

Ec. 100B, 585. Used Mtrls

As goes Ohio, so goes the nation.

BANKS ON THE RUN

THE EIGHTIES HAVE been hard on U.S. financial institutions. In 1981 declining energy prices and stagnating real estate values left many commercial banks and thrifts holding almost worthless loan agreements. In 1982 the entire savings and loan industry was threatened with bankruptcy, until Congress approved a new kind of creative accounting that let essentially insolvent institutions stay in business. When the Third World debt crisis erupted, the largest banks were faced with the prospect of seeing billions of dollars in loans default with no way to collect them. And in 1984, 79 banks went under, including Continental Illinois, the eighth largest bank in America. This year has brought a farm bank crisis that rivals that of the Depression. Banks in the Midwest are collapsing at the rate of one a day. Some analysts are predicting the loss of 750 farm-state banks by December.

Still, depositors' confidence in their banks never flagged. Problems that would certainly have sparked bank runs earlier in the century came and went without incident. There is a simple reason for this sense of security: federal deposit insurance, initiated during the Depression, was working. Customers believed that their money was safe, even if their bank went bust.

That sense of confidence was shattered for a small group of depositors on March 14, when a Cincinnati talk-show host warned his listeners of impending "disaster" at 71 state-chartered thrifts that were not part of the federal insurance system. The only deposit insurance these small institutions had was with the privately owned Ohio Deposit Guarantee Fund. It promised to protect all deposits "in full" with its \$136 million in assets. Unfortunately for the thrifts and their customers, that fund had been completely wiped out five days earlier by the failure of one bank—Home State. The Ohio legislature quickly threw in \$90 million, but everyone knew it was too little, too late. That afternoon lines began to form in front of the privately insured thrifts. Rumors proliferated and confidence eroded, prompting a classic bank run. By five the next morning, Ohio governor Richard Celeste ordered all 71 thrifts to lock their doors for at least three days.

Banking officials across the country spent the next week quietly meeting to devise plans in case the run spread to state-chartered institutions outside Ohio. International currency traders drove the dollar sharply down—breaking a 14-year record for one-day declines.

Meanwhile Governor Celeste, Federal Reserve Board chairman Paul Volcker, and Cleveland Fed president Karen Horn worked with federal deposit insurance agencies to prop up the threatened institutions. Within a week many of them had reopened without incident, after preliminarily qualifying for federal deposit insurance.

The Ohio case was a reminder of how quickly bank runs

can start. Our financial system depends upon a shared trust that banks and thrifts offer a refuge for depositors. With increasing speculation, sour energy loans, Third World debt, and farm bankruptcies threatening unprecedented numbers of institutions, that sense of refuge depends increasingly on deposit insurance—to keep an isolated collapse from turning into a widespread run.

Ohio is not the first state with privately owned deposit insurance funds to experience a run in recent times, and it will probably not be the last. In 1976 Mississippi declared a bank holiday for its state-chartered savings and loans associations after the private deposit insurance fund was wiped out by the failure of Bankers Trust Savings and Loan Association. Mississippi too ordered all institutions to obtain federal deposit insurance before reopening. In February 1983 two privately insured Hawaiian thrifts were closed by the state, prompting a run on the state's largest savings and loan association after newspaper stories linked it with the failed banks. The Hawaiian legislature quickly passed legislation requiring all banks to have federal deposit insurance. Barely nine months later, Nebraska's largest savings bank, Commonwealth Savings, folded. The Commonwealth failure wiped out the entire private guarantee fund for the state and losses to depositors are expected to reach \$30 million. To date, not one depositor has recovered a penny.

ELEVEN STATES still rely on private insurance funds to guarantee deposits in state-chartered banks or thrifts, and according to press reports, at least 15 other states are actively interested in starting such a system. As might be expected, these efforts at privatization have the full support of the Reagan administration.

The lure of private insurance is clear. Small thrifts and banks that stay out of the national deposit insurance system can avoid federal regulations and federal auditors. Consequently they can pay customers higher interest rates for deposits than the 5.5 percent federally insured thrifts are allowed to pay. They also escape the strict portfolio requirements that have kept federal institutions from making risky but high-paying investments. For years these private funds and their insured institutions have been benefiting from the atmosphere of calm that federal deposit insurance has created within the banking industry. In the cases of real trouble the surviving institutions were ordered to get federal deposit insurance and the private funds folded. After a few days only the depositors who lost money remembered there had ever been a problem.

But the current drive to create more private funds is akin to begging for bank runs. Never has a private insurance fund been severely tested and survived. Even small claims seem to stretch the funds' ability to pay depositors. In Colorado half of the private insurance fund has been used to cover failures in recent years, and just one failure wiped out Iowa's two-million-dollar private plan. The Iowa fund is currently collecting assessments for the next two years, in advance, to pay off depositors of that one failed institution. Although both of these funds expect to recover mon-

ey from liquidation procedures, that process can take years. In the meantime they hobble along, hoping nothing else goes wrong.

According to a December 1984 study by the Federal Deposit Insurance Corporation, the problems of Ohio, Nebraska, Iowa, Hawaii, and Colorado could be repeated in many other states. No private fund has enough money to cover even four percent of the deposits they insure. In essence, these funds are not offering insurance, they're offering a lottery for depositors willing to bet there will be no major trouble. That FDIC study praised Ohio for having a "sizable fund" and "insurance coverage against substantial losses."

The failed Ohio Guarantee Fund demonstrated that once a private fund gets into financial trouble, it has few options. Federal deposit agencies have the credit of the U.S. Treasury to back them up. Private insurers have only their own limited resources. Most do not even have a line of credit with their states, and the balanced budget requirements in many state constitutions keep them from ever promising full credit to the private funds.

The federal agencies are also better equipped to spot troubled banks before they become failing institutions. The government funds combine fiduciary liability with significant supervisory authority over the institutions they insure, thus giving federal auditors substantial incentives to root out problems early on. In contrast, as the Federal Deposit Insurance Corporation recently concluded, "the [private] guaranty programs have little or no control over their membership; typically, state authorities regulate and supervise the depository institutions."

Many private funds may have a substantial monetary interest in correcting institutional problems, but they have virtually no power to make the necessary changes. State regulators, who may have the power, have no direct financial incentive to intervene, especially when there is political pressure to keep the problems secret. Early reports indicate that Ohio regulators first spotted Home State's difficulties in 1982, but did little about them for motives that are gently referred to as "political."

ADEQUATE supervision is particularly important as deregulation moves forward, taking banks and thrifts into risky new areas of investment like the repurchase agreements and reverse repurchase agreements that sparked the Ohio crisis. As the Ohio thrifts discovered, one of the greatest risks of their newly increased freedom is their heightened vulnerability to fraud and speculation. The only way to spot that kind of trouble is with aggressive auditors who have both the power to force institutions back into line, and the incentive to do so.

The federal insurance agencies are not infallible, as the failures of Penn Square Bank in Oklahoma and Continental of Illinois made clear. Budget limitations, staff constraints, and the blinding quickness of new financial developments have seriously strained federal supervisors. Still, the structure for adequate supervision is in place.

This term Congress will be considering substantial bank

reform legislation, and as the legislators expand the powers of banks and thrifts, they should also expand the deposit safeguards for bank and thrift customers. The first step is to end the anachronistic system of private deposit insurance. Congress should set a time after which all banks and thrifts in the United States must qualify for federal deposit insurance or fold. For the nearly 1,000 banks and thrifts now under private insurance plans it would be a time of reckoning. In Ohio almost half of the closed institutions are considered to be too weak to open unless they are merged or bought by other thrifts. But such a move would strengthen the banking system and dramatically reduce the chance of a small bank failure setting off a widespread run.

And if legislators have any questions about the superiority of federal deposit insurance, they should ask the Kansas Investment Certificate Corporation. Kansas's private deposit insurance fund invests its money only with institutions that are federally insured.

RICHARD MEDLEY

Richard Medley, formerly the chief economist for the House Banking Committee, is at work on a book called *How Safe Are Our Banks?*

How capital punishment affirms life.

DEATH AND JUSTICE

LAST DECEMBER a man named Robert Lee Willie, who had been convicted of raping and murdering an 18-year-old woman, was executed in the Louisiana state prison. In a statement issued several minutes before his death, Mr. Willie said: "Killing people is wrong. . . . It makes no difference whether it's citizens, countries, or governments. Killing is wrong." Two weeks later in South Carolina, an admitted killer named Joseph Carl Shaw was put to death for murdering two teenagers. In an appeal to the governor for clemency, Mr. Shaw wrote: "Killing is wrong when I did it. Killing is wrong when you do it. I hope you have the courage and moral strength to stop the killing."

It is a curiosity of modern life that we find ourselves being lectured on morality by cold-blooded killers. Mr. Willie previously had been convicted of aggravated rape, aggravated kidnapping, and the murders of a Louisiana deputy and a man from Missouri. Mr. Shaw committed another murder a week before the two for which he was executed, and admitted mutilating the body of the 14-year-old girl he killed. I can't help wondering what prompted these murderers to speak out against killing as they entered the death-house door. Did their newfound

Money Supply Expands \$2.1 Billion

5-17-85 IV-2

NEW YORK (AP)—The nation's basic money supply shot up \$2.1 billion in early May, the Federal Reserve Board reported Thursday, leaving the measure known as M1 above the Fed's growth target.

The surge in M1 was a surprise to many analysts who had been predicting a decline in the measure of funds readily available for spending and who had been hoping that the combination of a slowdown in money growth and a sluggish economy would persuade the Federal Reserve to push interest rates lower.

Fed policy-makers are scheduled to consider strategy at a meeting Tuesday in Washington, and predictions have been rampant in financial markets that there would be a cut in the discount rate—the interest on Fed loans to banking institutions—before that session.

The discount rate has stood at 8% since last December.

David Jones, an economist at the government securities firm Aubrey G. Lanston & Co., said that, with M1 still growing faster than the Fed would like and with Congress yet to complete action on reducing the size of the deficit, "the Fed might delay any easing move somewhat."

But Jones said he still believed it inevitable that the Fed will accommodate lower interest rates because of continued signs of sluggish economic growth.

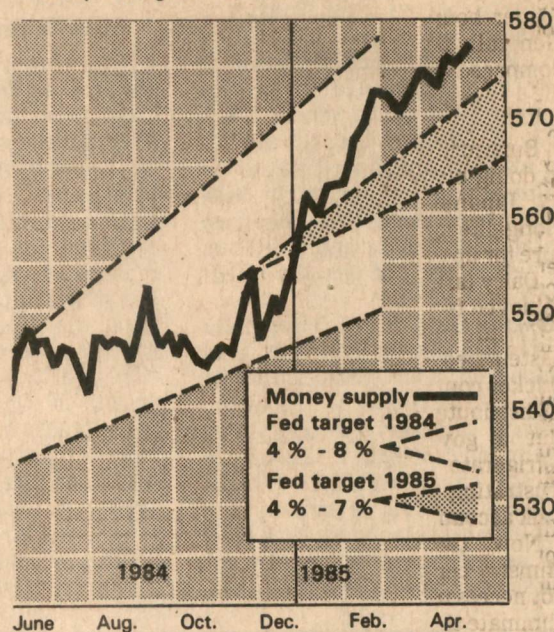
"The markets are very edgy at the moment, waiting for the Fed to drop the shoe," said Jeffrey Leeds, an economist at Chemical Bank. "The odds slightly favor a cut in the discount rate in the next several weeks."

The rise in M1 in early May was especially disappointing to financial economists because it reversed a slowdown in money supply growth that began in April.

The Fed reported that M1 growth was a moderate \$2.9 billion in April, that a broader measure known as M2 fell \$1.6 billion last month and that an even broader measure, M3, rose \$1.8 billion. M1 is reported weekly, while M2 and M3 are reported monthly.

M1—Currency in circulation, plus demand deposits and other checkable deposits at banks and thrift institutions. It includes Super NOW accounts.

Weekly averages in billions of dollars.



Source: Federal Reserve Board

Los Angeles Times

The Fed said M1 rose to a seasonally adjusted \$577.6 billion in the week ended May 6 from a revised \$575.5 billion in the previous week. The previous week's figure originally was reported as \$575.2 billion.

M1 includes cash in circulation, deposits in checking

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izing its soundness and forcing it to lay off many employees.

In its actions against Icahn, including a federal suit filed Wednesday in New York, TWA has charged that he plans to liquidate assets and abandon operations to provide funds for his "speculative investments."

In its filing with the Department of Transportation, TWA also sought to prevent Icahn from using his equity position to change TWA's management, financial or operating structure or make changes "that would render TWA unfit to perform the air service contemplated by its certificates."

The airline also sought to have DOT prevent Icahn from acquiring any additional stock and order him to divest himself of the shares that he owns.

A spokesman at the Department of Transportation said the final decision on such a case would be made by Matthew V. Scocozza, assistant secretary for policy and international affairs. If the case is handled on an emergency basis, anyone supporting or opposing the petition must respond by June 13. If not, the department will hold hearings according to its own timetable.

waiver from Federal Communications Commission rules that prohibit common ownership of daily newspapers and major broadcast outlets in the same area, according to two newsroom employees who asked not to be identified.

But FCC officials and industry analysts said it is extremely unlikely that such a waiver would be granted.

Paper 'Is Profitable'

"All we know is what was said in the press conference in New York," Daily News Editor Tim Kelly said. "We have not talked to the FCC. As far as I know, no decision has been made."

Thomas Griffiths, vice president of marketing, said that, despite the millions of dollars that Tribune Co. has poured into Daily News operations, the paper "is profitable and has been profitable since they (Tribune Co.) bought it." But its growth in circulation and size has undoubtedly made the paper much more expensive to produce, and some analysts believe that could eventually erode its profits.

Its position in the lucrative Southern California market makes the paper attractive for acquisition,

Paid Circulation

Last year, the Daily News posted the fastest percentage growth among the larger daily newspapers in Southern California, according to the Audit Bureau of Circulations, which is the standard auditing service for the nation's 1,700 daily newspapers. It increased its circulation to 141,690 from 132,672 in 1983.

Since Tribune Co. bought the paper, the Daily News has been converting to paid circulation from the free delivery that built it into a highly profitable advertising medium in the San Fernando Valley.

Between 1973 and 1981, the Daily News cut the number of free subscriptions by more than 50% to 82,463 in 1981 from 215,397 free copies in 1973. Meanwhile, the paper doubled its paid subscribers to 114,099 from 57,276 in 1973.

The paper had paid weekday circulation of 145,523 as of March 10. But the easy part of that growth appears to be about over.

Now, however, there are fewer than 3,000 copies given away. In light of the difficult task ahead, the Daily News has instituted manage-

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Secret Negotiations Began in March

Behind the Scenes of the Allied-Sig

By BILL RITTER and ROBERT E. DALLOS, *Times Staff Writers*

SAN DIEGO—At first, the three executives from Allied Corp. and Signal Cos. discussing a possible merger over a clandestine dinner "just

What had started as a tentative discussion about a joint Signal-Allied bid to buy Hughes Aircraft had matured into a discussion about

exchanged Signal, while share of the

MONEY

Continued from Page 2

accounts and non-bank travelers checks.

For the latest 13 weeks, M1 averaged \$573 billion, a 10% rate of gain from the previous 13 weeks.

The Fed, which tries to provide enough money to keep the economy growing without reviving higher inflation, has said it would like to see M1 grow between 4% and 7% from the fourth quarter of 1984 through the fourth quarter of 1985.

M1 rose to an average \$575 billion in April from \$572.1 billion in March.

M2, which includes M1 and adds to it such things as savings accounts and deposits in individual money-market mutual funds, fell to \$2.427 trillion in April from \$2.4286 trillion in March.

M3, which includes M2 and less liquid accounts, such as 90-day bank certificates of deposit in excess of \$100,000, rose in April to \$3.0575 trillion from \$3.0557 trillion.

Analysts said the rise in M1 in early May could have reflected income tax refund payments by the government and the monthly payment of Social Security benefits. The drop in M2, the analysts said, may have reflected income tax payments in April made with withdrawals from money-market accounts.

In separate reports:

- The Federal Reserve Bank of New York said commercial and industrial loans at major New York City banks rose \$499 million in the week ended May 8, compared to a gain of \$722 million a week earlier. Commercial paper—short-term corporate IOUs—outstanding nationwide rose \$1.22 billion in the week ended May 8 after rising \$1.75 billion in the previous week.

