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A Maine Response

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Three perspectives: The impact of public policy on the competitiveness of Maine's business and industry

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The twentieth anniversary of the Governor's Economic Development Conference last October focused on the impact of public policy on the competitiveness of Maine's business and industry. Among many other important presentations, the University of Maine-sponsored conference featured a televideo keynote address by the Clinton Administration's top economic advisor, Laura D'Andrea Tyson. Tyson's remarks, which detailed the Administration's policy initiatives meant to enhance the nation's competitiveness relative to the international economy, are presented in this issue of Maine Policy Review, along with two other presentations as representative of the quality of the discussion that occurred at the conference. UNUM Chief Executive Officer James F. Orr III cautioned conference attendees that, while President Clinton deserves credit for some of his early initiatives, the path to establishing a national economy that will position the U.S. for the next century is a long and difficult one. Finally, Warren C. Kessler, president of Kennebec Health Systems, assesses Clinton's health reform proposal.

A Maine response

by James F. Orr

Introduction

In considering "A Maine Response," I would like to first encourage everyone in Maine not to take a narrow, parochial view of economic events. For more than 100 years, successful Maine enterprises have known their futures are closely linked with the national and, yes, even the global economies. That context will be the focus of my response to Dr. Tyson.

Recently, the Clinton Administration has begun to use the theme of "economic security" to link its efforts on issues such as the budget, health care reform and the North American Free Trade Agreement (NAFTA). Certainly, economic security is a worthy objective, one we can all understand and support. The administration deserves a great deal of credit for recognizing that our nation needs to face some tough challenges and take some bitter medicine. But I will offer a cautionary note. We are only at the start of the road, not the end. It will take more than a good speech or the signing of a law to set the economies of Maine and our nation on a proper footing for the next century. Much has been started, but much is left to do. We all have an important role to play in these developments in the years to come.

The federal budget

I would like first to discuss the recent budget agreement, signed this past August. The administration deserves credit for taking a step toward reducing the deficit. Over the past twelve years, the federal debt has more than quadrupled. Such a high level of debt places the nation at risk.

Some data indicate the enormity of the struggle that lies ahead. During the Reagan and Bush presidencies, the national economy grew by \$3 trillion. So, too, did the national debt. The Congressional Budget Office projected recently that the U.S. economy will grow by \$1.35 trillion between now and 1996. But the national debt will grow by even more -- \$1.37 trillion!

Within the next five years, the Congressional Budget Office predicts that the average interest rate on federal borrowings will reach a low point, and will start to rise rather dramatically. Unless the federal deficit declines significantly by the late 1990s, total interest payments on our national debt will start to expand at a rapid clip. Higher interest rates and/or inflation could well result. Most people will recall the impact of high inflation and interest rates in the late seventies and early eighties, the era of stagflation.

Significantly, more than sixty percent of the spending reductions in the recent budget bill do not go into effect until 1997 -- that is, until after the next Presidential election. It would be easy for the government to resist implementing those cuts, to resist causing pain to constituents. Even today, barely two months since the signing of the budget bill, a survey of business economists revealed that they expect the package to deliver just \$125 billion of deficit reduction. That is only one-quarter the amount promised in the bill. Elected officials in Washington need our support to reduce the deficit. Without such support from home, they may well be tempted to delay the tough choices. That will put all businesses, in Maine and across the nation, at risk.

The best foundation for a growing business sector, in Maine, in America or in any nation, is a sound macroeconomic policy. A recent study indicated there are four keystones to encouragement of economic growth: a sound fiscal policy; a sound monetary policy; a healthy environment for external investment; and investment in human resources, the current and future workers of the country. Maine has put great effort in recent years into developing its human resources, through improving elementary and secondary education. The state has made good progress. UNUM is also making great strides toward developing into a "learning organization," a place where learning is continuous and a part of everyone's job. But all these efforts could be for naught without appropriate policy at the federal level. We, in Maine, are working on our side of the equation, working to improve our business competitiveness. Will the federal government keep working on its side? That is why we must be concerned and informed.

We should give the Administration credit where it is due. For now, its grade on budget policy is "incomplete." The Administration's final grade is not solely up to them; it is up to all of us, as well.

Health care reform

The second issue I would like to discuss is the issue of health care reform. It is closely related to the first issue, the budget, since nearly twenty percent of the federal budget is devoted to health care. In fiscal 1994, the federal government will spend more than \$230 billion on the two largest national health programs, Medicare and Medicaid.

Again, the Administration deserves credit for addressing health care. At present, health care consumes fourteen percent of the U.S. gross domestic product. Health spending is increasing at

two or three times the rate of inflation, becoming a larger component of the expense structures of many businesses. Without action soon, as the more than 70 million "baby boomers" (aged 30 to 50) near their retirement years, health care could consume thirty percent of the nation's economy and perhaps more. Under those circumstances, it would be such a large component of the economy that it would be politically impossible to do anything constructive about it.

The federal government is already heavily involved in the health care arena. Today, more than thirty percent of the dollars spent on health care in the U.S. come from the federal government, a proportion that is sure to grow in the years ahead. It is clearly time for choices, tough choices. But it is important to businesses here in Maine and across America that they be the right choices. We must bring the spiraling cost of medical care under control. The health and competitiveness of American businesses demand it. But because the majority of people are, on balance, happy with their doctor and the care they receive, these changes will be a difficult balancing act.

