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Reinventing the (Broken) Wheel

President Bush's "Management Agenda" is the latest in a long string of attempts to make government accountable. Like its predecessors, this effort to focus on "how government should work, not on what it should do" will produce marginal benefits at best. Genuine accountability would require first asking under what conditions a Federal role is necessary.

As millions of taxpayers begin to prepare their income taxes, President Bush and Congress begin their annual debate about how to divvy up the resulting largess. This year, the Government will spend over $2 trillion on approximately 1,000 Federal programs. Just what are we getting for our money? More than we used to, in one way at least: under the President's new initiative, government agencies are now scored on how well they perform.

In August 2001, President Bush launched his "Management Agenda," which includes five government-wide initiatives. According to Bush, these initiatives—strategic management of human capital, competitive sourcing, improved financial performance, expanded electronic government, and budget and performance integration—cover the areas with "the most apparent deficiencies where the opportunity to improve is greatest." Accordingly, each government agency's "current" performance as well as its "progress" toward implementing the initiatives are now rated using a scorecard, which employs a grading system: green for success, yellow for mixed results, and red for unsatisfactory.

The scorecards that rate "current" performance have now been released—and they portray a sea of red. The Office of Management and Budget claims this "reflects the state of the government this Administration inherited.... The marks that really matter will be those that record improvement, or lack of it, from these starting points.... Over time, the scores should improve as departments and agencies correct the problems."

A Road Well Traveled

This is not the Government's first effort to make itself more efficient. President Bush's demand for "measurable results" is but the latest in a series of attempts by administrations to instill accountability.*

For example, following World War II, the Hoover Commission was established to reorganize and downsize the government's departments and agencies. The Commission recommended that program budgets should be "performance" oriented. That is, they should focus on a program's function or activity and the accomplishment of its purpose, not just the use of inputs. Despite its promise and some successes, most program activities were never adequately linked with their costs.

The next attempt to reign in Government inefficiency was President Johnson's "Planning, Programming, and Budgeting System," which was based on a system the Department of Defense had used since 1961 to evaluate and decide among alternative methods of accomplishing military missions. Johnson hailed this initiative as a way to control Federal programs and budgets, rather than "having them control us."

Johnson's system was formally discontinued in 1971. It failed in part owing to the government's increased use of grants, which made it difficult to obtain information on program performance. More important, it did not solve a key problem inherent in virtually all government programs: how can one allocate resources "efficiently" when the people who allocate them are politicians and political appointees and they have competing political priorities?

In 1970, President Nixon proposed his own accountability program. He adopted "Management by Objectives," a popular management technique used in the private sector at the time. The idea was to centralize goal-setting decisions while allowing managers leeway to choose how best to achieve the goals. Nixon proclaimed: "By abandoning programs that have failed, we do not close our eyes to problems that exist; we shift resources to more productive uses." This initiative, like its predecessors, failed to produce much in the way of results. Most agencies could not or would not define their objectives in measurable terms.

While campaigning for the presidency, Jimmy Carter characterized the Federal budget as "inefficient, chaotic, and virtually uncontrollable by either the President or Congress." He then promised to balance the budget within his first term and to reform the Federal budgeting system by introducing yet another initiative, "Zero-Based Budgeting." This approach called for all expenditure proposals to compete for funding on an equal basis—starting from "zero," as opposed to an accepted "base" of past spending. This, too, was a bust; most agencies requested funding based on past levels, the process reportedly increased the existing paperwork burden by 229 percent, and few budgetary actions were based on it.

President Reagan took a different path. Reagan created the "Private Sector Survey on Cost Control," better known as the Grace Commission, to "work like tireless bloodhounds to root out government inefficiency and waste of tax dollars." Unlike previous attempts at reform, in which public officials tried to adopt private management techniques, the Grace Commission was composed of corporate executives. Ultimately they made 2,478 specific recommendations designed to save taxpayers billions, all supposedly without eliminating essential services.

The most startling revelations in the Commission's report received a great deal of publicity, such as the finding that the

* For a full discussion of past Federal initiatives and the evolution of the concept and techniques of performance budgeting, see the Government Accounting Office report, "Performance Budgeting: Past Initiatives Offer Insights for GRPA Implementation," (GAO/AIMD-97-46) available at www.gao.gov.

government was providing free towing services to yacht owners and paying $511 for 60-cent light bulbs. Most of the report's suggestions, however, went largely unreported and were not acted on. The Grace Commission did have one lasting effect. After it disbanded, its chairman, Peter Grace, founded a private watchdog group, Citizens Against Government Waste, to carry on the mission of eliminating waste, mismanagement, and inefficiency in the Federal government. (See below.)