- The Fed said the federal funds rate, the interest rate on overnight loans between banks and a peg for many other short-term interest rates, averaged 8.14% in the week ended Wednesday, down from 8.19% in the previous week.

- The Fed estimated that borrowings from the Federal Reserve System averaged \$839 million a day in the week ended Wednesday, up from \$515 million in the previous week.

- Free reserves in the banking system, an indicator of surplus funds available to banks, was revised to \$165 million in the two-week period ended May 8, compared to \$500 million in the previous two weeks. The original estimate of free reserves was \$250 million in the latest two weeks against \$490 million in the previous period.

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Riverside, California • Saturday, May 18, 1985

Riverside Final

25¢

Fed reduces its lending rate to lowest in 7 years

By MARTIN CRUTSINGER

WASHINGTON (AP) — The Federal Reserve Board, moving to stimulate a sluggish economy, yesterday lowered its lending rate to banks and other financial institutions to 7.5 percent, the lowest level in almost seven years.

The one-half percentage point drop in the discount rate was expected by many analysts to accelerate a trend toward lower interest rates throughout the economy.

Minutes after the Fed's announcement, Citibank in New York, the nation's second-largest commercial bank, and No. 3 Chase Manhattan lowered their prime

lending rates to 10 percent — the lowest level in 6½ years.

The two banking giants followed the lead of eighth-ranked Bankers Trust Co. of New York, which had lowered its rate to 10 percent on Wednesday. Analysts predicted other banks will follow suit.

The Fed action had immediate after-effects.

In foreign exchange markets, the dollar staged a broad retreat, and slid slightly further in slow after-hours trading after the Fed announced it had cut its discount rate.

Within minutes of the Fed's announcement, the dollar slipped to 3.0530

West German marks from 3.0620 marks and from 3.0975 marks late Thursday.

Expectations that the Fed would reduce the discount rate from the 8 percent level that had prevailed since December has been a factor undercutting the dollar. Lower interest rates in the United States make returns less attractive on dollar-denominated investments.

The stock market, which closed before the Fed announcement, posted a broad gain, riding an afternoon wave of buying. The advance lifted several market indicators to record or near-record levels as the market closed out its second straight week of gains.

The Dow Jones average of 30 industrials climbed 7.29 to 1,285.34, finishing the week with a net rise of 11.16 points.

The Fed said it took action because of "relatively unchanged output for some time in the industrial sector of the economy, stemming heavily from rising imports and a strong dollar."

The U.S. economy turned in an anemic growth rate of 1.3 percent during the first three months of this year, the slowest pace since the end of the last recession.

The weak growth had raised concerns that the economy could teeter into another recession in coming months and had led to pressure on the central bank to

loosen its credit controls as a way of spurring economic growth.

A change in the discount rate is the most dramatic tool the Federal Reserve has for signaling its intentions. The discount rate is the interest rate that the Fed charges in loaning money to banks and it is one of a variety of ways that the Fed influences interest rates and the growth of the nation's money supply.

The discount rate has not been as low as 7.5 percent since August 1978, when it was 7.25 percent. Beginning in the fall of that year, the central bank began raising the discount rate in a series of steps

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Americans: Japan a threat to jobs, but U.S. also at fault

By WILLIAM M. WELCH

WASHINGTON (AP) — Americans see Japan as presenting a serious threat to U.S. jobs but they also point blame at this country for the big trade imbalance, a survey released yesterday said.

The poll of American attitudes toward Asia found 80 percent said Japan poses a serious threat now to U.S. workers, far ahead of the threat listed for any other country.

"That sense of threat provides a basis for what was seen on Capitol Hill with the explosion after the voluntary quotas on auto exports was dropped," said William Watts, who designed and analyzed the survey.

The survey was conducted among 1,350 Americans by The Gallup Organization for Potomac Associates, a tax-exempt public policy research group headed by Watts. It was done in association with the Johns Hopkins School of Advanced International Studies, where Watts is a teacher.

Asked to assess blame for the United States' trade deficit — more than \$120 billion last year, and \$37 billion of that with Japan — 46 percent said it is primarily the fault of the United States, blaming high wages, restrictive government policies and inefficient management and labor practices.

Thirty-six percent said it was the fault of other countries and their lower

wages, artificial barriers and other unfair trade practices.

At a panel discussion on the survey, Watts said he also found:

✓ Americans hold overwhelmingly positive feelings about Japan, with 84 percent offering positive views and 12 percent negative. That was the same response Watts said he found in a similar poll done in 1980.

✓ In terms of popularity among Americans, the survey found the most favored nations in Asia and the Pacific are Australia, Japan and New Zealand.

✓ Americans hold some stereotyped views of Asia. The most frequently listed adjectives for the region were "crowded,"

"underdeveloped," "political unrest," and "poor sanitation." However, Japan was seen differently from most other Asian countries, with respondents calling it "industrialized," "crowded," "well educated," and "modern."

Watts said the survey found a reluctance by Americans to make other countries a scapegoat for trade problems, a finding he said is duplicated in other surveys. "I don't consider this a one-time fluke, but a willingness to point the finger at ourselves," he said.

Seventy percent of those surveyed said the United States should come to the defense of Japan if attacked by the Soviet Union or China, while 21 percent dis-

agreed. Seventy-six percent said the United States should defend European allies if attacked.

By contrast, 37 percent said they were willing to defend Taiwan against China and 32 percent said they were willing to defend Thailand against Vietnam. While a majority said the Philippines should be defended, support for that country has declined sharply since 1980.

The survey was conducted in personal interviews Feb. 22 to March 3 among adults 18 or older. Watts said it had a margin of error of plus or minus 3 percentage points. He said the questions were confined to Asian countries of the Pacific rim and did not include India.

The World

A-2

The Press-Enterprise

Saturday, May 18, 1985

Lima police round up suspects in bombings



Pope hears call to revise church policy on women

By BRUCE BUURSMA
Chicago Tribune

ANTWERP, Belgium — Pope John Paul II was warned yesterday that the growing "women's



Rates . . .

(From Page A-1)

designed to wring inflation out of the economy.

The Fed raised the discount rate to a record high of 14 percent by the spring of 1981. While inflation was brought under control, the high interest rates also brought on the steepest recession since the Great Depression.

Allen Sinai, chief economist for Shearson Lehman Brothers, said the rate reduction "is a clear signal of the central bank's concern over the weak U.S. economy and particularly the near-recession in U.S. manufacturing."

Sinai predicted that all major banks would drop their prime

lending rate to 10 percent on Monday, helping to send other interest rates down as well.

"The central bank is trying to engineer a soft landing for the economy with real economic growth of around 3 percent to 4 percent without re-igniting inflation," he said. "This move helps."

Jerry Jasinowski, chief economist for the National Association of Manufacturers, termed the Fed's action "great news" for the economy because it signaled that the central bank was "anxious to loosen credit in order to stimulate a rebound."

Michael Evans, head of a Washington economic forecasting firm, predicted a big rally by the stock market next week because of the Fed's action.

Fed Cuts Key Loan Rate to Stimulate Economy

Charge for Lending to Banks Falls to 7.5%, Lowest in Nearly 7 Years; More Institutions Reduce Prime

By TOM REDBURN, *Times Staff Writer*

WASHINGTON—The Federal Reserve, worried about the lingering weakness of the U.S. economy, Friday lowered the lending rate it charges banks and other financial institutions by half a percentage point to 7.5%.

The Fed's discount rate, which has not been so low in nearly seven years, hit a record high of 14% in the spring of 1981. The latest move is the third time that the Fed has lowered the rate since last November.

The discount rate is one of the blunter instruments used by the Fed to help influence broad economic conditions, and any move in the rate is widely regarded as a clear signal of the central bank's often-murky intentions about the proper direction for interest rates. By lowering the rate, the Fed is hoping to encourage more borrowing, thereby stimulating the lagging economy.

"This Is the Signal"

"This is the right move at the right time," said Irwin Kellner, chief economist at Manufacturers Hanover Bank in New York. "It shows the Fed's priorities are clearly in favor of promoting growth in the economy. This is the signal the banks have been waiting for."

Indeed, only minutes after the Fed's announcement, New York's Citibank and Chase Manhattan Bank, the nation's second and third largest commercial banks, cut their prime lending rates to 10% from 10.5%. Another major bank, Bank-

ers Trust Co. of New York, had lowered its rate to 10% on Wednesday, and analysts predicted that other big banks would quickly fall in line now that Citibank and Chase have moved.

The Fed, in a typically cryptic statement explaining its move, said that it was acting in part because of "relatively unchanged output for some time in the industrial sector of the economy, stemming heavily from rising imports and the strong dollar."

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FED: Interest Rate on Loans to Banks Cut to Spur Economy

Continued from Page 1

The most recent figures for the nation's gross national product, adjusted for inflation, pointed to an annual growth rate of just 1.3% in the first quarter of this year. And several analysts said that they expect revised estimates, to be released by the Commerce Department next Tuesday, to show that the economy grew even more slowly than that.

Industrial production has grown barely at all since last summer and, even though many leading economists expect economic growth to pick up later this year, others have become so discouraged by the latest business reports that they have begun to warn of the dangers of a recession.

"I'm a little surprised the Fed moved so quickly, but it is clearly good news," said Jerry J. Jasinowski, chief economist for the National Assn. of Manufacturers. "It indicates they are concerned that

growth in the second quarter is going to be very slow. This should set the stage for a rebound, but interest rates may have to come down a bit more before we will see a real turnaround."

In an interview Wednesday, Preston Martin, vice chairman of the Fed's board, said that he was disappointed in the economy's performance and hinted that the Fed was prepared to see interest rates fall further in an attempt to prevent a so-called "growth recession"—economic growth so anemic that unemployment rises.

Most interest rates have fallen in recent weeks, in part because of the expectation that the Fed would be forced to ease credit conditions to prevent further economic slippage.

The Fed anticipated criticism that its latest reduction in interest rates, by encouraging more borrowing, might allow the nation's money supply to grow too fast. It

noted that inflation remains "relatively well contained in the goods-producing sectors of the economy, and sensitive commodity prices are generally at the lowest levels in about two years."

The Fed's statement added that "growth of the monetary aggregates has slowed appreciably, although M-1 (the most closely watched money supply figure) has remained somewhat above the path implied by the annual target."

The Fed announced Thursday that M-1, a measure of money in cash and checking accounts, had jumped more than expected in the previous week. But M-2, which adds most saving accounts and money market funds to M-1, dropped last month for the first time in five years.

The Fed's policy-making arm, the Federal Open Market Committee, will meet for two days next week, and several analysts predicted that it would make further

decisions then to encourage faster economic growth.

But economists were wary of forecasting additional interest rate declines.

"The discount rate has a lot of symbolic importance in ratifying drops in interest rates," said Michael Bazdarich, a monetary analyst at Claremont Economics Institute in Claremont, Calif. "But we won't be able to tell for a while whether the Fed is going to actively push rates down further."

And Kellner predicted that the bank prime rate would stabilize at 10% for a while until it is clear whether the economy is moving up or down. "This is just the medicine the economy needed," said Richard Rahn, chief economist at the U.S. Chamber of Commerce and a frequent critic of the Fed. "The key thing is to keep the recovery going."

The Fed, following practice, an-

Doctor Strike Deepens

SANTO DOMINGO, Dominican Republic (UPI)—Physicians in this Caribbean island nation extended a strike Friday by walking out of government-run hospitals and clinics, where they had been providing emergency services during a five-day-old strike. The doctors are demanding a doubling of their wages, which now average \$217 a month.

SAVE 43%
Short Sleeve
SPORT SHIRTS
Now \$16
Reg. \$28

Dacron® Blend, Machine Wash.,
Permanent Press

Don Loper, Damon, Lilly Dache, Lee,
London Fog, Jantzen, Arrow, Hobie,
Members Only, Sansabelt, Haggar,
Polo Beach, Oleg Cassini, Golden
Vee, Wrangler, Pierre Cardin, Sergio
Valente, Harris Casuals, Levi's Jeans



"Consider the rich, how they become so. Either they or their ancestors before them have taken from others, and that which they have taken, the others have lost. The very essence of their richness is that there are many poor. If all were rich, there would be no sense in wealth, no power in it, for there would be none willing to serve. It is plain to anyone who can think that richness means possessing material things and excluding others from possession thereof. Of such is the kingdom of Mammon.

"And what is the kingdom of God? In the region of the mind the situation is exactly the opposite; the wealth of one is the wealth of all, and the highest joy of possession is that the thing possessed may be shared by all and be of benefit to all, with no diminution to anyone. ... my pleasure is in communicating to you ... and exactly proportionate to my success ... is my own gratification. ... each gives something which all mankind may enjoy forever, and no one's pleasure in "As You Like It" or in the "Fifth Symphony" or in an understanding of the movements of the planets is any less because at the same time millions of other people are having that same pleasure."

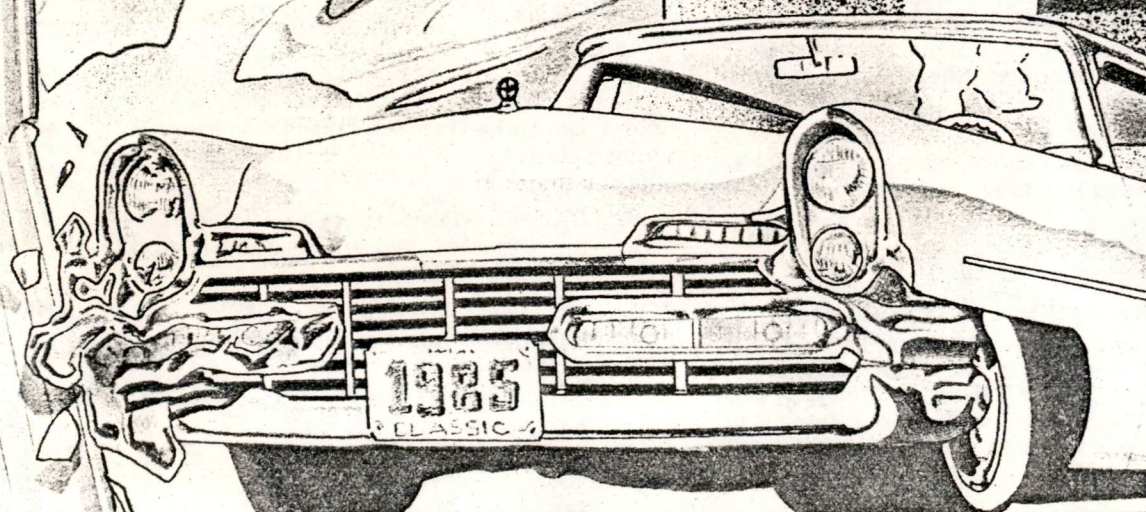
--- Upton Sinclair, THE GOOSE STEP, 1922, p.383



deposits

The Fall of The Idea of THRIFT

*How the economists came
to label virtue a vice.*



WHO'S WHO in the Administration

Did you scratch your head when the White House proposed that Reagan and other top officials take a 10 percent pay cut? Did they at last see the point of having those who are well-off share in the sacrifices they ask of others? Unfortunately the answer is no. The idea didn't come from Reagan or any member of his staff. It was **Bob Dole's**....

Samuel B. Pierce Jr., the secretary of Housing and Urban Development, is said to be planning to leave within the next year to resume the practice of law with his old New York firm. A good many administration lawyers have similar timetables for their exits. The financial rewards of the law tend to fall most generously on those who leave while their old administration friends still have a few years left in power. That way the departing lawyer—and his potential clients—know that he still has the right phone numbers....

Our sources tell us that the White House will try to satisfy **Jeane Kirkpatrick's** frustrated ambition, which has led her to announce that she will return to private life, with a manufactured job that will sound impressive but will not give her the power she wants. The negative word about her at the White House is that she's indiscreet....

In

DEFENSE

Principal Deputy Assistant Secretary for Public Affairs—**Fred S. Hoffman** has been a Pentagon correspondent for the Associated Press.

STATE

Assistant Secretary for Public Affairs and Department Spokesman—**Bernard Kalb** has been State Department correspondent for NBC News.

TREASURY

Deputy Assistant Secretary for Public Affairs—**Roger Bolton** was director of speechwriting for Reagan-Bush '84.

