

Doing in the Deficit

The advocates of big government are at it again. Their latest ploy to permanently increase the size and power of government is the claim that we *must* have a tax increase in order to reduce an unending stream of federal budget deficits. Indeed, dismay over the deficit projections is leading even reasonable people to concede that, while spending cuts are needed, there's no way to balance the budget without a tax increase, as well.

This ostensibly neutral conclusion is actually an endorsement of bigger government. It ignores the fact that federal revenues have grown enormously over the past four years, keeping pace with the growth of gross national product (GNP). The problem is simply that government spending grew even faster, as Congress proved unable to discipline itself and stop giving away our money to every interest group in sight.

Numerous analyses during the past few months have shown that modest, achievable reductions in the growth of federal spending, combined with normal postwar rates of economic growth, can eliminate the deficit entirely in a few years, with no tax increase.

- New York economics consultant A. Gary Schilling, for example, shows what happens if the growth of federal spending is limited to just the rate of inflation (that is, zero *real* growth) for four years. Assuming real GNP growth of 4 percent a year and modest (3 percent) inflation, the deficit would be nearly zero by 1990. And if interest rates declined significantly, a balanced budget could occur as early as 1988.
- Alan Reynolds of the economic consulting firm Polyconomics uses slightly different assumptions—4.2 percent real GNP growth, interest rates down by two percentage points, inflation at 3.8 percent, and much more modest spending restraint—to reach a balanced budget by 1988.
- Even a *two-year* freeze only on *nondefense* discretionary spending (that is, *excluding* Social Security and Medicare, as well as the defense budget) plus 4 percent GNP growth would shrink the deficit to \$58 billion by 1989, according to a special study by the Congressional Budget Office.

The key to achieving any of these results is to prevent government from growing faster than the economy. And the two essentials for doing that are (1) to control federal spending, (2) to resist incentive-killing tax increases.

How realistic is the 4 percent annual growth assumption? For the two decades from 1948 through 1968, average growth was 3.9 percent per year. From 1960 through 1969, it averaged 4.7 percent, declining to 3.7 percent for 1970-79. Thus, the Congressional Budget Office's baseline projection of 3 percent average annual growth for 1980-89 is in fact a pessimistic view.

Some analysts think the economy can grow even faster than the 4 percent range. Richard Rahn of the Chamber of Commerce and consultant Pierre Rinfret argue that tax cuts and deregulation have fostered major increases in productivity that increase the economy's real growth potential to between 5 and 6 percent a year. Such growth could produce a 1989 federal budget *surplus* of nearly \$100 billion, according to Rahn's analysis.

The latest Washington buzzword is a "one-year spending

freeze"—holding expenditure levels constant for a year to allow revenues time to catch up. The advantage of this tactic is that it short-circuits the special-interest constituencies for each particular spending program, by going after all programs at once. A significant drawback is that most of those who support a freeze do so except for some major pet programs—*except* for the defense budget, say, or *except* for aid to the poor, or *except* for Social Security.

A more basic problem is that a spending freeze leaves every single spending program in place, to rise up again the following year. Yet the sad fact is that there are hundreds of programs for which there is no real justification and which should be *eliminated*, not frozen. What kind of fantasy world do we live in where we pretend that the federal government has enough extra revenue to be able to "share" \$4.6 billion of it with state governments each year? Why should \$7 billion of our tax dollars be loaned or given to middle-class college students each year? Why should \$20 billion be doled out to farmers not to grow crops? On what grounds should a handful of urban transit riders (or an even smaller handful of Amtrak riders) be able to get cheap rides at everyone else's expense? Questions like these could fill volumes, accounting for well over \$100 billion of grants and subsidies each year.

Then there are the so-called entitlement programs—some \$400 billion worth. Only about \$60 billion of that is aid to poor people, where the recipient has to pass a means test to get aid. The other \$340 billion goes to anyone: Social Security (all you have to do is be old, not poor), Medicare (same thing), and federal pensions (you have to have been a soldier or bureaucrat). All of these programs are out of control, paying out far more than their recipients ever paid in. They represent an open-ended claim on our children and their children—the kind of claim that prompted Peter Grace's ads showing a baby saddled with a \$50,000 burden. While a freeze on these heretofore sacrosanct programs would be a welcome first step, all must be fundamentally reformed. It's high time Congress faced the issue—which they'll refuse to do if bailed out by another tax increase.