Entrenched bureaucrats and other special interests viewed the Grace Commission report and other earlier efforts that focused on reducing waste, fraud, and abuse as antagonistic. Critics said this hindered reform. To contend with this problem, the Clinton Administration appointed Vice President Al Gore to head the "National Performance Review." This effort at "reinventing government" started with the premise that government can be made to work, and Gore actively sought the views of bureaucrats about how to fix things. He proposed that eliminating "red tape" would lead to results. For example, instead going through a burdensome requisition process to buy screws, why not simply send someone with a credit card to the neighborhood hardware store where they cost just a few cents? Unfortunately, few asked what would prevent the employee from stopping along the way to make personal purchases.

How Do You Measure "Successful Government"?

President Bush's initiative to hold government accountable has already produced some successes. For example, this year the Office of Management and Budget for the first time in its history requested bids to print the annual Federal budget (a set of phone-book size documents), rather than follow the traditional practice of automatically turning the work over to the Government Printing Office (GPO). Several bids came in, and although the GPO was eventually chosen from among them, the printing cost was 23 percent less than the previous year, and the lowest in 20 years.

Despite this example and a few others, the Administration is likely to face great difficulty in holding agencies accountable. Their performance is tied to goals that, for many programs, are unattainable or defined in terms that are too broad or, in a few cases, just plain ridiculous.

For example, as Ben Powell wrote in "A 'Poor' Accounting of the Poor" (*Economic Education Bulletin*, July 2000) noncash benefits are not figured in when the government calculates poverty rates. This means that no matter how much government housing, food stamps, or Medicaid benefits are provided to the poor, not a single one of them will be lifted out of poverty as the government measures it. Thus, the "war on poverty" is defined in such a way that it will never be won! Of course the poverty thresholds could be adjusted to reflect government support, but then the programs would be in jeopardy of effective spending cuts.

Another baffler is the Minority Business Development Agency, created by executive order in 1969. This agency's stated purpose is "to support minority business enterprise." However, the first of its three goals is to "develop an entrepreneurially-innovative market-focused economy." Not only is this an absurdly broad goal, but if the agency was serious about achieving it, it should immediately close its doors. It won't. Rather, it will simply choose another (unattainable) goal.

This agency, with a program funding level of $29 million, is small potatoes. How about a larger program, such as direct crop payments, that is budgeted at $5.2 billion? According to its review: "the purpose of the program is clear.... Direct payments are designed as part of a safety-net for farmers, however they are going to about 41 percent of all farmers, 85 percent of which have annual sales of at least $50,000.... Outside sources have reviewed the program and determined that it has provided support in maintaining farm income but has not been effective in reducing the need for additional government subsidies." No surprise here: Safety-nets encourage farm businesses to depend on government support payments. So, is

Over a Barrel

In 1789, the First Congress of the United States convened in Washington and debated whether to build a lighthouse on Cape Henry near the entrance to Chesapeake Bay. That lighthouse was not only the first Federal building authorized by the U.S. Government, it was also the beginning of "pork barrel" spending.

American word scholar William Safire traces the origin of the term "pork barrel" back to the pre-Civil War practice of slave owners distributing salt pork to their slaves from huge barrels. The analogy to government-patronage projects was first made in 1919 when, according to Safire, a journalist wrote that "Oftentimes, the eagerness of the slaves would result in a rush upon the pork barrel, in which each would strive to grab as much as possible for himself. Members of Congress, in their rush to get their local appropriation items, behaved so much like Negro slaves rushing to the pork barrel."

