

4-10-1992

## Levy in the News Clippings

Hyman P. Minsky Ph.D.

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**THE JEROME LEVY ECONOMICS INSTITUTE  
OF BARD COLLEGE**



***IN THE NEWS...***

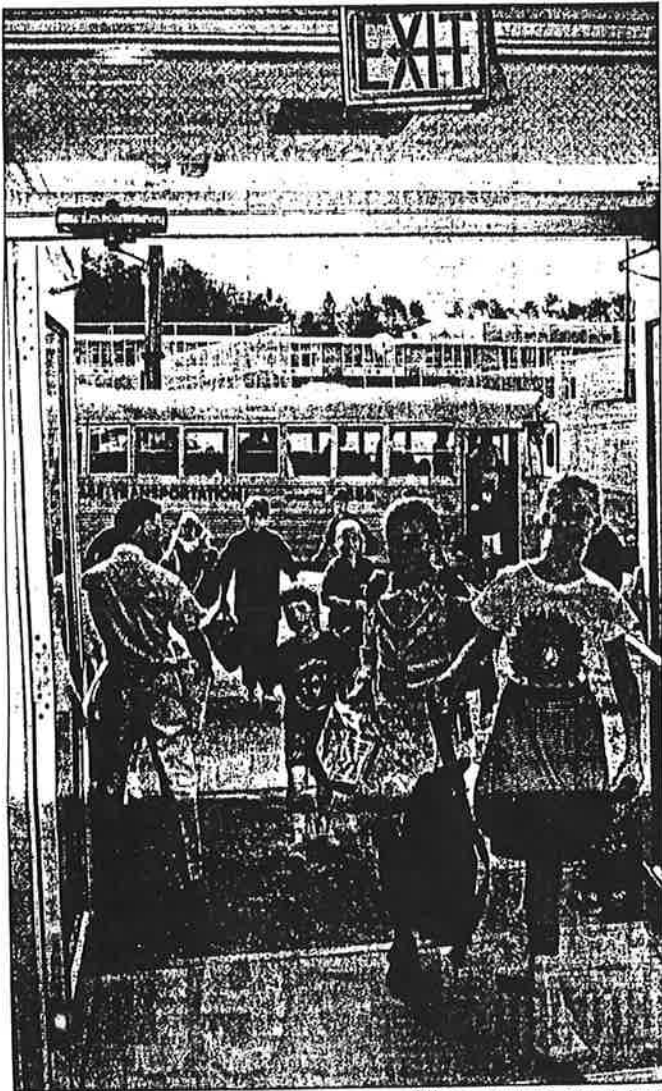
# Poughkeepsie Journal

9/10/92

SINCE 1785 ■ NEW YORK STATE'S OLDEST NEWSPAPER

50 CENTS

## W faces in schools



Alden Place Elementary School pupils enter the building Wednesday for the Millbrook school's first day. Principal John Yarochowicz, left, greets pupils.

By Robert V. Niles/Poughkeepsie Journal

## Speeding tickets down 70%

compared with 578 during the same period last year.

Statewide, troopers wrote 25 percent fewer speeding tickets this Labor Day weekend over last. Capt. Thomas Larkin said the numbers don't necessarily represent a diminished effort.

"It is and it isn't. Last year we had a speed enforcement detail that we didn't have this year," Larkin said.

Last year, he said, between 18 and 25 extra troopers were assigned to the detail, which included aerial surveillance and targeting of specific roadways. Larkin said he did not know how many extra troopers

were on the road this past weekend.

Larkin and others denied that troopers made a concerted effort to write fewer tickets because of a contract impasse that has been dragging on for the past 18 months, saying that poor weather — and the accompanying decrease in traffic — also contributed to the decline.

"Obviously, we're going to monitor that (possibility)," said state police Col. James McMahon. "We take traffic safety as a serious responsibility."

State Police Police Benevolent Association officials did not return repeated calls Wednesday.

## N.Y. poised for rebound in economy

### But nation a drag on state, observer says

The Associated Press

ALBANY — New York is positioned better than most states to emerge from the recession, but real recovery awaits economic improvements beyond the state's borders, an economist says.

"New York can go no faster than the national economy," said Walter Goldstein, a professor of public policy and international relations at the State University of New York at Albany. "New York cannot escape from the trends of the national economy."

And Goldstein said there was little to be hopeful about on the national economic landscape.

The drain of the national debt is compounded by the debt load being carried by American businesses and consumers, he said.

American workers displaced by the decades-long downturn in manufacturing jobs — what Goldstein called "metal-bashing" jobs — continue to flounder, with no one seeming to have a clear idea how they can be productively retrained.

"If there is one thing our economy needs more ... it is the training of labor," Goldstein told about 100 people Tuesday night at a forum sponsored by the American Society for Public Administration. "We have a ridiculously undertrained, underemployable work force."

He said there are signs that the United States will come out of the recession as Europe did from downturns of the 1970s — with a "no-growth recovery." Jobs that have been lost in the last few years will, for the most part, stay lost, he said. Many people turned out of their jobs will have to find new careers.

"There is no increase in jobs and there is not likely to be," he said.

In fact, he added, "One of the things that we have to get used to is that things could get worse."

Despite that gloomy assessment, Goldstein said New Yorkers have reasons for optimism that those in other states don't.

"New York could be positioned for a relatively strong comeback if the national economy rebounds in the next couple of years," he said.

Small- and mid-sized companies in New York have done better than their counterparts in Western states at drumming up business, he contended, and added that New York's work force is generally more skilled than the national average.

## Bard expert pessimistic

By Alison Bethel  
Poughkeepsie Journal

Unless the incoming federal administration shows some "real concerns" about turning the economy around, not only will there be little hope for a recovery, but even less hope for New York state, said a noted local economist.

Disagreeing with the assessment of Walter Goldstein, State University of New York at Albany professor of public policy and international relations, economist Dimitri Papadimitriou said Wednesday:

"The economy's sluggish pace will change very little — or even slow — actually, in the next half of the year. I don't see any signs that there is going to be a recovery."

"For anyone to say that there is recovery, I don't believe that there is the evidence there," said Papadimitriou, executive director of The Jerome Levy Economics Institute at Bard College in Annandale-on-Hudson.

Papadimitriou comments came in response to a speech by Goldstein in which he said New York state is positioned for "a relatively strong comeback" if the economy rebounds in the next two years.

Goldstein also predicted a modest economic recovery by the end of the year or early next year — a possibility Papadimitriou doubts.

"Once the summer jobs end, unemployment will be high again," he said. "The deficit is going to probably be higher because there will be a reduced federal tax refund. If there are going to be fewer refunds, then there will be less money to spend, lower demand and therefore not an economic recovery ... And corporate profits also will be sliding."

Papadimitriou did say, however, that if some major action were taken by the federal government, the state would be "a primary candidate to be the beneficiary of the government action because we are positioned well in terms of the number of industries we have ... And let's not forget the educational sector, which is quite substantial in New York. But they (the federal government) would have to take some major action."

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## NEW YORK

\$2.50 • AUGUST 24, 1992

The Bottom Line/Christopher Byron

### SLOWLY SUBMERGING NATION

#### THE ELECTION WON'T CHANGE IT

WHEN IT COMES TO THE ECONOMY, WILL IT make much difference who actually ends up winning in November? To hear Bill Clinton tell it, only the Democrats have a program capable of turning around twelve years of Republican neglect. George Bush, of course, will tell you that the real reason for the economy's mess isn't Republican neglect but a Democratic Congress that has refused to enact almost any economic bill the president has sent it.

But step back a bit from the day-to-day noise of the political campaign, and look at the larger picture. What one sees is evidence of an economy that is not going to

"We all squint at monthly and quarterly changes," says Dalio. "So we fail to observe how our relative living standards are declining as against those of other nations over long time frames. Countries evolve at about the same rate that children grow—you can never see it happen, but before you know it, major changes have occurred."

In Dalio's view, strong economic growth is a function of three things—cheap labor, high savings and investment, and hard work—and the U.S. has been short of all three for decades. "Politicians promise painless solutions," says Dalio. "But the truth is, they don't exist."

David Levy, director of forecasting for the Jerome Levy Economics Institute, as-

drag on the economy has to do with something that no one can really do much about: The private sector is basically fully invested. Spending by business accounts for the overwhelming bulk of capital investment in the economy, and as the data plainly show, the nation has all the factories, office buildings, shopping centers, and so on that it's going to need for many years to come.

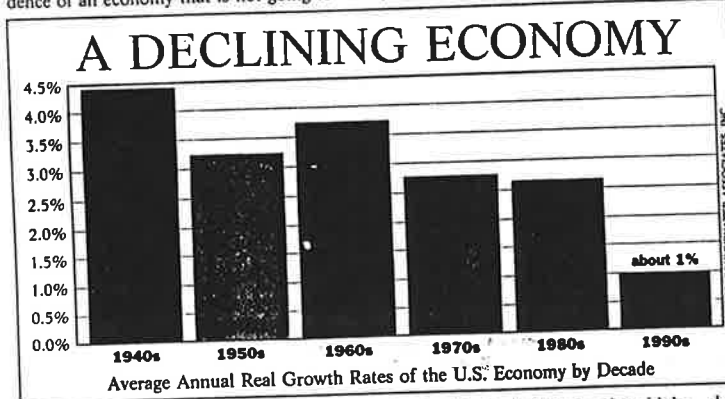
"Capital investment is by far the most important element in keeping the economy growing in a healthy way," says Levy. "Yet since 1985 we've been experiencing chronic weakness in this area, and it's been getting steadily worse. It's now at the lowest level since World War II, and there's no reason to think the trend won't continue."

Data supplied by Bridgewater Associates underscores the problem. Generally speaking, the fastest-growing economies in the world are also the ones with the greatest per capita investment in business: Singapore, Korea, Malaysia, and so on. But of the world's 30 largest non-Communist economies in 1990, the U.S. ranked a pathetic twenty-eighth in capital investment as a percent of gross domestic product, behind even such economic basket cases as Chile and Greece.

Last week, I checked with IBM to see what that company's capital-spending plans were for the year ahead. A company spokesman confirmed the trend that Levy described for the economy as a whole: The company's capital spending began to level off in the late eighties and now is beginning actually to decline. In 1993, according to a forecast by the Value Line investment survey, spending by IBM on new plants, equipment, and production facilities is expected to shrink by 6 percent, to \$5.6 billion.

All sorts of euphemisms have been trotted out to describe this process of cutting back on spending and investment—downsizing and restructuring, to name but two. Yet every dollar not spent by one company is a dollar not earned by some other firm. More than that, when the cutbacks come in investment spending, the lost opportunity for greater output by a firm spreads out into the future for years to come, crimping growth for the entire economy.

Economists cite a number of political and social forces that converged in the seventies and eighties to mask this trend. When inflation exploded in the seventies



improve to any significant degree, no matter who becomes president. There's an opportunity in this situation, for as I've argued before in this space ("The Bottom Line: Strike Up the Bonds," February 24), slow growth is bad for stocks but good for bonds—and slow growth looks likely to be with us for some time to come.

How long? Real long. As the chart on this page shows, over the past 52 years—a half-century of history in which the U.S. has been led by ten presidents—the growth rate of the U.S. economy has relentlessly slowed except for a bump in the sixties caused by superheated spending on Vietnam.

From such evidence, economists like Ray Dalio of Bridgewater Associates, a leading pension-investment firm, draw the obvious conclusion: The U.S. is no longer the pacesetter of world economic growth. Rather, it has become what might be termed a newly submerging nation, mired in a bog of long-term structural decline—something that Dalio can be eloquent about.

sociated with Bard College, also thinks the politics of the campaign is obscuring the big picture. "When you consider what needs to be done to prevent the outlook for the economy from getting any worse, it makes a great deal of difference who the next president is," he says. "But in terms of major trends, there's no question that we're in a period of slow growth that will go on for years."

Levy argues that budget deficits are not necessarily bad on their face. He says, for example, that public-sector deficit spending for things like roads, bridges, and education is badly needed to offset declining investment by the private sector. He is one of the most vocal economists to urge that national accounts be divided into capital and operating budgets. This way, taxpayers can insist that operating accounts be kept in balance while permitting borrowing for capital projects—that is, for the kind of long-term investments for which it makes sense to go into debt. Unfortunately, in Levy's view, the real

and family budgets began to be squeezed sharply for the first time in the postwar era, housewives by the millions entered the work force. But, says Dalio, that growth is now over, and women entering the work force are mainly replacing those who leave. In the late seventies, as oil prices exploded, there was also a one-shot surge in business investment for such things as drills, rigs, and refineries. But, says Levy, that trend, too, is now long since over.

Where, then, is the hope for tomorrow? Many experts see a reason for optimism in the millions of immigrant workers clamoring to enter America and work hard for low pay. But no one seriously contends that immigration alone can turn this economy around, and the spending plans of Clinton and even Bush aren't likely to do the job, either.

As a result, economist Dalio counsels taking a lesson from history. "The rise and fall of civilizations can be traced to their attitudes toward work and debt," says Dalio. "When countries are poor and think of themselves that way, they save their money, and capital goes into investment instead of consumption. As a result, their economies grow rapidly." That, says Dalio, is what is currently happening with the fast-growth economies of the Pacific Rim.

After the first stage, though, comes the next—when countries at long last get rich. The trouble is, they begin behaving that way, and consumer debt rises while everyday people take to driving around in Mercedes-Benzes. In Dalio's view, Japan is now entering this phase even as the U.S. is now leaving it for the third and penultimate phase of the cycle—the one in which countries start getting poorer but don't want to admit it.

The final stage of the cycle is reached when countries at last wake up to the bitter truth that they're no longer rich and once again begin saving and investing because there's simply no other choice. Argentina, which early in this century enjoyed one of the world's more robust economies only to see it frittered away in the excesses of Perónism, is a good example. The U.S., says Dalio, is an example of a country agonizing over whether to face up to what lies ahead if it doesn't change its ways.