Finally, there are the hundreds of businesses that are run by the federal government. Some were identified by the Grace Commission: hydroelectric plants, military commissaries, the Washington, D.C., airports, veterans' hospitals. Others include huge commercial forests, grazing lands, the postal and weather services, printing plants, and hundreds more. A massive privatization program, on the scale of Margaret Thatcher's, should be drafted to sell off all these businesses, with the proceeds (as in England) applied to the national debt.

In short, there is no earthly reason for increasing the government's tax take. Just getting rid of a fraction of the federal government's vast assortment of subsidies and boondoggles would easily reduce federal spending below the level of federal revenues. And normal economic growth—if not hobbled by new taxes—will do the rest.

Robert W. Poole, Jr.

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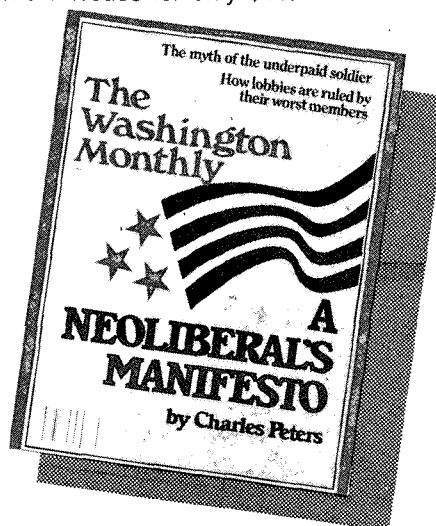
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Let... ters

Tax Breaks Are Subsidies?

I am appalled at the logic Michael Berryhill displays in his article "How the Rich Get Richer in Texas" (Dec. 1984). He says that industrial development bonds (IDBs) are a subsidy to the rich because the interest off of these bonds is tax-exempt. By not having to pay taxes on this income, the owner of this bond is getting a tax cut.

Tax cuts are subsidies? If the government allows me to keep a little more of my own money, I am being subsidized? Next you will be telling me that if a thief decides not to rob me, he is giving me something!

Berryhill also makes the point that IDBs are bad because they distort the marketplace. But the present tax system we have also distorts the marketplace. I hope that one day we will be blessed with a much lower tax rate. But to get to this lower tax rate there first have to be tax cuts. It is pretty hard to visualize a tax cut that does not make some people unhappy. So when I see someone taking advantage of a tax "loophole" that I can't, I don't yell for his taxes to be increased; I yell for mine to be lowered.

Maybe the solution to the market distortion that IDBs cause is to make the interest from all bonds tax exempt. That would be the attitude I would have expected REASON to take.

Ronald Swerlein
Longmont, CO

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The More the Merrier

Your article on Texan industrial development bonds is weak and fundamentally flawed. The IDB is an arrangement whereby the interest on a bond sold by a private borrower to a private lender is exempt from federal taxes. Every IDB is a partial restoration of somebody's right to be free of federal taxes. . . . IDBs are a step toward freedom. Their proliferation is highly desirable.

Bryan Coupal
Riverdale, MD

The editors reply: In a screwed-up world, things are never simple. The tax reduction in the case of IDBs goes to the bond buyers. But those aren't "the rich who are getting richer" in REASON's article. It's the developers, jeans makers, discount-store operators, and so on down the list, financing their enterprises via bonds that are low-interest because of the buyers' tax exemption—these are the big winners. But not every aspiring profit maker gets to take advantage of this cut-rate financing. IDB use is rationed—by politicians. It's an unsavory arrangement with predictable consequences documented in Michael Berryhill's article.

The local politicians love it, because they have goodies to dispense at no apparent cost. But there *are* costs, in opportunities foreclosed for less well placed enterprises, to take one poignant example. *A* could have built a hotel and made a go of it except for *B*'s getting a competitive advantage via a lower-interest loan for construction of a competing hotel. *B* didn't *take* anything from *A* that was rightfully his. But it's nevertheless a lousy result of a politicized market—and worth reporting as such, whatever should be done about it. Ultimately, yes, a truly free society. In the meantime, let's understand the often hidden consequences of a convoluted system.