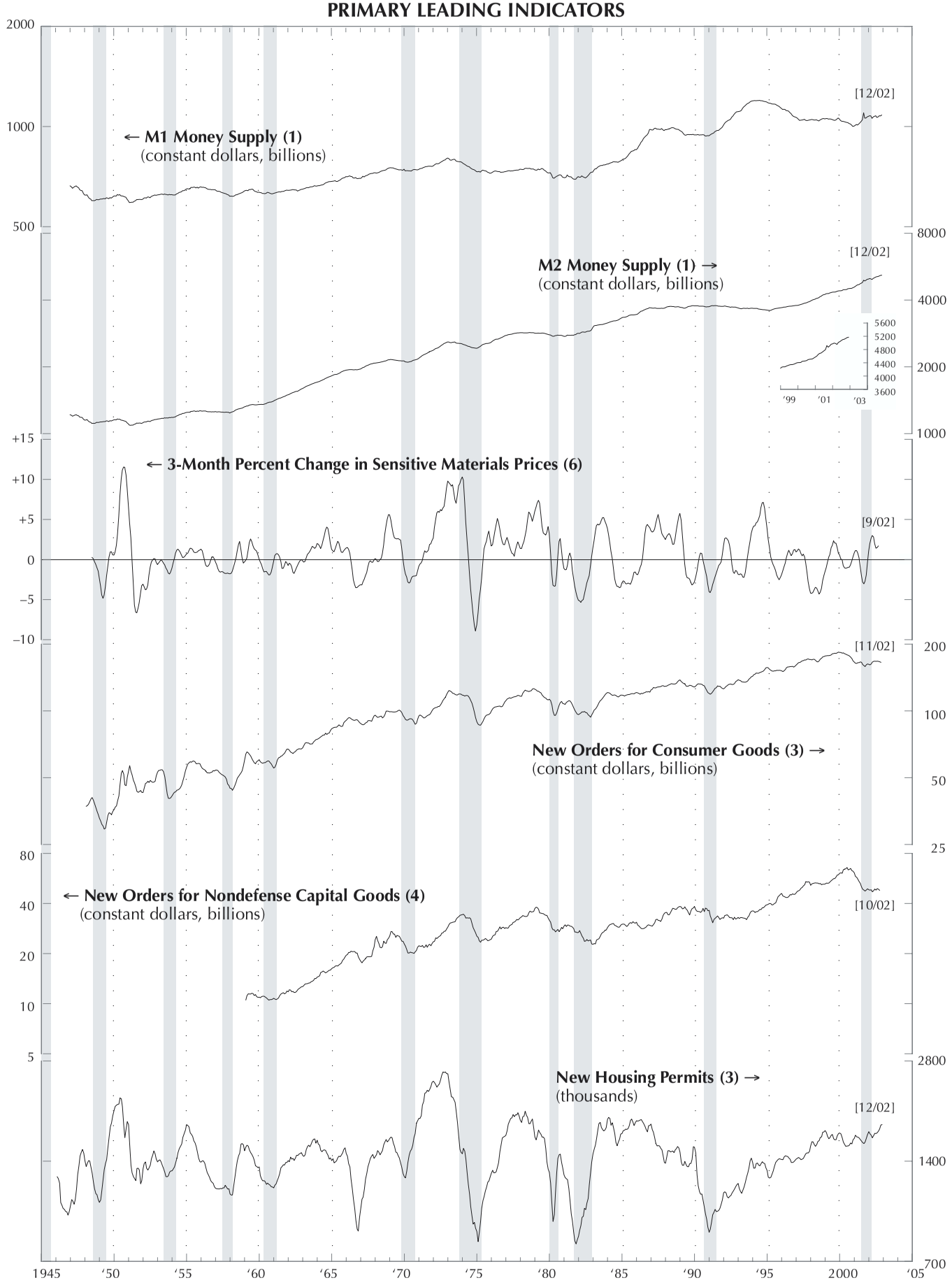
Each year the Citizens Against Government Waste, a nonpartisan organization whose roots can be traced back to President Reagan's Grace Commission, publishes a booklet that lists the most blatant examples of pork-barrel projects and their sponsors. All the items in the *Congressional Pig Book Summary* meet at least one of seven criteria:

- Requested by only one chamber of Congress;
- Not specifically authorized;
- Not competitively awarded;
- Not requested by the President;
- Greatly exceeds the President's budget request or the previous year's funding;
- Not the subject of Congressional hearings; or
- Serves only a local or special interest.