AGENCIES AND COMMISSIONS

Postmaster General, United States Postal Service—**Paul N. Carlin** has been the Chicago regional postmaster.

Administrator, Environmental Protection Agency—**Lee M. Thomas** has been assistant administrator in charge of the agency's hazardous waste programs.

Out

AGRICULTURE

Deputy Secretary—**Richard E. Lyng** will resign. Assistant Secretary for Economics—**William G. Leshner** is resigning.

Assistant Secretary for Natural Resources and Environment—**John B. Crowell Jr.** is returning to Portland, Oregon to practice law.

HEALTH AND HUMAN SERVICES

The man most likely to replace **Nancy Harvey Steorts** as chairman of the Consumer Product Safety Commission is Commissioner **Terrence M. Scanlon**. Scanlon's a Democrat, but his politics have not endeared him to the consumer movement. For example he was the only member of the commission who voted to allow companies to export products that CPSC deemed unsafe for Americans....

The Reagan White House continues to live out the worst nightmares of Moral Majoritarians in the conduct of various high officials' private lives. One prominent male member of the White House staff took a trip while the president was in Santa Barbara. The official word given the White House press corps was that he was on a brief vacation. The reporters knew he was in the company of a young woman who was not his wife—that is, all but one of them did. That reporter sent out a story over the wires that mentioned the staff member's being on vacation. His wife had been under the impression that he was hard at work and was not amused. At the same time a senior male member of the national security staff has been carrying on simultaneously with a female subordinate and a female television reporter....

Assistant Secretary for Legislation—**John F. Scruggs** is joining the lobbying firm of Gold and Liebengold, Inc.

HOUSING AND URBAN DEVELOPMENT

Undersecretary—**Philip D. Abrams** is leaving to establish a building and construction company in Denver, Colorado.

INTERIOR

Assistant Secretary for Land and Mineral Management—**Garrey E. Carruthers** will teach at New Mexico State University.

Assistant Secretary for Indian Affairs—**Kenneth L. Smith** is returning to his Oregon ranch.

Director, National Park Service—**Russell E. Dickenson** will retire and serve on the National Parks Advisory Board.

STATE

Assistant Secretary for Public Affairs and Department Spokesman—**John Hughes** is resigning to return to journalism.

TREASURY

Deputy Treasurer—**David Q. Bates** will join the Washington office of the Houston law firm of Reynolds, Allen & Cook.

AGENCIES AND COMMISSIONS

Administrator, Environmental Protection Agency—**William D. Ruckelshaus** has resigned.

Chairman, Consumer Product Safety Commission—**Nancy Harvey Steorts** has resigned.

Chairman, Civil Aeronautics Board—**Dan McKinnon** left on December 31. The agency closed that day.

~g. byron peck~
Efr

1923

1945

1957



by Phillip Longman

During the early months of 1958, as the unemployment rate approached a new postwar high of 6.8 percent and business profits slumped, the Eisenhower administration found itself besieged from all quarters with demands that it take drastic action to avert the coming depression. Ike listened to the prophets of crisis, and chose his course: he twice went before the public to admonish that it was Americans' patriotic duty to save less and to Buy Now.

Phillip Longman is a Princeton, New Jersey, writer.
Illustration by Byron Peck

Advertisers across the country immediately seized upon this happy new presidential theme, launching hundreds of "confidence" or "prosperity" drives to reinforce Ike's message to the consumer. An association of Cleveland auto dealers invented the slogan "YOUAUTOBUY"—later adopted by the whole industry—and was quickly rewarded with invitations to the White House and a favorable mention at Ike's weekly news conference. Businessmen in Boston offered "POPS," for "Power of Positive Selling"; Cleveland city fathers elected a "Miss Prosperity" to reign over antirecession parades and street rallies.

In April *The Wall Street Journal* reported that "a massive antirecession psychological offensive... is just getting under way in nearly every major city in the U.S. Already in existence are 'Operation Optimism,' 'Keep Detroit Dynamic,' 'Crusade for Confidence,' 'Buy and Be Happy,' and 'O.K. Ike.'" Even the banks joined in the siren call, abandoning their usual admonishments to thrift. "Ah gwan," the Bank of Saint Louis urged in a Sunday newspaper ad, "buy that new car." Another bank in St. Louis had a similar message for would-be savers: "In times such as these, excessive savings can be as harmful as excessive spending." Auto dealers in Essex County, New Jersey, according to the *Journal*, mounted a joint radio campaign to warn the public: "Buy Now. The Job You Save May Be Your Own." Elsewhere in New Jersey, a tire store used the slogan "Buy, Buy, Buy," adding, "It's your patriotic duty."

Out of such raw material was woven that great, woolly, socio-economic paradigm of the 1950s: the idea of the Mass Consumption Society. Ike's faith in the power of positive selling was evidence of a powerful, new, bi-partisan consensus in American economic thought: that, for better or for worse, the nation's future prosperity no longer depended much on individual savings, hard work, or initiative but more on the present population's propensity to consume.

A penny spent

In the 1870's a most eminent Victorian and popular moralist, Samuel Smiles, became famous for his lively defense of the opposing notion, then the orthodoxy of the striving middle classes in both Europe and America. "It is the savings of the individual which compose the wealth—in other words, the well-being of every nation," Smiles asserted in a relentless volume entitled simply, *Thrift*. "On the other hand, it is the

wastefulness of individuals which occasions the impoverishment of states. So it is that every thrifty person may be regarded as a public benefactor, and every thriftless person as a public enemy." For Smiles, as for most Americans of his era, individual thrift was not only a virtue in itself; its widespread practice was considered a first requisite of civilization and nation-building.

Why is it that today, such adulation of individual thrift is virtually absent from our economic debate? Oddly, it is still official U.S. policy to encourage many other nations to submit their citizens to a strict regime of thrift. In the cases of Brazil and Mexico, for example, we have been quick to call for "austerity plans" as a condition for further credit. When it comes to others, we readily acknowledge that no nation can continually borrow in order to finance personal consumption; we insist, in effect, that the citizens of these debtor countries adhere to an ethos of thrift, as our Victorian forebears once did, to furnish capital necessary for economic growth. Yet even as the U.S. is now rapidly reverting to its nineteenth-century status as a net debtor nation, no one here is proposing that we once again celebrate individual thrift as a social virtue.

Instead, we debate the size of the federal deficit, the money supply, the value of the dollar, tax rates and other technical, microeconomic factors. Yet our present debt crisis is also bound up with what John Maynard Keynes liked to call "the habits of the community"—specifically, in the general demise of the thrift ethos over the last generation. Consider, for example, that despite the enormous federal deficits incurred under Reagan, the amount owed by individual debtors (approximately \$1.7 trillion) is still, as of this writing, greater than the national debt. During just the past four years, consumer installment buying has increased by almost 30 percent. In the first half of 1984, mortgage and consumer borrowing together absorbed more than 38 percent of all funds raised in the U.S. credit markets. The debts of people, no less than those of the state, are depleting the supply, and running up the cost, of capital available for productive purposes.

That even middle-class citizens now typically neglect to save enough to pay their own way through retirement or to be secure against even a small reversal of fortune causes a clamor for "entitlements," which of course prompts in turn still more public borrowing. These trends argue for a fundamental change in our thinking about the respective roles of individual savings and consumption in our society. Such changes, however,

The thrift ethos hasn't always been the province of Wall Street Republicans. During the twenties the liberal Thrift Movement promoted values and themes that presaged the environmental movement of today.

will not come easily. Despite their new "supply-side" rhetoric, conservatives have, by and large, renounced their traditional role as defenders of the thrift ethos, celebrating instead the idea that the nation can borrow and spend its way to lasting prosperity. (See "What the Democrats Could Learn from Jack Kemp," page 28.) Yet for liberals, especially, the question of how best to oppose this spend-thrift policy poses tremendous difficulties. At their root is liberalism's longstanding ambivalence about the purposes of thrift.

Can an ethos of capital stewardship, of principled regard for the financial and economic interests of future generations, be reconciled with the prevailing values and attitudes of modern day liberalism? Or must such questions always be the province of economic royalists—Wall Street Republicans and other rentiers? It is useful to recall that an important precedent for a thrift ethic does exist within the liberal tradition itself.

The reign of the stewards

The Thrift Movement, as it was called, reached its apex in this country, as well as in England, during the early 1920s. In many respects, its values and themes presaged those of the environmental movement of our own time, but with

a significant difference. The partisans of Thrift abhorred waste and applauded conservation, but unlike today's conservationists, extended their values to the arena of finance. It was an ethos directly inspired by the conduct of the Great War.

In 1920, the editors of *The Annals of the American Academy of Political and Social Science* devoted a special issue to the Thrift Movement. In an introductory essay, economist Roy G. Blakey explained the philosophy of the cause and its origins in the homefront experience of the Great War. "Many realized for the first time that it was a matter of life and death to thousands of soldiers and of civilians also, whether they wasted or whether they conserved food and fuel," Blakey wrote. "Instead of suggesting stinginess, it came to connote *proper use*.... It was closely associated with effectiveness, loyalty, patriotism, victory."

The Thrift Movement was an odd fusion of many diverse interests and constituencies. Andrew Mellon was an outspoken apostle of the cause; so was Stuart Chase, the well-known author and perennial weathervane of fashionable liberal opinion, who in 1928 wrote a popular book called *Waste*. "We are deluged with things," Chase complained, "which we do not wear, which we lose, which go out of style, which disappear anyhow. . . endless jiggers and doodads and contrivances. Here, it seems, the advertiser plays on the essential monkey within us—grabbing for a rose only to pick it to pieces, petal by petal."

Professional social workers of the era, as well as many partisans of the labor movement, also promoted the ideal of thrift or its variant, "wise spending," convinced that it was the surest way for members of the working class to help themselves. Samuel Crowther, in his 1920 book, *Why Men Strike*, connected the thriftiness of the working class to broader social concerns. Universal thrift, he argued, would "not only destroy the budding idea of the proletariat, but also provide ever-increasing facilities for higher production at higher wages. . . . [It] transforms the man from a mere industrial parasite into a sturdy member of society." In his popular *Book of Thrift*, T. D. MacGregor cast the movement in terms of the class struggle. "We the everyday men and women are the backbone of this country," MacGregor wrote. "Let us economize! Let us save! Let us do our share in making this country the great financial power of the world! Our millions of workers can do this, not the capitalists!"

Between 1912 and 1924, the amount of money deposited in savings banks increased more than



Little AMERICANS *Do your bit*

Eat Oatmeal-Corn meal mush-
Hominy - other corn cereals -
and Rice with milk.
Save the wheat for our soldiers.
Leave nothing on your plate



UNITED STATES FOOD ADMINISTRATION

two and a half times, according to a contemporary survey by the American Bankers Association; the per capita savings rate nearly doubled, from \$89 to \$186. While much of this new thrift was attributed at the time to the aggressive marketing campaigns waged by the nation's banks and insurance companies, as well as to the general rise of wages over inflation, it was also commonly accepted that the new impulse to save was inspired in large part by a genuine social ethos of self-help, conservation, and stewardship.

Capitalist counterpunch

Why did the Thrift Movement fade? Given the threat the cause posed to the immediate interests of mass merchandisers, it is not surprising that the initial assaults came from capitalist quarters—principally from retailers, who found it increasingly difficult to unload their more impractical wares. In 1926, a business group calling itself the National Prosperity Bureau sprang into existence to promote easy spending and thereby counter this threat. As bemusedly reported by *The Nation*, the Bureau was “getting up at four o'clock these cold winter mornings to plaster our shop windows with posters of a figure of Uncle Sam sitting at the throttle of a locomotive. Surrounding him is the inscription: ‘Full speed ahead! Clear the track for prosperity! Buy what you need now!’”

The same sentiment emerged in an article in the *The Atlantic Monthly* that same year. Entitled “The Dilemma of Thrift,” and written by William T. Foster, a former president of Reed College, and a businessman named Waddill Catchings, the article bestowed new intellectual respectability upon the idea that extravagant spending was now the nation's best guarantee of prosperity. “What a mess we get into!” the authors complained. “We celebrate ‘Buyers Week’ and ‘Thrift Week’ at one and the same time. By investing our savings, instead of spending them, we deny ourselves today in order to produce more in the future, although we are already equipped to produce more than we know how to use...” The consumer clearly was the hero under this analysis, while the saver enriched himself at the expense of the common good.

While this formulation was widely and vigorously condemned as heresy at the time, it soon enough became a point of liberal orthodoxy, the first premise of the New Deal economics and of the post-war consumer society. Anyone who has endured freshman economics during the last 30 or so years has probably encountered it in Paul

A. Samuelson's all-time best-selling college textbook, *Economics*—the “paradox of thrift.” In the 1964 edition of his text, Samuelson instructed, “What once was a social virtue [i.e., savings] may [in times of depression] become a social vice. What is true for the individual—that extra thriftiness means increased savings and wealth—may then become completely untrue for the community as a whole.”

Keynes to the kingdom

During the Depression years, the Thrift Movement's emphasis on conservation of natural resources remained an important influence on mainstream liberalism. (There was the Civilian Conservation Corps, for example, and numerous New Deal bureaucracies dedicated to the problems of soil erosion and forest management.) But after the shock in 1929, most liberals swiftly repudiated the ideal of thrift in economics. The downturn, they believed, had been caused by an excess of savings, particularly on the part of the rich; industry was overbuilt, and the only hope for prosperity was to promote the common man's ability, and proclivity, to buy. Stuart Chase was quick to catch the new paradigm. Having published only three years earlier a spirited book in defense of thrift, by 1931 he had almost completely reversed his position. “For what are we accumulating?” Chase asked in a pamphlet entitled *Out of the Depression*. “At what moment in our economic history do we propose to cash in and enjoy the triumph of our thrift?”

The New Deal, as is often noted, began in a spirit of pragmatic experimentation. Though Roosevelt campaigned in 1932 on the promise of a balanced budget, he was not really committed to any particular economic theory: his intention, as he said early on, was to try everything and see what worked. By the end of the first term, the idea that had come to prevail was prosperity through mass consumption, promoted via large deficits, expanded relief, encouragement for organized labor, and other policies that secured the common man against want.

The unfortunate implication—that thrift itself was obsolete, if not socially deviant—was extremely popular, and not only with liberal intellectuals. It became a part of the folk wisdom of the era. Dr. Francis Townsend, promoting his scheme to give every citizen over age 65 a guaranteed monthly check of \$200 (financed by a 2 percent national sales tax), was quick to reassure younger citizens that his plan would benefit them as well. “Every person accepting this

monthly pension," Townsend's proposal stipulated, "shall agree under oath to spend it within the boundaries of the U.S. within 30 days." This free spending by the old, he promised, would bring swift prosperity for all generations. His movement nearly succeeded but was preempted by the passage of the Social Security Act in 1935.

The following year Lord Keynes published his monumental *General Theory of Employment, Money and Interest*. Gauging the book's actual influence on the course of American politics during the 1930s remains tricky, for it was not widely read in this country at the time, even by professional economists. But there is no doubt that Keynes's elegant algebraic demonstrations of the potential imbalance between savings and consumption under laissez-faire capitalism, combined with his fine writing, exalted social standing, and sterling academic credentials, all made a profound impression on certain influential American academics and intellectuals.

Remember, though, that what we now call Keynesianism was flourishing before Keynes's book. Basically, he confirmed popular liberal opinion of the day: excess saving and investment were the major causes of the Depression, and government could provide a cure by incurring large deficits, sponsoring public works projects, and generally redistributing income away from the rich and into the pockets of those more likely to spend it. Keynes, of course, conceived the need for such measures as temporary—at least in his more sober moods. For boom periods, he prescribed that government raise taxes and cut expenditures in order to forestall inflation. But throughout his career, he tended to deemphasize this side of his theory, as did virtually all of his later disciples. As Robert Lekachman would write in the sixties, one of Keynes's significant "successes" was "the weakening of the identification between virtue and thrift."

Were liberals of the 1930s justified in their mounting opposition to thrift? The answer is probably yes, for that point in history. The problem was not so much the New Deal prescription itself as it was the way this particular response to particular economic circumstances took root as a permanent cultural attitude.

Mobilizing for abundance

In the popular estimation of the time, it was the mobilization for World War II that ended the Depression, not the New Deal. While this judgment was a hard point with liberals of the day, it did not upset their arguments against personal

and national thrift. Indeed, the war experience itself seemed to vindicate their idea that the nation could borrow and spend its way to prosperity.

