Pathfinder

CENTER FOR EDUCATION AND RESEARCH IN FREE ENTERPRISE
TEXAS A&M UNIVERSITY COLLEGE STATION, TEXAS 77843

March 1986 Volume 8 Number 1

AN IMPORTANT MESSAGE FROM A BUSINESS LEADER

This paper is based on excerpts from the speech J. Peter Grace made at the Third Annual Editor's Conference hosted in San Antonio, Texas, by the Center for Free Enterprise. The selection of excerpts was made by the Pathfinder *editors.*

We were out in L.A. in Century City and President (Ronald) Reagan said to me, "You know, when I was governor out here in California, there were more federal employees all over the state than state employees. I couldn't imagine what they were all doing, but it was none of my business. I was only governor. But now I'm President. I understand California. Will you find out for me how many federal employees there are in California, where they're located and what they're doing?"

"Sure, sure, Mr. President," I said. So I rushed back to Washington, I ran up to the OMB and I asked them the questions.

"Well, we don't have any of that," they said. I said, "You are the ones I was going to have get the information for me." "Well, we don't have it."

So I said, "Look, if I don't have that next week, I'm going to hold my first press conference and announce that the federal government occupies 2.6 million square feet of office space. That's four times all of the office space of the 10 largest cities in America, including all that empty space down in Houston. And, furthermore, the payroll is $62 billion, the pension liability is $550 billion, and nobody down there can tell you who is getting it, where they are, or what they're doing."

They said, "You wouldn't hold such a press conference." I said, "Yes, I will if you don't get me that information." They said, "We'll see what we can do." I said, "I thought you might rethink your position."

The problem in Washington is all Congress. I have to run this little company called W. R. Grace & Co. I got them down to three simple powers: organize it, set the compensation, control capital expenditures. If you control those three powers you can run any company. Now, the President has none of those powers. He can't organize the company; only Congress can organize the government. Can he set pay scales? No, the President can't do it; and, although 43 governors of our states have line-item veto power, the President has no line-item veto power.

The Veterans' Administration operates, as you know, many hospitals and nursing homes. They build nursing home beds for $64,000 a bed. That's four times the private sector cost of $16,000. They build hospital beds for $192,000 a bed; that's twice the private sector cost of about $91,000.

You take one buck at the end of 1983, then borrow it at 10 percent. Between the end of 1983 and the year 2000, compound that out and you will see that every dollar is $71, because you're borrowing it and you're borrowing the interest, and you're borrowing the interest on the interest, and you're borrowing the interest on the interest on the interest, and that accumulates out to $71. So our $140 billion a year is $9.8 trillion. I never knew about trillions until I got down to Washington. When you get into trillions, you approach infinity. If somebody was born at the minute that Jesus Christ was born and started counting seconds, he'd be at 62.5 billion today—that's six and a quarter percent of a trillion. You know how long it takes to count a trillion seconds?—31,700 years.

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I heard Senator (Robert) Dole the other day; he's the majority leader. He said that if you're hanging around with nothing to do, come on down to the Senate. You'll watch all those speeches being made and nothing going on at all and you think, where am I? But don't worry about it. If there are not many people down there on the floor, you're lucky, because you can't do business in the Senate without a quorum. As long as there are only three to four people on the floor, the country is in good hands. He said it's only when 50-60 in the Senate are down there that you want to be concerned.

We went over to the Defense Department and asked them about that. "What the hell is going on? Why are you paying $675 for toilet seat covers?" . . . It's gotten to the point where the most expensive order that a commanding officer can give his men is, "Gentlemen, be seated."

The only guy who's not mad today about sending his money to Washington is Bob Hope. I asked him why. He said, "That's where the best jokes are."

Take a little thing like electric power rates. I'll bet the power costs in Houston are about eight cents a kilowatt hour. In San Diego it's 12.3 cents a kilowatt hour. But in the Northwest where the power marketing system is owned by the federal government, it's only 2.3 cents. The U.S. taxpayer is paying the difference. I was arguing with the House committee on that and a congressman from the Northwest said, "You're not going to do anything about this power marketing situation. You're not going to touch that." I said, "Why don't you stick it up to a national referendum and see how you come out?" So we recommended that they privatize the whole northwest power marketing situation and save $19 billion. You know what the Congress did? As soon as we came out with the report, the Congress renewed it (contract) for 30 years at a cost of $876 billion.

