

- OPIC has provided no insurance for investors in China since June, where they were actively involved prior to that.
- We have admitted scores of refugees escaping China seeking asylum into the U.S., and the number of asylum requests granted is up sharply.

MOST-FAVORED-NATION (MFN) TRADE STATUS FOR CHINA

- o The Administration and Congress both share the same goals in China--make clear our deeply held views on human rights and encourage conciliatory policies and a reinvigoration of political and economic reform.
- o The President, after careful consideration, decided to extend China's most-favored-nation (MFN) trade status for another year. In reaching this determination, the President weighed not only the requirements of the Jackson-Vanik amendment, which obligate him to consider whether MFN renewal would substantially promote freedom of emigration, but also the broader question of whether MFN would advance the cause of human rights and reform in China. On balance, the President concluded that extending MFN would promote US objectives in both these areas and protect other vital US interests as well.
- o Emigration. Approximately 17,000 Chinese emigrate from the mainland to the United States every year. This emigration flow has continued since the military crackdown in June 1989. While the Chinese Government has imposed some new travel restrictions on students, it has continued to permit emigration travel since Tiananmen. US numerical limitations, and not Chinese restrictions, limit the number of Chinese who emigrate to the United States.
 - In our judgment, continuation of MFN status will help to preserve the gains already achieved on freedom of emigration and encourage further progress in the future. Thousands of Chinese families have been reunited in the United States through emigration. The contacts which these immigrants maintain with friends and relatives in China help to encourage positive change there and promote friendly relations with the US. Denying China MFN status removes an important incentive for permitting emigration and invites retaliation in the form of new travel restrictions.
- o Broad Human Rights. The President believes that a continuation of MFN for China is vital to advancing the cause of human rights and in supporting those Chinese who seek a modern, progressive China.
- o Granting China MFN status, which is the tariff treatment the US accords all but a small number of its trading partners, was one of the key elements in a package

normalizing diplomatic relations in 1979-80. It signaled that the US would treat China as an equal with other countries and facilitated a major expansion in our economic relations. But MFN's impact extended far beyond commerce and trade.

- o The prospect of rapid modernization through increased trade and investment with the US encouraged a broader opening to the West, gave further impetus to market-oriented economic reforms, created expanded opportunities for people-to-people contacts, and justified the sending of thousands of China's best and brightest students to the US for higher education where they were exposed to Western values and democratic ideals.
- o Denying MFN status would adversely affect our ability to maintain those contacts and thereby to help sustain the impetus for internal reform.
 - China would view MFN denial as a hostile act, and a further deterioration in the relationship would result.
 - In this strained atmosphere, Chinese contacts with Americans across the board--business, academic and scientific--would be more difficult and may be severely curtailed. Those Chinese with an interest in furthering China's opening to the West and seeking positive change would be most affected.
 - MFN denial would likely bolster the position of conservatives in the leadership who want to restrict Western influence, give internal policies a more ideological orientation and maintain strict government controls on society and the economy. On the other hand, reformers, who could up until now point to substantial benefits from good relations with the US and a deepening of market-oriented policies, would be put on the defensive.
- o MFN denial would remove an important incentive for China to take into account a broad range of US interests--on human rights, missile and arms sales, fair trade practices abroad, and cooperation on regional issues, such as Cambodia and Korea.
- o Allied Solidarity. The US and its G-7 allies (France, Germany, UK, Japan, Canada and Italy) have thus far maintained a united position on China policy. Since the Paris Summit in July 1989, there has been a G-7 consensus against a general resumption of World Bank lending to China. Other G-7 countries have also suspended arms exports to China and are limiting high-level contacts.