In a 1941 book entitled *Boom or Bust?*, Blair Moody, a progressive U.S. senator from Michigan, articulated the lesson most liberals were taking from that year's sudden recovery, as America armed and fed a warring world: "If government spending on arms can make the factories whirl," Moody asked, "why cannot the factories and farms be made to whirl by the spending of the people...?" "In other words," the senator continued, "if we turn our productive power loose when the war is over, and call overproduction by its real name, under-consumption, why would not that provide the answer for which we are all looking?"

Starting in early 1943, a myriad of public and private commissions as well as individuals began issuing manifestos along this line, including (inevitably) Stuart Chase. "Building up our industrial plants over the past 200 years, it has been inevitable that the producer should have first consideration," Chase said in an address given that May. "But now our plant is substantially built. After the war it looks as though it [will] be super-built. . . . Large sections of our magnificent new plant will just have to stand and rot, unless we develop methods to get its fabulous output into the hands of the people, unless we have mass consumption."

Whereas the home-front experience of World War I had inspired a widespread abhorrence of waste, and an impulse to thrift in peacetime, the country's leading liberal opinion-makers drew an opposite lesson from World War II: the problem of production had been solved, and the nation's primary postwar challenge was to consume. In 1944, Robert Nathan, an economist and rising star among the administration's braintrusts during the war, wrote in *Mobilizing for Abundance* that postwar prosperity would require fundamental changes, not only in the role of government, but also, and more profoundly, in the culture itself. "People find it hard to believe that if they spend more they will have more," Nathan commented.

For Nathan, as for many liberals of the era, the solution, in part, was to expand "social security," as the term was then used in its broadest sense. So long as the mass of Americans remained financially unprotected against the hazards of unemployment, illness, and forced retirement, they would continue to put away

In promoting the consumption we need to stimulate the economy, government and business in the postwar era unfortunately have encouraged habits of high consumption and self-indulgence that are harmful to long-term prosperity.

money for a rainy day. "Nobody is going to spend these accumulated savings if he does not know where next week's income is coming from," argued a social security expert named Eveline Burns. But "if a man has a modest assured income, he may be inclined to spend some of these accumulated savings, as the economists hope he will spend them." In other words, the guiding purpose behind the liberal welfare state was not just to protect the unfortunate against life's exigencies, it was also to depress the savings rate and thereby secure prosperity for all.

The American quarter-century

The early postwar years are well-remembered as an era of national preoccupation with foreign intrigues: the Nuremberg trials, the recriminations over Yalta and the U.N., the Berlin blockade, the loss of China, and the mounting hysteria over communist infiltration of the State Department and other institutions of government. We tend to forget the anxiety most Americans also felt concerning the economy. In 1946, successive strikes against the auto companies, Big Steel, the coal industry, and the railways paralyzed the country, prolonging shortages of many consumer items for many months. Returning servicemen faced an acute housing crisis and a tight job market. Inflation punished everyone. In light of the national experience since 1929, many doubted that the country could avoid depression for long without the stimulus of another major war.

Within just a few short years, however, these worries not only eased, they gave way to unprecedented economic optimism. This was particularly so among liberal intellectuals. For students of the postwar era, one of the most perplexing riddles is how a generation of leading

economists and opinion-makers who had witnessed the surprise and trauma of the great Depression suddenly could become so convinced that the country had entered a new unbounded age of almost automatic affluence.

As it turned out, there was good reason to believe that the country was headed for a prolonged period of prosperity. For the first time in American history, the majority of families would soon own, or at least hold a mortgage on, their own homes; standards of education and health care would improve dramatically; by purchasing on the installment plan, even families with a modest income could soon afford a new car, a television, a dishwasher, garbage disposal, and other household conveniences never dreamed of by the previous generation. Up until roughly the time of the Vietnam war there were persuasive reasons to believe that, as Chase had hinted, the time had come to "cash in on the triumph of our thrift."

First, to many observers, the era between the two wars seemed to be marked by a slow pace of technological development between the two wars. The telephone, the electric light, the airplane, the automobile, the radio—all were invented before the Great War. In the absence of dramatic new inventions, it occurred to people such as Alvin Hansen that capital formation was no longer the pressing concern it once had been. Since the pace of technology had slackened, existing plants and equipment would become obsolete more slowly. The more immediate problem was over-production, which could be cured only by increased consumption.

World War II, of course, brought forth a plethora of new technologies—plastics, jet propulsion, nuclear power—all of which, to be fully pursued, required enormous capital investment. But the war experience also brought forth other, countervailing factors. The baby boom, for example.

The sheer size of this generation seemed to guarantee that the economy would continue to grow, with only a minimum of investment. By the early fifties, the Keynesian notion that consumer demand determined investment was firmly in place and seemed validated by recent experience. Accordingly, many economists were convinced that the baby boom alone would provide long-lasting prosperity; as its members grew older, they would create an ever-expanding market, which, in turn, would automatically call forth new capital investment, as new profit opportunities became available. The prediction turned out to

be accurate for as long as most members of the baby boom were too young to join the labor force.

Conversely, it occurred to many economists (Samuelson prominent among them) that because of the baby boom, the burden of the compounding national debt, as well as the eventual cost of Social Security and other old age benefits for their own generation, would be spread across a greatly expanded younger population. So there did not seem to be much need to promote increased individual saving for retirement nor to feel inhibited, in the arena of public finance about borrowing against future production to fund the welfare state.

"In dispassionately analyzing the growth of the [national] debt, one error we must avoid," Samuelson wrote in the 1955 edition of his textbook. *"We must not forget that the real national product of the United States is an ever-growing thing.* Population increase has slowed down but little, and for a long time our numbers will continue to grow. . . . What seemed like a big debt in 1790 would be nothing today. What our children will come to regard as a big debt, our great-grandchildren may consider relatively unimportant."

Finally, after World War II, there was the obvious observation that America had become the most powerful nation on earth. While there was much anxiety about the communists, few people seriously doubted that the country would succeed in at least containing the threat. Accordingly, the nation's existing industrial base and technological superiority seemed secure, at least until the rest of the world recovered from near total economic ruin. In the end, the hopes for an American Century proved exaggerated, of course. But for a long time, the country could reasonably expect to dominate its trading partners without any special effort.

A permanent deficit

How, then, did liberals of the last generation go wrong in disparaging thrift? One lesson we can take from their experience is to appreciate more fully the fragile relationship between our cultural values and the way we manage or manipulate the economy. Between roughly the mid-1920s and mid-1960s there was, in a narrow, technical sense, good cause to believe that some sort of real imbalance existed between what we could produce on the one hand and consume on the other. But the remedy adopted—the systematic promotion of mass consumption—

led to an erosion of the traditional American values of work, thrift, and self-reliance. For awhile, we could afford to become somewhat more self-indulgent as a people. Today, the ever-increasing sense of entitlement present even in our middle class has become wholly out of joint with the actual productive potential of our economy.

This raises a hard question. We all, I'm sure, feel the tension between the roles of producer and consumer. Capitalism requires, on the one hand, that the mass of citizens be thrifty, hard-working, and willing to defer immediate gratification in order to build up and finance new production. On the other hand, the system sometimes requires—particularly during periods of recession, when profitable investment opportunities decline—that we consume more and more of the surplus that results from our labor and savings, for otherwise there will be no market for new enterprise. In pursuit of that end, government and business can easily wind up encouraging habits of high consumption and self-indulgence that are inimical to the requirements of production and, indeed, to the long-term interests of the society itself.

As Daniel Bell has written, "By the 1950s, the pattern of achievement remained, but it had been redefined to emphasize status and taste. The culture was no longer concerned with how to work and achieve, but with how to spend and enjoy. Despite some continuing use of the language of the Protestant ethic, the fact was that by the 1950s American culture had become primarily hedonistic, concerned with play, fun, display, and pleasure—and, typical of things in America, in a compulsive way."

By the mid-1960s, there remained little in the nation's mainstream culture that could serve as a check against hedonism and self-indulgence. Government policy since the end of the war had promoted a fantastic expansion of consumer installment buying, and had punished savers through a variety of tax measures and banking regulations that diverted credit away from productive uses. The Wagner Act, Social Security, the G.I. Bill, V.A. and F.H.A. mortgage guarantee programs and other federal measures had made a middle-class income and lifestyle possible for millions who otherwise would have remained on the farm or in the old neighborhood. But such policies did not foster—rather, they tended to erode—those familiar bourgeois values of thrift, initiative and self-reliance that are so essential to the workings of capitalism.

No single idea can possibly explain, of course,

the unprecedented revolution of American culture during the 1960s. But surely, many of the predominating values of that decade were inspired, or at least informed, by the vague notion that government could secure lasting affluence for all, without any immediate sacrifice of private consumption. While tenured educators, social critics and presidential advisors spoke incessantly of "the challenge of abundance" and "the miseries of affluence," fiscal policy followed Keynesian prescriptions for reversing depressions, although no depression existed.

Academic economists, for example, celebrated Kennedy's enlightened understanding of "the thrift paradox" after he intentionally ran up the projected deficit in the 1964 budget. The measure, now championed by the supply-siders, stimulated the economy to dizzying new heights; but it also marked a dramatic transformation in our political culture: never again would we find the will as a nation to avoid deficit financing of our annual wants, whether in periods of growth or recession. The actual constituency for thrift in government receded at that moment into a permanent minority.

Lyndon Johnson's decision, in 1966, to meet the mounting cost of the Vietnam war through borrowing rather than by increased taxation sealed the pattern. Even in wartime, Americans learned, there was no longer any need for thrift on the home front, no reason to save up victory bonds, endure rationing, or indeed to make any sort of economic sacrifice. Instead the war brought compounding affluence to those lucky enough to stay home. Success seemed to come with no price in self-denial. As growth came to seem automatic, factional greed met with greater public tolerance, since no claim against the commonweal seemed to come at the expense of any other. The needs for which people used to save—retirement or unemployment, a child's education, buying a house—were now met increasingly by the subsidies and tax benefits of the welfare state.

The most important case in point, as far as public finance was concerned, was that of senior citizens, who, beginning in the late sixties, became increasingly militant and effective in their demands for subsidy as a generation. Between 1969 and 1979, nonmeans-tested federal spending for the elderly nearly quadrupled, from \$38.8 billion to \$148.5 billion. During that same period, the percentage of all federal spending committed to the elderly increased by almost a third, so that by 1979 the 11 percent of the population that was over 65 claimed more than 30 percent of the

entire federal budget.

The largest cause of this jump was increased Social Security and Medicare spending. While the skyrocketing cost of these programs partly resulted from the expanding number of citizens of retirement age, large increases in *individual* benefit levels also played an enormous role. By 1982 a typical Medicare recipient was entitled to benefits worth an estimated 22 times the amount he or she had previously contributed to the system in payroll taxes. But most of the increased spending was consumed by members of the middle class. The expectation of such a bonus—of senior citizens' benefits far in excess of one's contributions during one's working years—was a departure from the traditional idea that ordinary, middle-class Americans should strive to pay their own way through life.

Coincidental with this increased spending for the elderly was a transformation in the prevailing attitude toward retirement itself. Increasingly this came to be seen as a positive time of life—a just reward of leisure, travel, and creative consumption. As late as the 1950s, most older Americans, when polled, regarded retirement as an institution solely for the handicapped or infirm, and accordingly hoped to work for as long as they were physically able. But among the present older generation, this ethos has almost completely disappeared. In 1950 more than half the men over 65 were still in the work force, while today that number has dwindled to one-fifth. The percentage of men retiring before 65 has more than doubled since the mid-1950s, despite dramatic gains in life expectancy. As Frances Fitzgerald has noted: "In the 1960s and seventies, American parents worried about the kids of the Woodstock generation 'dropping out of the system'; in fact, as we now discover, it was their fathers who were dropping out, in droves."

Thrift and civilization

The constellation of self-denying values that made possible our nation's productive achievements and material well-being—preeminently the willingness to defer some present consumption in order to realize greater future happiness—required hundreds of centuries to evolve in the West; such values are still largely absent from the "developing" world, and this, surely, has something to do with its poverty. In America, the most influential members of the present older generation erred by taking the "Victorianism" of their elders too much for granted. It was, in fact, the rarest and most fragile of all

cultural forms, and the true source of our national might over the long haul. Yet intellectuals of the last generation dismissed its utility, railed against its spiritual oppressiveness, and then were soon enough astonished by its almost complete collapse during the 1960s—before many had even realized their own middle age.

In the minds of many Americans, the low growth, rampant inflation, and shortages of the 1970s eventually came to be a kind of symbolic punishment for the nation's excesses during the previous decade. During his first campaign and early years in office, Jimmy Carter played with sincerity and skill to this new spirit of repentance, through self-conscious displays of old-time religion, stern injunctions to thrift in the use of natural resources, and calls for economy in government. During the latter part of the seventies, the rise of the New Right and Ronald Reagan also seemed at first to be animated by the same vague national yearning for a return to traditional values.

But in retrospect, these new currents were more ambiguous than they at first seemed. During the election of 1980, for example, Carter found himself attacked simultaneously as a spendthrift liberal and as a true believer in an anti-American "era of limits." Reagan, while railing against the profligacy of liberalism, promised to reindustrialize and remilitarize the country with no attendant sacrifice of private consumption. Although Reagan never used the word, he excoriated Carter again and again for his counsel of thrift, such as his moralizing pleas that Americans reduce their energy consumption in the national interest. By cutting taxes instead, Reagan promised, he would stimulate new investment and higher consumption, close the budget deficit, and still have money left over for an arms buildup. The American Dream of the postwar era was not over, he seemed to be saying; one could still have one's cake and eat it too.

Today there can be no doubt that Reagan is the true legatee of the ethos of free spending, high consumption, and growth by deficit. His promise of easy affluence is so essentially liberal—as the term has come to be understood since the New Deal—that no matter how extreme and profligate his policies, no present-day liberal can persuasively oppose them—a Democrat of Mondale's age and experience least of all. Under Reagan, Americans have become as dependent on the savings of foreigners to maintain their standard of living as we ever were dependent on foreign sources of energy. Far from routing Keynes from

the temple, Reagan has made him the foundation.

By this late date we must frankly admit that as a nation we cannot continue to subsidize so much present consumption by drawing upon the future. We must once again submit to a regime of thrift, or else find more and more of our options as a society constrained by debt service and slow growth. This means not only that Americans must save more, but that we must use the resulting pool of capital for productive purposes rather than for financing credit card purchases, real estate deals, corporate takeovers or the mounting cost of entitlement programs. One person's "savings" are of little net social benefit if they merely feed someone else's gold speculation or consumer debt. Members of the middle class, in particular, need to return to a stance of self-reliance—saving during their middle years to meet the real cost of their retirement, rather than depending so much on the next generation to subsidize their "golden years."

There are, I think, reasons for cautious optimism in this regard. The recent rehabilitation of the entrepreneur is a hopeful sign, while the baby boom's oft-noted demand for high-quality, "useful" products—a phenomenon that has become the bane of many mass marketers—may betoken a certain generational rejection of the mass-consumption ethos.

Again, the values of stewardship and husbandry embodied in the environmental movement may be part of a quickening sense of responsibility to future generations that can be made to apply in matters of public and personal finance as well. Finally, the increasing fascination with high-technology works against the old paradigm of a fully matured economy of abundance requiring little capital investment.

In the end, the proper rate of savings is determined not by utility functions nor by statistical comparisons with the past, but by the real cost of our ambitions for the future. It is not necessary, nor even desirable, that we become a nation of stern Victorians. Samuelson was right to teach America's college students that too much thrift could, paradoxically, be a social vice in economic hard times. But we need to weigh our present appetites in the balance against our financial responsibility to future generations, as well as to our future selves; and we need tax and banking policies that reflect this necessity. While peculiar economic conditions may have allowed the last generation to succeed for a while without regard for thrift, younger Americans will not get away with repeating their example. ■

*Many copies
on Reserve*

deposits

The Fall of The Idea of THRIFT

*How the economists came
to label virtue a vice*



WHO'S WHO in the Administration

Did you scratch your head when the White House proposed that Reagan and other top officials take a 10 percent pay cut? Did they at last see the point of having those who are well-off share in the sacrifices they ask of others? Unfortunately the answer is no. The idea didn't come from Reagan or any member of his staff. It was **Bob Dole's**. . . .