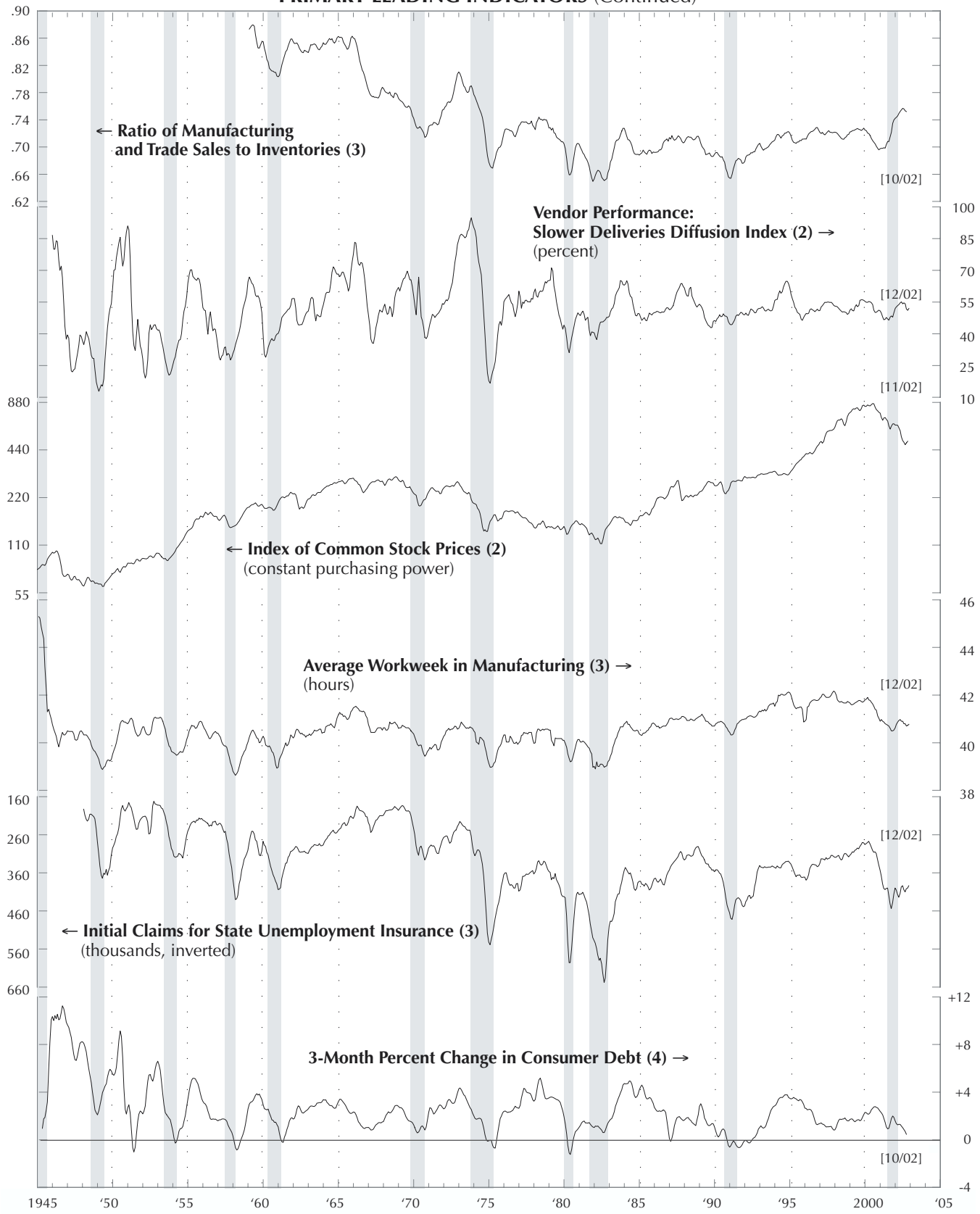
According to Citizens Against Government Waste, Congress included 8,341 pork projects costing $20.1 billion in the 13 appropriations bills in 2002. It has appropriated a total of $140 billion in pork-barrel spending since 1991. (For examples of how the money was spent, see www.cagw.org.)

No matter how wasteful it is, there is virtually no chance that pork spending will be substantially cut, let alone eliminated. The cost per household of these programs is small because the few million dollars or so that each program costs is spread across nearly 105 million households. The prospective gains to taxpayers from killing such programs are trivial, while the prospective losses to the narrow constituency that benefits from them are much larger. This gives the beneficiaries a much stronger incentive to lobby against spending cuts.