Where does all this leave the individual investor? Six months ago, I argued that the economy was in a box and that low growth in the nineties meant that "bonds will almost certainly outperform stocks." Since then, the stock market has barely budged, but the bond market has boomed, returning investors nearly 10 percent on their money in little more than a half a year's time. And here's the good news: If experts like Dalio and Levy are right, this is an opportunity that's going to go on rewarding investors for years to come. ■



# Poughkeepsie Journal

# BUSINESS

Local people 2  
Local stocks 2  
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# E

SUNDAY, AUGUST 16, 1992

## Bard economists see tough road, need for repair

By Allison Bethel  
Poughkeepsie Journal

Want an end to this recession — and quickly? Don't bet on it, scholars at the Jerome Levy Economics Institute at Bard College predict.

Economic conditions likely will go unchanged until the end of the year, they said.

There is little reason to believe the recession will ease as quickly as the federal administration would have its citizens believe, according to Dimitri Papadimitriou, the institute's executive director. Parts of the problem, said the experts, include a lack of consumer confidence, wages that don't go far and banks that don't lend money.

Economic indicators are being misinterpreted and misrepresented, they said. The reality is people find it harder to step toward the American Dream.

"People are finding it hard to have a car, to send their kids to college," said Hyman P. Minsky, Levy Institute distinguished scholar. "Before the Reagan era . . . if you had a regular blue-collar job, that was a reasonable expectation. Now that isn't."

Real weekly earnings of blue-collar



Margaret Flitsch/For the Poughkeepsie Journal

Bard College Levy Institute economists Hyman Minsky, left; Dimitri Papadimitriou, center; and Randall Wray offer views.

workers have fallen 20 percent since 1973, according to Randall Wray, resident scholar at the institute and an assistant professor at the University of Denver.

Real earnings stand at 1959 levels, he said. In fact, studies show average weekly

earnings for Dutchess County manufacturing jobs decreased nearly 8 percent between June 1991 and June 1992.

Studies of the second quarter seem to validate the opinions of Minsky, Wray and Papadimitriou.

By June, Dutchess had lost 6,800 jobs Ulster had lost 3,300 and Orange had lost 1,200 from June 1991.

Most disheartening, the economists said is that one of seven New York City residents, or 1 million people, were receiving some sort of public assistance as of July.

And, said Papadimitriou, the economy grew by 2.9 percent in the first quarter but dropped by 1.4 percent in the second.

### Needed: Government action

Those statistics, he said, will not change unless there is government action to stimulate growth.

"Unless that happens, the trough may go even lower," said Papadimitriou, adding that the investment community is waiting to see some kind of program from the federal government to help the economy get back on its feet.

"Unless you see that, one will not see growth in the economy," he said. "We're stuck unless there's a unified economic program to bring us out of this . . . I think consumer confidence can be raised if there is some glimpse of hope. But there's nothing out there."

To make matters worse, Wray said, consumers continue to repay debts they incurred in the '80s. He said 17 percent of after-tax income is going to repaying debt.

# NEWS

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# NEW YORK POST

AUGUST 3, 1992

## BUSINESS AND INVESTMENT NEWS & VIEWS

### Only a Pollyanna would fail to see reason to worry

IT IS starting to look like time to resume serious worrying about the economy.

Evidence abounds: IBM offers an attractive early retirement package in hopes of shedding 20,000 workers, and 32,000 accept; a small upstate community is devastated by Smith-Corona's decision to move a manufacturing operation to Mexico; preliminary data show that second-quarter Gross Domestic Product growth fell to one-half the weak level of the first quarter.



GERARD BRAY

True, I'm cherry-picking examples to make my point. True, there are data from which you can draw some hope. But, you've got to be Pollyanna or on some other planet not to smell the worry and trouble.

Help from Washington? Don't bet on it. The President is behind in the polls, and beginning to remind me somewhat of a rabbit who's been running flat out for a long time and still hears the dogs close behind.

Even in better times, the Darman-Brady-Boskin-Baker braintrust wasn't hitting economic home runs.

The strategy has been to force interest rates down. They're down. The recovery is stumbling at best, over at worst. Money can't get much cheaper.

Now, with virtually all the cards dealt, desperation may prompt some unusual plays.

Consider the sale of F-116 fighter jets to Taiwan. It may be a good economic idea, it may be a bad economic idea. It can't be both. The President has opposed and blocked selling the Taiwanese these jets. So, the Taiwanese have let it be known that they are seriously considering buying French-made Mirage fighters instead.

On Wednesday General Dynamics, which makes F-116s in a Fort Worth plant, said it will lay off 5,800 workers because it can't do the deal with the Taiwanese.

On Thursday the President, whom you remember calls Texas home and is running against another Southerner, gave an interview to the Texas state radio network. He said he is going to reconsider his decision not to let the

Taiwanese buy F-116s. Lest there be any doubt about this little-reported story, White House spokesperson Judy Smith confirmed it for the Associated Press. "We really are going to reconsider," she said.

The point is simple. If 5,800 Texas jobs can prompt reconsideration of such important policy decisions as international warplane sales, imagine what may happen if the White House decides that Michigan — with all those unemployed auto workers — is a must-win state.

Why, the White House might finally smarten up and play hardball with Japanese automakers. Desperate men make desperate moves, but sound economic policy is usually not born of desperation.

However, even if the puzzle palace on Pennsylvania Avenue keeps its cool, it may be too late to avoid more serious blood-letting in the economy.

I'm hardly the only one who is worried. Consider the following from Industry Forecast, the excellent newsletter produced by David A. Levy and S Jay Levy in Chappaqua, Westchester County.

"The federal deficit, which swelled in the first quarter, boosting profits and growth, failed to provide further support in the second quarter. Aggravating matters was America's trade performance, which took a decided turn for the worse. The expanding trade gap and the end of the surge of the Treasury deficit, along with ongoing contraction of nonresidential construction and increased consumer saving, are terminating the 1992 recovery."

The Levys, independent economists not burdened with having to make a case for any investment or the purchase of any consumer goods, have a good record of correctly predicting the economy.

Right now, they believe the country is in a "contained depression" and they don't see significant improvement soon. Among their forecasts:

■ "We continue to expect yields on long-term Treasury bonds to fall to 6.5 percent or less and on three-month bills to shrink below two percent in 1993."

■ "Recent employment declines and shrinking wage raises are ominous signs. 1992 Holiday sales will fall below stores' modest expectations."

■ "We hold to our forecast that profits will sag in this half and be sharply lower in the first half of 1993. Next spring, the 1992 fiscal stimulus provided by the decrease in withholding tax rates last March will be reclaimed in one fell swoop by the Treasury. Higher tax payments and lower refunds will reduce the deficit — and profits."

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# Forbes

August 3, 1992 Four Dollars

## WHAT'S AHEAD FOR BUSINESS

EDITED BY HOWARD BANKS

### Will profits flatter only to deceive?

DID CORPORATE PROFITS peak in the second quarter? That's the view of respected economist S. Jay Levy, chairman of the Jerome Levy Economics Institute of Bard College. Based on his analysis of the flow of funds in the economy, Levy thinks profits will now generally decline, at least through the first half of 1993.

That would be a depressing reversal from what happened in the first quarter of this year. According to the Commerce Department's Bureau of Economic Analysis, preliminary estimates show that pretax profits from current production for all corporations increased by \$31.4 billion in the first quarter, to an annual rate of \$355 billion. This was up from a \$9.6 billion increase in the preceding quarter and, says the BEA, it was the biggest quarterly jump in almost five years.

But, cautions Levy, that first-quarter jump was from a low point caused by the recession, and most of it was the result of higher government deficit spending in the first quarter. "The surge in public spending has receded, and there is nothing to replace it," he says.

The consensus view of the 52 economists surveyed by the Blue Chip Economic Indicators is that profits for 1992 as a whole will increase by 18%, and by another 13% or so in 1993. But more caution. Warns Blue Chip's Randell E. Moore: "This forecast swing may exaggerate what's actually happening to profitability."

Both Moore and Levy point out that another important factor in the profits uptick has been corporate cost-cutting, mostly by downsizing and laying off workers. And where business is picking up, rather than adding workers, companies are working existing employees longer. The average workweek has recently been at its longest since the mid-1960s.

All that, the economists say, works to depress consumer confidence, and therefore economic demand.

"The whole economy looks rather shabby right now," says Levy. And now predictions for economic growth in 1993 are being pared even from earlier measly forecasts of around 3%. Until the economy gets a burst of life from somewhere, there is zero possibility that profits will show the 40%, followed by 24%, jumps that they did in 1983 and 1984, in the early days of the last big recovery.

There are some consolations buried in today's slough of despond, however. All of the painful cost-cutting is resulting in a much more competitive U.S. economy. Witness the U.S.' improved trade performance. Inflation remains firmly under control. Wage increases in the private sector remain modest, and in most cases below the inflation level. (The public sector, however, is a different story—see page 38.) The prices paid for industrial raw materials are inflating at under 2% a year. And competition from foreign suppliers makes it hard for companies to raise prices.

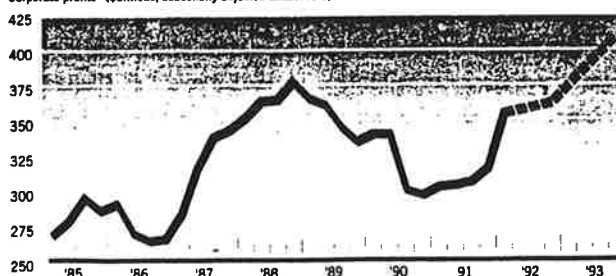
That, of course, is why nominal corporate profits are not rising very fast. But it is illuminating to look at profits in real terms, too. This shows that the latest recession has truly been mild. In real (1987) dollars, corporate profits bottomed last year at \$262 billion. That was miles better than the \$181 billion nadir in 1982 at the bottom of the last recession. This year profits are expected to hit an annual rate of around \$300 billion, and maybe \$327 billion next year.

That is actually better than in any year, except for 1987 and 1988, at the absolute peak of the Reagan growth period.

**Pretax corporate profits jumped in the first quarter, but some economists fear that profits growth over the coming 18 months may not be as good as this forecast suggests.**

### The best since 1989

Corporate profits<sup>1</sup> (\$billions, seasonally adjusted annual rate)



<sup>1</sup>Including inventory valuation adjustment and capital consumption adjustment. <sup>2</sup>Estimated annual average.

Source: The Survey of Current Business, Blue Chip Economic Indicators



# U.S. NEWS & WORLD REPORT

AUGUST 3, 1992

RECEIVED JUL 30 1992

## BUSINESS

# Taking air out of the recovery

*The great American debt binge of the 1980s is preventing the economy from gaining altitude*

**F**ederal Reserve Chairman Alan Greenspan is an old hand at disarming his critics and calming the panicked. But he was on the defensive last week during a tense trip to Capitol Hill to deliver the Fed's assessment of an economy that seems to be melting down just as the presidential campaign heats up. Senate Democrats charged that the economy is "wounded and struggling" and subjected their witness to a bruising interrogation. Greenspan gamely insisted that the recovery is gaining momentum but acknowledged that the economy is suffering through "an extremely painful transition."

Even the unflappable Greenspan cannot dismiss the vexing and painful question of this stagnant summer: What's wrong with the recovery? Factory output, which surged an average of 4.1 percent in the recovery years of 1971, 1976 and 1983, has inched upward just 0.8 percent this cycle. Employers, who created a blistering 358,000 jobs per month in the 1983-84 recovery, haven't added one net new job in the last year. Unemployment now stands at an eight-year high of 7.8 percent, and the Democrats smell blood. Last week, the Bush camp lashed back, hinting at a new economic recipe of its own and labeling the manifesto of Democratic nominee Bill Clinton "smoke and mirrors." But can Bush really talk? The president's approval rating for economic policy has plummeted to a piddling 18 percent. And no wonder. The economy grew at a miserable annual rate of 1.1 percent during Bush's first three years in office—the worst record since World War II—and the federal debt has exploded by 57 percent to \$4.1 trillion.

As Greenspan noted in his testimony, this recovery is different from any in the last 50 years, and the dominant differ-

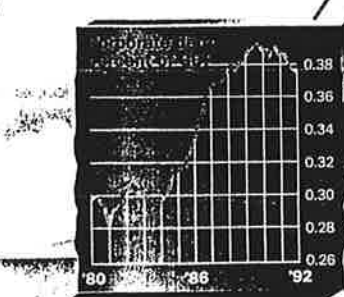
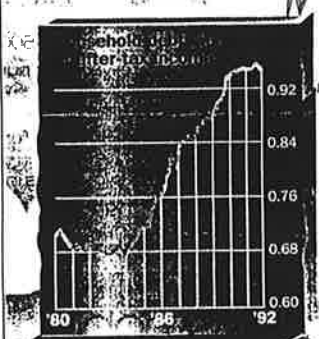
ence is debt. The nation's total debt from consumers, businesses and government more than doubled in the last 10 years to \$11.3 trillion. But in a development that defies postwar credit history, the economy has been unable in this recovery cycle to "reliquefy," or pay down debt and position itself for fresh spending. Economist Bruce Steinberg of Merrill Lynch & Co. estimates that the nation's debt dropped by 3.4 percent in the 1973-75 recession and by 4.3 percent in the 1979-81 downturn as Americans paid off loans and relied on high inflation to shrink their remaining IOUs relative to rising prices and incomes. The current cycle, by contrast, has seen real debt decline by just 2.3 percent.

**Dangerous debt.** Trapped by stubborn debts and recalcitrant bankers, consumers and businesses cannot embark on a fresh round of borrowing necessary to spark new production and hiring. Although no one wants to repeat the reckless leveraging of the 1980s, prudent credit is the



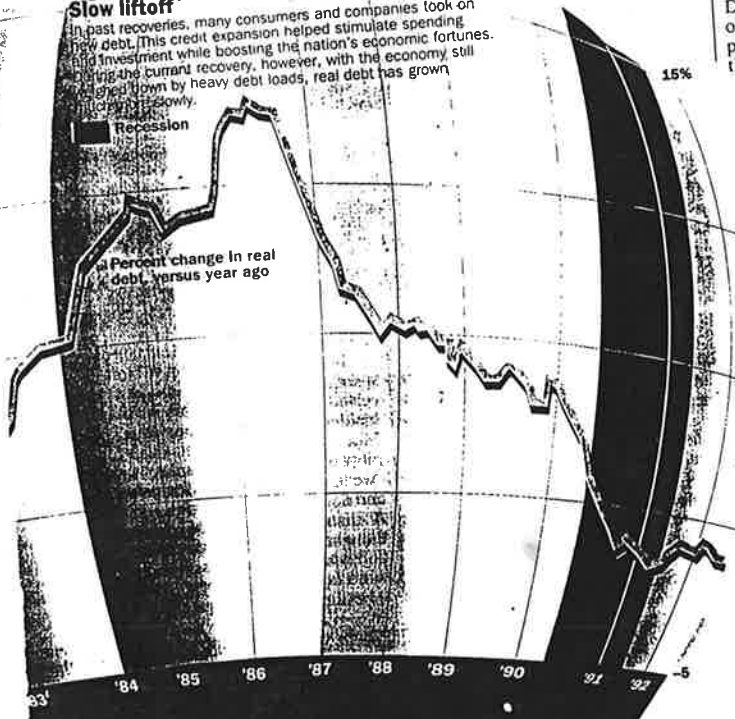
### Tied down by debt

Excessive borrowing by households, corporations and the federal government in the 1980s helped cause the recent recession and has left all sectors of the American economy with exceedingly high debt burdens. Until these onerous credit obligations are worked down, new debt will continue to grow slowly and the recovery will languish.



