DR. LAWRENCE: Thank you very much. It's a real pleasure to be here today. I think your Commission has a very important task and I think in particular, not only in providing policy advice, but in educating the public.

The central message that I would like to underscore is that not all current accounts are created equal. Basically, we have to understand the drivers that lie behind a current account. You know, we talk in our language, the language we use, whenever a current account moves more towards deficit, we call it a deterioration; and whenever it moves towards surplus, we call it an improvement. What I would suggest and what I do in my testimony is to argue that, in fact, some deficits may be good and other deficits may not be good. What really matters are the other associated features of what's inducing those particular deficits and we cannot naively assume, simply because we have a deficit, automatically that there will be certain consequences. In particular, it is crucial to distinguish deficits which actually reflect a “bust” in savings, a reduction in national savings, from those which reflect a rise in national investment.

Likewise, some deficits could be associated with falling employment, others with rising employment and clearly that's an important distinction.

In my comments, I would like briefly to make six observations about this deficit; three about its causes and three about its consequences.

Firstly, the recent increases in deficit are clearly associated with a strong U.S. economy and with weakness abroad. If you look at the chart in my written testimony, you can see vividly, as Mr. Barbera indicated, that for a period of time we had a deficit of modest proportions, about 1 percent of GNP. Basically, in 1997 as the foreign economic growth collapsed, we saw the large emergence of our deficit. And so what we can see then is that the United States has become a more attractive location for investment, leading the dollar to appreciate; and secondly, foreign economic growth has slumped. And so in a sense, the proximate cause of this deficit is the relative strength of the U.S. economy.

Secondly, this deficit reflects stronger national investment rather than weaker national saving and in the table in my written statement, I outline the way in which this deficit is a striking contrast to the deficit of the 1980s. In the 1980s what we saw was net investment actually declining as a share of net national income so that the decline in savings was associated with an investment bust. By contrast, what we have seen in the 1990s is an investment led-recovery. It needs to be recognized that we're better off having that investment than we would be without it. Indeed, that investment has been one key element in the recovery of productivity growth and so we need to understand that it is an important driver of this expansion.

And thirdly, obviously, the deficit, in part, does reflect a stronger dollar, but again there's an important distinction here when we look where the money is going. In the 1980s, we can understand that those higher real interest rates, which attracted capital and caused the dollar to appreciate, were essentially coming to finance more consumption. What we find in this case from a national standpoint is that we're funding more investment. Those are critical differences.

Let me also make three observations about associations and consequences of the deficit. The first is clearly we've had an astoundingly strong U.S. economy, very strong gains in job creation. We just issued a report recording the passage of 21 million additional jobs since January 1993 and this simply exposes the folly of those who say that you can automatically go from the existence of a deficit of a certain dollar value to a certain number of consequences for employment.

Second, this deficit has also been associated with an economy that is creating good jobs. Recent analysis by the Council of Economic Advisers and the Department of Labor has found that 81 percent of the new jobs are located in industry and occupation categories that are paying above median wages. We excluded professional occupations from our sample and we still found that 71 percent of the new jobs are in categories paying above median wages. And we've also excluded those with college degrees, and if we look at only those with high school degrees, we again find a disproportionate numbers in those categories which pay the highest wages.

In addition, what's striking about this recovery is that we have seen that real wage growth has not been confined simply to the high-wage workers, but we've seen gains across the board. The remarkable feature of our economy is that while we have never been more open, never been subject to more technological change, we have also seen that it is possible to grow in a high pressure economy without any deterioration in equality.

When you look at the measures for poverty, the measures for income distribution, and the measures for wage growth, you see this is recovery which has been broadly shared across workers in the economy.

However, my sixth point is that, particularly since the Asian crisis, we have seen that the deficit has been associated with considerable dislocation in the manufacturing sector. Again, you can see the chart in my written testimony which outlines the fact that, for the initial years of the recovery through 1997, we had robust employment growth in manufacturing. But what we've seen more recently is declines in manufacturing and these are spelled out in greater detail in the testimony.

When it comes to policy, I would like to put forward four principles very briefly. It's hard to be precise about the desirable level of the current account and again, my message would be what really matters is what brings about a change in the current account and there are four principles.

Firstly, it's better to reduce the current account through faster growth abroad than through slower growth at home. The wrong way to reduce it is through a recession in the United States.

Secondly, it's better to reduce the deficit through increased domestic saving than through reduced domestic investment. Again, the role of the budget surplus is very important.

Thirdly, given the requisite changes in savings and investment behavior, it's better to complement the adjustment through opening markets abroad than through closing them in the United States. Protectionism at home should play no part in our responses to the current account deficit. By contrast, when we open large foreign markets, we can stimulate our exports and improve the terms at which we trade.

And finally, as Secretary Summers has emphasized, we do have an interest in a strong dollar. It's better to accomplish current account adjustment through faster foreign growth and opening foreign markets than it is through a decline in a value of the currency.

Thank you.

VICE CHAIRMAN PAPADIMITRIOU: Thank you very much. Dr. Stern?