Samuel B. Pierce Jr., the secretary of Housing and Urban Development, is said to be planning to leave within the next year to resume the practice of law with his old New York firm. A good many administration lawyers have similar timetables for their exits. The financial rewards of the law tend to fall most generously on those who leave while their old administration friends still have a few years left in power. That way the departing lawyer—and his potential clients—know that he still has the right phone numbers. . . .

Our sources tell us that the White House will try to satisfy **Jeanne Kirkpatrick's** frustrated ambition, which has led her to announce that she will return to private life, with a manufactured job that will sound impressive but will not give her the power she wants. The negative word about her at the White House is that she's indiscreet. . . .

In

DEFENSE

Principal Deputy Assistant Secretary for Public Affairs—**Fred S. Hoffman** has been a Pentagon correspondent for the Associated Press.

STATE

Assistant Secretary for Public Affairs and Department Spokesman—**Bernard Kalb** has been State Department correspondent for NBC News.

TREASURY

Deputy Assistant Secretary for Public Affairs—**Roger Bolton** was director of speechwriting for Reagan-Bush '84.

AGENCIES AND COMMISSIONS

Postmaster General, United States Postal Service—**Paul N. Carlin** has been the Chicago regional postmaster.

Administrator, Environmental Protection Agency—**Lee M. Thomas** has been assistant administrator in charge of the agency's hazardous waste programs.

Out

AGRICULTURE

Deputy Secretary—**Richard E. Lyng** will resign. Assistant Secretary for Economics—**William G. Leshner** is resigning.

Assistant Secretary for Natural Resources and Environment—**John B. Crowell Jr.** is returning to Portland, Oregon to practice law.

HEALTH AND HUMAN SERVICES

The man most likely to replace **Nancy Harvey Steorts** as chairman of the Consumer Product Safety Commission is Commissioner **Terrence M. Scanlon**. Scanlon's a Democrat, but his politics have not endeared him to the consumer movement. For example he was the only member of the commission who voted to allow companies to export products that CPSC deemed unsafe for Americans. . . .

The Reagan White House continues to live out the worst nightmares of Moral Majoritarians in the conduct of various high officials' private lives. One prominent male member of the White House staff took a trip while the president was in Santa Barbara. The official word given the White House press corps was that he was on a brief vacation. The reporters knew he was in the company of a young woman who was not his wife—that is, all but one of them did. That reporter sent out a story over the wires that mentioned the staff member's being on vacation. His wife had been under the impression that he was hard at work and was not amused. At the same time a senior male member of the national security staff has been carrying on simultaneously with a female subordinate and a female television reporter. . . .

Assistant Secretary for Legislation—**John F. Scruggs** is joining the lobbying firm of Gold and Liebengold, Inc.

HOUSING AND URBAN DEVELOPMENT

Undersecretary—**Philip D. Abrams** is leaving to establish a building and construction company in Denver, Colorado.

INTERIOR

Assistant Secretary for Land and Mineral Management—**Garrey E. Carruthers** will teach at New Mexico State University.

Assistant Secretary for Indian Affairs—**Kenneth L. Smith** is returning to his Oregon ranch.

Director, National Park Service—**Russell E. Dickenson** will retire and serve on the National Parks Advisory Board.

STATE

Assistant Secretary for Public Affairs and Department Spokesman—**John Hughes** is resigning to return to journalism.

TREASURY

Deputy Treasurer—**David Q. Bates** will join the Washington office of the Houston law firm of Reynolds, Allen & Cook.

AGENCIES AND COMMISSIONS

Administrator, Environmental Protection Agency—**William D. Ruckelshaus** has resigned.

Chairman, Consumer Product Safety Commission—**Nancy Harvey Steorts** has resigned.

Chairman, Civil Aeronautics Board—**Dan McKinnon** left on December 31. The agency closed that day.

~g.byron peck~
8/1

1923

1945

1957



by Phillip Longman

During the early months of 1958, as the unemployment rate approached a new postwar high of 6.8 percent and business profits slumped, the Eisenhower administration found itself besieged from all quarters with demands that it take drastic action to avert the coming depression. Ike listened to the prophets of crisis, and chose his course: he twice went before the public to admonish that it was Americans' patriotic duty to save less and to Buy Now.

Phillip Longman is a Princeton, New Jersey, writer.
Illustration by Byron Peck

Advertisers across the country immediately seized upon this happy new presidential theme, launching hundreds of "confidence" or "prosperity" drives to reinforce Ike's message to the consumer. An association of Cleveland auto dealers invented the slogan "YOUAUTOBUY"—later adopted by the whole industry—and was quickly rewarded with invitations to the White House and a favorable mention at Ike's weekly news conference. Businessmen in Boston offered "POPS," for "Power of Positive Selling"; Cleveland city fathers elected a "Miss Prosperity" to reign over antirecession parades and street rallies.

In April *The Wall Street Journal* reported that "a massive antirecession psychological offensive... is just getting under way in nearly every major city in the U.S. Already in existence are 'Operation Optimism,' 'Keep Detroit Dynamic,' 'Crusade for Confidence,' 'Buy and Be Happy,' and 'O.K. Ike.'" Even the banks joined in the siren call, abandoning their usual admonishments to thrift. "Ah gwan," the Bank of Saint Louis urged in a Sunday newspaper ad, "buy that new car." Another bank in St. Louis had a similar message for would-be savers: "In times such as these, excessive savings can be as harmful as excessive spending." Auto dealers in Essex County, New Jersey, according to the *Journal*, mounted a joint radio campaign to warn the public: "Buy Now. The Job You Save May Be Your Own." Elsewhere in New Jersey, a tire store used the slogan "Buy, Buy, Buy," adding, "It's your patriotic duty."

Out of such raw material was woven that great, wooly, socio-economic paradigm of the 1950s: the idea of the Mass Consumption Society. Ike's faith in the power of positive selling was evidence of a powerful, new, bi-partisan consensus in American economic thought: that, for better or for worse, the nation's future prosperity no longer depended much on individual savings, hard work, or initiative but more on the present population's propensity to consume.

A penny spent

In the 1870's a most eminent Victorian and popular moralist, Samuel Smiles, became famous for his lively defense of the opposing notion, then the orthodoxy of the striving middle classes in both Europe and America. "It is the savings of the individual which compose the wealth—in other words, the well-being of every nation," Smiles asserted in a relentless volume entitled simply, *Thrift*. "On the other hand, it is the

wastefulness of individuals which occasions the impoverishment of states. So it is that every thrifty person may be regarded as a public benefactor, and every thriftless person as a public enemy." For Smiles, as for most Americans of his era, individual thrift was not only a virtue in itself; its widespread practice was considered a first requisite of civilization and nation-building.

Why is it that today, such adulation of individual thrift is virtually absent from our economic debate? Oddly, it is still official U.S. policy to encourage many other nations to submit their citizens to a strict regime of thrift. In the cases of Brazil and Mexico, for example, we have been quick to call for "austerity plans" as a condition for further credit. When it comes to others, we readily acknowledge that no nation can continually borrow in order to finance personal consumption; we insist, in effect, that the citizens of these debtor countries adhere to an ethos of thrift, as our Victorian forebears once did, to furnish capital necessary for economic growth. Yet even as the U.S. is now rapidly reverting to its nineteenth-century status as a net debtor nation, no one here is proposing that we once again celebrate individual thrift as a social virtue.

Instead, we debate the size of the federal deficit, the money supply, the value of the dollar, tax rates and other technical, microeconomic factors. Yet our present debt crisis is also bound up with what John Maynard Keynes liked to call "the habits of the community"—specifically, in the general demise of the thrift ethos over the last generation. Consider, for example, that despite the enormous federal deficits incurred under Reagan, the amount owed by individual debtors (approximately \$1.7 trillion) is still, as of this writing, greater than the national debt. During just the past four years, consumer installment buying has increased by almost 30 percent. In the first half of 1984, mortgage and consumer borrowing together absorbed more than 38 percent of all funds raised in the U.S. credit markets. The debts of people, no less than those of the state, are depleting the supply, and running up the cost, of capital available for productive purposes.

That even middle-class citizens now typically neglect to save enough to pay their own way through retirement or to be secure against even a small reversal of fortune causes a clamor for "entitlements," which of course prompts in turn still more public borrowing. These trends argue for a fundamental change in our thinking about the respective roles of individual savings and consumption in our society. Such changes, however,

The thrift ethos hasn't always been the province of Wall Street Republicans. During the twenties the liberal Thrift Movement promoted values and themes that presaged the environmental movement of today.

will not come easily. Despite their new "supply-side" rhetoric, conservatives have, by and large, renounced their traditional role as defenders of the thrift ethos, celebrating instead the idea that the nation can borrow and spend its way to lasting prosperity. (See "What the Democrats Could Learn from Jack Kemp," page 28.) Yet for liberals, especially, the question of how best to oppose this spend-thrift policy poses tremendous difficulties. At their root is liberalism's longstanding ambivalence about the purposes of thrift.

Can an ethos of capital stewardship, of principled regard for the financial and economic interests of future generations, be reconciled with the prevailing values and attitudes of modern day liberalism? Or must such questions always be the province of economic royalists—Wall Street Republicans and other rentiers? It is useful to recall that an important precedent for a thrift ethic does exist within the liberal tradition itself.

The reign of the stewards

The Thrift Movement, as it was called, reached its apex in this country, as well as in England, during the early 1920s. In many respects, its values and themes presaged those of the environmental movement of our own time, but with

a significant difference. The partisans of Thrift abhorred waste and applauded conservation, but unlike today's conservationists, extended their values to the arena of finance. It was an ethos directly inspired by the conduct of the Great War.

In 1920, the editors of *The Annals of the American Academy of Political and Social Science* devoted a special issue to the Thrift Movement. In an introductory essay, economist Roy G. Blakey explained the philosophy of the cause and its origins in the homefront experience of the Great War. "Many realized for the first time that it was a matter of life and death to thousands of soldiers and of civilians also, whether they wasted or whether they conserved food and fuel," Blakey wrote. "Instead of suggesting stinginess, it came to connote proper use. . . . It was closely associated with effectiveness, loyalty, patriotism, victory."

The Thrift Movement was an odd fusion of many diverse interests and constituencies. Andrew Mellon was an outspoken apostle of the cause; so was Stuart Chase, the well-known author and perennial weathervane of fashionable liberal opinion, who in 1928 wrote a popular book called *Waste*. "We are deluged with things," Chase complained, "which we do not wear, which we lose, which go out of style, which disappear anyhow. . . endless jiggers and doodads and contrivances. Here, it seems, the advertiser plays on the essential monkey within us—grabbing for a rose only to pick it to pieces, petal by petal."

Professional social workers of the era, as well as many partisans of the labor movement, also promoted the ideal of thrift or its variant, "wise spending," convinced that it was the surest way for members of the working class to help themselves. Samuel Crowther, in his 1920 book, *Why Men Strike*, connected the thriftiness of the working class to broader social concerns. Universal thrift, he argued, would "not only destroy the budding idea of the proletariat, but also provide ever-increasing facilities for higher production at higher wages. . . . [It] transforms the man from a mere industrial parasite into a sturdy member of society." In his popular *Book of Thrift*, T. D. MacGregor cast the movement in terms of the class struggle. "We the everyday men and women are the backbone of this country," MacGregor wrote. "Let us economize! Let us save! Let us do our share in making this country the great financial power of the world! Our millions of workers can do this, not the capitalists!"

Between 1912 and 1924, the amount of money deposited in savings banks increased more than



Little AMERICANS *Do your bit*

Eat Oatmeal-Corn meal mush-
Hominy - other corn cereals -
and Rice with milk.

Save the wheat for our soldiers.

Leave nothing on your plate



UNITED STATES FOOD ADMINISTRATION

two and a half times, according to a contemporary survey by the American Bankers Association; the per capita savings rate nearly doubled, from \$89 to \$186. While much of this new thrift was attributed at the time to the aggressive marketing campaigns waged by the nation's banks and insurance companies, as well as to the general rise of wages over inflation, it was also commonly accepted that the new impulse to save was inspired in large part by a genuine social ethos of self-help, conservation, and stewardship.

Capitalist counterpunch

Why did the Thrift Movement fade? Given the threat the cause posed to the immediate interests of mass merchandisers, it is not surprising that the initial assaults came from capitalist quarters—principally from retailers, who found it increasingly difficult to unload their more impractical wares. In 1926, a business group calling itself the National Prosperity Bureau sprang into existence to promote easy spending and thereby counter this threat. As bemusedly reported by *The Nation*, the Bureau was “getting up at four o'clock these cold winter mornings to plaster our shop windows with posters of a figure of Uncle Sam sitting at the throttle of a locomotive. Surrounding him is the inscription: ‘Full speed ahead! Clear the track for prosperity! Buy what you need now!’”

The same sentiment emerged in an article in the *The Atlantic Monthly* that same year. Entitled “The Dilemma of Thrift,” and written by William T. Foster, a former president of Reed College, and a businessman named Waddill Catchings, the article bestowed new intellectual respectability upon the idea that extravagant spending was now the nation's best guarantee of prosperity. “What a mess we get into!” the authors complained. “We celebrate ‘Buyers Week’ and ‘Thrift Week’ at one and the same time. By investing our savings, instead of spending them, we deny ourselves today in order to produce more in the future, although we are already equipped to produce more than we know how to use. . . .” The consumer clearly was the hero under this analysis, while the saver enriched himself at the expense of the common good.

While this formulation was widely and vigorously condemned as heresy at the time, it soon enough became a point of liberal orthodoxy, the first premise of the New Deal economics and of the post-war consumer society. Anyone who has endured freshman economics during the last 30 or so years has probably encountered it in Paul

A. Samuelson's all-time best-selling college textbook, *Economics*—the “paradox of thrift.” In the 1964 edition of his text, Samuelson instructed, “What once was a social virtue [i.e., savings] may [in times of depression] become a social vice.” What is true for the individual—that extra thriftiness means increased savings and wealth—may then become completely untrue for the community as a whole.”

Keynes to the kingdom

During the Depression years, the Thrift Movement's emphasis on conservation of natural resources remained an important influence on mainstream liberalism. (There was the Civilian Conservation Corps, for example, and numerous New Deal bureaucracies dedicated to the problems of soil erosion and forest management.) But after the shock in 1929, most liberals swiftly repudiated the ideal of thrift in economics. The downturn, they believed, had been caused by an excess of savings, particularly on the part of the rich; industry was overbuilt, and the only hope for prosperity was to promote the common man's ability, and proclivity, to buy. Stuart Chase was quick to catch the new paradigm. Having published only three years earlier a spirited book in defense of thrift, by 1931 he had almost completely reversed his position. “For what are we accumulating?” Chase asked in a pamphlet entitled *Out of the Depression*. “At what moment in our economic history do we propose to cash in and enjoy the triumph of our thrift?”

The New Deal, as is often noted, began in a spirit of pragmatic experimentation. Though Roosevelt campaigned in 1932 on the promise of a balanced budget, he was not really committed to any particular economic theory: his intention, as he said early on, was to try everything and see what worked. By the end of the first term, the idea that had come to prevail was prosperity through mass consumption, promoted via large deficits, expanded relief, encouragement for organized labor, and other policies that secured the common man against want.

The unfortunate implication—that thrift itself was obsolete, if not socially deviant—was extremely popular, and not only with liberal intellectuals. It became a part of the folk wisdom of the era. Dr. Francis Townsend, promoting his scheme to give every citizen over age 65 a guaranteed monthly check of \$200 (financed by a 2 percent national sales tax), was quick to reassure younger citizens that his plan would benefit them as well. “Every person accepting this

monthly pension," Townsend's proposal stipulated, "shall agree under oath to spend it within the boundaries of the U.S. within 30 days." This free spending by the old, he promised, would bring swift prosperity for all generations. His movement nearly succeeded but was preempted by the passage of the Social Security Act in 1935.

The following year Lord Keynes published his monumental *General Theory of Employment, Money and Interest*. Gauging the book's actual influence on the course of American politics during the 1930s remains tricky, for it was not widely read in this country at the time, even by professional economists. But there is no doubt that Keynes's elegant algebraic demonstrations of the potential imbalance between savings and consumption under laissez-faire capitalism, combined with his fine writing, exalted social standing, and sterling academic credentials, all made a profound impression on certain influential American academics and intellectuals.