**Slow liftoff**

In past recoveries, many consumers and companies took on new debt. This credit expansion helped stimulate spending and investment while boosting the nation's economic fortunes. In the current recovery, however, with the economy still weighed down by heavy debt loads, real debt has grown slowly.



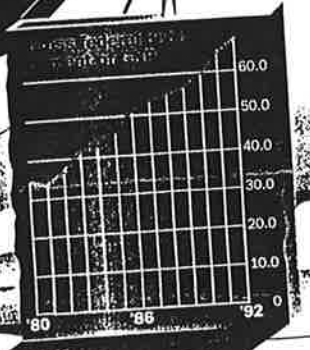
fulcrum that boosts housing, autos and business investment. Says economist David Levy, "Credit expansion is not only a normal part, it's an essential part of a growing economy." And yet the nation's past debts stand in the way of future growth. "Debt is the major impediment to a robust recovery," says economist and money manager Henry Kaufman. "There is simply no precedent for this in our postwar experience."

As the nation faces these uniquely troubled times, it is unclear who—if anyone—can rescue the beleaguered economy. Consumers, who account for two thirds of all spending in America, more than doubled their debt loads in the last 10 years to some \$4.1 trillion and now devote almost 20 cents out of every dollar of disposable income to debt service, up from 15 cents a decade earlier. People apparently slept easily with growing debt burdens in the 1980s, because their homes appreciated almost 8 percent annually and their disposable incomes rose a healthy 3 percent every year. But disposable income, after slipping 0.1 percent last year, is expected to grow just 2 percent this year, and household net worth actually dropped slightly in the first quarter of 1992, for the first time in at least 30 years. "Consumers don't feel wealthy," says Robert Johnson of Purdue University. "A home they bought for \$150,000 isn't worth \$150,000 now. That's depressing, and they don't feel like spending money."

This combination of debts from the past and stagnation in the present makes consumers wary about borrowing against the future. Consumer installment borrowing, which spurred ahead by some 12 percent in the economic recoveries of 1976 and 1983, has actually slipped 1.4 percent in the last year as anxious consumers have begun to pay down uncomfortable debt balances. Even with the addition of new mortgages and home-equity loans, total household debt grew just 4 percent last year, the slowest pace on record, says Merrill Lynch's Steinberg. Total consumer spending, which typically jumps 3.5 percent in the early stages of a recovery, has climbed just 2.1 percent in this cycle.

American business, whose investments account for about 13 percent of the country's spending, is making better progress than American households in paring down debt. In the year that ended last March, businesses trimmed their

Note: Real debt reflects private, nonfinancial obligations.  
 USN&WR—Basic data: Merrill Lynch, Department of Commerce, Federal Reserve Board, U.S. Office of Management and Budget  
 MOO LITTLE—USN&WR



debt loads by \$15 billion to less than \$3.5 trillion, the first time in at least 15 years that business obligations had shrunk year over year. Still, corporate debt remains equal to nearly 38 percent of gross domestic product, the highest level in at least 25 years. And interest payments, though they have fallen from their 1990 peak, still consume almost 25 percent of corporate cash flow, compared with about 20 percent 10 years ago.

**Battered balance sheets.** Chief financial officers might be congratulating themselves for their debt-reduction efforts, but they still must cope with badly battered balance sheets. For one thing, much of the debt on corporate books today was incurred in poorly conceived speculative ventures. But shrinking asset values and corporate profits, which have fallen to 2 percent of gross domestic product after interest payments are taken out — the lowest level in more than 30 years — have seriously reduced the economic viability of many of these deals.

The result is that bank lending to business is lagging well behind the pace of normal recoveries. Bank loans for commercial and industrial projects, which grew 1 percent in the 1976 recovery and 5.5 percent in the 1983 recovery, have actually skidded 4.5 percent this year. Cautious banks are pouring money into the safe securities of the U.S. government instead, and bank investments in government securities now equal 97 percent of commercial and industrial loans, the highest ratio on record, according to Carroll McEntee & McGinley Inc., a New York securities firm.

Corporate debt-service costs might have fallen even further if business weren't paying a huge price for the federal government's staggering budget deficit, estimated at a record \$333 billion to \$400 billion this year. These troubling numbers have kept long-term interest rates hovering between 7 and 8 percent, or an unusual 4 percentage points above the inflation rate. Washington's deficit is expected to remain at uncomfortable levels in the near future, and this means that real long-term interest rates could very well stay at historic highs despite the fragile economy.

Eventually, Chairman Greenspan insists, consumers and businesses will trim their debt loads so that vigorous new spending can begin and a robust recovery can unfold. But eventually is a long time for business owners whose cash registers aren't ringing, for workers who are standing on swelling unemployment lines and for a president whose own job security is now very much in doubt. ■

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BY DAVID HAGE

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# U.S. News & World Report

\$2.50

July 20, 1992

## ON THE ECONOMY

BY JOHN LISICIO

# To have and have not

**T**his is an open letter to the 10 million unemployed and the hundreds of thousands who will soon join their ranks. Don't believe anything you see or hear about the economy being in recovery. I know you have read a lot about it in this very space, but the last several weeks' worth of data strongly suggest it was just another false dawn. Recovery has become nothing more than a term that the fat cats on Wall Street use to keep the money pouring into the financial markets. As far as they're concerned, the weaker the recovery, the better. A sluggish economy keeps pressure on the Federal Reserve to push down interest rates even further, which lures more money out of maturing certificates of deposit and into the stock market. As long as business conditions remain too sluggish to produce new jobs, there's no threat of wage inflation, which makes bonds a good deal as well.

If you feel lousy, it's with good reason. Corporate America has been maximizing shareholder value on the backs of the working stiff ever since the man who thinks a bar code is a trendy way to signal for another gin and tonic moved into the White House 3½ years ago. It's a ghoulish scenario. Easing credit is supposed to spur reasoned investment, but the nearly 70 percent reduction in short-term rates engineered by the Federal Reserve since February 1989 has done nothing but stimulate frenzied speculation. Blue-chip stocks have advanced 45 percent over that stretch, but payroll employment has inched up a fraction of 1 percent, leaving more than 3.7 million people who have entered the labor force since that time without jobs. The chasm between stock prices and job growth stretched even wider as the Fed turned more aggressive in lowering rates. Between October 1990 and July of this year—a period that saw the Fed drop the discount no less than seven times—the Dow Jones industrial average soared 1,000 points, while nonfarm payrolls were winnowed by 1.2 million. Billie Holiday had it right: Them that's got, shall get; them that's not, shall lose—and in ever increasing numbers. It's a progression that can end only in social upheaval. How can we bequeath a massive federal deficit to our descendants and not create the jobs they need in order to make the payments?

**More job cuts.** I know it's small solace for all you folks struggling just to make ends meet, but let's hope there's strength in numbers. The strength to demand a new deal. Mobil, Amoco and Unocal announced permanent staff reductions totaling 11,600 last week, while oil-indus-

try executives estimate at least 50,000 jobs will be eliminated this year. Braniff Airlines went down for the third time, throwing at least an additional 2,000 people out of work. McDonnell Douglas Corp. said that 40,000 workers will be laid off if the sale of 72 F-15 jet fighters to Saudi Arabia is nixed. New Jersey said it must trim thousands of government jobs to close its budget gap, and the National League of Cities reported that 54 percent of 620 cities and towns are operating in the red. That's up from 52 percent last year. The Children's Defense Fund found the number of poor children increased by 1 million to 11.2 million between 1979 and

1989, a period that does not encompass the current recession. The child advocacy group's study of U.S. Census data showed child poverty increased in 33 states and that 17.9 percent of kids under 18 are poor. So I ask you, if the recovery was weak to begin with and the news keeps getting worse, how can it still be a recovery?

Yet the newspapers persist in calling it that, despite all the discouraging news on durable goods orders, housing, consumer credit, chain-store sales and money supply. Some goofy apologists for supply-side economics lay all of the blame for the stagnant job market on the failure to cut the capital-gains tax. A fuzzy logician at a prominent think tank cited the "cruel

costs" of raising the minimum wage. And one muddled mind even went as far as to assert that the main problem with the employment situation is that too many people expect to find jobs. Don't you get it? The only thing between you and a better tomorrow is a diminished expectation or two.

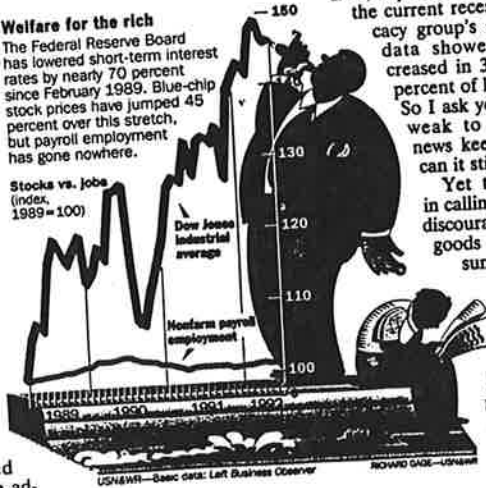
No, this isn't a recovery at all. The best name for it was coined by David and Jay Levy of Levy Economic Forecasts in Chappaqua, N.Y., some two years ago. They call it a "contained depression," an extended period that is likely to include a number of economic peaks and troughs. Neither the brief spurt in the summer of 1991 nor the more promising rebound earlier this year was anything more than a cruel hoax. They didn't represent the end of the continuing crisis, nor its many problems: business overcapacity, deflation, unemployment and financial imbalances.

It's time for all of us to face up to the sad truth. The economy isn't accelerating, it's just circling faster and faster around the drain.

### Welfare for the rich

The Federal Reserve Board has lowered short-term interest rates by nearly 70 percent since February 1989. Blue-chip stock prices have jumped 45 percent over this stretch, but payroll employment has gone nowhere.

### Stocks vs. Jobs (index, 1989=100)



USNEWS—Basic data: Left Business Observer  
HOWARD GAGE—USNEWS

# Survey: Small firms feel recession blues

By Edwin B. Lake  
Poughkeepsie Journal

Small and mid-sized New York state businesses may be breathing easier, most of them still hear the footsteps of the recession behind them, according to a poll conducted for the Fleet Financial Group, a state banking company.

Some 94 percent of those responding to the Fleet New York Poll said they believe the recession is continuing — a drop of 98 percent who said "yes" to that question in last December's survey. Interestingly, 84 percent of the bankers surveyed answered the recession is continuing, down 16 percent from last December.

The poll, conducted for Fleet by Penn & Schoen Associates of New York, indicated 53 percent of those surveyed think the recession will last another year or more.

Upstate business owners were the most optimistic — 41 percent believe the recession will last for another year, while 35 percent gave the recession six months or more; 20 percent said it will extend for one to three months more.

## Game plan changing

But some business and economic experts who examined the results did not line up behind the findings.

"My feeling is we are dealing here with more than a recession," said Elliot Rudoy, dean of community services and special programs at Dutchess Community College. "I think we're dealing with a whole restructuring of the way business and industry operates."

The recession has created a change in the game plan that businesses must follow,

he said.

"They have to do something to put themselves back into competitive positions," Rudoy said. "I think companies will have to look at their clients in a different way."

They must respond accurately and efficiently to their customers' needs; gone are the days when a company can produce goods and expect there will be ready buyers, he said.

Economist Dimitir Papadimitriou, executive vice president of Bard College and executive director of the Jerome Levy Economics Institute, said he felt the tone of the survey was slanted toward executives and not workers.

"New York state has been hard hit. Even though one may see some signs of improvement, the signs indicate a very weak recovery," he said.



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# NEWS

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## CLINTON

▶ CAN HE DO IT FOR THE DEMOCRATS?