Dissent on Cuba

As Bob Poole's sister, I can at least be thankful that he acknowledged the fact, in referring to "Miami's Cuban Miracle" (Nov. 1984), that "many Miami residents resented the 'invasion' of Cubans" (Notes). However, he did not live in Miami during the *main* influx of Cubans, as my parents and I did. The article by George Gilder is totally one-sided.

When the first few arrived they were pleasant enough, because there weren't many of them. But their numbers soon grew alarmingly, and they became rude and arrogant as they *took over* the city.

They made no attempt to get along with or to get to know the American community. They set up their own little Cuba instead. Is it any wonder they were resented?

Yes, they set up businesses but employed only their own people (at least in the beginning) and spoke only Spanish in front of American customers in *our* stores when they knew English. The Cuban people could have done much to ease the resentment had their attitude been a bit different.

Laurie Poole
Fort Pierce, FL

Witness to a Miracle

As a native Miamian who spent his teen years witnessing the epochal changes brought about by the Cuban immigration in the decade of the '60s, the feature article by George Gilder, "Miami's Cuban Miracle" (Nov. 1984), brought tears of joy to my eyes. It has taken more than two decades for this story to be written, exploding the myth of the dependent immigrant further draining the social-service resources of a city.

As a high-schooler, I remember the terror-stricken faces of the immigrant teens as they entered school for the first day to face a xenophobic Anglo student body. I remember my parents agonizing over losing their jobs to immigrant labor.

In 1972, after an eight-year hiatus, I returned to Miami to work and live. Did the prophecies of doom uttered earlier by the fear-mongers materialize? No. I found a prosperous, vibrant city welcoming me back. I bought a home in "Little Havana" and lived among the industrious Cubans, watching the process of transformation take place around me. Those terror-stricken teens were prosperous bilingual citizens now with children of their own.

Another eight years has passed since my career has taken me to another southern city, Houston, with its own share of Latin immigration issues to face. I visit Miami occasionally and see the children of the children of the original refugees from the early '60s. Their language and customs are indistinguishable from the Anglos. Many cannot speak Spanish or choose not to.

This is the pattern of all immigration waves: the Italians, Irish, Poles, Germans, Jews, and more recently Mexicans. Each has enriched America with a rich cultural heritage, but not before encountering fierce social obstacles thrown in their way by fearful Americans. Perhaps now we can admit, for each mouth

(Continued on p. 59)

15 YEARS FOR ACCURACY IN MEDIA

Since 1969, Accuracy in Media has been hammering away at Big Media's errors, distortions and suppression of important stories. We didn't think to ask anyone to send us comments on our 15th anniversary, but here are some that have been volunteered that readers might appreciate.



BENJAMIN C. BRADLEE
Executive Editor, *Washington Post*

"(Accuracy in Media is) the name of a bunch of knee-jerk conservatives based in Washington who earn a pretty good living and a lot of notoriety hectoring the networks, The New York Times and The Washington Post. They are, in my opinion, a perversion of the words 'accuracy in media'..."

MIKE ZAGARELL, Editor, *Daily World*
(Organ of the Communist Party, USA)

"One of the organizations built in the Nixon years and used effectively today for this purpose (to take over the media) is a group known by the misnomer AIM, Accuracy in Media... In addition to organizing campaigns against specific writers, AIM also places condemnatory and redbaiting ads in papers, attacking the media for those few times it veers away from a pro-corporate stand."



DAVID BRINKLEY
Host of ABC's "This Week"

(Commenting on Irvine's charge that some journalists would have liked to have broken the secret of the Grenada rescue operation in advance)

"I think it is one of Reed Irvine's feverish fantasies, one of many I have heard from him. It is only slightly more ridiculous than a dozen others I have heard from him. I find it outrageous. I find it to be a lie, and I find it insulting."