PRIMARY LEADING INDICATORS

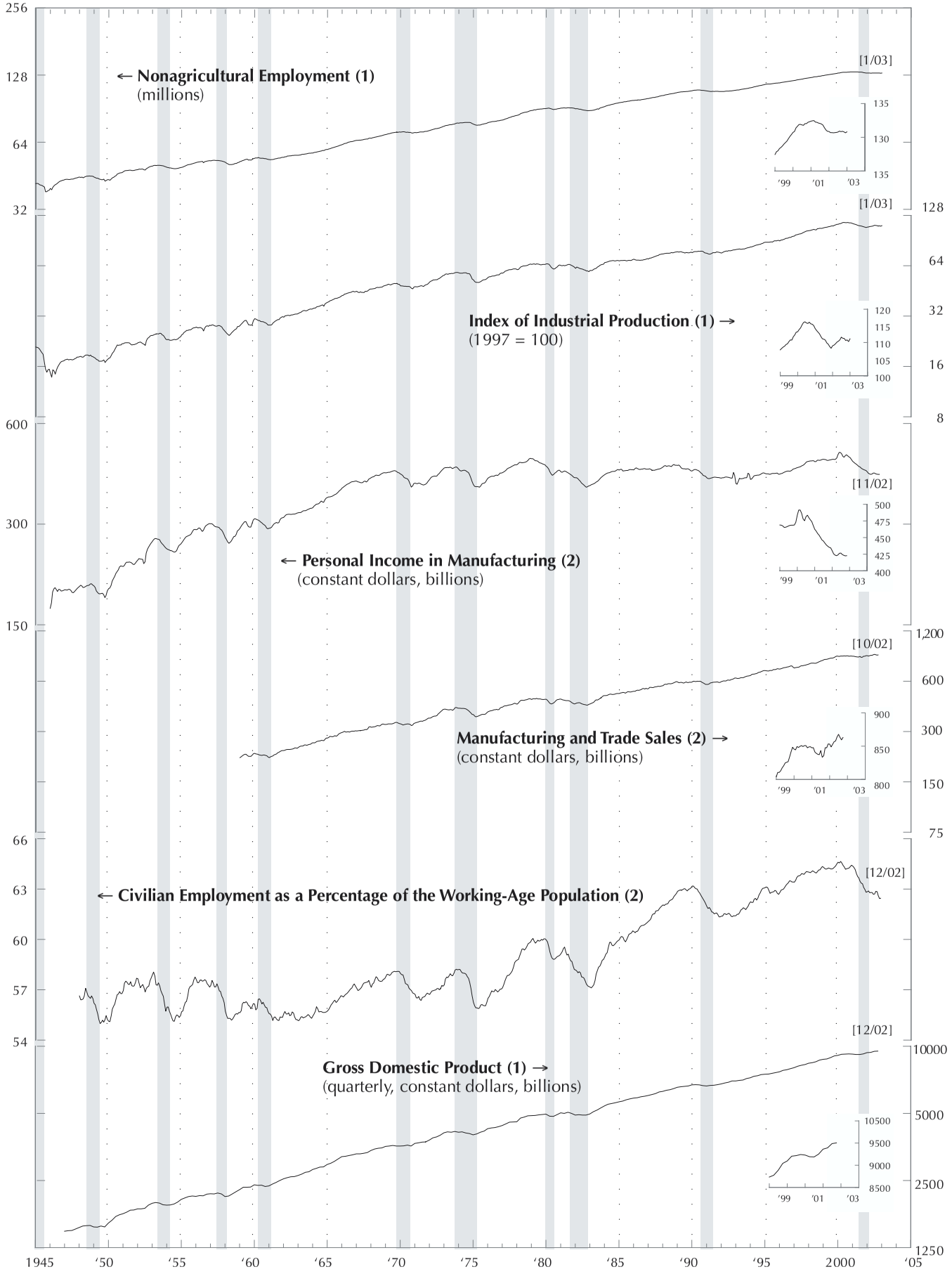


PRIMARY LEADING INDICATORS (Continued)