▶ HOW HE SEES THE WORLD

# BusinessWeek

\$2.50

A McGRAW-HILL PUBLICATION

JULY 20, 1992

# The Recovery WHY SO SLOW?

PAGE 60

LOST JOBS  
JUST AREN'T  
COMING

CONSUMER  
BALANCE SHEETS  
ARE WORSE THAN

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ESTATE  
SLUMP IS  
DEEPENING

THE LIST GOES ON:  
NO WONDER THIS  
REBOUND FEELS  
LIKE RECESSION

02600

# THE RECOVERY: WHY SO SLOW?

**POWERFUL BARRIERS TO GROWTH ARE KEEPING THE ECONOMY IN LOW GEAR**

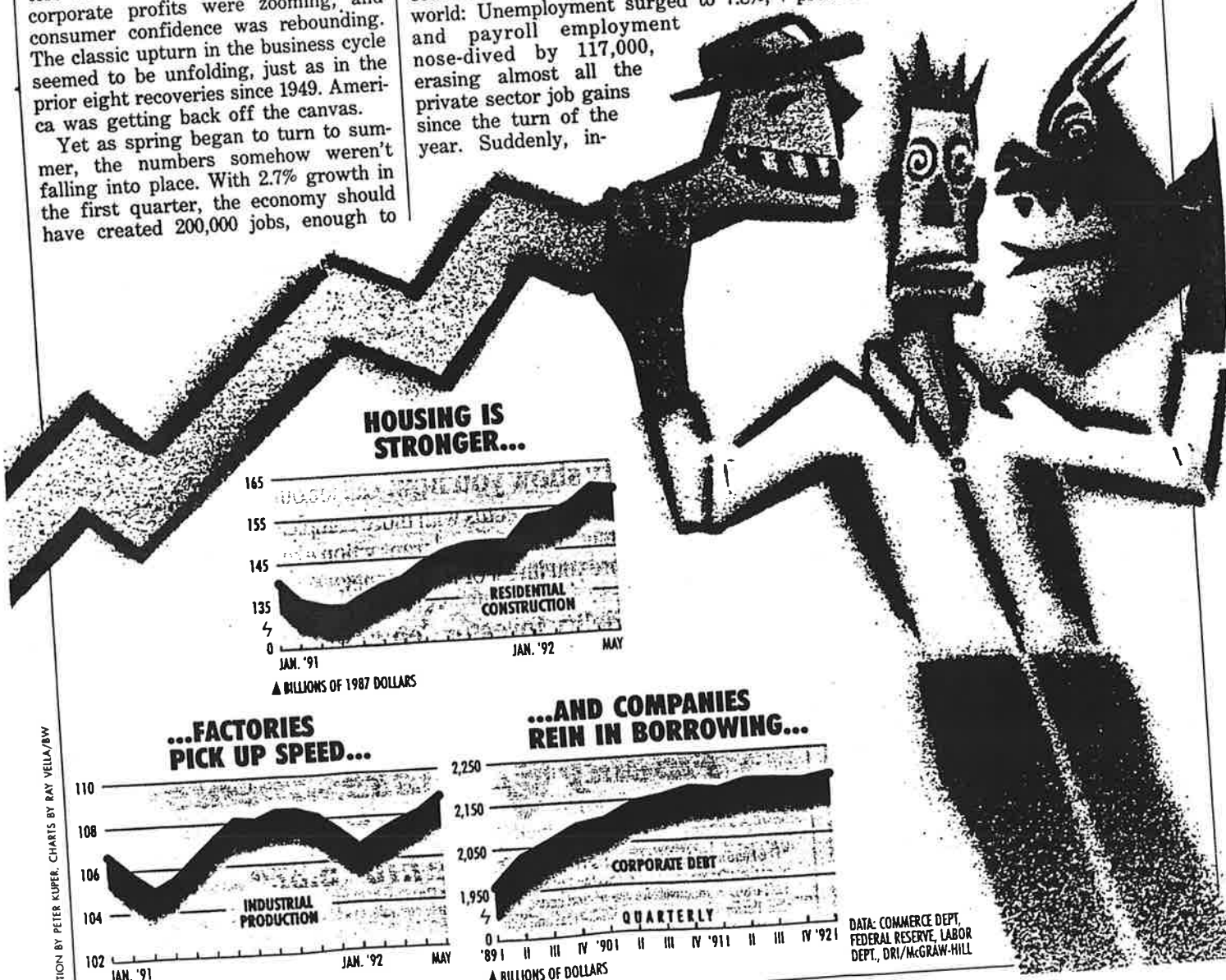
**F**or a brief time this spring, it looked as if three years of economic stagnation, including two quarters of outright decline, were over. The economy expanded for four quarters in a row, housing was reviving, corporate profits were zooming, and consumer confidence was rebounding. The classic upturn in the business cycle seemed to be unfolding, just as in the prior eight recoveries since 1949. America was getting back off the canvas.

Yet as spring began to turn to summer, the numbers somehow weren't falling into place. With 2.7% growth in the first quarter, the economy should have created 200,000 jobs, enough to

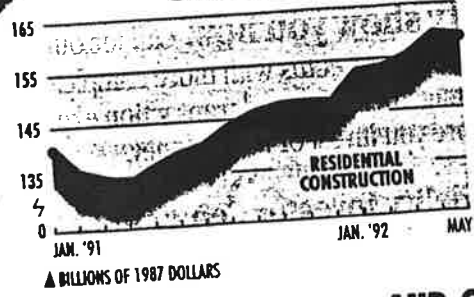
keep recovery on track. Instead, private payrolls declined. And April and May brought further hints that business was reluctant to hire and consumers were hesitant to spend. It was June's jobless rate, though, that shocked business executives and policymakers around the world: Unemployment surged to 7.8%, and payroll employment nose-dived by 117,000, erasing almost all the private sector job gains since the turn of the year. Suddenly, in-

stead of expanding, the U.S. economy appears ready to stall out, just as it did last summer.

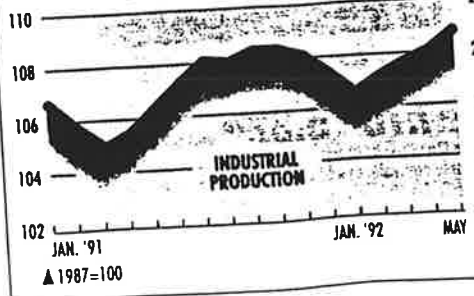
What's going wrong? Everyone knew that the financial excesses of the 1980s had left behind some structural barriers to growth. But the economy's long-term problems are turning out to be far



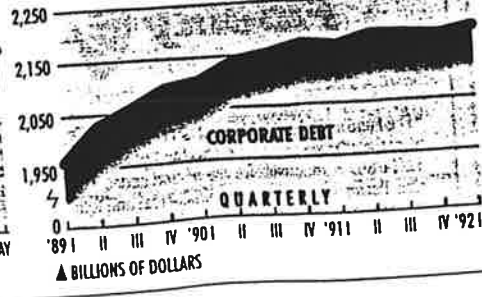
**HOUSING IS STRONGER...**



**...FACTORIES PICK UP SPEED...**



**...AND COMPANIES REIN IN BORROWING...**



DATA: COMMERCE DEPT, FEDERAL RESERVE, LABOR DEPT., DRI/MCGRAW-HILL

ILLUSTRATION BY PETER KUPEK. CHARTS BY RAY VELA/BW

started to hire at this stage of the business cycle. But not this time. Unable to raise prices in today's disinflationary environment and battered by global competition, companies feel that they need to shed even more workers in order to survive. Since the June drop in employment was announced on July 1, Amoco Corp. said that it will cut 8,500 jobs by the end of 1993. Aetna Life & Casualty Co., the giant insurance company in Hartford, will eliminate 10% of its total work force, or 4,800 jobs, by the end of next year. That comes on top of 2,600 jobs cut last year. "Many companies really are now realizing they are living in a global economy," says Christopher J. Steffen, executive vice-president and chief financial and administration officer for Honeywell Inc., which expects to cut 100 jobs this year by attrition. "They have to be substantially more efficient, and they're not hiring people like they did."

**POLITICAL GRIDLOCK.** Look at Ryder System Inc., one of the nation's largest truck-rental and -leasing companies. It has pared its employees down from 46,000 to 40,000 over the past three years. And even though Ryder's earnings of \$17.4 million were a long shot better than the loss of \$2.2 million a year earlier, the company doesn't have any plans to add workers soon, says M. Anthony Burns, chief executive at Ryder. And Dallas-based SnyderGeneral Corp., one of the country's largest makers of commercial air-conditioning and air-filtration products, has had a hiring freeze on for the past six months. The \$850 million revenue company also cut its 1992 capital-spending budget by about 20%, to \$2.8 million. "Our major concern is that we could fall back into a recession awfully easy," says Richard W. Snyder, the company's chief executive. "We need to make sure the economy has really turned."

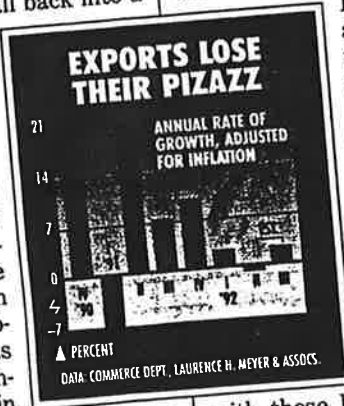
What's holding back new hiring in many cities is the plunge in commercial construction. Since May, 1991, construction of office buildings, hotels, and the like has dropped by 27%, compared with the 18% gain after the last recession, when it was a major engine of growth. This decline has affected more than just construction workers and real estate developers: The ripple effects have hit everyone from lawyers to cement manufacturers. There's no hope for a turnaround anytime soon. "You've got to be a real advanced stage, black-belt masochist" to lend to developers, says Richard L. Huber, vice-chairman of Continental



Bank Corp. Without loans, developers can't even start to think about building.

Much of the job weakness in manufacturing has one cause: The continuing demobilization of the U.S. defense economy. Defense contractor Hughes Aircraft Co., based in Southern California, recently announced plans to lay off more than 9,000 workers, or 15% of its current work force. In Massachusetts, Raytheon Co. is cutting an additional 700 jobs on top of last year's 4,900 job cut.

Without the defense cuts, manufacturing would be much stronger. Indeed, out of the 190,000 jobs lost in manufacturing over the past year, about two-thirds were in defense-related industries such as aerospace and communications equipment. And the cuts are having a disproportionate impact on income. Indeed, with defense spending dropping, the government sector has become a drag on the recovery rather than a plus. Paralyzed by a \$350 billion budget deficit, Congress and the Bush Administration had hoped that the economy could recover without help from



with these layoffs hitting some of the nation's most skilled and best-paid workers, the cuts are having a disproportionate impact on income.

## BANKS

PROFITS ARE UP SHARPLY—A RESULT OF FALLING RATES FOR DEPOSITORS AND THE CONTINUED HIGH COST OF BORROWING

fiscal policy. And for a while in the spring, it looked as if they were right. Now, the economy is staggering, but the huge deficit and political gridlock make it hard to increase federal spending or to cut taxes.

Yawning budget deficits at the state and local level are also holding back the recovery. In California, for instance, the governor and legislature are battling over how best to eliminate a nearly \$11 billion deficit hobbling a state economy that ac-

counts for more than 13% of the nation's output (page 67).

For all the structural problems, the U.S. economy is not about to shift into reverse. It does have a forward momentum that will keep it growing, albeit slowly. Autos are getting a kick from easy money and pent-up demand. In June, Detroit sold cars at a 6.8 million annual rate, up substantially from May. And dealers say people are now coming in to buy, not just to look. Karen M. Tibus, the owner of Saturn of Plymouth in Plymouth, Mich., says things have been going so well for her dealership that customers have to wait an hour-and-a-half to talk to a salesperson. "We're gonna have a very empty lot real soon," she reports.

The \$5.8 billion mobile-home industry is also looking up. After seven years of depressed results that wiped out half the industry, shipments started turning up sharply at the beginning of 1992. "It's about time," says Nicholas J. St. George, president and CEO of Oakwood Homes Corp. in Greensboro, N. C., which is the second-largest company in the industry.

Other types of businesses are also doing well. General Mills Inc., for example, racked up a 16% gain in net income in the fiscal year that ended May 3 and the company intends to boost capital spending somewhat over the next three years. Even small businesses a



more pervasive and far harder to overcome than economists, the Bush Administration, and even the Federal Reserve Board ever imagined. And this failure to understand just how deep-seated the barriers to growth really are led to a series of bad economic forecasts and feeble policy responses.

When the recession first started in July, 1990, most forecasters—including Federal Reserve Chairman Alan Greenspan—blamed it on the Persian Gulf war and expected a few modest cuts in interest rates to get the economy moving once the war was over. Then, when the recovery didn't materialize in 1991, most people thought that a few more interest-rate cuts by the Fed would do the trick, as they have in every recession since 1948. But that, too, failed to work. By now, the Fed has cut interest rates 18 times since 1989, and the economy is still mired in the longest period of stagnation since World War II.

And every time one problem seemingly abates, another unpleasant surprise pops up. Everyone worried about leveraged buyouts and the debt burden that

corporations piled up in the 1980s. But even as companies get their borrowing under control, it's consumer debt that's still too high. The banking system has avoided the collapse that some feared and returned to profitability again, but business and consumers are still paying through the nose for loans. Forecasters knew about coming defense cuts, but they thought that it would be a gradual process so the economy would be able to absorb most of the laid-off workers. Instead, the defense cuts have been deep and sudden. Everyone knew the glut of office space would linger for years, but the impact on local economies of plummeting construction spending has been far worse than anyone anticipated.

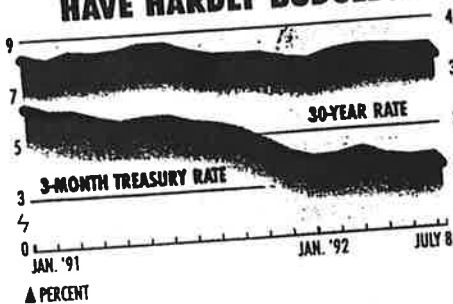
Companies that were supposed to have nearly completed restructuring seem to have started a new round of firings. In the past two weeks alone, many blue-chip companies have announced new layoffs. A second wave of firings is not supposed to happen when the economy is turning up.

Add all the unforeseen structural

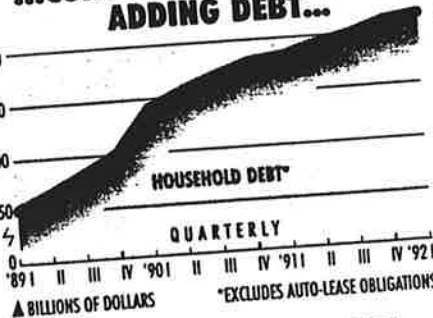
problems together, and the economy could stay flat for months. Before Election Day rolls around, the unemployment rate is almost sure to top 8%. And some fear that stagnation could continue into 1993 and beyond. Says Conway G. Ivy, vice-president and treasurer of Sherwin-Williams Co.: "We don't see signs of fundamental problems in our economy being corrected, so we see a likelihood of a sluggish, slow-growth economy for the next couple of years." **BIG PLUS.** That doesn't mean the U.S. is going to sink into a new recession. Economic growth, however slow and halting, is still being propelled by many of the same cyclical forces that have driven recoveries in the past. Low short-term interest rates—the lowest in 29 years—are making some types of borrowing more attractive. From cereal makers to mobile-home manufacturers, many businesses have seen a sales rebound. Auto sales at the end of June were running at a relatively strong 7.5 million annual rate. Housing has revived from its 1990 lows. And while weakness abroad has slowed U.S. ex-



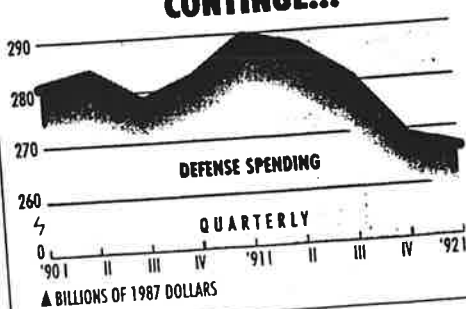
**...BUT LONG-TERM RATES HAVE HARDLY BUDGED...**



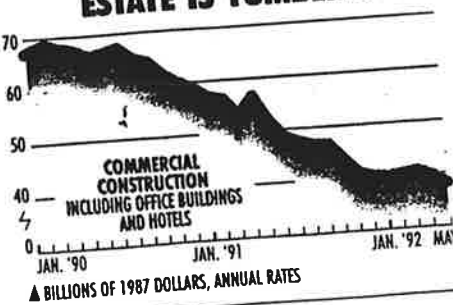
**...CONSUMERS ARE STILL ADDING DEBT...**



**...DEFENSE CUTBACKS CONTINUE...**



**...AND COMMERCIAL REAL ESTATE IS TUMBLING**



port growth, exports still remain a big plus for the economy.