- While our allies all agree China should do more to improve the human rights situation, they also believe that MFN is important and plan to continue this trade status for China. The US would be the only Western country to withdraw MFN if the President did not renew the waiver. We believe a united G-7 position puts more pressure on China than unilateral US actions.
- o Economic Implications. The economic consequences of removing China's MFN status would also be severe--for US business, US consumers, Hong Kong and workers in export industries in China.
 - o Since receiving MFN status in 1980, US-China trade has nearly quadrupled, reaching \$18 billion in 1989. US exports totalled \$6 million, and China remains a potentially large market for a broad range of US products. Major US exports are: wheat, commercial aircraft, phosphate fertilizer and high-tech equipment, such as computers and scientific instrumentation. (See attached fact sheet for details.)
 - o The US has become China's largest market, absorbing 25 percent of China's total exports. China's top 20 exports to the US by value would face average duty rates of nearly 60 percent if MFN status is revoked--in some cases ten-times higher than with MFN privileges.
 - o Retaliation is a certainty. China would apply its higher non-MFN duty rates to imports from the US and could use a variety of administrative measures to restrict market access by US companies (e.g., through foreign exchange allocations, import licenses, quality standards and restrictions on imports competing with local production).
 - o US firms that have worked hard over the last ten years to develop business ties and market share within China would lose that business--perhaps permanently--to other suppliers in Europe and Japan. No other Western country is planning to deny China MFN status. Retaliation therefore would be on focused US firms.
 - o Effect on Consumers. US consumers would also suffer. MFN denial would lead to sharply higher prices on imports from China. Chinese manufacturers currently supply one-third of American toy consumption, 10 percent of footwear consumption, close to 15 percent of imported apparel consumption and a rapidly increasing volume of consumer electronic products. According to the US-China Business Council, non-MFN tariffs would increase the landed cost of Chinese products by 40 percent. Given the mix of Chinese exports to the US, the impact of increased prices is likely to fall disproportionately on low-income consumers.

- o Hong Kong Impact. Revoking MFN status would also have long-term negative effects on Hong Kong, threatening the island's stability and prosperity in the run-up to 1997 when Beijing reassumes control.
 - Hong Kong entrepreneurs have invested in thousands of Chinese enterprises, particularly in Guangdong's Pearl River delta region in South China, to take advantage of low-cost manufacturing. Hong Kong-invested enterprises in South China employ some 2 million Chinese. An additional 10,000-15,000 South China enterprises do processing and assembly work for Hong Kong companies.
 - Of a total of \$25 billion in Chinese exports to Hong Kong in 1989, \$24 billion were re-exported to other countries. The United States is by far the largest market for Chinese reexports through Hong Kong, taking more than \$8.5 billion in 1989.
 - The dropoff in Chinese exports to the US would have a direct impact on Hong Kong firms involved in transshipment of goods to the US, including banking, insurance, shipping, and legal services.
 - MFN withdrawal would be a serious blow to confidence in Hong Kong. Net emigration from Hong Kong is now running about 40,000-50,000 annually, resulting in a serious shortage of skilled labor and mid-level managers. A sharp deterioration in US-China trade relations would heighten concerns about Hong Kong's future at a time when confidence is already weak because of Beijing's heavy-handed suppression of dissent on the mainland.
- o In short, the President has decided to extend China's MFN status because it serves clear US interests in several important areas--emigration and human rights, the need for reform in China, US business, US consumers and Hong Kong's stability and confidence.
- o Need for Further Human Rights Improvements. In notifying Congress of his determination to renew MFN for China, the President emphasized that he remains seriously concerned about human rights violations in China and is personally disappointed that the Chinese Government has not taken more decisive steps to demonstrate a commitment to internationally accepted human rights, despite repeated expressions of concern by the US and many other Western countries. The President has also indicated that the US Government intends to press vigorously during the coming year for significant improvement in China's human rights practices.

- o Sanctions to Continue. The extension does not signal a return to business as usual with China. The President has reaffirmed that he will maintain the sanctions against China he authorized in June 1989 on arms exports, high-level government exchanges and postponement of multilateral development loans.
- o We should not let our frustration with Beijing's slow response to our concerns lead us to take unilateral actions which, in the end, only serve to undercut our long-term objectives. Denying MFN would do just this. It would also result in the United States losing the leverage it has gained over the last decade to influence positively the course of human rights developments in China.

ECONOMIC IMPACT OF DENYING CHINA MFN STATUS

Impact on China:

- o Foreign Exchange: Estimates range from a drop of between \$3 billion to as high as \$6 billion, depending on how China would react. Due to large portion (25%) of export sales to the US market, Beijing would likely try to maintain a portion of its current sales to the US. It would also try to shift high-duty exports to other markets such as Japan and Europe, but this would be difficult because market access is more restrictive.
- o Debt Repayment: Could seriously affect China's ability to repay its foreign debt, estimated at \$42-44 billion. Debt repayment will peak during 1992-1993, when China will need to repay \$10 billion annually, up from \$4-\$6 billion in 1990. Changed trade outlook could force a reevaluation of China's debt servicing capacity and consequent lowering of its creditworthiness. New commercial lending would become more costly and difficult to arrange.
- o Employment: Difficult to determine. Most severe impact would be regional, concentrated in coastal provinces (e.g., Guangdong and Fujian) and open cities. These provinces are the most dependent on foreign trade and overseas investment, particularly from Hong Kong and Taiwan.
- o Economy: Would complicate Beijing's efforts to pull its economy out of its current slump. GNP growth rate plummeted to 4 percent in 1989 from 11 percent in 1988.