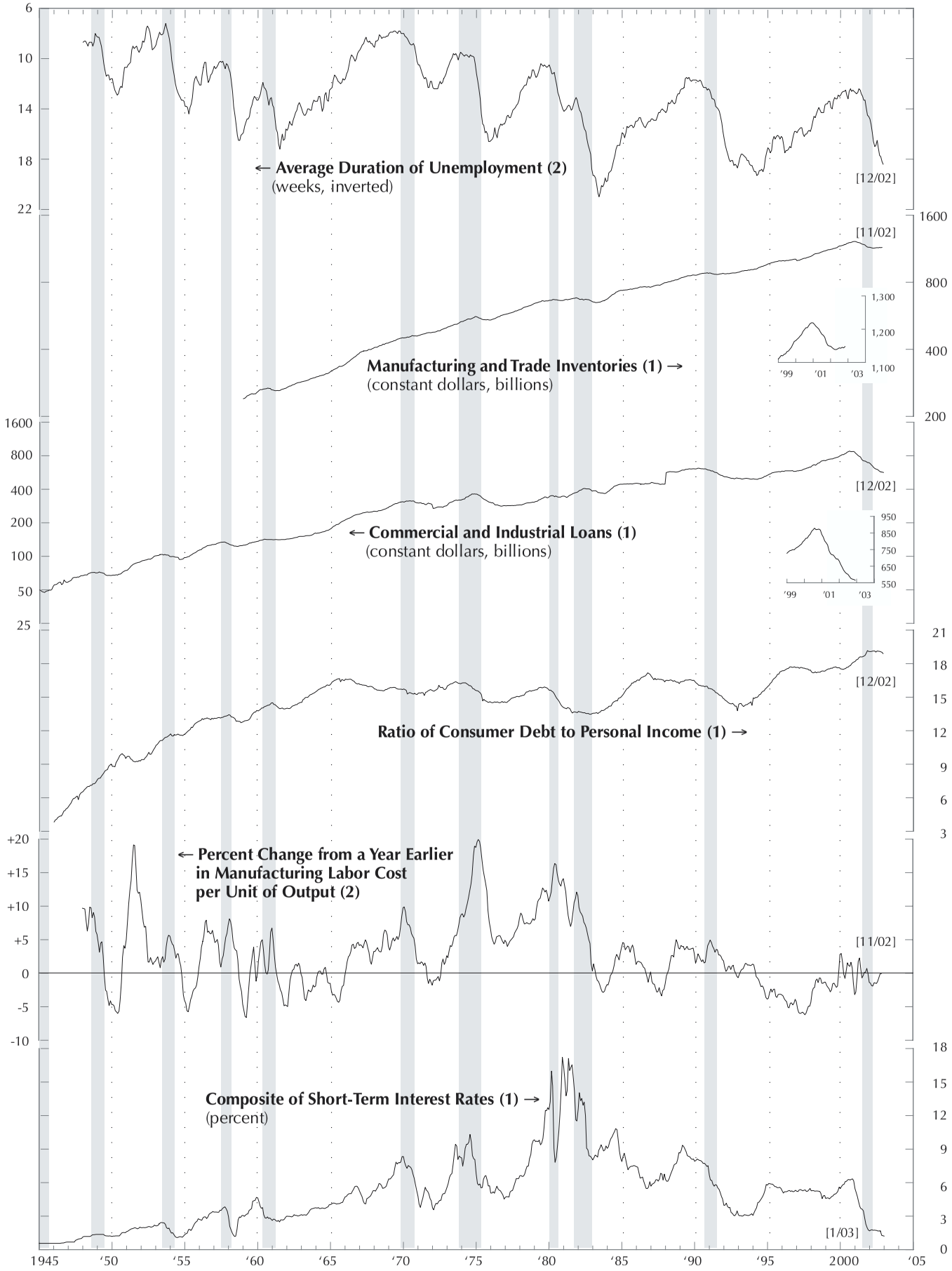


Notes: 1) Shaded areas indicate recessions as dated by the National Bureau of Economic Research. 2) The number in parentheses next to the name of a series is an estimate of the minimum number of months over which cyclical movements of a series are greater than irregular fluctuations. That number is the span of each series' moving average, or MCD (months for cyclical dominance), used to smooth out irregular fluctuations. The data plotted in the charts are those MCDs and not the base data. The number in brackets is the latest month for which the moving average is plotted. 3) The insets in selected charts show recent trends more clearly. These insets have arithmetic scales, even when the main chart is plotted on a ratio scale.

PRIMARY ROUGHLY COINCIDENT INDICATORS



PRIMARY LAGGING INDICATORS



the program a success, or not?

Genuine Accountability

Limited space does not permit us to analyze every program, but similar results could be expected if we did. As Thomas Sowell has observed:

> Bureaucracies are, by definition, controlled by administrative or political decision, not by incentives and constraints communicated through market price fluctuations. While an ordinary business enterprise is constrained to keep its costs of production below the value of the output to the consumer—and has incentive to keep it as far below as possible—such incentives are not merely absent in a bureaucracy but are replaced by other incentives and constraints in the opposite direction.

President Bush's initiative to reduce waste and promote greater efficiency in government is likely to be most successful with regard to programs engaged in activities that closely resemble those of private industry, such as the printing of the government's budget. But in many cases, achieving private-sector-style efficiency will be impossible. At bottom, businesses must serve customers or cease to function. In contrast, there are few unambiguous measures of how well government agencies are functioning—and none as clear and effective as a bottom line.

It is obvious that the lack of accountability in many government programs is a product of the policies upon which they are based. Thus, reviewing only "how government should work, not what it should do," will produce marginal benefits, at best. Genuine accountability requires asking whether a Federal role is necessary in the first place. ❑

BUSINESS-CYCLE CONDITIONS

The leading indicators suggest the economy will continue to expand. However, many of the leaders and coinciders are far from robust, and if they were to weaken in the next few months the business outlook could worsen quickly.

Among our 12 primary leading indicators, the latest data show that both *M1 money supply* and *M2 money supply* increased in December. (M1, M2 and other dollar-denominated series are reported in constant dollars to adjust for price inflation.) Ignoring last month's downward revision, M1 has been improving since August 2002. The latest increase warranted upgrading the series' cyclical status from probably expanding to clearly expanding. M2, a broader measure of circulating purchasing media, continued its well-established upward trend—hitting yet another new high.