Remember, though, that what we now call Keynesianism was flourishing before Keynes's book. Basically, he confirmed popular liberal opinion of the day: excess saving and investment were the major causes of the Depression, and government could provide a cure by incurring large deficits, sponsoring public works projects, and generally redistributing income away from the rich and into the pockets of those more likely to spend it. Keynes, of course, conceived the need for such measures as temporary—at least in his more sober moods. For boom periods, he prescribed that government raise taxes and cut expenditures in order to forestall inflation. But throughout his career, he tended to deemphasize this side of his theory, as did virtually all of his later disciples. As Robert Lekachman would write in the sixties, one of Keynes's significant "successes" was "the weakening of the identification between virtue and thrift."

Were liberals of the 1930s justified in their mounting opposition to thrift? The answer is probably yes, for that point in history. The problem was not so much the New Deal prescription itself as it was the way this particular response to particular economic circumstances took root as a permanent cultural attitude.

Mobilizing for abundance

In the popular estimation of the time, it was the mobilization for World War II that ended the Depression, not the New Deal. While this judgment was a hard point with liberals of the day, it did not upset their arguments against personal

and national thrift. Indeed, the war experience itself seemed to vindicate their idea that the nation could borrow and spend its way to prosperity.

In a 1941 book entitled *Boom or Bust?*, Blair Moody, a progressive U.S. senator from Michigan, articulated the lesson most liberals were taking from that year's sudden recovery, as America armed and fed a warring world: "If government spending on arms can make the factories whir," Moody asked, "why cannot the factories and farms be made to whir by the spending of the people. . . ?" "In other words," the senator continued, "if we turn our productive power loose when the war is over, and call overproduction by its real name, under-consumption, why would not that provide the answer for which we are all looking?"

Starting in early 1943, a myriad of public and private commissions as well as individuals began issuing manifestos along this line, including (inevitably) Stuart Chase. "Building up our industrial plants over the past 200 years, it has been inevitable that the producer should have first consideration," Chase said in an address given that May. "But now our plant is substantially built. After the war it looks as though it [will] be superbuilt. . . . Large sections of our magnificent new plant will just have to stand and rot, unless we develop methods to get its fabulous output into the hands of the people, unless we have mass consumption."

Whereas the home-front experience of World War I had inspired a widespread abhorrence of waste, and an impulse to thrift in peacetime, the country's leading liberal opinion-makers drew an opposite lesson from World War II: the problem of production had been solved, and the nation's primary postwar challenge was to consume. In 1944, Robert Nathan, an economist and rising star among the administration's braintrusts during the war, wrote in *Mobilizing for Abundance* that postwar prosperity would require fundamental changes, not only in the role of government, but also, and more profoundly, in the culture itself. "People find it hard to believe that if they spend more they will have more," Nathan commented.

For Nathan, as for many liberals of the era, the solution, in part, was to expand "social security," as the term was then used in its broadest sense. So long as the mass of Americans remained financially unprotected against the hazards of unemployment, illness, and forced retirement, they would continue to put away

In promoting the consumption we need to stimulate the economy, government and business in the postwar era unfortunately have encouraged habits of high consumption and self-indulgence that are harmful to long-term prosperity.

money for a rainy day. "Nobody is going to spend these accumulated savings if he does not know where next week's income is coming from," argued a social security expert named Eveline Burns. But "if a man has a modest assured income, he may be inclined to spend some of these accumulated savings, as the economists hope he will spend them." In other words, the guiding purpose behind the liberal welfare state was not just to protect the unfortunate against life's exigencies, it was also to depress the savings rate and thereby secure prosperity for all.

The American quarter-century

The early postwar years are well-remembered as an era of national preoccupation with foreign intrigues: the Nuremberg trials, the recriminations over Yalta and the U.N., the Berlin blockade, the loss of China, and the mounting hysteria over communist infiltration of the State Department and other institutions of government. We tend to forget the anxiety most Americans also felt concerning the economy. In 1946, successive strikes against the auto companies, Big Steel, the coal industry, and the railways paralyzed the country, prolonging shortages of many consumer items for many months. Returning servicemen faced an acute housing crisis and a tight job market. Inflation punished everyone. In light of the national experience since 1929, many doubted that the country could avoid depression for long without the stimulus of another major war.

Within just a few short years, however, these worries not only eased, they gave way to unprecedented economic optimism. This was particularly so among liberal intellectuals. For students of the postwar era, one of the most perplexing riddles is how a generation of leading

economists and opinion-makers who had witnessed the surprise and trauma of the great Depression suddenly could become so convinced that the country had entered a new unbounded age of almost automatic affluence.

As it turned out, there was good reason to believe that the country was headed for a prolonged period of prosperity. For the first time in American history, the majority of families would soon own, or at least hold a mortgage on, their own homes; standards of education and health care would improve dramatically; by purchasing on the installment plan, even families with a modest income could soon afford a new car, a television, a dishwasher, garbage disposal, and other household conveniences never dreamed of by the previous generation. Up until roughly the time of the Vietnam war there were persuasive reasons to believe that, as Chase had hinted, the time had come to "cash in on the triumph of our thrift."

First, to many observers, the era between the two wars seemed to be marked by a slow pace of technological development between the two wars. The telephone, the electric light, the airplane, the automobile, the radio—all were invented before the Great War. In the absence of dramatic new inventions, it occurred to people such as Alvin Hansen that capital formation was no longer the pressing concern it once had been. Since the pace of technology had slackened, existing plants and equipment would become obsolete more slowly. The more immediate problem was over-production, which could be cured only by increased consumption.

World War II, of course, brought forth a plethora of new technologies—plastics, jet propulsion, nuclear power—all of which, to be fully pursued, required enormous capital investment. But the war experience also brought forth other, countervailing factors. The baby boom, for example.

The sheer size of this generation seemed to guarantee that the economy would continue to grow, with only a minimum of investment. By the early fifties, the Keynesian notion that consumer demand determined investment was firmly in place and seemed validated by recent experience. Accordingly, many economists were convinced that the baby boom alone would provide long-lasting prosperity; as its members grew older, they would create an ever-expanding market, which, in turn, would automatically call forth new capital investment, as new profit opportunities became available. The prediction turned out to

be accurate for as long as most members of the baby boom were too young to join the labor force.

Conversely, it occurred to many economists (Samuelson prominent among them) that because of the baby boom, the burden of the compounding national debt, as well as the eventual cost of Social Security and other old age benefits for their own generation, would be spread across a greatly expanded younger population. So there did not seem to be much need to promote increased individual saving for retirement nor to feel inhibited, in the arena of public finance about borrowing against future production to fund the welfare state.

"In dispassionately analyzing the growth of the [national] debt, one error we must avoid," Samuelson wrote in the 1955 edition of his textbook. *"We must not forget that the real national product of the United States is an ever-growing thing.* Population increase has slowed down but little, and for a long time our numbers will continue to grow. . . . What seemed like a big debt in 1790 would be nothing today. What our children will come to regard as a big debt, our great-grandchildren may consider relatively unimportant."

Finally, after World War II, there was the obvious observation that America had become the most powerful nation on earth. While there was much anxiety about the communists, few people seriously doubted that the country would succeed in at least containing the threat. Accordingly, the nation's existing industrial base and technological superiority seemed secure, at least until the rest of the world recovered from near total economic ruin. In the end, the hopes for an American Century proved exaggerated, of course. But for a long time, the country could reasonably expect to dominate its trading partners without any special effort.

A permanent deficit

How, then, did liberals of the last generation go wrong in disparaging thrift? One lesson we can take from their experience is to appreciate more fully the fragile relationship between our cultural values and the way we manage or manipulate the economy. Between roughly the mid-1920s and mid-1960s there was, in a narrow, technical sense, good cause to believe that some sort of real imbalance existed between what we could produce on the one hand and consume on the other. But the remedy adopted—the systematic promotion of mass consumption—

led to an erosion of the traditional American values of work, thrift, and self-reliance. For awhile, we could afford to become somewhat more self-indulgent as a people. Today, the ever-increasing sense of entitlement present even in our middle class has become wholly out of joint with the actual productive potential of our economy.

This raises a hard question. We all, I'm sure, feel the tension between the roles of producer and consumer. Capitalism requires, on the one hand, that the mass of citizens be thrifty, hard-working, and willing to defer immediate gratification in order to build up and finance new production. On the other hand, the system sometimes requires—particularly during periods of recession, when profitable investment opportunities decline—that we consume more and more of the surplus that results from our labor and savings, for otherwise there will be no market for new enterprise. In pursuit of that end, government and business can easily wind up encouraging habits of high consumption and self-indulgence that are inimical to the requirements of production and, indeed, to the long-term interests of the society itself.

As Daniel Bell has written, "By the 1950s, the pattern of achievement remained, but it had been redefined to emphasize status and taste. The culture was no longer concerned with how to work and achieve, but with how to spend and enjoy. Despite some continuing use of the language of the Protestant ethic, the fact was that by the 1950s American culture had become primarily hedonistic, concerned with play, fun, display, and pleasure—and, typical of things in America, in a compulsive way."

By the mid-1960s, there remained little in the nation's mainstream culture that could serve as a check against hedonism and self-indulgence. Government policy since the end of the war had promoted a fantastic expansion of consumer installment buying, and had punished savers through a variety of tax measures and banking regulations that diverted credit away from productive uses. The Wagner Act, Social Security, the G.I. Bill, V.A. and F.H.A. mortgage guarantee programs and other federal measures had made a middle-class income and lifestyle possible for millions who otherwise would have remained on the farm or in the old neighborhood. But such policies did not foster—rather, they tended to erode—those familiar bourgeois values of thrift, initiative and self-reliance that are so essential to the workings of capitalism.

No single idea can possibly explain, of course,

the unprecedented revolution of American culture during the 1960s. But surely, many of the predominating values of that decade were inspired, or at least informed, by the vague notion that government could secure lasting affluence for all, without any immediate sacrifice of private consumption. While tenured educators, social critics and presidential advisors spoke incessantly of "the challenge of abundance" and "the miseries of affluence," fiscal policy followed Keynesian prescriptions for reversing depressions, although no depression existed.

Academic economists, for example, celebrated Kennedy's enlightened understanding of "the thrift paradox" after he intentionally ran up the projected deficit in the 1964 budget. The measure, now championed by the supply-siders, stimulated the economy to dizzying new heights; but it also marked a dramatic transformation in our political culture: never again would we find the will as a nation to avoid deficit financing of our annual wants, whether in periods of growth or recession. The actual constituency for thrift in government receded at that moment into a permanent minority. *a bum rap ... Nixon's the one*

Lyndon Johnson's decision, in 1966, to meet the mounting cost of the Vietnam war through borrowing rather than by increased taxation sealed the pattern. Even in wartime, Americans learned, there was no longer any need for thrift on the home front, no reason to save up victory bonds, endure rationing, or indeed to make any sort of economic sacrifice. Instead the war brought compounding affluence to those lucky enough to stay home. Success seemed to come with no price in self-denial. As growth came to seem automatic, factional greed met with greater public tolerance, since no claim against the commonweal seemed to come at the expense of any other. The needs for which people used to save—retirement or unemployment, a child's education, buying a house—were now met increasingly by the subsidies and tax benefits of the welfare state.

The most important case in point, as far as public finance was concerned, was that of senior citizens, who, beginning in the late sixties, became increasingly militant and effective in their demands for subsidy as a generation. Between 1969 and 1979, nonmeans-tested federal spending for the elderly nearly quadrupled, from \$38.8 billion to \$148.5 billion. During that same period, the percentage of all federal spending committed to the elderly increased by almost a third, so that by 1979 the 11 percent of the population that was over 65 claimed more than 30 percent of the

entire federal budget.

The largest cause of this jump was increased Social Security and Medicare spending. While the skyrocketing cost of these programs partly resulted from the expanding number of citizens of retirement age, large increases in individual benefit levels also played an enormous role. By 1982 a typical Medicare recipient was entitled to benefits worth an estimated 22 times the amount he or she had previously contributed to the system in payroll taxes. But most of the increased spending was consumed by members of the middle class. The expectation of such a bonus—of senior citizens' benefits far in excess of one's contributions during one's working years—was a departure from the traditional idea that ordinary, middle-class Americans should strive to pay their own way through life.

Coincidental with this increased spending for the elderly was a transformation in the prevailing attitude toward retirement itself. Increasingly this came to be seen as a positive time of life—a just reward of leisure, travel, and creative consumption. As late as the 1950s, most older Americans, when polled, regarded retirement as an institution solely for the handicapped or infirm, and accordingly hoped to work for as long as they were physically able. But among the present older generation, this ethos has almost completely disappeared. In 1950 more than half the men over 65 were still in the work force, while today that number has dwindled to one-fifth. The percentage of men retiring before 65 has more than doubled since the mid-1950s, despite dramatic gains in life expectancy. As Frances Fitzgerald has noted: "In the 1960s and seventies, American parents worried about the kids of the Woodstock generation 'dropping out of the system'; in fact, as we now discover, it was their fathers who were dropping out, in droves."

Thrift and civilization

The constellation of self-denying values that made possible our nation's productive achievements and material well-being—preeminently the willingness to defer some present consumption in order to realize greater future happiness—required hundreds of centuries to evolve in the West; such values are still largely absent from the "developing" world, and this, surely, has something to do with its poverty. In America, the most influential members of the present older generation erred by taking the "Victorianism" of their elders too much for granted. It was, in fact, the rarest and most fragile of all

cultural forms, and the true source of our national might over the long haul. Yet intellectuals of the last generation dismissed its utility, railed against its spiritual oppressiveness, and then were soon enough astonished by its almost complete collapse during the 1960s—before many had even realized their own middle age.

In the minds of many Americans, the low growth, rampant inflation, and shortages of the 1970s eventually came to be a kind of symbolic punishment for the nation's excesses during the previous decade. During his first campaign and early years in office, Jimmy Carter played with sincerity and skill to this new spirit of repentance, through self-conscious displays of old-time religion, stern injunctions to thrift in the use of natural resources, and calls for economy in government. During the latter part of the seventies, the rise of the New Right and Ronald Reagan also seemed at first to be animated by the same vague national yearning for a return to traditional values.

But in retrospect, these new currents were more ambiguous than they at first seemed. During the election of 1980, for example, Carter found himself attacked simultaneously as a spendthrift liberal and as a true believer in an anti-American "era of limits." Reagan, while railing against the profligacy of liberalism, promised to reindustrialize and remilitarize the country with no attendant sacrifice of private consumption. Although Reagan never used the word, he excoriated Carter again and again for his counsel of thrift, such as his moralizing pleas that Americans reduce their energy consumption in the national interest. By cutting taxes instead, Reagan promised, he would stimulate new investment and higher consumption, close the budget deficit, and still have money left over for an arms buildup. The American Dream of the postwar era was not over, he seemed to be saying; one could still have one's cake and eat it too.

✓ Today there can be no doubt that Reagan is the true legatee of the ethos of free spending, high consumption, and growth by deficit. His promise of easy affluence is so essentially liberal—as the term has come to be understood since the New Deal—that no matter how extreme and profligate his policies, no present-day liberal can persuasively oppose them—a Democrat of Mondale's age and experience least of all. Under Reagan, Americans have become as dependent on the savings of foreigners to maintain their standard of living as we ever were dependent on foreign sources of energy. Far from routing Keynes from

the temple, Reagan has made him the foundation.

By this late date we must frankly admit that as a nation we cannot continue to subsidize so much present consumption by drawing upon the future. We must once again submit to a regime of thrift, or else find more and more of our options as a society constrained by debt service and slow growth. This means not only that Americans must save more, but that we must use the resulting pool of capital for productive purposes rather than for financing credit card purchases, real estate deals, corporate takeovers or the mounting cost of entitlement programs. One person's "savings" are of little net social benefit if they merely feed someone else's gold speculation or consumer debt. Members of the middle class, in particular, need to return to a stance of self-reliance—saving during their middle years to meet the real cost of their retirement, rather than depending so much on the next generation to subsidize their "golden years."

There are, I think, reasons for cautious optimism in this regard. The recent rehabilitation of the entrepreneur is a hopeful sign, while the baby boom's oft-noted demand for high-quality, "useful" products—a phenomenon that has become the bane of many mass marketers—may betoken a certain generational rejection of the mass-consumption ethos.