Washington seems to have done a heroic job in rescuing the banking system. Sure, the cost of the savings and loan bailout has soared, but few savers have lost money, and there have been no bank runs. Two years ago, commercial banks, too, were in their worst shape in 60 years, reeling under an avalanche of commercial real estate loans gone bad. Yet over the past year, the profits of financial corporations, including banks, are up 40%, compared with 23% for all other corporations—a stunning reversal.

But the recovery is being hurt because the gains for the banks have come at the expense of savers and borrowers. As the Fed cut short-term interest rates from 9.85% in 1989 to 3.25%, the banks eagerly slashed the rate they paid depositors while hardly lowering their lending rates to borrowers. The widening spread between long and short rates hurt depositors, while keeping the cost of borrowing high. If the prime rate had fallen as much as CDs, banks would be charging 4.5% instead of 6% for borrowing, which would sure-

# Cover Story

ly stimulate the economy. "The shape of the Treasury yield curve is 'bankfare' or bank welfare," says David A. Levy, director of the forecasting center at the Jerome Levy Economics Institute.

What's more, bankers are shoring up the bottom line by being stingy with loans to businesses that could stimulate the economy. Instead, bankers are being cautious and investing unprecedented sums in default-free government securities. Over the past year, commercial banks invested \$115 billion in Treasury securities and cut back on their commercial and industrial loans to business by \$28 billion, which is hardly a recipe for recovery.

**BUSTED BOOMERS.** Economists were overly optimistic on recovery because they failed to fully grasp the new dynamics of consumer debt. In the past, consumers cleaned their balance sheets in recessions and the first year of recovery, which left them room to boost demand by borrowing more. But over the past two years, household debt rose by 10.2%, while aftertax income rose by only 9.4%. That's much different, for example, from the recession of 1974-75, when income rose much faster than consumer debt from the spring of 1974 to the beginning of 1976.

True, the most obvious type of consumer debt has fallen. Installment credit, including auto loans, has dropped by 10 billion over the last year. But that's far outweighed by the increase in second mortgages, including home equity loans, which rose by \$27 billion in 1991 alone. What's more, the



government's figures for consumer debt don't even count auto leasing, which has become increasingly popular. For example, General Motors Corp.'s SmartLease program leased 195,000 cars and trucks in 1991, up 86% from the previous year. In the first quarter of 1992, their lease volume was up 15% over a year ago—and none of these auto-lease obligations show up in the consumer-debt numbers.

In the past, consumers have been bailed out of their debt binds by rising incomes and by inflation—especially rising home values, which lowered the real value of their debt. Not this time. Real wage rates are declining at about 0.4% a year, putting the squeeze on consumers, and inflation has fallen to a negligible 3% annual rate. And last year's plunge in housing prices left many families with no financial cushion. The result: Consumer credit delinquencies are rising, and, according to the American Financial Services Assn., per-

at Moody's Investors Service Inc. And while consumers are still struggling with their debt burdens, anyone with savings is being hurt by the falling interest rates that were supposed to revive the economy. For example, after the Fed cut the discount rate, California's Bank of America cut its passbook savings rate from 3.25% to an astonishingly low 2.75%, and others followed suit. And rates below 3% could soon be common.

**JOB FREEZE.** Even before the most recent cuts, low interest rates were devastating people who depend on savings. Maria Smith (not her real name), a widow who lives in a condo in Orlando, Fla., put her money into certificates of deposit when her husband died 18 months ago. Everything was fine when those CDs were paying around 7%. But now that CDs are paying 3%, her income dropped from \$25,000 in the first quarter of last year to \$14,800 in the first quarter of this year. And she ran into a cash-flow crunch when her payments for income taxes and expenses outstripped her income by \$4,600 this year. Although she is still comfortably well-off, she is worried. "You don't want to use your principal," she says. "You would like to live on the interest that is coming in." As hard as low interest rates are on the elderly, the threat of job losses is shattering the average worker's confidence. Normally, companies would have

## DEFENSE

TWO-THIRDS OF THE 190,000 FACTORY JOBS LOST OVER THE PAST YEAR HAVE BEEN IN MILITARY-RELATED INDUSTRIES

sonal-bankruptcy filings in the first quarter of 1992 are up 10% over a year earlier. "We have a long way to go in rebuilding household balance sheets," says John Lonski, economist

## EXPORTS

SLUGGISH EUROPEAN ECONOMIES AND A SLOWDOWN IN JAPAN HAVE LED TO FLATTER SALES OF AMERICAN GOODS ABROAD



(TOP TO BOTTOM) PHOTOGRAPHS BY ALAN LEVENSON; ALEXANDER MARES-MANTON

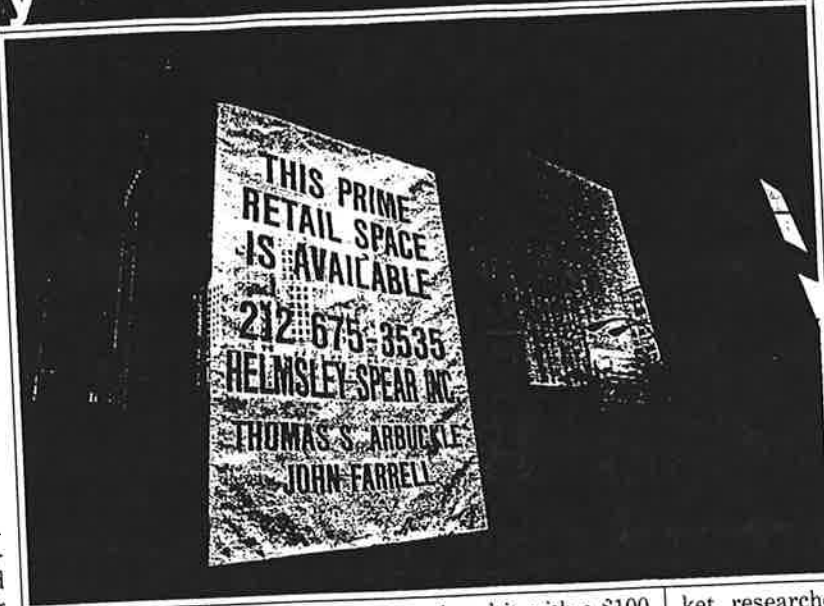


# Cover Story

seeing improvement. With his MBA in telecommunications complete in 1991, Stephen K. Morris, 37, of Piedmont, Calif., opened a consulting practice. "Clients are increasing the number of projects and the hours involved," he says. "They are definitely looking at an improved economy and improved sales."

**HOT FRIDGES.** The housing market, too, is getting better, despite some erratic swings. In Pittsburgh, for example, housing starts and home sales are holding up, and loan demand for mortgages and refinancings remains sturdy, says Stuart G. Hoffman, chief economist at PNC Financial Corp. And sales of refrigerators, stoves, washers, and other major appliances have been reasonably strong, perhaps because consumers simply have to replace models as they break down. Through May, major-appliance shipments were up 5.7% from a year earlier, and appliance makers such as General Electric Co. and Frigidaire Co. expect a modest increase in sales in the second half of the year.

Another piece of good news is that unlike individuals, corporations have streamlined their balance sheets. In each of the past two quarters, nonfinancial corporations raised new net equity capital at an annual rate of \$50 billion. They've also taken advantage of lower interest rates to reduce their overall debt payments. Carnival Cruise Lines Inc., for instance, called a zero-coupon convertible paying an interest



rate of 7.5% and replaced it with a \$100 million convertible paying 4.5% and some bank borrowings. Ryder has also cut its debt from \$3.1 billion to \$1.9 billion in the past two years. "Our financial condition is stronger than it has been in a decade," says Chief Executive Burns.

As a result, corporate debt has hardly grown over the past year. This has left companies poised for expansion once the economy shows some real signs of strength. For the first time in months, healthy companies are visiting First Union Corp., a major bank in Charlotte, N.C., window-shopping for rates and loan terms. And in Boulder, Colo., loan demand is particularly strong among high-tech and biotechnology companies that are expanding or relocating to the area.

Exports are still a source of strength for the U.S. economy, even though their growth has slipped in recent months as Europe and Japan slowed

## REAL ESTATE

COMMERCIAL CONSTRUCTION, A MAJOR ENGINE OF GROWTH IN THE 1983 REBOUND, IS STILL PLUMMETING

down. Lackluster growth overseas accounts for the leveling off in semiconductor sales, says James D. Feldhan, executive vice-president at mar-

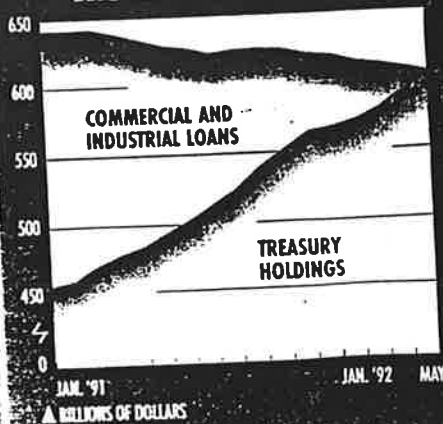
ket researcher In-Stat Inc. America's largest exporter, Boeing Co., is busy building planes, but its backlog of overseas orders is starting to fall.

Still, U.S. companies are no longer hobbled by a higher cost of capital than their foreign competitors, and hourly labor costs in the U.S. are among the lowest in the industrialized world. Combined with the falling dollar, that has kept U.S. goods and services competitive abroad.

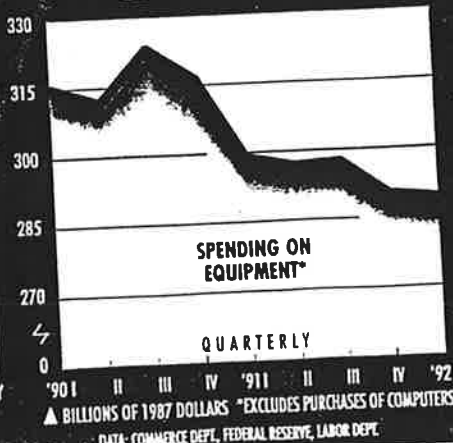
Right now, that is not enough to overcome the structural barriers and spark a healthy rebound. But monetary policy is easy enough and pent-up demand for housing and autos strong enough to ensure that the recovery will not abort.

By Christopher Farrell and Michael J. Mandel, with John Meehan in New York, Lois Therrien in Chicago, Zachary Schiller in Cleveland, Chuck Hawkins in Atlanta, Gail DeGeorge in Miami, and bureau reports

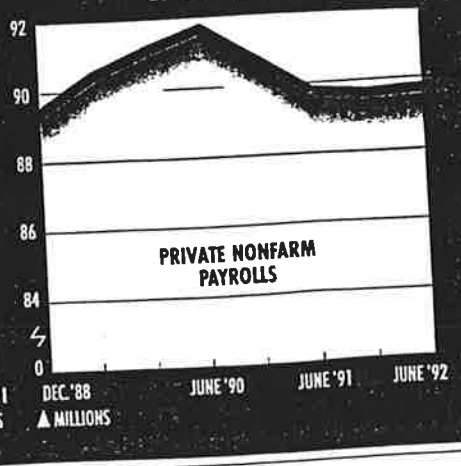
### BANKS BUY TREASURIES INSTEAD OF LENDING...



### ...WHILE COMPANIES CUT INVESTMENT...



### ...AND DON'T REHIRE WORKERS



CHARTS BY KAT VELLA/BW

DATA: COMMERCE DEPT., FEDERAL RESERVE, LABOR DEPT.

# NEWS

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## The Atlanta Journal THE ATLANTA CONSTITUTION

SUNDAY, JUNE 14, 1992

# Strong stock market bodes well for incumbents

By Bill Hendrick  
STAFF WRITER

**New York** — Because everyone loves to see their assets rise in value, President Bush may still have an edge in November.

Art prices that crashed in 1991 are starting to rise; the stock market is trading near its all-time high; Broadway ticket prices are up; even home values are finally beginning to edge upward again.

Rising values and a brighten-

ing economy historically have been good signs for incumbent presidents. That's because people vote their pocketbooks, and when their pocketbooks seem to be getting fatter, they don't see much reason to change leaders.

So even though some polls show Mr. Bush doing poorly against Democrat Bill Clinton and independent Ross Perot, experts say the president's popularity should rebound, unless:

► The fledgling economic recovery peters out and the unem-

ployment rate keeps rising.

► Wall Street's big-time investors get nervous that Mr. Bush really could lose, causing a major plunge in stock prices.

So far this year, the Dow Jones industrial average has risen 190.45 points and has pushing the index to 22 all-time highs.

"Stocks do well in election years, at least 2 percent better than in non-election years," said William N. Goetzmann, a Columbia University finance professor

who has studied trends in stock prices and elections dating back 200 years.

### Historic trends

Mysteriously, stock prices have risen in 28 of 41 presidential election years since 1828, according to the Foundation for the Study of Cycles in Irvine, Calif.

In eight of 13 presidential election years in which inflation-adjusted stock values fell, incumbents or their parties were

ousted. In 18 of the 28 years in which stock values rose, incumbent parties held onto the White House. In 10 contests since 1828, incumbents lost even though stocks rose.

