CONTENTS

	Page
CHAPTER 1. THE MAKING OF THE NEW ECONOMY	19
The Economy from 1973 to 1993	21
What Makes the Economy New?	22
Sustaining the Virtuous Cycle	24
Information Technology and the New Economy	25
The New Trend in Productivity Growth	26
Sources of Growth: Capital, Labor Quality, and Total Factor Productivity	26
Productivity Increases by Sector and Industry	30
Learning from the New Productivity Trends	33
Innovations in the Information Technology Sector	34
Growing Competition	34
Organizational Changes	36
Innovations in Compensation and Finance	37
New Complementarities	38
Innovation Throughout the Economy	38
New Production Methods	39
Changes in Inventory and Supply Chain Management	39
New Relationships with Customers	40
Shifting Corporate Boundaries	40
Behind the New Trends: The Role of Policy	41
Fiscal Discipline	42
Investing in People and Technology	43
Setting the Rules for Fair and Open Competition	45
Social Policies	47
Challenges for the Future	48
Preserving Fiscal Discipline	49
Nurturing a Vibrant Private Sector	50
Ensuring That Globalization Enhances the New Economy	50
Creating an Economy That Works for All	51
CHAPTER 2. MACROECONOMIC POLICY AND PERFORMANCE	55
The Year in Review	57
Private Domestic Spending	60

AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

Page
Government Spending and Fiscal Policy 63
International Influences 64
Monetary Policy and Financial Markets 65
Labor Markets and Inflation 68
The Economic Outlook 70
The Near-Term Outlook 71
Productivity and the NAIRU 73
Inflation Measurement and the Federal Surplus 74
The Stock Market, Saving, and Consumption Prospects 75
The Long-Term Projection 77
The Fiscal Terrain in the New Economy 79
Strong Public Saving: The Payoff from Deficit Reduction 80
What Caused the Surpluses? 83
The Importance of Maintaining Fiscal Discipline 87
Conclusion 93
CHAPTER 3. THE CREATION AND DIFFUSION OF THE NEW ECONOMY ... 95
The Advance and Convergence of Information Technologies 98
Why Is the U.S. Economy Awash in Technology? 103
The Demand for New Technology 104
Financial Market Developments 106
R&D in the New Economy 110
Intellectual Property Protection 118
A Favorable Alignment 119
Doing Business in the New Economy 120
New Developments Inside Plants and Firms 121
Changes in Firm Boundaries 128
Competition and Strategy 136
Understanding Performance Gains 138
How Do Technology and Organizational Change Improve Performance? 138
The Dynamics of Market Competition 140
Conclusion 142
CHAPTER 4. THE NEW ECONOMY IN A GLOBAL CONTEXT 145
The Role of Trade Liberalization in Promoting Globalization 147
Globalization and Economic Performance 148
Scale and Network Effects 148

Page
Competition and Innovation 149
Changes in the Global Organization of Production 150
Better Technology, More Trade 153
Technology and Knowledge-Based Products in U.S. Trade and Investment Flows 155
New Challenges 157
The U.S. Trade Balance and Current Account 158
Raising Performance in Other Countries 161
The Importance of Institutions and Policy 166
Raising Incomes in Developing Countries 169
Adjusting to Change at Home 173
Trade and the Environment and Labor Standards 175
Challenges for Legal Frameworks 176
Making Globalization Work 180
Opening Markets to Trade and Investment 182
Conclusion 185
CHAPTER 5. LIVING IN THE NEW ECONOMY 187
Good News from the American Economy 188
Helping Families Help Themselves 193
Welfare Reform 193
Making Work Pay 198
Reaching out to Underserved Communities 204
Education in the New Economy 209
A Role for Federal Education Policy 209
Reducing Class Size 211
The Importance of Teachers 212
The Need for Modern Schools 216
New Educational Technology and Internet Access 216
Standards and Accountability 219
Increasing Public School Choice 220
Helping Students Make the Transition from Secondary School to College 222
Innovation and Access in Health Care 223
Technological Innovations 223
Organizational Innovations to Control Health Care Costs 225
Improving Health Insurance Coverage 229
Building Livable Communities 236

Page
Business and Suburbanization 237
Sprawl and Its Challenges 238
Regional Coordination and Sprawl 239
Individual Decisions and Sprawl 239
The Administration's Response 241
Conclusion 242

CONCLUSION: ACHIEVEMENTS AND CHALLENGES IN THE NEW ECONOMY 245
Technology's Role in the New Economy 247
The Role of Policy in Supporting the New Economy 249
Globalization and the New Economy 250
Harnessing the New Economy 250

APPENDIXES

A. Report to the President on the Activities of the Council of Economic Advisers During 2000 253
B. Statistical Tables Relating to Income, Employment, and Production 267

LIST OF TABLES

1-1. Accounting for the Productivity Acceleration in the 1990s 28
1-2. Labor Productivity Growth by Industry, Selected Periods, 1989 to 1999 32
2-1. Growth of Real GDP and Its Components During 1998–99 and 2000 58
2-2. Administration Forecast 72
2-3. Accounting for Growth in Real GDP, 1960–2008 78
2-4. Components of Federal Budget Outlays 84
3-1. Content and Commerce on the Internet 102
4-1. Source of Inputs Used in Production by U.S. Multinational Corporations at Home and in Foreign Affiliates 153
4-2. Changing Composition of U.S. Trade Flows 156