Again, the values of stewardship and husbandry embodied in the environmental movement may be part of a quickening sense of responsibility to future generations that can be made to apply in matters of public and personal finance as well. Finally, the increasing fascination with high-technology works against the old paradigm of a fully matured economy of abundance requiring little capital investment.

In the end, the proper rate of savings is determined not by utility functions nor by statistical comparisons with the past, but by the real cost of our ambitions for the future. It is not necessary, nor even desirable, that we become a nation of stern Victorians. Samuelson was right to teach America's college students that too much thrift could, paradoxically, be a social vice in economic hard times. But we need to weigh our present appetites in the balance against our financial responsibility to future generations, as well as to our future selves; and we need tax and banking policies that reflect this necessity. While peculiar economic conditions may have allowed the last generation to succeed for a while without regard for thrift, younger Americans will not get away with repeating their example. ■

Huge Marketing Push for Credit Cards

By JOHN M. BRODER,
Times Staff Writer

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V-1

HIGHEST DOLLAR VOLUME

Issuer	1984 transactions in billions
1. American Express	\$38.20
2. Citicorp*	14.16
3. Sears Stores	13.60
4. Montgomery Ward Stores	7.42
5. Bank of America	6.26
6. J.C. Penney Stores	5.89
7. AT&T Telephone	5.80
8. Shell Oil	3.73
9. First of Chicago Bank	3.30
10. Amoco Oil	3.23

*Citicorp includes Visa, MasterCard, Diners, Carte Blanche, Choice & Private Label.

MOST USED

Issuer	Number of transactions in millions
1. American Express	461
2. Sears Stores	365
3. Citicorp*	360
4. AT&T Telephone	323
5. Montgomery Ward Stores	204
6. Shell Oil	197
7. Amoco Oil	186
8. Texaco Oil	179
9. J.C. Penney Stores	165
10. Exxon Oil	162

Source: The Nilson Report

Watch your wallet. The plastic pushers are on the prowl.

Financial and retail behemoths, led by Citicorp, Sears and American Express, are stuffing mailboxes and flooding the airwaves with sales spiels for their credit cards.

Driven by brisk consumer credit spending and fat profit margins, the card merchants are spending hundreds of millions of dollars to persuade consumers to take their card and use it.

But beneath the glib television ads and the enticing direct-mail appeals lies a quiet, long-term strategy that promises to change the structure of American consumer finance. The three giants are becoming, in effect, nationwide banks built on plastic.

Bought Small Banks

"It's their way of getting into interstate banking by first getting their card in your pocket," said John H. Bennett, chief of marketing for Visa International, bank-card firm. "It's national banking via plastic instead of bricks and mortar."

Sears has bought small banks in California, Delaware and South Dakota and will begin offering savings and credit services to its 57 million card holders. Citicorp, already the nation's largest banking company, is spreading nationwide through acquisitions and mass credit card giveaways.

And American Express, through its Shearson Lehman Bros. brokerage offices and its Delaware bank, soon will be able to provide its upscale card customers with nearly all the traditional services of a bank.

Federal law bars banks from operating across state lines. But a 50-year-old loophole allows banks and other financial institutions to offer limited consumer banking services nationwide. Citicorp, Sears and American Express are exploiting gaps in the law to establish multibillion-dollar interstate networks that are banks in everything but name.

While Congress debates proposals to close the loophole, the credit card game has become picking off the most credit-worthy and highest-volume customers from the competition, while further sharpening marketing tools to

identify potential new card-carriers.

One card-company executive calls the increasingly sophisticated credit and consumer analysis "peeling the onion."

Thus, American Express mails Ivy League seniors a green card pitch ending "Don't leave college without it," and Citicorp markets its Preferred Visa card to well-heeled young professionals as "The card to end all cards."

Sears, Roebuck & Co. is pursuing a wholesale strategy to move its massive middle-American card base from housewares to individual retirement accounts.

Standard bank cards are being sold with "enhancements" such as free travel insurance, discounts on long-distance telephone service, national access to cash machines and comput-

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CREDIT: Firms Push Hard in Marketing Cards

Continued from Page 1

erized comparison shopping. The premium cards offer higher credit limits and such perks as guest membership in country clubs, limousine service and rewards for heavy spending akin to those given by airlines to frequent fliers.

Once the consumer's wallet is pried open, the idea is to sell as many additional financial services as possible—from money-market accounts to discount brokerage to insurance. The ultimate aim, the card issuers say, is to enable Americans to carry their bank in their hip pocket.

The three big firms come to the arena from different core businesses: Sears from retailing, Citicorp from banking and American Express from charge cards. But through acquisitions and aggressive diversification, the three companies are bearing down on the American consumer with very similar packages of financial services. All are built on a 3½-by-2½-inch piece of plastic.

With an estimated 708 million credit cards already in Americans' hands, why are the card dealers so hard at work?

Industry executives and analysts say the card wars are heating up in part because today's interest rate structure yields unusually high profits. Banks pay between 8% and 9% for funds, while credit card interest charges average 19.4%. The more a bank can lend out on a 10% "spread," the blacker the bottom line.

Just a few years ago credit card operations were money losers for banks. Money was expensive while credit card interest rates were kept low by state laws. Consumer credit was deliberately squeezed down by Federal Reserve Board policy. Losses from fraud and bad debts were mounting because banks lacked the sophisticated credit analysis tools they've since developed.

Spread Widened

"Two or three years ago these credit card businesses were terribly under water," said Frank Partel, an American Express executive vice president. "What's happened since is that state interest rate ceilings have been lifted and the cost of funds has declined dramatically."

"That's brought more players into the game, thus you're seeing a flurry of marketing in your mailbox."

Partel's comments lead to the second key reason for the push in plastic. The credit card market is already nearly saturated, so the effort now is to steal market share from the other guy.

"They're not trying to get new people, they're trying to get you away from somebody else," said H. Spencer Nilson, a Santa Monica analyst who tracks the credit card industry. "They're trying to hit different sectors of the market with specialized appeals."

That helps explain why one Los Angeles woman receives three or four preapproved bank card applications each week sent by banks

from Delaware to Washington. One offers a \$5,000 credit limit, one charges no annual fee, one gives bonuses for big spending. She's shopping around for the best deal.

Other consumers are less discriminating. A Port Chester, N.Y., man simply signed the applications and sent them in. He quickly found himself with four bank cards and \$6,000 in debt at interest rates between 18% and 21%.

"He called in the other day and said he had owed all this money and had just lost his job," said Marla Kaplan, associate director of Bankcard Holders of America, a Washington-based consumer organization. "I suggested he go to a credit counseling service and they recommended bankruptcy."

"The trouble is these banks don't talk to each other about who they're going to solicit. So the consumer gets all these preapproved applications and think they're gifts from God. They get bombarded and start borrowing more and more, and there's a change in the financial situation and they're in trouble."

Citicorp, with about 14 million cards in circulation, is the biggest bank credit card issuer in the country and the most prolific mail solicitor. It owns Diners Club and Carte Blanche, the premium travel and entertainment cards, as well as its own Choice card. It also sponsors about 7.4 million MasterCard and Visa cards.

Heavy Promotion

More than 140 million Americans carry one or both of the bank cards, which are issued and administered by banks across the country. The MasterCard and Visa names are licensed to banks for a fee by MasterCard International and Visa International, which are in essence credit card marketing cooperatives funded by banks. Each firm will spend about \$25 million this year to advertise its plastic products, industry analysts said.

Individual banks—led by Citicorp—will spend much more.

Citicorp's stated strategy is to take on American Express in the business travel field and every other bank in the country in the bank card arena. It will spend an estimated \$150 million to \$200 million this year to convince consumers that "the bank makes the difference."

"This push has been going on for the last four years, with exceptionally heavy mailings in 1984 and 1985," said Ira Rimerman, chairman of Citibank's bank card division. "We're going after new consumer families who we think are credit-worthy, and we're taking share away from other issuers."

"We're also out to get the consumer to 'trade up' to our Preferred Visa card by offering services and features that the consumer perceives to be valuable."

In addition to mailbox-stuffing, Citicorp for the first time is running a nationwide television ad campaign. One spot features Shirley Simmons, mother of fitness pitchman Richard Simmons, peddling a stationary bicycle her son bought

her through a Citicorp credit card promotion. Another commercial has James Doohan, who played Scotty on the TV series "Star Trek," beaming up his garage door with a new electric opener bought the same way.

Citicorp this spring also launched a "new" Diners Club card in an effort to wake up that card's 5 million somnolent customers. The reformulated card is aimed directly at corporate travelers, offering airport limousines, hotel suites at single-room prices, office services for traveling executives and health-club privileges in cities across the country.

James Emshoff, former marketing director at Campbell's Soup, recently was given the job of revitalizing Diners Club. He acknowledges that the division probably will lose money for a year or two, but said Citicorp can be very patient when it thinks it has a potential money maker.

Interesting Area

"Before we made this announcement, Diners was in a position to be a casualty in the credit card battle. Now we've got a chance to carve our own niche. This area is going to be very interesting over the next four or five years," Emshoff said.

American Express, the acknowledged industry pacesetter, is not sitting still. With 14.7 million card holders, it dominates the lucrative travel and entertainment field. Its envied card base is composed of Americans who earn, spend and travel far more than average.

The firm is adding 2 million new card holders a year and showing annual earnings increases of 20%, according to Jerry Welsh, American Express' worldwide marketing chief.

The fast-talking Tennessean, a former professor of Russian language and literature, said the company has targeted recent college graduates and young professionals for its most intense marketing efforts. Along the way, he said, the company has learned something surprising about "yuppies"—young urban professionals.

'Trade-Up' Strategy

"As we developed our 'Interesting Lives' campaign, we stumbled upon a lot of unexpected things about young people. They're more diverse, energetic and public-spirited than the yuppie myth would have you believe. We're going to lead a campaign to abolish the ugly yuppie stereotype of a bunch of baby-boomers sitting around choking on their frivolous creature comforts."

One TV spot features an unpretentious young assistant district attorney taking his crusty father out to lunch with his new American Express card.

American Express also is pursuing a "trade-up" strategy to move selected green card holders into its "prestige" gold and platinum cards. About 3.3 million card holders have already signed up for gold cards, despite the \$65 annual fee (the standard card fee is \$45), and a select few—those who charged

\$10,000 or more last year on their cards—are being asked to shell out \$250 a year for platinum plastic. It's too early to tell whether this crowd will find the status is worth the price.

The wild card in the deck is Sears' new Discover card, unveiled in April and set for test marketing in Atlanta this fall. Everyone in the credit card business is paying attention. You don't ignore a whale in your swimming pool.

"These are smart people," said Welsh of American Express. "We have a lot of respect for Sears. You've got to respect a company that has an account relationship with 40% of American households."

"People said Sears couldn't sell insurance. They said Sears couldn't open financial service centers. The challenge of their Discover card is to build a base of service establishments that accept it, and that's not an inconsequential problem."

The Discover card will tie together a range of financial services offered through the Sears Financial Network, including insurance, brokerage and money-market accounts. It also will provide conventional bank card capabilities, according to Edward A. Brennan, president and chief operating officer.

Brennan announced late last month that American Airlines, Budget Rent-a-Car, Denny's Restaurants and Hospital Corp. of America have agreed to accept the card and that a major hotel chain soon will follow. The card also will grant electronic access to savings and investment accounts offered through Sears-owned banks across the nation.

"Most importantly, the Discover card will provide a special opportunity for customers to build their savings," Brennan said. "They will have access to the new family savings account. This will provide a tiered interest rate structure that will increase with the account's balance."

Sears' move into the credit card business illustrates the further blurring of the definition of banking since deregulation swept through the financial industry beginning in 1980. It also offers evidence that in the money business, as in many others, there ultimately isn't room for more than a handful of players to compete nationwide.

"Sears' entry concerns us and pleases us both," said Bennett of Visa. "They're formidable. But they have to be. This is a formidable business."

Merc Considers Closing Illinois Yards to Futures

PEORIA, Ill. (AP)—The Chicago Mercantile Exchange is again considering closing the two remaining delivery points east of the Mississippi River for cattle sold on futures markets—at Peoria and Joliet.

The exchange withdrew an earlier request for the closures last month, bowing to opposition from area livestock growers. But Michael Gorham, the exchange's vice

U. S. Credit Card debt up to \$1043, end of '84.
Doubled from '79.

Australia Firm Ups Norris Oil Stake to 42%

11-16-84

LV-1

By PATRICK BOYLE,
Times Staff Writer

After a six-month courtship, the U.S. subsidiary of an Australian firm said Thursday that it has acquired a controlling interest in Ventura-based Norris Oil Co. and replaced top management.

Norris said it agreed to issue 950,000 shares of stock to Abeg Hydrocarbons Inc. for \$3.8 million, or \$4 a share. The transaction will increase Abeg's share in the company to 42%.

Norris also said Thursday that it lost \$466,575 in the third quarter on revenues of \$546,713. The results increased the loss for the first nine months of the year to \$788,673, up from a loss of \$374,810 in the first nine months of 1983.

The company attributed the loss to a 60-day closing of the company's Colorado gas wells after the purchaser temporarily stopped buying gas and the 85-day shut-down of its best producing oil well because of sand in the well bore. The gas wells are back in production, and the company said it expects the oil well to resume operating by Thanksgiving.

In trading Thursday on the over-the-counter market, Norris stock closed at a bid price of \$3.75, down \$0.125.

The Abeg transaction is expected to give Norris a badly needed infusion of cash and help it reverse more than a year of losses on its oil and gas operations.

Abeg is a wholly owned subsidiary of Entrad Ltd., a Melbourne, Australia, firm primarily engaged in the manufacture of clothing and

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shopping center development.

Abeg President J. S. Dorobek was named president and chief executive of Norris, replacing Thomas Hooker, who resigned. Dorobek is also president of Beverly Hills-based American Frontier Exploration Inc., another Abeg subsidiary. Entrad Managing Director Abraham Goldberg was named chairman of Norris, the company said, replacing Henry H. Neel.

Once a growing and profitable oil and gas producer, Norris has been losing money for the last two years because of depressed energy prices and a shortage of capital to maintain existing production. Its problems were compounded in mid-1983, when company Chairman Edward J. Carr, who had built the company almost from scratch, became ill and had to resign as chief executive.

When Carr died last May, Abeg acquired the stock in Norris left to his estate and began purchasing additional shares in the company while seeking seats on the board of directors.

Looks like the case of a co.
that got too extended & can't
meet its payroll.

29 'non-bank' banks get initial OK

WASHINGTON (AP) — Removing yet another barrier to interstate banking, a federal bank regulator gave preliminary approval yesterday for some of the largest U.S. bank holding companies to set up shop across state lines.

The action was certain to fuel a controversy over "non-bank" banks or consumer banks, which accept demand deposits or make commercial loans, but do not perform both functions, as full-service banks do.

Several members of Congress have vowed to push for legislation that would force companies to get rid of any limited-service banks formed after July 1, 1983.

C. Todd Conover, comptroller of the currency, gave tentative clearance to 13 bank holding companies — including Citicorp, the nation's largest, and Chase Manhattan Corp., the third-largest — to set up 29 non-bank banks in nine states.

The states are Colorado, Florida, Hawaii, Minnesota, New Hampshire, Ohio, Pennsylvania, Vermont and West Virginia.

The decision was attacked by the Independent Bankers Association of America, which earlier had called for Conover's resignation over the issue.

"He is undermining the rights of the states and state legislatures to determine the financial structure of the states," said Ken Guenther, executive director of the association, which represents about 7,600 small- and medium-sized banks.

Willis Alexander, executive vice president of the 13,200-member American Bankers Association, said, "It's regrettable it's come down to this. We asked the last Congress to resolve this issue. They didn't. We hope the next one will."

In announcing his decision, Conover restated his belief that "these banks are clearly legal under existing law."

He noted that he had imposed

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C. Todd
Conover



two moratoriums on the chartering of such banks over a period of 18 months, to give Congress time to act on the issue.

When it failed to do so last month, Conover said, "I felt compelled to begin acting on these applications."

The applications approved yesterday are the first of 332 pending in the comptroller's office. The Federal Reserve Board must give its approval on the banks before Conover gives final clearance for their operation. The comptroller's office supervises 4,700 national banks.