Stocks weren't widely held by the public until after World War I. But the ups and downs of the market have come to be viewed as a barometer of the economy, because shares of companies rise in good times, along with wages and job availability.

Many academicians insist that presidents since the earliest days of the republic have manipulated the economy in election years to keep themselves or their parties in power, and their evidence is more than ample.

"The only thing that could explain the relationship between election years and the stock market is the transfer of wealth by the government," Dr. Goetzmann said. "It's the government doling out money for a trickle-down effect, like Bush is doing."

Yale Hirsch, a Wall Street historian who has studied correlations between stock prices and political races, claims stocks have scored a net gain of 250 percent in presidential election years since 1832, compared with a net decline of 10 percent in post-election years.

#### 'Pumping up' the economy

"It has always been the deliberate policy of incumbents to do what they can to pump up the economy," said New York University economist William J. Baumol. "Whenever the government has an option on the timing of starting some public works project, construction of an airport, things like that, it saves up the funds until the year before the election."

In his State of the Union speech this year, Mr. Bush ordered agency heads to speed up "discretionary" spending.

Government spending on borrowed money "has pumped profits into the economy," said New York economist S. Jay Levy. But by the fourth quarter, he added, a "deterioration of general economic conditions" is likely.

Dr. Goetzmann has dug even deeper into art archives than into stock market history, scrutinizing prices of paintings and other works in America and Europe back to the 1600s.



BILL HENDRICK/Staff

**"Stocks do well in election years, at least 2 percent better than in non-election years,"** says William N. Goetzmann of Columbia University, who has studied such trends.

He says art prices tend to start rising when economic conditions improve, as do stock prices. That has been the case not just since the New York Stock Exchange was founded 200 years ago, but for 100 years before that, he concluded after studying London stock prices in the 1700s.

Though art prices began plunging in 1989 when the U.S. and Japanese economies started slowing, "things have started to level off" and even to rise a little, said Gilbert Edelson of the New York-based Art Dealers Association of America.

That is a good sign for the economy, because art prices rise when wealthy people feel more secure, said Robert S. Salomon Jr., chief investment officer of Salomon Brothers Asset Management Inc. And wealthy people, generally, are the ones in positions to create jobs.

#### Wall Street psychology

Wall Street's rally, in turn, may be partly responsible for a recent upturn in consumer sentiment. In a phenomenon known as the "wealth effect," psychologists say even people who don't own stock feel more secure when they hear on the news that the Dow is rising.

Consumer confidence, which fell to a 10-year low earlier this year, has been rising steadily for several months, helping to explain increases in consumption spending, auto and home sales, and rising home prices.

A weekly consumer "comfort" index by Money Magazine/ABC News rose last week to its highest level since last September. Other confidence measures, by the Conference Board in New York and the University of Michigan, also have been rising.

The National Association of Homebuilders said last week that home prices rose across the country last month, even in the long-beleaguered Northeast.

Although many experts predict the economy will grow at a slow pace this year compared with most post-recession periods, they're relatively optimistic.

Laurence H. Meyer, a well-known forecaster based in St. Louis, predicts growth this year of 2.7 percent, compared with 0.3 percent in 1991. The government says the economy grew at a faster rate in the first quarter than it has since Mr. Bush's first three months in office.

Still, it takes a growth rate of about 3 percent to push the unemployment rate down much.

### **Income a key factor**

Real disposable income — an important measure of buying power — will increase only 1.9 percent, Dr. Meyer predicted. But that's better than last year's 0.5 percent rise.

According to research by Yale political scientist Edward R. Tufté, odds are more than 3-to-1 that incumbent parties will lose in election years when real disposable income increases less than 3 percent.

For now, the economic numbers look better for Mr. Bush than the figures gathered by political pollsters. But there is plenty of time left before November, and polls have proved wrong many times.

"It's a delicate matter of timing," said Dr. Baumol, of New York University. "Bush would be in trouble if the election were held today. But my impression is, conditions are getting better very slowly."

# NEW YORK

June 8, 1992

## The Bottom Line/Christopher Byron **BALANCING ACT**

### MISGUIDED BUDGET BUSTERS

THERE'S AN UNFUNNY MOMENT IN THE 1980 movie *Fatso* when overweight Dom DeLuise confronts a chained and padlocked refrigerator in his kitchen and, defying his relatives, begins desperately ripping the chains away to get at what's inside.

The scene suggests a spectacle that may soon begin unfolding in real life in Washington. Call it budget bulimia, as Congress and the White House, after two decades of binge/purge deficit spending, prepare to take up a proposal by Democratic Senator Paul Simon of Illinois. Its purpose: to chain and padlock the door to the Treasury through a balanced-budget amendment to the Constitution.

For now at least, about the only voice speaking out against the proposal belongs to Leon Panetta, Democratic chairman of the House Budget Committee. Last week, Panetta called a press conference in Washington to drive home the message that somewhere between \$550-billion and \$600 billion in spending cuts and tax increases would be needed to bring the budget into balance by 1997 whether a balanced-budget amendment becomes law or not.

"The fact is, we don't need a constitutional amendment to balance the budget," said Panetta. "We have all the constitutional power we need to do the job. All it takes is leadership and the will to do it."

Panetta's point was a good one, for whether an amendment becomes law or not, it will only be through cuts such as those outlined at his press conference that Congress will ever be able to balance anything. Nor was Panetta the only person putting forth a list of axable government programs last week.

From the opposite end of the political spectrum, the conservative Heritage Foundation weighed in with its own list of goodies. Included on the list: \$2.2 billion in savings from eliminating the Superconducting Supercollider, \$9.7 billion from scrapping the space station, \$2.4 billion from selling off the Naval Petroleum Reserve, \$26 billion from eliminating agriculture crop supports,

\$5 billion from axing dairy subsidies, and \$795 million from scrapping the preposterous "Honey, Wool, and Mohair" subsidy program.

Surging spending for programs such as these is a key reason the budget is out of control, and for that the White House is as much to blame as Congress itself. As a top staffer for the Senate Appropriations Committee put it last week, "We're getting awfully tired of hearing all this stuff from the White House about congressional profligacy. The fact is that President Bush has never sent us a balanced budget even once."

could not be worse. Reason? Like a junkie from the streets, the economy has by now become so addicted to red ink that it can't risk going cold turkey without inviting cold sweats and convulsions. In fact, economists such as David Levy of Levy Economic Forecasts warn that without continued deficits, the economy would begin lurching back into recession all over again.

As Levy explains it, with the economy weak, deficit spending by Washington is offsetting the collapse of private investment in everything from homes and office buildings to airplanes, cars, and factories—a condition that Levy says is likely to last for several more years.

"People supporting the balanced-budget amendment are thus advocating the most disastrous economic-policy course imaginable," says Levy. "Were the amendment to be adopted and serious attempts made to enforce it, the economy would fall into a deep, uncontained depression and the budget would still not be balanced."

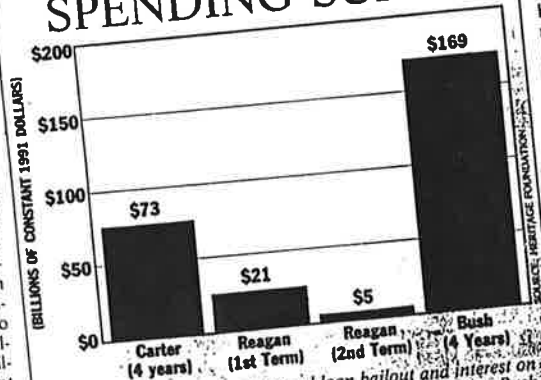
Nonetheless, a groundswell of support for a balanced-budget amendment appears to be growing in Washington. In the view of Norman Ornstein, the congressional-affairs expert at the American Enterprise Institute, the groundswell is the culmination of nearly twenty years of failed efforts, by Democrats and Republicans alike, to curb the growth in deficit spending.

Call it the politics of frustration. There's been the 1974 Budget Reform Act, the 1986 Gramm-Rudman-Hollings Deficit Reduction Act, and, most recently, the appallingly misguided budget summit the federal government held in 1990. Through them all, the federal debt has swelled and swelled, from \$380 billion in 1970 to what the Congressional Budget Office now estimates will reach an astonishing \$4 trillion by this coming September.

"We've tried flyswatters and hand grenades and even bazookas to deal with this problem," says Ornstein. "Now it seems we're going to try dropping an A-bomb."

A constitutional amendment to require a balanced budget is hardly a new idea. A proposal for such an amendment was ad-

### SPENDING SURGE



Even leaving out the savings-and-loan bailout and interest on the federal debt, growth in domestic spending by George Bush is 70 percent greater than growth in domestic spending by Ronald Reagan and Jimmy Carter combined.

In fact, as the chart on this page vividly shows, domestic spending during the four years of the Bush administration already dwarfs the spending that took place during the twelve years of the Reagan and Carter presidencies. As Scott Hodge, a budget analyst at the Heritage Foundation, points out, Congress's own budget is up by 32 percent since 1989, the Interior Department's budget is up by 36.5 percent, and the Transportation Department's budget is up by 25 percent.

Unfortunately, few in Washington seem even remotely interested in actually doing something about this mess, most preferring the Pilate-like approach of calling for a constitutional amendment, then washing their hands of responsibility for what may happen next. Yet the timing for such an amendment



vanced, without noticeable success, by Ronald Reagan as long ago as the early days of his first term, in 1981. Since the mid-eighties, the idea's chief proponent in Washington has been Simon of Illinois, and he, too, has not had much success with it, at least until recently.

Yet now the mood is changing. Sources in both the House and Senate say there will be a debate on his bill—as well as on a piece of House-side companion legislation—in June. Thereafter, say these sources, the chances are good for passage by the end of July.

"If that happens, 30 states will ratify it within a year," says Thomas Mann of the Brookings Institution in Washington. "After that, there's a good chance for eight more states to follow suit within six months." That would give a total of 38, the minimum number needed for the amendment to become law.

Just as Ross Perot has surged to overnight political stardom on a simplistic promise of straightening out government with plain talk and "electronic town hall" meetings, so too has Simon gained backers for his bill because of its beguiling simplicity. Basically, the proposed legislation would require the president to submit only balanced budgets to Congress. If Congress wanted to add spending to a budget thereafter, it could only do so if three-fifths of both the House and the Senate voted to allow it.

Of course, almost any such amendment would invite abuse. Budgets might be made to seem balanced if phony economic assumptions were used, inviting endless rounds of constitutional lawsuits. Or, as Ornstein puts it, Congress could conceivably try to balance its budgets by wiping out federal funds for programs that require matching contributions from the states. The states would then have to pick up the tab, pushing their own budgets out of whack even as federal deficits began to shrink.

Why then do so many in Congress seem to find the bill appealing? Some of the measure's supporters no doubt genuinely believe the amendment will work. Others seem to agree with former congressman William Frenzel, onetime ranking minority member of the House Budget Committee, who endorsed the amendment in House testimony, saying that Congress should adopt the proposal "because you have proved you cannot do anything else."

Yet Ornstein warns that still others in Congress support the amendment not because they think it will work but because they see it as a risk-free vote—enabling them to appear politically correct on the deficit issue while secretly and cynically hoping that the states will fail to ratify the amendment once Congress approves it. Of such calculations is economic policy being made in Washington these days. ■

# The Incredible Shrinking Middle Class

AMERICAN DEMOGRAPHICS

ITHACA, NY  
MONTHLY 35,000

MAY 1992

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**America's shrinking middle class is a well-known trend. This study explains why it's happening. "Economic migrants" into upper and lower classes became more numerous in the 1980s. Women's earnings became more important to middle-class families. But in most families, the man's earnings still have the biggest influence on life's ups and downs.**

by *Greg J. Duncan, Timothy M. Smeeding, and Willard Rodgers*

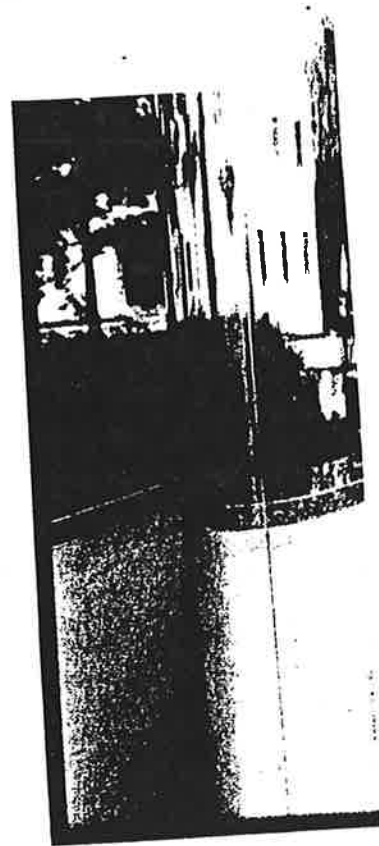
**F**or more than a quarter century, researchers have watched an uneven but unmistakable decline in the size of America's middle class. The overall distribution of wages and earnings has become more unequal. The

share of total household income derived from earnings has fallen, while the share derived from capital investments has grown.