Page

List of Charts

1-1. Growth in Real Household Income by Quintile, 1973–93 and 1993–99 20
1-2. Growth in Gross Domestic Income Due to the Information Technology Sector 25
1-3. Output per Hour in the Nonfarm Business Sector 27
1-4. Producer Price Index for Electronic Computers 30
1-5. Indicators of Growth in Information Technology Activity 35
1-6. Information Technology Firms 36
1-7. Inventory-to-Sales Ratio in Manufacturing and Trade 40
1-8. Mergers and Acquisitions Involving U.S. Firms 41
1-9. Federal Budget Balance 43
1-10. Computer Imports and Exports as a Share of Computer Purchases and Production 46
2-1. Growth in Real GDP 58
2-2. Growth in Output per Hour in the Nonfarm Business Sector 59
2-3. Consumption and Disposable Income 60
2-4. Personal and Wealth-Adjusted Saving Rates 61
2-5. Real Investment in Equipment and Software 63
2-6. Actual and Structural Federal Budget Balances 64
2-7. Equity Prices 66
2-8. Contributions to Growth in Market Capitalization 67
2-9. Selected Interest Rates and Yields 68
2-10. Consumer and Import Prices 70
2-11. Nonfarm Business Compensation per Hour and Unit Labor Costs 71
2-12. Net Worth-to-Income Ratio and Consumption Rate 75
2-13. Actual and Projected Federal Budget Balances 81
2-14. Actual and Projected Debt Held by the Public 81
2-15. Public, Private, and National Saving 82
2-16. Growth in GDP and Adjusted Gross Income (AGI) 86
2-17. Population Aged 65 and Over and Outlays for Social Security and Medicare 89
2-18. Long-Term Budget Balance Projections Under Different Policy Assumptions 90
3-1. Real Investment in Information Technology 98
3-2. Prices and Real Investment in Computers and Peripheral Equipment 99

		Page
3-3.	Prices and Real Investment in Software	100
3-4.	Employment in Computer and Data Processing Services	101
3-5.	Venture Capital Investment	107
3-6.	Number and Gross Proceeds of Initial Public Offerings	109
3-7.	First-Day Returns for Initial Public Offerings	110
3-8.	Real Research and Development Spending by Source and Type	111
3-9.	Total Expenditures on Industrial R&D by Firm Size	113
3-10.	New Domestic Strategic Technology Alliances	117
3-11.	Firms Introducing or Expanding Nonexecutive Stock Option Plans, 1996–98	127
3-12.	Employment in Management Consulting and Employment Agencies	131
3-13.	Tobin's *q* in the Nonfinancial Corporate Sector	137
3-14.	Business Failures	141
3-15.	Real Corporate Profits	141
4-1.	Imports and Exports by End-Use Category	156
4-2.	Trade in Capital Goods and Selected Components	157
4-3.	Growth in Real GDP by Region	158
4-4.	The Trade Deficit and the Real Effective Exchange Rate of the Dollar	159
4-5.	Saving, Investment, and the Current Account Balance	159
4-6.	OECD Estimates of Growth in Potential Output	162
4-7.	Change in Average Annual Productivity Growth from 1990–95 to 1996–99	163
4-8.	Indicators of the Pervasiveness of Information Technology	165
5-1.	Unemployment Rates by Race and Hispanic Origin	190
5-2.	Poverty Rates by Race and Hispanic Origin	190
5-3.	Maximum Real EITC Benefit by Family Earnings, 1993 and 1999	199
5-4.	EITC Benefit and Labor Force Participation of Unmarried Women with Children	200
5-5.	Real Minimum Wage Combined with the Real Maximum EITC Subsidy	201
5-6.	Poverty Rates in Metropolitan and Nonmetropolitan Areas, 1993 and 1999	208
5-7.	Revenue per Pupil by Source and Income Quartile of School District, 1994–95	210

		Page
5-8.	Share of U.S. Public Schools with Internet Access	217
5-9.	Sources of New Computers Received by Elementary Schools in 1997–98	219
5-10.	Health Expenditures and Enrollment in Health Maintenance Organizations	228
5-11.	Average Federal Tax Benefit for Health Expenses, 2000	230
5-12.	Health Insurance Coverage of Those under Age 65, by Type and Income, 1999	231

List of Boxes

2-1.	Are Treasuries Being Swapped out of Their Benchmark Role?	69
3-1.	Federal R&D and Commercial Technology: Licensing, Cooperation, and Partnerships	116
3-2.	Information Technology in the Machine Tool Industry: The New Economy Helps the Old	123
4-1.	A New Role for Multinational Firms	151
4-2.	Information Technology and Cross-Country Differences in Measuring Economic Growth	164
4-3.	Reforming International Institutions	180
4-4.	The Global Promise of Biotechnology	183
5-1.	The Workforce Investment Act	196
5-2.	Rewarding Effective Teachers	214
5-3.	Reducing the Digital Divide	218
5-4.	Ensuring That Gains Are Maintained	221
5-5.	The Rise of E-Health: On-Line Medical Information	227
5-6.	Challenges to Smart Growth in Atlanta	240
5-7.	Examples of Smart Growth	242