The employment situation improved slightly. The 3-month moving average for *initial claims for state unemployment insurance* decreased to 394,000 per week in December, the lowest rate since March 2001. The series, plotted on an inverted basis for analysis, is now appraised as clearly expanding. Both the number of unemployed persons and the unemployment rate remained modest, at 8.3 million and 5.7 percent, respectively.

The base data for *new orders for consumer goods* decreased 0.7 percent, rendering the series cyclically indeterminate. *New orders for nondefense capital goods* remains cyclically indeterminate as well, despite its base data increasing by 2.6 percent. As can be seen in the accompanying historical charts, the former series improved modestly between October 2001 and June 2002 before leveling off. In contrast, business spending never bounced back—orders for nondefense capital goods remain near a cyclical trough.

New housing permits reached another new high in January, despite the series' base data falling 5.6 percent to a seasonally adjusted annual rate of 1,781,000. The National Association of Home Builders' housing market index, a measure of builder sentiment about sales and buyer traffic, fell two points in February to 62 points. An index reading above 50 indicates that more builders view sales conditions as good than as poor. Although optimism and permits fell, housing starts rose to their highest monthly level since mid-1986.

The *ratio of manufacturing and trade sales to inventories* remains appraised as probably expanding following an increase in its base data for November and an upward revision in October's data. The sales-to-inventories ratio has weakened somewhat after reaching its latest peak in July 2002. Contraction in this series is an indication that manufacturing inventories are building up faster than sales, which could lead to cutbacks in production and further losses in manufacturing employment. Employment in the sector decreased another 16,000 in January, following December's loss of 80,000 jobs. Those production workers with jobs put in fewer hours during January. The *average workweek in manufacturing* decreased from 40.9 to 40.8 hours per week. The status of this series is indeterminate.

Although the base data for the *3-month percent change in sensitive materials prices* increased for the fourth consecutive month, the series' six-month moving average does not exhibit a discernable cyclical trend. Similarly, the January base data for *vendor performance*, the percentage of purchasing managers reporting slower deliveries from their suppliers, improved, rising to 52.6 percent. Its moving average increased as well, but not by enough to warrant upgrading. Both series remain cyclically indeterminate.

The base data for the 3-month *change in consumer debt* decreased in December to -0.04, confirming the series' well-established downtrend. Although the base data are below zero in absolute terms (meaning consumers are paying down debt), what matters for this analysis is what is happening to the *change* in consumer debt—i.e., whether the rate at which they are paying down debt is increasing or decreasing. The Federal Reserve reported that credit-card debt outstanding fell $8.4 billion in December (seasonally adjusted), the largest monthly decline in dollar terms since the data were first collected in 1968, but not the largest percentage decline. Regardless, it is unusual for revolving debt to contract, let alone by a substantial amount.

No new data were available for the *index of 500 common stock prices*. According to its latest appraisal, the series has a well-established downtrend.

With this month's changes, 71 percent (five out of seven) of the leading indicators with apparent cyclical trends are expanding, down four percentage points from last month when 75 percent (six out of eight) were expanding. An index reading above 50 suggests that expansion is more likely than contraction over the next several months. However, because the calculation of this index ignores those indicators with no identifiable trend, the favorable outlook suggested by the index deserves scrutiny. If one or more of the five indeterminate series were to develop a downward trend in the next month or two, the index could drop quickly.

AIER's cyclical score—a purely mathematical assessment of the leading indicators—is useful because it takes into account all 12 leaders regardless of their cyclical status. Over the past few months, the cyclical score, currently at 72, has been rising steadily despite modest weakening in the percent of leaders expanding. This is because, in order to reduce the inci-

dence of "false signals" of recession, the cyclical score provides for a heavier weighting of increases in a series' data than of decreases. Thus, the cyclical score is less volatile than the percent of leaders expanding.

Among the six primary roughly coincident indicators, *Gross Domestic Product* increased at an annual rate of 0.7 percent in the fourth quarter of 2002. The lower GDP growth was attributable to a slowdown in household spending and downturns in inventories and exports. Government spending and residential investment accelerated during the quarter. The series remains appraised as clearly expanding.

Following an upward revision to the October data, *manufacturing and trade sales* increased 0.8 percent in November. The series' 2-month moving average strengthened slightly but not enough to warrant upgrading the series' status from probably expanding.

The *civilian employment to population ratio* base data for January increased to 62.5 percent following three months of decline. The moving average also increased slightly, barely discernable on its 33-month decline. The series remains appraised as contracting. *Personal income in manufacturing* also has a clearly-established downtrend, despite the 0.4 percent increase in its base data in December. Production workers, on average, earned $14.98 per hour and $512.32 per week.