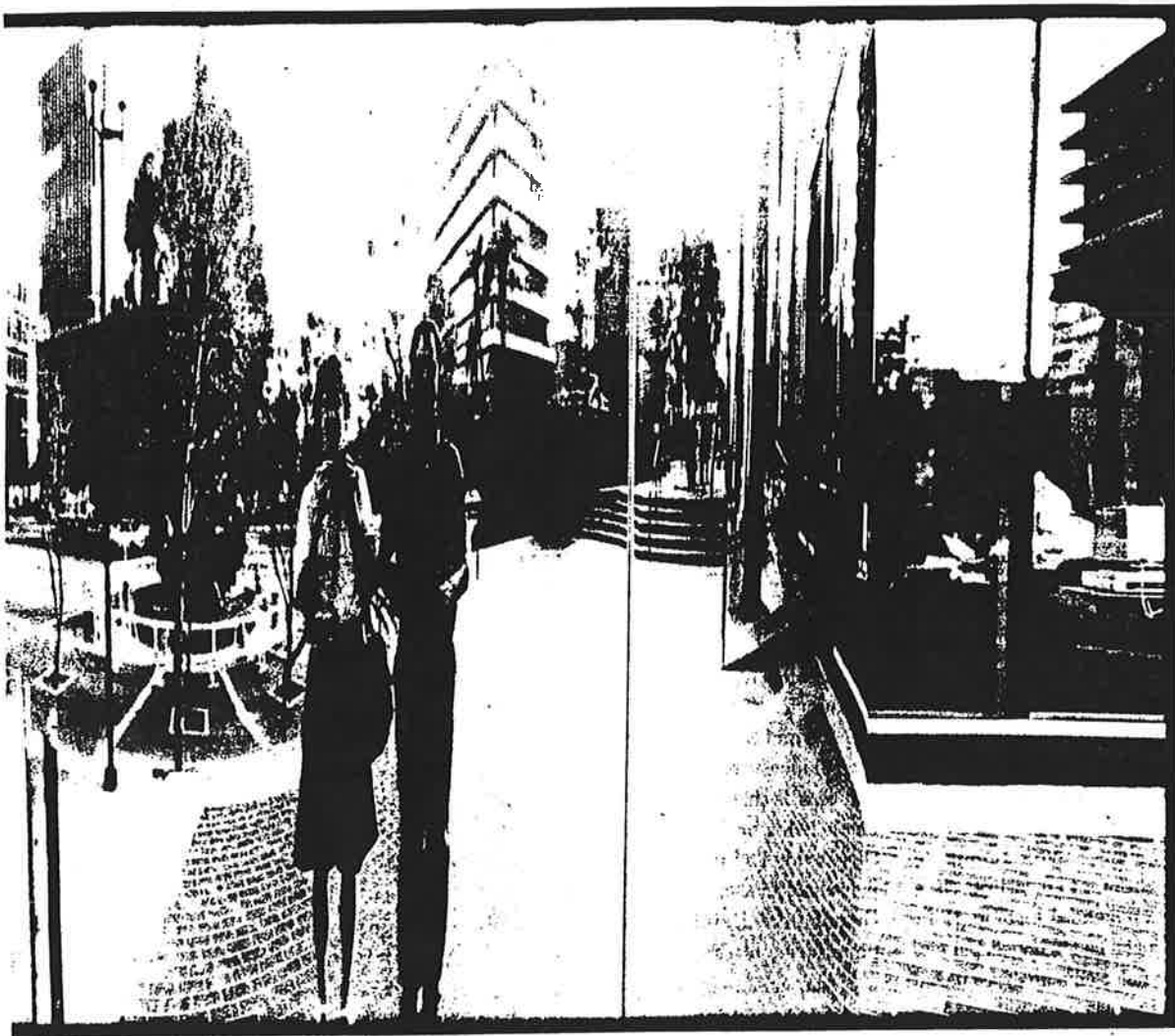
Social researchers usually rely on cross-sectional surveys—snapshots of household conditions at certain points in time—to study the economic conditions of Americans. But this method can only reveal net changes in income distribution. It cannot show another important aspect of the issue, which is the movement of families into and out of the middle class.

To study the economic migration of Americans, we looked at 22 years of data

*Greg J. Duncan and Willard Rodgers are with the Survey Research Center at the University of Michigan. Timothy M. Smeeding is with the Metropolitan Studies Program at Syracuse University. The research for this article was sponsored by the Jerome Levy Economics Institute.*



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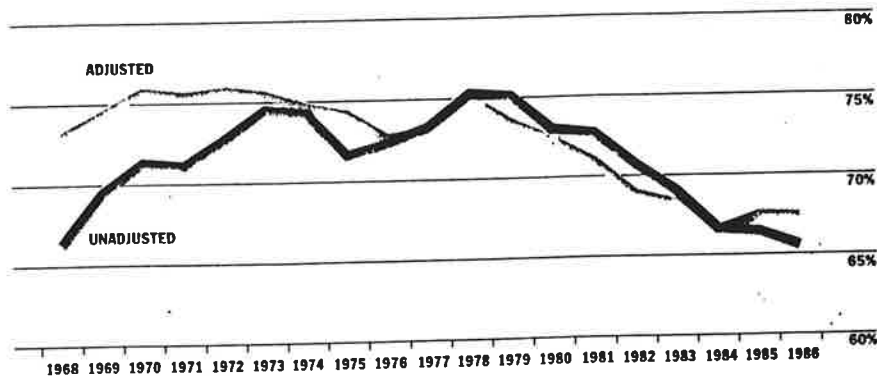


DEDE HATCH (PHOTO) ROBERT ACETO (HAND COLORING)

# THE DISAPPEARING MIDDLE

*The share of adults who are middle class declined from 75 percent in 1978 to 67 percent in 1986.*

(percent of middle-income adults aged 25 to 55, by two different measures,\* 1968-86)



\* The unadjusted measure is the share of all adults aged 25 to 55 with after-tax incomes between \$18,500 and \$55,000 in 1987 dollars, including food stamps. The adjusted measure is the share of all adults aged 25 to 55 with an income-to-needs index between 2 and 6. An income-to-needs index of 1 indicates that a family is at the poverty threshold.

Source: Authors' calculations based on the Survey Research Center's Panel Study of Income Dynamics

(1968-89) from the Survey Research Center's Panel Study of Income Dynamics (PSID). This study attempts to follow all members of its nationally representative sample through time, so it provides a unique historical record of a family's financial ups and downs.

The data show that the 1980s were simultaneously a time of enhanced upward mobility and more frequent downward mobility.

## THE SHRINKING MIDDLE

The public debate on the middle class focuses on prime-age adults: those who are old enough to be independent of their parents, but too young to be candidates for retirement. Accordingly, we limited the sample to adults aged 25 to 55.

There is no standard definition for the term "middle class," even among researchers who attempt to measure "class" by measuring household income. Some studies adjust incomes for household size, while others do not. Some analyses use after-tax income to chart economic fortunes,

but most use pretax money income. And some researchers define affluence in terms of an absolute dollar figure, while others measure it relative to a distribution.

We developed two measures of economic status, one of which adjusts a household's income for household size. Both measures are based on after-tax household income, and both set the boundaries of middle income between the 20th and 90th percentile of the sample. Since food stamps are arguably equivalent to cash, we include their dollar value as a component of household income.

Our unadjusted measure places the boundaries of the middle class between \$18,500 and \$55,000 in 1987 dollars. The second measure, which adjusts for household size, is characterized by an income-to-needs index based on the official poverty threshold. The index equals 1.0 when a household's income is equal to the poverty threshold.\* Using this measure, the boundaries of the middle class fall be-

\* In 1991, the poverty threshold for a family of four was about \$13,500.

tween the index values of 2.0 and 6.0, or two to six times the poverty line.

Both of our measures reveal similar economic pictures. And when our PSID data are compared with the Census Bureau's Current Population Survey, both indicate similar declines in the proportion of middle-income households.

Our PSID analysis also reveals the story behind the overall census numbers. Using the household-size adjusted income index, we found that smaller households helped to increase the proportion of prime-aged adults in the middle class during most of the 1970s, but failed to prevent a dramatic decline in the size of the middle class in the 1980s.

Seventy-five percent of 25-to-55-year-olds were middle income in the early 1970s. This share fell in the mid-1970s, and again reached 75 percent in the late 1970s. Then it plummeted to 65 percent in 1983, and it had recovered only slightly (to 67 percent) in 1985-86.

The income-to-needs index shows even steeper declines. Only about 65 percent of prime-aged adults in 1985 were middle class according to this measure.

**After 1980, it became more difficult to escape from poverty.**

A growing number of upper-income households drew people out of the middle class in the late 1970s and throughout the 1980s. Between 1979-80 and 1985-86, the proportion of high-income households grew from 8 percent to over 13 percent. The income-to-needs measure shows that the share increased from 10 percent to over 16 percent.

The erosion of the middle class becomes even more pronounced if you account for household size. While a substantial percentage of middle-class adults have moved into upper-income brackets, an even greater fraction are joining America's poor. This raises two important questions: what kinds of people cross these economic

boundaries, and what life events determine their income losses or gains?

### THE ECONOMIC MIGRANTS

Over a typical five-year period during the 1970s and 1980s, nearly 7 percent of adults with initial after-tax household incomes of between \$18,500 and \$55,000 ended the period by making more than \$55,000 a year. A much larger share of initially high-income adults—more than 29 percent—dropped into the middle class. In addition, one-third of low-income adults succeeded in making the transition to a middle-class life, while 7 percent of middle-income adults fell below the lower-income limit. The smaller share of people in the upper- and lower-income groups means that the actual numbers of people making these transitions were more nearly equal than these proportions suggest.

Married couples dominate the group that successfully makes the transition from a lower to a higher income. This was especially true before 1980, when married couples accounted for 90 percent of all transitions into high-income status. But they also accounted for 79 percent of transitions from high- to middle-income status.

The probability that a female head of household would move into the upper-income group improved after 1980. Most of the upwardly mobile women were highly educated, young, and childless. Their good fortune was due to real earnings growth.

In the late 1960s and in the 1970s, the transitions into and out of the middle class roughly canceled each other out. But in the 1980s, all four transition streams tended to sap the middle class. A higher percentage of individuals climbed into high-income status, while a smaller share fell out. A lower proportion of low-income individuals moved into the middle class, while a larger share dropped down.

### LIFE'S UPS AND DOWNS

A college education is the single most important factor in facilitating favorable economic transitions and avoiding unfavorable ones. Also, transitions into high-in-

# The EXPERTS *Speak*

*Our authors predict that America's middle class will continue to shrink in the 1990s. What do other experts say?*

"SOMEBODY who wanted to be hopeful would have two good reasons. One is that the current period of corporate restructuring will bring about a rise in productivity and a rise in real wages. Rising real wages were the basis of the big growth of the middle class in the 1950s and 1960s. The second reason is that the earnings gap between college-educated people and high school graduates has been extremely volatile over the last 20 years. There are some reasons to believe that this gap will begin to close again in the 1990s."

—Frank Levy, professor of economics at the School of Public Affairs, University of Maryland, College Park

"THE most pertinent question may be, 'What will be the change in consumption?' Consumer debt has exploded. Increases in household equity during the 1980s have increased homeowners' ability to borrow. For the lower class, this is not true. Credit is less available to the poor, and they don't own homes.

"The shrinking middle class suggests changes that are much more profound than the data suggest. Changes in family structure will have much more impact than economic conditions. There are more single-parent families. There is less marriage. That is a profound set of changes that has much more potential to upset the fabric of society."

—Robert Avery, professor, Department of Consumer Economics and Housing, Cornell University, Ithaca, New York

"THERE may be a force in the near future that could cause real wages to fall. The increase in college graduates that began in the 1980s could cause a glut of college-educated workers. This could diminish the earnings gap between college-educated workers and those without a college education."

—McKinley Blackburn, assistant professor of economics, University of South Carolina, Columbia

"DURING the 20 years from 1969 to 1989, the proportion of children whose relative incomes were less than half the median grew from 19 percent to 29 percent. Given the growth in single-parent families and the reduction in the supply of good-paying jobs, it is difficult to be optimistic about a reversal of this trend."

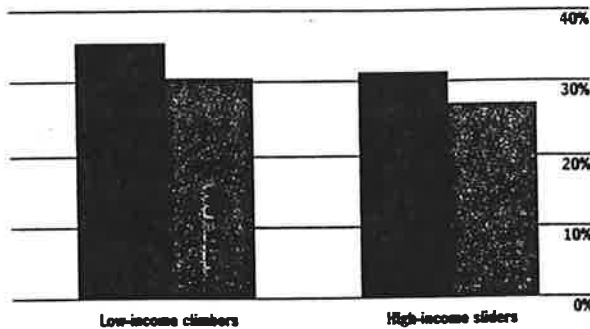
—Jack McNeil, economist at the Census Bureau



# FEWER MOVING IN

*Rich or poor, fewer people moved into the middle class after 1980.*

(percent of adults aged 25 to 55 moving into the middle class from lower-income groups and upper-income groups, 1968-79 and 1980-87)

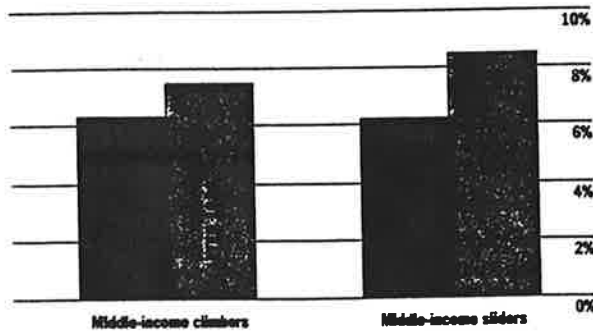


Source: Panel Study of Income Dynamics

# MORE MOVING OUT

*In the 1980s, middle-income people found it easier to achieve wealth and harder to avoid poverty.*

(percent of middle-income adults aged 25 to 55 moving into upper-income groups and lower-income groups, 1968-79 and 1980-87)



Source: Panel Study of Income Dynamics

come status are more common among older adults than younger adults. Being under age 35 or black hinders one's upward mobility. Both before and after 1980, blacks were only half as likely as others to move into high-income status, even after adjusting for differences in schooling,

household composition, age, and income.

After 1980, it became more difficult for Americans to move out of the low-income group. Only college-educated adults had a significantly higher-than-average chance of rising into the middle class. Blacks and women heads of household continued to have difficulties breaking out of the lower-income group. And being young gave an edge to economic climbers in the 1970s, but not in the 1980s.

Overall, a smaller share of adults dropped out of the upper class after 1980. But the probability of falling from middle-income to lower-income status increased significantly after 1980. Women heads of households and blacks maintained their already higher-than-average risk of downward mobility. The risk was much lower than average for people with at least a high school education.

## EARNINGS INEQUALITY

Our study found that the biggest single factor behind the withering of the middle class is the growing inequality in the distribution of men's earnings.

Women's earnings are becoming more and more important to family finances, but men's earnings play the dominant role in most economic transitions. This is true both before and after 1980. For both men and women, the economic rewards of a college degree in-

creased dramatically, while less-educated adults often saw the real value of their earnings decline.

Higher rates of pay, rather than overtime or second jobs, account for most of the favorable transitions driven by men's earnings. But upward mobility associated with women's earnings was evenly split between pay increases and longer hours. Downward transitions for men were usually associated with job loss. For women, changes in both wages and hours accounted for negative changes in earnings.