Impact on Hong Kong:

- o Trade: Almost 19 percent (\$8.4 million) of Hong Kong's \$44 billion of reexports were labor-intensive goods made in China destined for the US market. Tariff rates would jump ten-fold on many of these products, resulting in an estimated export decline between 25-50 percent.
- o Employment: Preliminary Hong Kong estimates indicate that a 50 percent drop in Hong Kong reexports of Chinese goods to the US would throw 20,300 employees out of work in a labor force of 2.8 million and cause Hong Kong's GDP to fall by \$590 million, reducing expected GDP growth by about 1 percentage point to 1.6 percent.

Impact on the US:

- o Trade Retaliation: Should the US withdraw MFN status from China, the Chinese would retaliate, increasing tariffs on imports from the US and using administrative measures to reduce imports from the US. Major US exports which could be affected include cereals, power generating machinery, aircraft, and fertilizer products.
- o Chinese Non-MFN Duties: The higher non-MFN tariff rates would increase the cost of US exports to China by up to 30 percent, depending on category. Chemicals, cotton yarns and fabrics, and electrical machinery would be more significantly affected.
- o Export Loss: The annual loss in US exports to China could be in the range of \$2 billion to \$3 billion, or about 33-50 percent of 1989 export levels. With a bumper harvest this year and increased imports from Canada, China could reduce significantly its grain imports from the US. Japan and West Germany are poised to displace US firms in contracts for industrial machinery and steel products. South Korea and Taiwan could move to pick up chemical and fertilizer business.
- o Effect on US Investment: US-invested joint ventures in China would be forced to pay higher duties on imported components. Their exports to the US would also be subject to non-MFN tariffs, in some cases ten-times higher than MFN rates, thereby undermining their economic and financial viability. According to Chinese statistics, at the end of 1989 there were 949 US-invested firms in China with a pledged investment of \$4.1 billion.
- o Effect on Consumers: Removal of MFN for China would lead to higher prices for American consumers. Non-MFN tariffs would increase US landed costs by an average of 40 percent and duty rates would average approximately 60 percent. Given the mix of Chinese consumer exports to the US, the impact will be disproportionately felt by low-income consumers. Duty increases will be high on low-margin consumer goods, such as shoes, clothing, electronic products, and toys.

M E M O R A N D U M

May 25, 1990

TO: SENATOR DOLE
FROM: JIM WHITTINGHILL
SUBJECT: FRENCH ABORTION PILL

In the event you get questioned about the French abortion pill company making donations to Republicans who are pro-life, here is what is going on:

The controversy began when former Senator and current candidate John Durkin charged that Congressman Bob Smith (NH) took a donation from the company who makes the French abortion pill -- RU 486.

The donation was from Celenese Corp., which was bought by Hoechts (HERKS), a German company in 1987. Hoechts, the parent company, now owns what is known as Hoechts Celenese.

Hoechts (the parent) also owns 50% of a French pharmaceutical company, Roussel Uclaf, maker of RU 486 (the pill). The French government evidently does not allow Germans to own more than 50% of its major corporations (World War II). The French government owns the other 50%. The Chairman of Hoechts is Catholic and tried to prohibit the manufacture of RU 486, but the French blocked the effort and moved ahead.

Hoechts Celenese does not have any pharmaceutical interests, and doesn't plan to. The majority of the business is textiles and chemicals. The corporate offices in New Jersey have been picketed by the National Organization for Women (and others) for not bringing the pill to the U.S.

Hoechts Celenese has contributed to many Republicans (including Dole for President, Dole for Senate '92, Campaign America and the Dole Foundation). Others are Helms, Gramm, Martin, Schneider, Thurmond, Cohen.

Their lobbyist called after hearing a remark about the Smith contribution that was made at the Dole for Senate breakfast. They aren't upset or anything, they just wanted you to know what was going on.

cc: JO ANNE

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