That's that way it goes. Amtrak started in 1971 on an experimental basis. It's cost $9 billion so far and is going to cost another $8 billion in the next decade. Between New York City, where I come from, and Boston, the subsidy on that ticket is 2.3 times the cost of air fare between New York and Boston. But we go right on with it. More special interests.

The Department of Defense spends $22.6 billion a year on spare parts, and the Navy only takes competitive bidding for 16 percent of it. That's why we're paying $91 for a two-cent screw and $346 dollars for a $7.50-hammer. That's why we even pay $679 for a toilet seat cover. We went over to the Defense Department and asked them about that. "What the hell is going on? Why are you paying $675 for toilet seat covers?" They say, "Well, the problem is the secretary hasn't taken a position on them yet." It's gotten to the point where the most expensive order that a commanding officer can give his men is, "Gentlemen, be seated."

The computers in the government. . . . There are 17,400 of them, 12,000 of them are obsolete. That's why the Social Security System paid $14.3 billion in checks to the families of dead social security recipients. I called Frank Carey up; he was the IBM CEO at the time. "Hey Frank, can you come down and help us with these computers?" "Sure." I sent his name to the White House. No way! Why not? Conflict of interest. We couldn't put anybody on the computer problem except people who had never dealt with computers.

If something is not done to stop this waste and inefficiency, and if they go right on spending the way they've been spending, you will have a deficit in the year 2000 (that's only 14 years away) of $1.966 trillion. The debt will be $13 trillion and the annual interest will be $1.5 trillion.

You take the defense situation. We found 4,000 military bases and they only need 326. We've got a military base in Fort Monroe, Virginia, that still has a moat around it. They've got one in Salt Lake City that was built to defend against the Indians. They just can't close them because Congress will not let them close them.

These liberal congressmen will tell you it's Reagan's tax cuts on the rich that cause the deficit. A question I got from a lady: "I don't remember seeing anything in your report about taxing the rich." I said to that woman reporter, "Let's put a 100 percent surcharge on all incomes of over $75,000, not 10 percent, but 100 percent." She said, "That would be good." And I said, "Hurray, now we can run the government for 7.2 days." And that's all it is. You take everybody's income over $75,000 that's not taxed and tax it, you can run the government for 7.2 days.

—J. Peter Grace
Chairman & CEO, W. R. Grace & Co.
Chairman, Private Sector Survey on Cost Control

THE GRAMM-RUDMAN BILL

Given the importance of the Gramm-Rudman Bill, Pathfinder *asked Senator Phil Gramm, a former colleague in the Department of Economics, to explain the bill in his own words.*

After three months of debate and repeated votes by both houses of Congress, the Gramm-Rudman balanced budget legislation has become law. During my seven years in Congress, no bill has been more thoroughly weighed and measured, analyzed and examined. Still, the public debate is far from over and there are two relevant questions we will continue to ask as we go forward under the provisions of Gramm-Rudman in the coming months and years:

- How did we reach this point?
- Where do we go from here?

In 1981, we adopted a change in federal policy aimed at changing the country by changing the policies of our government. We said we would stop inflation, the scourge of a whole generation, and we have. We stopped inflation cold.

We said we would end the economic stagnation that gripped America in 1981, and we have. We created 10.1 million new jobs —more permanent, productive, taxpaying jobs with a future than all the make-work government jobs programs adopted through the entire span of American history.

But the one promise we made in 1981 that we failed to deliver on was the promise to balance the federal budget. The Gramm-Rudman measure makes good on that promise by creating a mechanism to ensure the deficit is reduced—in an orderly, step-by-step, process—to zero by the end of the decade.

In a real sense, adoption of the Gramm-Rudman legislation reaffirms my faith in democracy. Every pro-spending special interest group in the country came out against the bill. They sent letters and lobbyists. But Congress knew that the people back home who do the work and pay the taxes were demanding that action be taken. For the first time in a long time, the public interest prevailed over the special interests.

But passage of this legislation marks only the beginning, not the end, of our work. In the coming weeks, months and years, every special interest group in America will continue to pursue deficit reduction at everyone's expense but their own.

