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FUTURE DIRECTIONS OF STATE ECONOMIC GROWTH

by Governor Pierre S. du Pont

While the nation has successively debated the economic policies of Presidents Ford, Carter, and now Reagan, a quiet yet dramatic change has taken place in the nation's economy. The past failings of federal economic policies has brought about a fundamental change in the nature of American federalism as the states and local governments have grown more assertive in protecting their own economic welfare. Because of the dismal performance of past economic policies, the states have stepped forward to become their own economic planners, stimulators and innovators.

Since the depression of the 1930's, and perhaps longer, the economic policy making of the nation has generally been left to the federal government. As those federal policies have failed us, the states have grown more aggressive in improving their own governmental finances and in seeking new business opportunities. The result is that the states are now eyeball deep in economic policy-making. I believe we are now making a positive and essential contribution towards improving the economic health and well- being of our nation and citizens.

President Reagan, who has embarked upon a bold and workable economic program and one which I believe will substantially improve the fortunes of our economy, clearly recognizes the trend of state involvement in economic policy making. At the White House this Spring, as he met with me and seven other governors, he correctly understood the need to reduce federal control over state programs. He told me that a significant feature of his program would be to combine federal grants so that the states would have more flexibility over the spending of those dollars and so that we can more accurately target those funds to the areas which need them most.

The states, the President says, are often more efficient and responsive. By funding through block grants, the States can gain added flexibility that can result in real savings. As we have seen with the deregulation of airlines and oil, by unshackling

business and government from over-regulation we can allow the genius of our economic system to work.

President Reagan's economic program is a welcome and vital change in federal policy. The road to an effective national economic policy is long and arduous, and while we in state government are supportive and aggressive participants in the national effort to improve our economic fortunes, we cannot afford to stand and wait. We must take what actions we can to protect and further our own economic interests.

The states, suffering as they have from years of befuddled federal policies, are beginning to assert themselves to protect their economic equilibrium. Our reasons are manyfold, partly the result of a desire for self-preservation for after all, the states are on the front lines of taxpayer dissatisfaction with national economic failures. Also, the failure of national economic stabilization policies and the resultant boom-bust cycles have played havoc with state revenues and consequently with our ability to provide the level of services demanded by our constituents as a result of these same policies.

There are other reasons as well. The states and their leaders, many of them former Congressmen like myself, have resolved not to repeat the errors of the past. Instead we have looked within our own state borders for economic stability and innovation rather than depending upon the federal government. Because many of those federal programs designed to help local problems have had the opposite effect, the federal government actually destabilized local economies and subverted local initiatives in many cases.

Look at what New York City Mayor Ed Koch, who was once one of the Congress' foremost liberals, had to say recently:
"There is no question that there is a decided difference in what I did as a Congressman and what I am doing as mayor when it comes to spending money. It isn't a difference in philosophy, it is that I didn't understand what I was doing when I was in Congress, because you spend other people's money. In Congress you are not aware of the cost of the programs because either the federal government is spending it and they print the dollars or, worse, you impose the cost on the cities. You just tell them what to do but you don't give them the money to do it.

"So now I am an executive. I look at what has to be done and I say to myself how could I have voted for those dumb programs?"

Finally, there is widespread agreement that this nation has become too diverse and the population centers have become so spread out that a highly centralized government no longer responds effectively to local needs. The states, acting singly or in concert can achieve many of the social and economic goals sought by Washington, in many instances more quickly and less expensively.

For example, in Delaware we are providing our young people with the opportunity to secure a job immediately upon graduation from high school. We've started a program -- with private, state and federal dollars -- to help place those high school seniors who would not ordinarily enter post secondary education programs to find a job in the private sector. Called Jobs for Delaware Graduates, it has proven to be enormously successful, placing some 77% of the students enrolled in the program in meaningful private sector jobs, with the support of Delaware's business, labor, community, government and education leaders. The cost per placement is 37% of the cost of similar job placement in the federally financed CETA program. Consequently, the states' in recent years have become more aggressive and sophisticated in shaping their own economic destinies. Dozens of states, including Delaware, have straightened out their finances and enacted spending and taxing limitations in an attempt to hold down the cost of government. We realized long ago that unbalanced budgets make poor economics as well as poor politics. We have sought a loosening of the strings on federal grants so we can spend the monies more efficiently. We are using our taxing authority less, to encourage more economic growth. We, as individual states, are initiating job training programs in the private sector to lessen the load on the taxpayers. And we have become more aggressive in the area of international trade. Half of the states now have one or more foreign offices boosting international trade.