Certainly, the government has a role in health care, especially to provide for those who cannot provide for themselves. But the number of people without health care for extended periods of time may be quite small, as low as two percent of the U.S. population, according to Professor Roger Porter of Harvard. Many businesses look with trepidation at new mandates or at new entitlements in the face of huge deficits. UNUM's position on the proposed long-term care entitlement, for example, is that the private sector is the best provider for people with the means to purchase insurance and that the public sector should cover those who cannot afford to insure themselves.

In the short run, any health care reform will most likely have a negative effect on the economy, in Maine and across the nation. Incomes of health care providers and others affiliated with the health sector of the economy are likely to decrease somewhat. Whether the changes are financed through employer mandates or taxes or some combination of the two, people who have insurance will ultimately cover those who do not have coverage. This will reduce the incomes and well-being of those now covered, if only slightly.

Society may benefit in the long run from health care reform. But this reform could test our altruism as a nation. Can we accomplish all this while reducing the deficit and growing the economy? Time will tell. While meriting an "A" for effort on the health care issue, the government has earned an "Incomplete" on this one, as well. Of the several plans before Congress, it is unclear which will be the basis for the legislation. We in Maine have a responsibility to speak up and make our opinions known. In a large respect, our fate lies within our own hands.

Free trade

The final issue I will address here is the North American Free Trade Agreement. Let me begin by asking you to suspend your disbelief for a moment and consider the following scenario: Suppose there were a 10-foot wall around Maine's borders. There would be some gates in the wall. As Tim Sample might say, there may be a narrow gate coming in and a wide gate going out. A business person inside those walls who wanted to sell something to someone in, say, New Hampshire, would have to pay a tax and the tax was so high that practically no one in New

Hampshire wanted these products. Assume the converse was true, as well: Maine would have its own special tax, and that it effectively limited sales of New Hampshire products in Maine.

Now ask some simple questions: How healthy would Maine's business be? How big could a business get if it could only rely on the state of Maine for its consumers? How profitable would this business become and how many people could it employ? Fortunately, the U.S. Constitution put an end to such practices in 1787, although the situation did, in large measure, prevail before then. But this is the basic issue we faced with NAFTA. It is best for the world economy if each nation produces what it can best produce. The economic law of comparative advantage is just as valid today as when David Ricardo voiced it in the nineteenth century.

But the drumbeat of opposition to NAFTA was loud. Prominent elected representatives from the industrial heartland believe the U.S. will lose high-wage, lower-skill jobs to Mexico, where labor rates are lower. We cannot ignore those fears. But we also need to consider all the jobs NAFTA will help create in the future. With NAFTA, incomes in Mexico will rise as Mexico exports more to the U.S. and Canada. And Mexicans will use this new income to buy more from the U.S. and from Canada. That will increase employment in U.S. and Canadian industries involved in international trade. Even if Mexicans chose not to buy more U.S. and Canadian goods, which is unlikely, they will put their export earnings to work in some way. That would be through direct investments in the U.S. and Canada, which would help lower our interest rates and increase employment in industries sensitive to changes in interest rates.

If Congress had failed to pass NAFTA, it would have raised serious questions about the future direction of relations between the U.S. and Canada. Given Maine's 500-mile shared border with Canada, that was a significant issue for Maine. The issue was especially important to UNUM. UNUM has been participating very aggressively in the Canadian insurance market for about five years now. We have 12 sales offices in Canada and are looking forward to continued growth there. On the other hand, UNUM currently conducts no business in Mexico. But the Mexican market has been essentially closed to foreign financial service providers. NAFTA will end restrictions on foreign ownership and market share in Mexico by the year 2000, which will present a significant potential opportunity for UNUM and for the entire insurance industry.

Unfortunately, the jobs that NAFTA will create in the future are now invisible. The politicians, however, can very clearly see the jobs that could go away. People in high-wage, lower-skill jobs, some of whom live in Maine, will require transitional assistance and retraining. This is very similar to the people affected by military base closing, an issue that will continue to affect Maine and the U.S. in the 1990s. But the only long-term solution is to create more high-wage, high-skill jobs, for that is where our competitive advantage currently lies.

As Joseph Schumpeter once wrote, "creative destruction" is one of the driving forces of the market economy. There are always industries where employment is declining. And there are always industries where entrepreneurs with ideas and vision are creating jobs. Herbert Stein, a former Council of Economic Advisors chairman, wrote recently that in 1980, 26 percent of all Americans worked in industries in which the total number of jobs declined in the 1980s. Did those Americans know in 1980 that their industries would shrink? Probably not. But was that job

reduction really a tragedy? In fact, total employment increased strongly during the 1980s, as other industries created nearly 20 million new jobs.

Free trade across international borders is the optimal long run solution in international economics, despite protestations to the contrary. The needs are great. The times are tough. And tough times require hard work and leadership, both from above and from below. The passage of NAFTA creates opportunities for businesses with vision, and I encourage Maine businesses to look with vision toward opportunities in the international market.

Conclusion

It would be easy for us, as Mainers, to sit here in this far northeastern corner of America, and simply observe events in Washington and the world. But I hope we reject that approach. For Maine's fate today is the fate of America. And our actions can affect much more than our special corner of the globe. We are linked, more than ever, with the world economy. Every business in Maine needs to understand there is no wall of safety stretching from Kittery to Fort Kent. So, as we consider the events before us and the major decisions facing policy makers, let us not enable people to say, as they did after the Presidential election of 1936: "As Maine goes, so goes Vermont!" Instead, we should live up to the saying: "As Maine goes, so goes the nation."

James F. Orr III is chairman and chief executive officer of UNUM Corporation and UNUM Life Insurance Company of America, and chief executive officer of Colonial Companies, Inc. He is past chairman of the Maine Coalition for Excellence in Education.

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