Gramm-Rudman puts the fat in the fire. Now, America must choose either to rend lard from that fat—which is my goal by controlling federal spending—or to put out the fire by raising taxes.

Our legislation does not dictate which choice is made, it only requires that a choice be made.

Another set of decisions poses the question of which programs will be reduced and which will grow. Specifically, the debate has raised the question of our national defense program.

The American people clearly support a strong defense. As long as we are efficient in providing it, they will continue to support our defense program. I believe the American people will pay for defense, for veterans' programs and for other programs that are reasonably conceived and efficiently operated. In the same vein, I am equally convinced that the American people will choose to reduce or eliminate those programs designed to serve only the special interests.

The questions will be easy ones for most people. Ask yourself, "Do I want my tax dollars to finance training for the soldiers, sailors, airmen, and Marines who defend our country? Do I want my tax dollars to subsidize fares for passengers on Amtrak?"

This legislation became law because Americans are already asking and answering similar questions. It will work because the questions will not go away, because the people who pay the taxes and pull the wagon in America know that it will work for them and for their children.

—Phil Gramm
U.S. Senator, Texas

JOINT STATEMENT ON TRADE POLICY

Reprinted from the Cato Policy Report, 1985

Today, as individuals associated with leading policy research organizations in Washington, D.C., we are joining together to express our concern over the growing calls for trade protectionism.

Support for free trade is almost universal among economists and others who have studied the issue. Yet, special-interest groups, finding themselves losing out in the marketplace, have been all too successful in their lobbying efforts, gaining special "protection" and thus limiting consumer choice. Such protectionist policies impose major costs on American consumers and unfairly restrict their ability to purchase those products they prefer. Rather than expanding employment, trade restrictions save jobs at the expense of others.

The U.S. economy as a whole is not suffering because of imports, contrary to protectionist claims. Employment has increased by eight million in the past five years. Manufacturing production is at an all-time high. Total output in the United States has increased 13 percent since 1980, while we moved from a big trade surplus to a trade deficit.

It is true that other nations impose obstacles to imports from us. We also impose obstacles to imports from other countries. The proper remedy for this is not to escalate a war of retaliatory protectionism. The remedy is to push for agreement on trade liberalization for all.

There are always some workers, firms and industries hurt by competition, whether foreign or domestic. But this competition is healthy. Protecting every worker, every firm and every industry from competition would stultify the American economy and diminish the incomes of the American people.

Our message today is a simple one. Congress should not repeat the mistakes of the past. As individuals associated with the American Enterprise Institute, the Brookings Institution, the Cato Institute and the Heritage Foundation, we urge all within Congress and the administration to avoid protectionist policies and to support expansion of international free trade.

—Robert W. Crandall
Senior Fellow
Brookings Institution

—Edward Hudgins
Walker Fellow in Economics
Heritage Foundation

—William A. Niskanen
Chairman
Cato Institute

—Herbert Stein
Senior Fellow
American Enterprise Institute

BRIDGING THE GAP BETWEEN ECONOMICS AND POLICY: THE CASE OF MINERALS

Over the years, many different issues have focused attention on problems of mineral economics and mineral supply. The oil crises, the "Club of Rome Report" and the "resource war" issue are cases in point. Today, concerns over the security of the minerals supply to the American economy are highlighted by events in South Africa. At the same time that the security of external supplies is being questioned, our domestic metal mining industry is still declining. This decline, which has been going on for years, resulted from a combination of interventionist measures, particularly in the areas of taxation, labor, and environment. Certainly the import dependency of U.S. industry on foreign strategic metal supplies has increased markedly during recent decades.

This article relates how, in one jurisdiction—the Ontario Ministry of Natural Resources—a program of mineral policy research and advice has been developed and followed for more than 10 years. This program merits a close look, if not emulation, by policymakers in other jurisdictions and policy areas.

But it is not only security-of-supply considerations that make it worthwhile to look at the way this program was developed and implemented, and at the results it yielded. There are three more reasons why it may be of interest to readers of the *Pathfinder.* First, the program was developed and is being implemented by individuals committed solidly to free market principles, and these principles have been applied in policy development in an environment that has not always been friendly to such ideas. Second, in light of the importance of Canadian mineral and energy supplies for U.S. strategic and industrial purposes, Ontario's leadership role in mineral policy development for all of Canada becomes relevant to the assessment of broad U.S. interests. And third, it has been a program in which a number of economists associated with the economics department of Texas A&M University have been deeply involved.