Nonagricultural employment, after falling in November and December, increased by 143,000 in January. Despite the improvement, the series remains indeterminate. Most of the new jobs originated in the service-producing sector, especially in retail sales. However, due to the way the labor data are seasonally reported, the employment numbers may not be as strong as officially reported. Ignoring seasonal adjustment, the retail sector *shed* 973,000 jobs. But since this number was fewer than usual after the holiday season, employment increased in the sector measured on a seasonal basis.

Industrial production increased 0.7 percent in January, reversing December's 0.4 percent decline. Most of the gain was attributable to an increase in the production of motor vehicles and parts. An unfavorable development is that the percent of industries that are expanding their output (over six-month spans) has steadily decreased since June 2002, falling from 66.3 percent to 46.8 percent.

Overall, 50 percent (two out of four) of the primary roughly coincident indicators with apparent cyclical trends are expanding, the same as last month. The cyclical score for our coinciders, which is similar to that calculated for the leaders above, remains above 50 at 65. Taken together, these indexes suggest that the economy is expanding.

There was some strengthening among our six primary lagging indicators. *Manufacturing and trade inventories* increased 0.3 percent in November, bolstering the series' clearly established upward trend. Continued increases since August in the *percent change from a year earlier in labor cost per unit of manufacturers' output* warranted upgrading the series to probably expanding. Unit labor costs for producing durable goods rose a modest 2.7 percent in the fourth quarter of 2002, compared with 7.0 percent increase in nondurable goods manufacturing.

Although the base data for the *average duration of unemployment* (inverted) were unchanged in January, its moving average decreased to a new low and is clearly contracting. While the average unemployment period is currently 18.4 weeks, half of all unemployed persons have been jobless for 9.8 weeks or less.

Commercial and industrial loans decreased, as did the *composite of short-term interest rates*. Both series are clearly contracting. C&I loans continues its 28-month contraction from its peak of $879.2 billion in August 2000 to a new low of $565.2 billion last December. Short-term rates, at 1.22 percent, also reached a new low.

The *ratio of consumer debt to personal income* decreased to 18.9 percent. Given that it remains near the cyclical peak it reached 13 months ago, the series is indeterminate. With the upgrade in unit labor costs, 40 percent (two out of five) of the laggers for which a trend is evident are expanding, up from 25 percent (one out of four) last month. ❑

Statistical Indicators of Business-Cycle Changes

Change in Base Data					Cyclical Status		
Oct.	*Nov.*	*Dec.*	*Jan.*	***Primary Leading Indicators***	*Dec.*	*Jan.*	*Feb.*
+	-[r]	+		M1 money supply	+?	+?	+
+	+	+		M2 money supply	+	+	+
+	+	+		Change in sensitive materials prices	?	?	?
+	-	-		New orders for consumer goods	+?	+?	?
+	-	+		New orders for nondefense capital goods	?	?	?
+	-	+	-	New housing permits	+	+	+
+[r]	+			Ratio of manufacturing and trade sales to inventories	+	+?	+?
-	-	+	+	Vendor performance	?	?	?
-	+	-		Index of common stock prices (constant purchasing power)	-	-	-
-	-	+	+	Average workweek in manufacturing	?	?	?
+	+	-	+	Initial claims for unemployment insurance (inverted)	+?	+?	+
-	-	-		Change in consumer debt	-?	-	-
				Percentage expanding cyclically	*75*	*75*	*71*
				Primary Roughly Coincident Indicators			
+	-	-	+	Nonagricultural employment	?	?	?
-	+	-	+	Index of industrial production	?	?	?
-	-	+		Personal income in manufacturing	-	-	-
+[r]	+			Manufacturing and trade sales	+	+?	+?
-	-	-	+	Civilian employment to population ratio	?	-	-
+	+	+		Gross domestic product (quarterly)	+	+	+
				Percentage expanding cyclically	*67*	*50*	*50*
				Primary Lagging Indicators			
+	-	-	nc	Average duration of unemployment (inverted)	-	-	-
-[r]	+			Manufacturing and trade inventories	+?	+	+
-	-	-		Commercial and industrial loans	-	-	-
-	-	-		Ratio of consumer debt to personal income	+?	?	?
+	nc[r]	+		Change in labor cost per unit of output, manufacturing	-?	?	+?
-	-	-	-	Composite of short-term interest rates	-	-	-
nc No change.	[r] Revised.			*Percentage expanding cyclically*	*33*	*25*	*40*

Under "Change in Base Data," plus and minus signs indicate increases and decreases from the previous month or quarter and blank spaces indicate data not yet available. Under "Cyclical Status," plus and minus signs indicate expansions or contractions of each series as currently appraised; question marks indicate doubtful status when shown with another sign and indeterminate status when standing alone.

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