Fourteen limited-service banks, under Conover's supervision, already are operating, according to spokeswoman Lee Cross. Others have opened their doors under state jurisdiction.

At issue in the dispute is the definition of a bank. The Bank Holding Company Act defines a

bank as an institution that both accepts demand deposits and makes commercial loans.

Non-bank banks generally accept deposits but don't make commercial loans. By not doing both, they skirt the holding company act, which prohibits interstate banking.

Of the newly approved applications, 17 quasi-banks will not make commercial loans and the other dozen will not accept demand deposits.

Critics fear the breakdown of state boundaries will allow the nation's biggest banks to move into their territory and take away a big chunk of their business.

In addition to Citicorp and Chase Manhattan Corp., bank holding companies that won approval included Rainier Bancorporation of Seattle, Security Pacific Corp. of Los Angeles, Mellon National Corp. of Pittsburgh, Irving Bank Corp. of New York, and First American Corp. of Nashville.

Others were First Bank Systems Inc. of Minneapolis; Barclays American Corp. of Charlotte, N.C.; Central Bancshares of the South Inc. of Birmingham, Ala.; First Union Corp. of Charlotte; Bank of Boston Corp. of Boston; and First Interstate Bancorp. of Los Angeles.

6-2-85 V-1

Oil-Service Firms Fall Victim to Clients' Woes

By JANE APPLGATE,
Times Staff Writer

Oilfield-service company executives who chanted "stay alive till '85," following the collapse of the market for drilling equipment and services three years ago, are finding little solace this year.

The volatile mergers and acquisitions reshaping the nation's oil companies are gobbling up billions of dollars once spent on exploration. Depressed oil prices and a glut of natural gas is further battering all but the strongest and most innovative oil-service companies.

"All this talk about how great it (restructuring) is for the industry doesn't create one new barrel of crude oil," said Jerry Neely, chairman and chief executive of Newport Beach-based Smith International. Smith, which makes drilling equipment, lost \$10.3 million in the

"Dollars are being taken away from exploration and funneled into servicing debt."

— Henry DeNero, partner in McKinsey & Co. consulting firm.

first quarter of this year, contrasted with net income of \$3.3 million a year earlier.

Neely says 1985 "will not be a particularly good year for Smith," especially since many oil companies are giving top priority to paying down the enormous debts they took on to defend themselves against hostile takeover bids.

In the last 18 months, major U.S. oil companies spent about \$56.6 billion on acquisitions and stock purchases, according to a recent

report by the investment firm of Morgan Stanley.

"Dollars are being taken away from exploration and funneled into servicing debt," said Henry DeNero, a partner in McKinsey & Co., a consulting firm.

Gene Kinney, editor of the Oil & Gas Journal, a trade publication, said in a recent interview: "The concern now is that the money stockholders receive in these buy-outs is not going back into the oil industry. This 'de-capitaliza-

tion' is a major factor in the failure of the drilling industry to recover from its slump."

Kinney estimates that U.S. oil companies will spend about \$35 billion in 1985 on drilling, exploration, production and offshore lease bonuses to replenish reserves. This compares to \$39.8 billion spent in 1984 and \$39.4 billion in 1983.

Analysts said the amount spent by oil companies on takeovers and defense strategies nearly equals the record \$58 billion pumped into drilling and exploration at the peak of the drilling frenzy in 1981.

Atlantic Richfield's recent decision to cut its exploration budget by 30% to 35% to \$900 million as part of its extensive corporate restructuring is just one example of reduced oil company spending. Throughout the oil industry, merged companies are consolidat-

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OIL: Companies Fall Victims to Clients' Woes

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ing operations and trimming exploration expenses.

In December, 1984, Gulf Oil and Chevron separately operated 49 rigs in the Gulf of Mexico and Louisiana state waters. A spokesman for the the combined companies said the total rig count has since declined to 32 working in the area.

"There is a drop, but it's (also) due to the low price of oil, the soft natural gas market and the lack of really good prospects to drill right at the moment," said Keith Owen, a Chevron spokesman.

Industry analysts agree that uncertainty about federal tax proposals affecting drilling, depressed oil prices and a surplus of natural gas contributes heavily to the industry's reluctance to drill for new supplies.

Hughes Suffered Loss

Outside investment in oil exploration by individuals and institutions has virtually dried up since changes in the federal tax laws reduced the tax write-offs for drilling programs to about 35% from up to 70% at the height of the domestic drilling boom.

"The only money available to the (service) industry is cash flow from (oil company) operations," said James Lesch, chairman of Houston-based Hughes Tool.

Last year, Hughes predicted a moderate drilling increase in 1985 based on what oil companies said they planned to spend. Instead, rig

activity slipped about 10% below last year's level. Hughes wrote off \$174.3 million in excess capacity in calendar 1984, reporting a net loss of \$133.8 million on revenues of \$1.2 billion.

Although oil companies are spending about 15% less on exploration this year than last, not every company embroiled in a fight for independence has turned its attention away from the oil patch. And industry executives said not every dollar spent on stock repurchases would have found its way into oil service company coffers.

Phillips Petroleum, which recently took on an additional \$4.5 billion in debt to thwart T. Boone Pickens Jr.'s attempt to gain control of the Bartlesville, Okla.-based company, is cutting elsewhere to maintain its exploration and production budget at last year's level.

"We still plan to spend \$1.4 billion on exploration and production in 1985, but we are being more selective in our spending," said Dan Harrison, a spokesman for Phillips. He said the company is selling about \$2 billion worth of assets and cutting operating expenses by \$200 million in 1985 and \$300 million in 1986 to help reduce its \$7.3-billion debt.

For Phillips and the other major oil companies intent on making the most of their tight budgets, the days of buying a half dozen drill bits off the back of a pick-up truck are numbered, according to Ed Williams, vice president of corporate development at Smith.

Exxon, intent on cutting costs, is buying a six-month supply of drill bits at a time to get the best price. In the past, bits were purchased as needed.

Uncertainty created by the oil industry restructuring colors every day for companies such as Smith. Smith's sales force not only has problems figuring out who to talk to in a newly merged company, Smith executives can no longer depend on oil company forecasts to make key decisions. "I recently called up six major oil companies to ask for copies of their 10-year forecasts," Williams said in a recent interview. "All but one company—Conoco—told me they aren't doing long-range forecasts anymore."

In the late 1970s, oil-service companies, buoyed by promises of \$70-a-barrel oil, scrambled to build equipment to serve 5,000 domestic drilling rigs. Today, with U.S. oil prices hovering around \$27 a barrel, a lean corps of service companies are fighting for the business generated by about 1,900 active drilling rigs. Price discounting is rampant and many companies say they are selling some products at cost.

Industry executives are in agreement that the companies destined to survive are those that offer drillers high-technology products designed to improve performance and cut costs.

Because of its state-of-the-art products line, New York-based Schlumberger, the industry levia-

than, has risen above the oil industry's restructuring.

"Our philosophy is to offer something that is needed even in bad times," corporate spokesman Seth McCormick said. Company officials told a recent gathering of industry analysts that its \$4 billion in cash gives Schlumberger the strength to weather even the worst of times.

Unlike its money-losing brethren, Schlumberger's income rose 11% to \$1.1 billion in 1984, on revenues of \$6.4 billion. McCormick declined to discuss how the oil industry restructuring has affected its business, saying "client relationships are sensitive."

Facing Disappointments

The service companies, which once garnered profits from supporting expensive, deep natural gas drilling operations, are facing disappointments on that front as well. On May 2, Omaha-based Internorth and Houston Natural Gas agreed to a \$2.3-billion merger that would create the longest gas pipeline in the United States. Two months earlier, Houston-based Coastal Corp. and American Natural Resources of Detroit announced their own \$2.5-billion merger.

Not only do these consolidations mean reductions in exploration and production budgets, but industry analysts say there is a 2 trillion-cubic-foot-a-year surplus of natural gas in the United States. If Canadian supplies are included, the surplus, or "gas bubble" as it is called, soars to 4.5 trillion cubic feet.

Monday, April 22, 1985

FOR WHAT IT'S WORTH / S.J. Diamond

Debit Cards Pay Off— and Do It Really Fast

Having shifted consumers from cash to checks to credit cards to teller machines, banks are now poised to tout debit cards—another step toward cashless, paperless, eventually bankless banking.

Like ATM cards, the new debit cards give consumers direct access to their own accounts. Unlike checks, they authorize withdrawals instantly and electronically. Unlike credit cards, which delay payment, they draw on deposited funds rather than a line of credit.

Unlike simple ATM cards, the new debit cards not only withdraw money but transfer it from the consumer's account to a merchant's at the point of sale, making "the proprietary ATM card," says Charlie Pedersen, senior vice president of California First Bank, "an all-purpose card with the convenience of a credit card." Says Thomas Collins, spokesman for Mobil Oil, which enthusiastically accepts the new cards at many locations, "it's a genuinely new way of paying for something."

Such electronic fund transfers cause great excitement among banks: Like the ATM, they're more "cost-efficient" (i.e., cheaper) than tellers or check processing. They're also profitable, because there won't be any "float" between the time a consumer tenders check or credit card for merchandise and actually settles up with the bank that pays the merchant.

Share Networks

There are even electronic networks gearing up to transfer such funds among banks at the point of sale. Visa is trying to perfect such an option for banks that are already members of its vast credit network. Banks are establishing shared ATM networks—for example, the new 80-member Star System in the Western states—so customers of one can get cash from another; these will eventually make "point of sale" transfers as well. Some banks are establishing networks just for point-of-sale transfers—the Interlink system, for one, started by California's five major banks—although they've barely begun marketing debit cards to either consumer or merchant.

Actually, the networks aren't so premature: Their existence guarantees a large pool of both merchants and consumers on the same shared system, which makes it more attractive to both. "It's the chicken and the egg problem," says Janie Nelson, vice president at Security Pacific Bank Card USA. "You gotta have the merchants before the consumer will sign up, and a lot of consumers to interest the merchants."

Banks think debit transactions are equally advantageous for retailers, reducing paper handling and not only revealing immediately whether the consumer has the money but earmarking it for transfer to the merchant. No credit risks, no bounced checks, just "100% guaranteed payment," Nelson says.

But retailers may have to upgrade their equipment to include electronic card readers and "PIN pads" (for consumers to punch in personal identification numbers). Moreover, there will probably be processing charges from their bank, as for credit card transactions, and some merchants think the processing is not worth it; Seattle-based Nordstrom stores dropped Visa entirely rather than accept Visa debit cards—a service, said Nordstrom, that replaced checks but at a higher cost to the store. (Rates right now are negotiable while banks try to build the market; merchants could probably even charge them.)

Pilot Programs

Some businesses are eager, however. Mobil Oil, which started pilot programs in 1983, will welcome the debit cards of cooperating banks at 3,600 of its 4,500 company-owned stations by year-end and already accounts for half of all retail debit card transactions in the country. Dealers like the ease of less paper and quicker credit checks and the influx of new customers drawn by "the discount associated with a cash purchase plus the convenience of plastic," Collins says. Debit cards clearly brought new business, he says, because sales increased while "both credit card purchases and cash purchases remained the same."

Two Lucky supermarkets in Southern California were equally enthusiastic over their experiment last year with Wells Fargo Bank's Express Banking cards. The so-called Express Purchase program—which put card scanner, PIN pad and "balance inquiry terminals" at the checkouts—"saves people time," says Ron Jones, assistant store manager in Orange. "They can do their part of the transaction while the checker's checking out their groceries, and they don't have to write a check." More than half of the Wells Fargo check writers who previously shopped at those stores, Wells Fargo adds, converted to Express Purchase.

But nobody can guarantee consumer reaction. Banks assume they'll welcome a check replacement good in other cities, with none of the usual wait for check approval. Debit cards, moreover, "should be less expensive than credit cards," says B of A executive vice president John Mickel, "because we're not extending credit."

A prime market, says Mickel, should be people who are "not credit-worthy or those not interested in credit—a large segment of retired people, or the 30% of credit card users who never revolve

Sunday, March 17, 1985

JOHN F. LAWRENCE

Hawaii Lesson: Soaring Values Carry Big Risk

One of the signs that attitudes have changed from the high-inflation days of the 1970s is that real estate is no longer the hot investment it was. Instead of assuming they'll see a quick profit, investors generally are looking farther ahead, if they're investing at all.

The change is particularly apparent in Hawaii, where a good many buyers and lenders have learned a hard lesson about downside risk.

Skyrocketing values in the '70s, partly a product of the period's inflation psychology, led to massive overbuilding of condominiums, resort units and other properties in the islands. Developers banked on strong demand from mainlanders attracted by the idea of a dream vacation home that would turn them a nice profit and give them some tax benefits as well.

Painful Ending

Speculative booms almost always have a painful ending. This one was helped along by a dramatic change in economic conditions. Interest rates soared and inflation cooled.

At one condo development on Kauai, the first units, built in the early '70s, sold for as little as \$50,000. Just before the boom ended in 1979, some of them reached nearly \$200,000. Just as in Orange County and other parts of California, demand was so great that new units often were sold by lottery.

Now times have changed. One Californian who bought into the Kauai project at \$160,000 now figures he'd be lucky to get \$125,000 for his unit. There are others on the market for as low as \$90,000. "If we'd known how much building was planned, we might not have bought," he says. "But times were so good, we didn't ask that many questions. And even if we had, we might have gone ahead anyway."

Fortunately for this investor, he wasn't one of those who bought on a shoestring, expecting to be able to get out quickly as prices rose. He has watched while other owners have lost their units. He considered walking away, but in Hawaii, unlike California, lenders can go after a borrower's other assets, not just the real estate investment, to satisfy a debt. "That's something else I wish I'd understood going in," he says. At present, he plans to hang on for better times.

11% Vacancy Rate

Hawaiian property generally hasn't fared as badly as his condo. But prices have come down some. One Honolulu business executive figures a condo he purchased for \$65,000 in the early '70s got as high as \$225,000 before dropping back to a current \$195,000. There's still an overhang of some 11,000 condos on the market, a vacancy rate of 11%.

Some units were built as part of resort complexes and are operated like hotel rooms. In these cases, rental income frequently has been disappointing for investors because occupancy rates have been low for much of the last five years.

This year, tourism is up and some resorts are sold out at least for the current peak season. But in some cases, room rates remain depressed by the oversupply of recent years.

While the Hawaiian speculative boom was unusually sharp, it was much like most booms elsewhere. What starts out as a healthy appreciation in values based on real demand turns unhealthy as the speculators join the serious investors in scrambling for property. That certainly happened in parts of California, where builders sold lots by lottery but many of the buyers had only one idea in mind—a quick resale and a quick profit.

In the end, there have to be people who want to occupy all the new units, or the bubble bursts. In many cases there weren't, and so it did.

Tax policy has played a role in some of this speculation, contributing the benefits of tax write-offs to the lure of exploding land values. Now, the proposed tax simplification plans being considered by Congress and the Administration would put a cap on deductions for interest paid on the mortgage loan for second homes. That has frightened would-be investors and compounded the overbuilding problem.

The lesson of the Hawaiian experience is a simple one. When prices of any investment, real estate included, go sky-high, it's best to remember how far is down.

John F. Lawrence is The Times' economic affairs editor.



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Government spending hailed as source of jobs

STANFORD (AP) — Dollar for dollar, domestic government spending tends to create more jobs than does spending by private industry, according to a study by a Stanford University expert.

9/26/83
The study implies that **tax cuts for business and consumers** wouldn't create as many jobs as an **equivalent increase in government spending**, said Russell W. Rumberger, a research associate at the Institute on Educational Finance and Governance.

Government money "is spent on services, which tend to be labor-intensive and therefore employ a lot of people," while private industry tends to invest more in buildings and machinery, Rumberger said.

Government spending also tends to help women and minorities, whose role in public jobs is far greater than in private sector employment, Rumberger said.

Rumberger's study found that a \$1 billion increase in private spending or transfer payments would create about **30,000 jobs in the private sector**.

If spent on national defense, the \$1 billion would result in about **46,000 jobs** — 16,000 in private industry, 16,000 in the military and 14,000 in the public sector, he estimated.

If spent by state and local governments, the money would create almost **50,000 jobs**, Rumberger said. And federal, non-defense spending would lead to about 51,000 jobs.

As a result, a shift of \$ billion from federal, non-defense spending to the private sector would reduce the total number of jobs by 20,000, Rumberger calculated.

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