In the early 1970s, the Ministry of Natural Resources of Ontario embarked on a program of developing an integrated mineral economic analysis and mineral policy advice capacity. It obviously was realized that policy debate in the board rooms and in the legislature was, on the one hand, heated by many popular misconceptions, and on the other hand, unaffected by purely academic abstract resource economics.

Last summer, four significant monographs were published by the Ministry in its Mineral Policy Background Series: *Productivity and Labour Costs in the Ontario Metal Mining Industry; Silver; An Analysis of Market Structure: The Nickel Industry; Selected Papers on Mineral Economics.* The September 1985 issue of the "Alert Letter on the Availability of Raw Materials," published by an influential Washington-based research and consulting firm in the strategic metals field, was devoted wholly to the reports published in the summer of 1985 as part of the Ontario program. It stated that, fortunately for observers of mining developments anywhere in the world, the mineral resources group continues to write or commission and then publish outstanding reports concerning mining trends in all of Canada and in the rest of the world as well.

Over the life of the program, 22 major mineral policy background papers have been published. The topics ranged from studies of specific metals to guides to legislation affecting the investment climate to the potential impact of seabed mining. Outside this program, it resulted in a hardback text, *The Economics of Mineral Extraction,* published by Praeger, and a very widely distributed monograph published by the International Institute for Economic Research, both coauthored by Texas A&M faculty members. Over the years, the program can claim some significant victories over the forces of interventionism. In 1973-74, its criticism killed the "Kierans Report," which advocated confiscatory taxation of "rent from mines." In its first background paper, *The Impact of Taxation and Environmental Controls on the Ontario Mining Industry,* it made the point that an increase in the mining tax rate could result in a substantial decrease in investment. The publication of the nickel commodity study in 1976 not only reduced to absurdity the then current expectations of a continued six percent yearly consumption growth, but also forecast the oversupply problem, which subsequently emerged—in the process blunting the force of opposition demands to enforce 100 percent domestic processing. More recently, in 1982, criticism prepared by this group forced the Canadian federal government under Trudeau to, in effect, withdraw its *Mineral Policy: A Discussion Paper,* which would have done to mining what Trudeau's New Energy Policy did to Canada's oil industry. With respect to these successes on behalf of the mineral investment climate, the claim of Richard N. Weaver that *Ideas have Consequences,* has indeed been substantiated.

There is little doubt that the combination of factual representation, analysis and interpretation represented in these publications greatly reduced the decibel level of public policy debate in the subject area, and reduced the potential for costly policy errors on the side of both government and private industry while sigificantly strengthening the awareness and impact of private enterprise principles.

U.S. industry and defense will, for many years to come, remain crucially dependent on many metals not produced within the United States. This is despite tremendous technological advances in material science applied to problems of substitution of domestic materials for those in which we are import-dependent. A considerable amount of such metals are produced and are imported into the United States from Canada. It is for this very compelling and immediate reason, as much as for the broader cause of maintaining a healthy free enterprise environment at home and among our neighbors, that this program of the Mineral Resources Branch of the Ontario Government should deserve close attention both as to its results and as to the *principles* embodied in its implementation. It is certainly one governmental program that is fully compatible with the aims of the Center for Education and Research in Free Enterprise, and which will, it is hoped, be continued for many years to come.

—Dr. Gerhard Anders
Ontario Ministry of Natural Resources
—Charles Maurice
Texas A&M University

DIRECTOR ON THE GO

MORE FROM EDITOR'S CONFERENCE

From Editors:

"Great conference! I reaped more benefit from this year's editor's conference than from any I have attended."

"It was a total success."

"I am working on a five-part series of editorial columns based on information obtained at the conference."

From Businessmen:

"Congratulations on truly a historic conference."

"The speakers were of the highest caliber and the whole conference was par excellence."

"The speakers were extraordinary, the topics were timely."

And Headlines:

White Says U.S. Losing Edge
San Antonio *Light*

White sees many Roadblocks after Tokyo Trip
Houston *Post*

Dr. Alan Meltzer: Future Mortgaged
San Antonio *Express-News*

Peter Grace Shouts It Out
Felix McKnight, Dallas *Times Herald*

State Budget Picture Looks Bleak
Beaumont *Enterprise*

Dr. Steve Pejovich talks to U.S. Senator Barry Goldwater during a reception and dinner given for Goldwater by the Heritage Foundation in Washington, D.C.