The withering of the middle class is marked by two major forces. First, there has been upward movement among prime-age men and women who managed to get and maintain large gains in their earning power. At the same time, lower-income households saw a stagnation of real earnings. In other words, the rich got richer and the poor got poorer.

The middle-class decline documented in our study may well continue into the 1990s. The recession of 1990-92 should further retard upward mobility for lower-income adults, while causing many borderline cases to fall into poverty.

The good news is that late 20th-century America has offered abundant opportunity for the upper-middle class. The bad news is that at the same time, it has reduced upward mobility among the working class and produced persistently high poverty rates for families with children. These two opposing forces are draining America's middle class.

## TAKING IT FURTHER

For a complete text of the original paper by Duncan, Smeeding, and Rodgers, call Greg Duncan at the University of Michigan's Survey Research Center; telephone (313) 763-5186. For a comparative study of low, middle, and higher-income households, see "Up and Down the Income Scale" in the July 1990 issue of *American Demographics*. And a detailed account of historical income trends can be found in "Trends in Relative Income: 1964 to 1989" *Current Population Reports*, Series P-60, No. 177, available from the U.S. Government Printing Office. Additional copies may be purchased by calling (800) 828-1133.

# US Mood Gloomy, but Not Nearly As Bad as '30s or '70s, Analysts Say

By Marshall Ingwerson

Staff writer of The Christian Science Monitor

WASHINGTON

**P**RESSURES for change continue to build in the American body politic.

The economy registered sobering new statistics, scaling back some of the optimism about how fast it was going to revive.

Housing starts fell 17 percent in April after rising in February and March, the largest drop in eight years. The trade deficit, which has been narrowing unsteadily since 1987, suddenly inflated in April.

Neither figure represents an actual downturn, as most economists read them. But this certainly is not a familiar pattern of recovery.

Familiar patterns are not holding in politics either. In a strong

sign of American dissatisfaction, a Time-CNN survey last weekend showed President Bush and the Democratic near-nominee Bill Clinton trailing an unannounced independent candidate with no political experience.

Ross Perot and Mr. Bush are generally within striking distance of each other in the polls these days, at between 30 and 35 percent. Mr. Clinton tends to run just behind them. (Ross Perot baffles analysts, Page 2.)

These views are fickle. Just over a year ago, Bush's approval ratings were close to 90 percent in many surveys; during his term he has had the highest popularity ratings in the history of polling. Now he is at his lowest approval rating ever.

Confidence in Congress, of course, is even lower, averaging around 20 percent. The last time approval of Congress was this low was during the Watergate scandal

in the early 1970s.

New York Gov. Mario Cuomo (D), at a Monitor lunch on Wednesday, explained the Perot support as a message to working politicians: "Everyone's saying, 'You're not giving us good-enough answers.'"

In the Bush administration, many officials are feeling the pressure for action on an urban agenda and are setting out their own markers. If they have not achieved some significant policy change by the end of next month, says Housing and Urban Development Secretary Jack Kemp — and other officials speaking anonymously — then White House seriousness about urban problems is open to question.

Congress is also feeling the heat of voter frustration. It is probably weeks away from voting to amend the Constitution to require balanced federal budgets

See US page 3

US from page 1

Some members long opposed to the amendment are giving up on balancing the budget through politics as usual. The deficit, nearing \$400 billion this year, keeps breaking records.

Some political scientists see the dissatisfaction among voters as mostly superficial compared to other times or other countries. "We're nowhere near crisis in our political system," says Michael Robinson, a public-opinion expert at Georgetown University. "It was much worse in 1968, when a third of young people seriously questioned the legitimacy of the United States."

"The degree of real underlying lack of confidence was much greater in the '30s and the '70s," says Everett Carl Ladd, director of the Roper Center for Public Opinion Research at the University of Connecticut.

Polls have become volatile, changing mirrors and magnifiers of public moods, he says, but Americans have a basic belief in their political institutions. "There's no great challenge to our value cosmology as in the Great Depression," says Dr. Ladd.

Yet most political strategists and poll readers are seeing levels of voter cynicism and anti-incumbent sentiment that they don't recall since at least the Carter years.

"We're setting some records for low trust in the institutions," says James Thurber, an American University professor and director of the Center for Congressional and Presidential Studies.

The economy is an important element in the political dissatisfaction in America. It continues to defy expectations, based on past recoveries, that its momentum will pick up. The bad news on

**'We're setting some records for low trust in the institutions.'**

— James Thurber,  
American University  
professor

trade and housing starts this week was not as bad as it appeared on the surface. Both measures had shown strength in previous months. And overall growth in domestic production rose to about a 2 percent annual rate during the first quarter of the year.

"But the first quarter gave rise to an optimism about the strength of the economy that really was not warranted," says Gail Fosler, chief economist of the New York-based Conference Board. In fact, she says, no sign has appeared of

anything approaching a normally robust recovery.

The housing construction industry has held steady this year, says S. Jay Levy, chairman of Levy Economics Institute.

The trade deficit has been on a plateau for about six months, he says, adding that the improved growth in the first quarter was largely due to the federal government's increased deficit spending.

Deficit spending is falling off somewhat through the rest of the year, and in the private economy, the forces of caution remain in a rough balance with the forces for growth, says Ms. Fosler.

Both economists expect growth to weaken late this year, creating — says Fosler — "great pressure for change" on the body politic. Attitudes have changed dramatically in the past few years, she says. The central concern of government officials has shifted from holding inflation down to expanding growth and jobs.

Professor Robinson says that the 1990s are characterized by a growing importance of the economy in national attitudes and a more palpable concern than ever about the breakdown of families and other social institutions. But, he adds: "Even when we were number one in everything, in the 1950s, we were terribly unhappy with where we were."

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BURRELLE'S

# Wholesale prices up 0.2% in April

## Expert: Economy not in jeopardy from inflation

The Associated Press

WASHINGTON — For the third straight month, wholesale prices, helped by a moderation in energy costs and the biggest drop in vegetable prices in nine months, edged up 0.2 percent, the government reported Tuesday.

So far this year, the Producer Price Index, a measure of inflation before it reaches consumers, has risen at an annual rate of just 1 percent, and many analysts believe the rest of the year will show little acceleration from that pace.

"The economy in terms of inflation is not in jeopardy at all. The unfortunate thing is that despite lower inflation, we don't have a sustained recovery," said Dimitri Papadimitriou, executive director of the Jerome Levy Economics Institute at Bard College, Annandale-on-Hudson.

But that might not be the case for long, economists said. If good news about consumer prices, to be released Wednesday, follows Tuesday's report, there's a better chance the Federal Reserve will cut interest rates and spur the sluggish economy.

"The Fed is very cautious about not lowering interest rates too much," said Ann Davis, a Marist College economics professor and director of the college's Bureau of Economic Research.

To that end, Federal Reserve Chairman Alan Greenspan said he would like to see virtually zero percent inflation before the Fed moves to try and boost the economy, Papadimitriou said.

The Producer and Consumer Price Indexes are not directly linked, though producer prices provide a rough estimate of what the consumer can expect to pay for goods in several months.

"Goods producing is just part of the cost. The consumer has service charges, . . . and services count very heavily," said Conference Board senior business analyst Delos Smith.

### Investors take profits

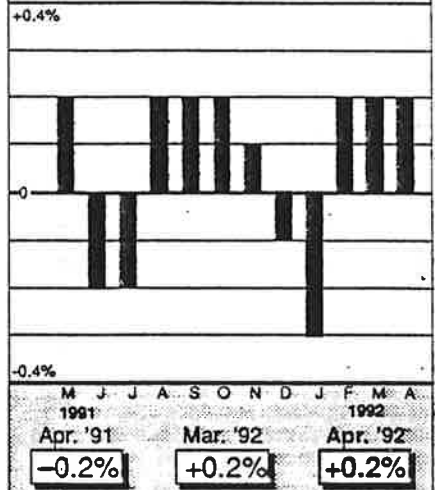
The prospect of further Fed rate cuts sparked a rally Monday on Wall Street as the Dow Jones industrial average set its 19th record close this year. Stock prices opened even higher Tuesday but then retreated as investors sold to reap profits.

The Fed last cut interest rates a month ago, hours after release of a PPI report showing prices rising 0.2 percent in March.

While some economists said another rate cut could have come as soon as Tuesday, most expect central bank to wait for today's reports on inflation at the con-

## Producer Price Index

For finished goods  
Seasonally adjusted change from prior month



Source: U.S. Dept. of Labor

Associated Press

While energy prices rose, the increase of 0.5 percent was less than half of a 1.2 percent spurt in March.

Analysts noted that about the only area where producer prices threatened to get out of hand was in the area of tobacco prices, which shot up 1 percent in April.

The moderation in energy prices combined with an actual drop in food prices, which edged down 0.3 percent. The decline was led by an 18.1 percent slump in vegetable prices, the biggest decline in this category since last July, as tomato prices fell by 56 percent and sweet corn prices dropped 49 percent.

The energy moderation reflected the fact that prices for natural gas and electricity fell during the month, helping to moderate gains in other energy categories.

Unlike in other sectors, natural gas and electricity prices have a direct impact on what consumers pay for their energy source since utilities are allowed to reflect the monthly cost of fuel on their bills, said Central Hudson spokesman Tim Massie. Consumers shouldn't expect to see their May bills go down because the utility was just granted a rate increase, Massie said.

Gasoline prices, which have risen steadily this year, were up another 1.4 percent in April, following a March increase of 1.1 percent. Home heating oil jumped an even sharper 4.6 percent last month.

Outside of the volatile energy and food categories, prices rose a modest 0.2 percent, the same as the overall number. Analysts said this showed that the underlying rate of inflation is remaining well behaved as well.

— Journal staffer Kimberly P. Harrison

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Dick Papiernik

## Governing and the economy

**W**ho causes inflation? That's what William F. Buckley Jr. asked in his best Buckleyesque manner as he immediately provided the answer: "Only the government can cause inflation. The private sector has never figured out how to do it. A dollar today is worth one-sixth of what it was worth in 1950, and we have government to thank for this."

Former senator and Democratic presidential candidate George McGovern parried the Buckley thrust to remind the audience at a recent Bard College debate that government also gave us anti-discrimination laws, anti-pollution laws, social security and unemployment compensation and laws protecting children and the safety of workers.

In addition, McGovern said, the government was in large part responsible for funding public television and that without such funding, Buckley could lose his job as host of "Firing Line." It was a fitting parry, since the topic of the debate was: "If you want more jobs, the government should get out of the way."

Buckley brought several nationally prominent public-policy experts to the Jerome Levy Economics Institute at Bard College a week ago Thursday to tape the two-hour debate. It was broadcast nationally on "Firing Line" Friday night.

It made me appreciate the inadequacy of programs that masquerade as presidential campaign debates.

For instance, on "Firing Line," the participants were able to demonstrate how serious debate could be not only intelligent and informative, it also could be humorously witty and even civil — well, mostly civil. I haven't found that combination in the presidential campaign debating.

Bard's Levy Institute, located on the Hudson about 70 miles south of Albany, has had a magnetlike pull on the powerhouse personalities who set the tone for public policy and economic discussion in this country.

Paul Volcker and Alan Greenspan, former and current chairmen of the Federal Reserve Bank, frequently participate in programs that bring in the top economists in the world to the school.

The "Firing Line" debate lined up Buckley with Herbert Stein, economist, author and former chairman of the Council of Economic Advisors under both Richard Nixon and Gerald Ford; plus Phyllis Schlafly, lawyer, author and commentator; and U.S. Rep. Richard K. Armey, R-Texas, an economist.

Lined up with McGovern were Michael Kinsley, a lawyer and an editor of *The New Republic*; Robert Eisner, author, economist from Northwestern University and past president of the American Economics Association; and Hyman Minsky, author and economist at Bard College.

Bard President Leon Botstein set the tone for innovation: "It's clear that we cannot sustain the normal progress that simply allows the good times to be followed by bad times and bad times by good times."

The affirmative group led by Buckley generally argued that as a matter of public policy, less government intrusion into the private sector is almost always better and leads to more productivity and growth in the economy.

On the other side, Bob Eisner captured the essence of the opposition when he said he would increase the scope of government as an economic engine.

"The real problem for the future is investment and saving," he said. "But I believe in leaving private investment to the private market. It's the public investment that we need, the investment in education, in research. If our 13-year-olds continue to score last in math and science compared with other developed countries, we're going to have a hard time competing in a modern and technologically advanced world."

Stein argued that government policy should be directed to encourage private investment in order to raise productivity of labor and that education expenditures should be redirected "in order to spend more on disadvantaged people."

Lest the group take itself too seriously, Eisner reminded all of them of an observation made by economist John Kenneth Galbraith: Economists asked to predict when we're going to get out of the recession fall into two groups — those that don't know and those that don't know they don't know.

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## Fine job on unemployment tonight

**U**<sup>7720</sup> **UNQUESTIONABLY** one of the most important issues in this election period is unemployment. That and taxes. And if you think solutions are easy after listening to the candidates debate, try listening to some knowledgeable economists on tomorrow's "Firing Line" (Ch. 13, 9 p.m.)

The question being debated is: "Resolved: If you want more jobs, the government should get out of the way."

For the resolution are: William F. Buckley, Jr., Rep. Dick Armey (R-Tex.), columnist and attorney Phyllis Schlafly and Herb Stein, senior fellow of the American Enterprise Institute.

Opposing the resolution are: George McGovern, former Democratic presidential candidate, Michael Kinsley, editor of the New Republic, Hyman P. Minsky of the Jerome Levy Economic Institute of Bard College, and Robert Eisner, professor of economics at Northwestern University.

You'll get a mini-education from the two hours, moderated by Leon Botstein, president of Bard College. The give and take is often witty, always intelligent and civil. In a nutshell, those for the resolution think the recession is policy-driven, that there should be less government interference, and then more jobs would be created by the private sector. Says Buckley: "Who causes inflation? Only the government can cause inflation. The private sector has never figured out how to do it."

McGovern points out if government were completely out of the picture there might not be public broadcasting and there would be no "Firing Line." He says the government is necessary "to protect workers and consumers and to strengthen the American economy."

It's a stimulating session, with these fine minds locking horns, all with good humor.

— Kay Gardella