But in our effort to accelerate economic growth and improve our own opportunities, we have often run afoul of federal policies. Some matters, such as education, corrections, and law enforcement are clearly of local concern, and should be handled at the local level. In many cases the federal government has sought to set guidelines or protect against injustice. But federal involvement has

gone far beyond such worthy objectives. For example, there are over 500 specific categorical grants provided by the federal government for particular purposes. These grants often by-pass the plans and policies of the states; they force the states to commit resources to areas of lesser concern and thus narrow the state's prerogative to implement effective local programs.

For example, in my home state, we sought to rebuild a bridge at a cost of $7 million. The federal government would provide us with the bulk of the funds, but only if the bridge cost $10 million or more. Other highway funds available to Delaware were restricted and could not be used. Seemingly the only way to obtain funding was to promise to pave the bridge in gold. Ultimately, a change in federal law was enacted by the Congress so we could rebuild this vital bridge. This example symbolizes the frustration felt by governors, mayors, and townspeople in dealing with the maze of government regulations and mandated expenditures of federal funds. A better solution -- and one being proposed by the Reagan Administration -- is to combine those 500 categorical grants into block grants to allow local autonomy in deciding when and where to commit resources.

On the other hand, increased federal assistance is appropriate in some areas, especially if the problems are the end result of federal policies. If education, corrections, and law enforcement are of local concern, then welfare, unemployment, and income support programs are clearly of federal concern, because the problems they address are problems largely caused by national economic policies.

For example, federally-mandated programs such as unemployment compensation should receive substantial federal support in those regions where there is a disproportionate level of unemployment. The major cause of the high level of U.S. unemployment (7.3 percent -- February) is the lack of real growth in the productive sector of the economy. The federal government's destabilization policies -- erratic money supply shifts, ballooning federal deficits, and regulations and restrictions on the actions of the private sector, have successfully prevented a national business climate which would be conducive to steady real growth and greater employment.

Seventeen states, including Delaware, have had to borrow heavily from the federal government to cover unemployment compensation payments. For example, every

time an automobile assembly plant lays off a worker for 2 1/2 weeks in Delaware, that worker exhausts the total pay-in by his company to cover the benefits to which he's entitled. Benefits for the remaining 23 1/2 weeks of unemployment benefits are paid for by drawing down upon the payments made by other employers and borrowing from the federal government. This imposes heavy costs on the firms within the states which maintain consistently high employment levels, and on all firms in the long run as the federal government imposes penalty taxes on states with extended deficits. States with relatively high levels of unemployment will face increasingly heavy business tax burdens, which will further discourage employment opportunities within those states. Certainly this is an area where increased federal responsibility is appropriate and necessary, and can give a real boost to economic development efforts within states and regions.

But state and local governments cannot sit back and await the conclusions of a national debate about federalism. While we are participating in that debate, aggressively and with some passion, the Governors are simultaneously moving rapidly on many other fronts to increase economic opportunities in our states.

The states are becoming much more effective than the federal government in removing deterrents to development. By improving state finances, balancing budgets and cutting taxes, states have not only cut the growth of government, but the burden as well. This helps local economies to flourish.

In Delaware, we responded in 1977 and 1978 when my administration took office. The first thing we did was reduce expenditures so that, for four years in a row now, the growth in total expenditures of state government in Delaware have fallen significantly short of the growth rate of inflation. In Delaware, inflation-adjusted spending is declining. In addition, we restored some sanity to our borrowings and undertook a capital expenditure control program to reduce debt service from over 15% of budget to the 11.6% it garners in 1981. Our goal is to drive debt service to 10% by 1984, a target we are going to exceed easily. Delaware has, in addition, eliminated all short-term borrowing to meet payroll and borrows long-term only to match the life of capital projects. In addition, we passed a constitutional amendment to limit spending to 98% of anticipated revenues and to require three-fifths vote to raise taxes. On top of all of this, we enacted a 9% cut in personal income taxes following a reduction in capital gains taxes in 1976. We have done

this on a bipartisan basis and involving both the public sectors and the private sectors.