In December and January, Dr. Steve Pejovich gave two television lectures in comparative economic systems. These lectures originated from San Antonio and were aired throughout Central Texas. The director also gave an in-service program at the Twin Creek Middle School in Houston.

Dr. Pejovich made two trips to Washington, D.C. First, he was invited to attend a testimonial dinner honoring Senator Barry Goldwater. The event was sponsored by the Heritage Foundation. A few weeks later, the director attended a testimonial dinner honoring Richard Ware, retiring president of the Earhart Foundation. The event was sponsored by the American Economy Institute, and was attended by more than 100 distinguished academic and business leaders including Milton Friedman and George Stigler, Nobel Prize winners in economics. Dr. Pejovich was one of four speakers at this event.

PATHFINDER

Volume 8, No. 1 March 1986

Published six times a year by the Center for Education and Research in Free Enterprise in cooperation with Educational Information Services, Texas A&M University, College Station, TX 77843. Telephone: 409-845-7722.

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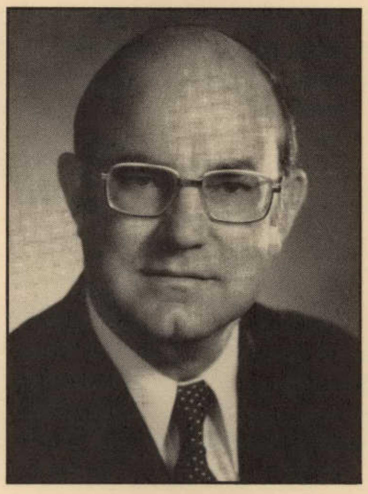
CARROLL PHILLIPS: NEW MEMBER OF CENTER'S BOARD OF DIRECTORS



Editor's Note: The center is pleased to welcome Carroll W. Phillips to its Board of Directors.

Carroll W. Phillips is a managing partner of Coopers and Lybrand's Houston office. He is a member of that firm's governing body of the partnership and the executive committee. He is a past president of the Texas Society of Certified Public Accountants and has served five terms as a member of that group's executive committee. Phillips graduated from Texas A&M in 1954, and is a member of the Texas A&M President's Council. He is extremely active in many civic and religious organizations. He and his wife, the former Grace Awalt of Dallas, and their three children—Carol Ann, Jim, and John—live in Houston.

Phillips was interviewed recently by Dr. Charles Maurice, coeditor of the *Pathfinder*. Portions of that interview are printed here.

Maurice: What do you see as the major accomplishments of the center over the past couple of years?

Phillips: The center set out years ago to become financially stable. While we certainly need a larger endowment, I think we have become financially stable. We are a respected force in the free enterprise area and we are ready to move on.

Maurice: What, in your opinion, should be the major goals of the center; do you think any changes should be made?

Phillips: We now have the opportunity to speak out on major issues, both for the nation and the state; for example, the issue of a state income tax and other issues important to business. We should be relevant to things happening now. I want the center to be viewed as a close ally to business, to be practical, to take stands on important issues.

Maurice: What is the trend today in political and economic philosophy?

Phillips: I have mixed feelings. For example, the Gramm-Rudman bill is a major step toward getting our fiscal affairs back in shape. I think the feeling is, let's get things in fiscal order; let the free market work. The free enterprise philosophy seems to be well supported. Of course, there is going to be some fall-out on some questions such as the falling oil market—especially in Texas—and the effect of deregulation in some markets such as the airlines. Is my $99 air fare worth reduced safety? I don't think so.

Maurice: What is your major concern for the country today?

Phillips: I worry about the reaction to the changes going on today. We have such an interrelated economy. What affects one part of the world affects everyone; for example, the debt of Mexico and other third world countries, in large part because of falling oil prices. This can have an overwhelming impact on the U.S. banking system.

Maurice: Are you optimistic or pessimistic?

Phillips: Optimistic. We'll survive. American business has amazing flexibility. It's the most flexible in the world. We are the greatest economy in history. The problem is we don't know how good we are.

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