And what was the result? It has been dramatic already. We are beginning to see the full impact of the spending reductions, the income tax reductions, and the financial stability mechanisms. Even after only very short lags, the results are encouraging. For the first time in over seven years, 1980 saw Delaware's unemployment rate fall below the national average. In fact, Delaware was the only state in the union whose unemployment average fell during 1980 while the national average was rising. In addition, growth of per capita personal income has turned around. Although year-end 1980 figures are not yet available, the October 1980 figures from the Department of Commerce place Delaware near the top with growth rates approaching those of Oklahoma, Texas, New Mexico, and Alaska (a growth rate at 12.4% significantly above the 11.3% national average). For the month of October, Delaware's growth rate in personal income was nearly the highest in the country. Similar indicators for property values, housing starts, and total employment are showing dramatic turn-around as well.

In short, we in Delaware are seeing very directly the benefits of financial stability and tax reductions. While the full impact of these policies we do not believe has yet been filled, we are sufficiently encouraged and heartened to maintain the course and to even improve upon it if we can.

We are also developing the economic tools necessary for economic growth. We are enacting tax incentive laws to encourage medium sized companies to grow and expand. With eight out of every ten new jobs created as the result of local business expansion, local incentives are essential if we are to increase the number of private sector jobs and reduce reliance upon public sector employment.

Tax-exempt financing, improved permit processes and special incentives to specific industries also play an important role in the new assertiveness by state economic development programs. Louisiana developed a program to draw the off-shore oil industry to its shores; Pennsylvania put together a package of incentives, including tax breaks, new highway construction, and low-cost financing for a new Volkswagen assembly plant; and Ohio and Tennessee did the same for two

Japanese auto companies. All the programs will create thousands of new jobs for the residents of those states.

In Delaware we enacted a series of changes in our banking laws to encourage large bank holding companies to create subsidiaries in our state to take advantage of attractive regulations and tax rates. Two have already committed; others have expressed a strong interest.

The passage of the legislation was the result of a community-wide effort for economic expansion, especially in industries which are growth oriented, which are non-polluting and which pay good wages. All segments of our community worked together to enact this legislation.

Delaware saw that the banking industry is changing. With the dawn of new electronics and telecommunication technologies, expanded services are now offered by financial institutions. At the same time, federal regulations are becoming obsolete and inter-state banking is going to become commonplace. In Delaware we saw the opportunity to bring some diversity to our economy and at the same time insulate ourselves against erratic federal policies and changes in the nation's economy.

The result of these state initiatives in Delaware and elsewhere in the nation is to provide an additional competitive factor in the national economy. Businesses now can seek additional opportunity for economic growth which may have not been present before. For example, banks, which were captive of cities and states because of federal and state laws, can now seek additional growth in other areas which may have not been financially or legally possible before.

Secondly, this competition fostered by states is healthy because it will force states to promote efficiency in the delivery of government services at the risk of placing too great a burden upon both individual taxpayers and local businesses.

Finally, sophisticated state economic development programs are the seeds of innovation and can be the tested in the soil of state programs before they are transferred in practice to other states or the federal government. If the program

works, it can be adopted for other states; if not, it won't become a burden shared by all of the states.

The tremendous national diversity and the spread of population centers have created a situation such that a highly centralized government no longer responds effectively to certain local needs. That is why I believe the individual states, acting singly or in concert, can achieve many of the social and economic goals sought by Washington, more quickly and less expensively. We are putting our beliefs to the test, involving ourselves in economic innovation, in economic planning, in economic progress. That in itself is a revolutionary concept in state and local government. While the national debate rages on, about inflation, about tax cuts, about the re-industrialization of America, with barely a press notice federalism has been reborn. State and local governments with the support of concerned community groups ranging from the AFL- CIO to the Business Round Table, have taken matters into their own hands, determined to reinvigorate their own economies with their own initiatives and their own resources. Two decades of federal economic planning have not served us well; we are determined to do better.

Fiscal reforms, stimulative tax cuts, constitutional limits upon the growth of the public sector, tax incentive packages, target industry recruitment programs, private sector involvement in public sector programs -- these are the initial results of the rebirth of federalism. These are the tools and techniques that Governors, Mayors, and community leaders are using to take control of the economic future of our own constituencies.

We believe such activities are good economics and good politics, good for the nation and good for the several states. But perhaps most significantly, they point the way to new opportunities for the private sector. You now have the opportunity, if you will use it, to become involved in the decision making process on a wide variety of issues - from local economic incentives, to workmen's compensation reform; from unemployment insurance and job training programs to tax reform. And that opportunity is perhaps the most significant aspect of our newly reborn federalism, for it is a return to the compact that was the intellectual basis of the ratification of our constitution two hundred years ago; that there are three full partners in the governance of our republic, the federal government, the state governments, and we the people of the United States of America.