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brickbats

The Social Security Administration is going bonkers as well as broke. It notified its district and branch offices to be on the lookout for people presenting phony hospital birth papers to obtain a Social Security card, which is a key to welfare benefits. Why the all-points bulletin? The bureaucrats are afraid that a Cabbage Patch doll may grow up and qualify for assistance. The doll craze spurred more than 100 hospitals to issue birth certificates to go with the dolls. Of course, the hospital papers say "Baby Doll Birth Certificates" and are signed with such names as "Dr. I.M. Happy and Dr. N. Good Hands." But SSA isn't taking any chances. Is this what Reagan meant when he said he's going to ferret out fraud in entitlement programs?

Clever church officials in Evanston, Illinois, had to find a way around the zoning board to extend a helping hand. An overnight shelter for the homeless in the basement of the First Baptist Church would violate zoning ordinances. So church officials now do a "prayer vigil." Needy people are invited to come in and pray—all night if they like.

Ah, glorious Sweden, where all of a citizen's needs are capably handled by the state from cradle to grave.

Social welfare authorities want to take three-year-old Mikael Johansson away from his natural mother and put him in a foster home. Does the mother beat or neglect the child? Well, not exactly—it's just that she is too overweight to care for him properly, say the slim folks at the social-welfare agency. They contend that Inger Johansson's appearance would have an adverse effect on the child. In the brave new world of the welfare state, only the thin and beautiful will be allowed to have children.

The fur is flying in Allen Park, Michigan, because Tiffany Lumia won \$400 worth of booze in a raffle sponsored by the city. Tiffany is a minor. Tiffany is also a two-year-old collie. Ronald Kozicki, a prelaw student who *didn't* win the raffle, says it's unfair. His bone of contention is that when city officials discovered that Tiffany's owner put the pooch's name in the raffle, they should have drawn another ticket so that a human could win it. It all seems pretty silly, but the whole dogfight is ending up in court. Kozicki may be the underdog in this case, but he's barking up the wrong tree. We're rooting for Tiffany.

The Air Force displayed some flabby thinking when it told a muscular sergeant to lose 26 pounds or

get out of the service. Staff Sgt. Paul Poulin, a 23-year-old body builder stationed at Elmendorf AFB in Alaska, is considered "clinically obese" even though the 203 pounds packed onto his 5-foot-6-inch frame is mostly muscle. Poulin's immediate commander is trying to get the brass to trim down its bureaucratic attitude. "Poulin is in no way overweight and is one of the hardest working, most knowledgeable and physically fit people I've seen in 16 years in the Air Force," his captain said. Hmm, sounds like Poulin hasn't got a chance.

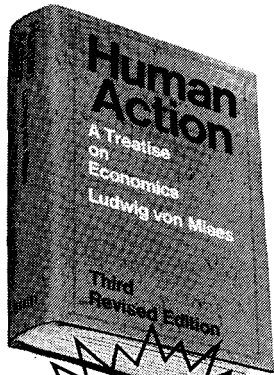
Chicago has somehow managed to survive for over 150 years without a "chief of protocol," but now, Mayor Harold Washington finds that his city must absolutely hire one—at \$36,000 a year. The protocol chief is needed to plan dinners, flower arrangements, and entertainment when important folks drop by for a visit. The mayor's opponents say the city needs a chief of protocol like it needs a third head, but the mayor is undaunted. What Chicago really needs is a chief of the departed to greet warmly all the corpses who find their way onto the election rolls every November.

From the Damned-if-you-do-damned-if-you-don't Department: Inmate Timothy Langley jumped at the chance to sue two Nashville court officers for \$70,000. The pair had the audacity to leave a sixth-story window open, giving Langley the opportunity to try to kill himself after a murder conviction. Langley survived the leap when his plunge was deflected by a tree. His suit contends the officers were negligent in leaving the window open. Wonder if he'll sue the guy who planted the tree?

Oh, the crime foisted on taxpayers in the glorious name of research! The British Health and Safety Executive has found that the noise of pigs squealing can reach 108 decibels at feeding time. Earmuffs are recommended for pig farmers. Not to be outdone by the erstwhile imperialists, Indian researchers have come up with an important project of their own. They're working to create a "gas-less" bean. A possible advertising slogan is "Gone Is the Wind."

—MARK EDWARD CRANE





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Mises has nothing but scorn for the phony “compassion” of the Marxians and Keynesians — because he sees how their theories actually breed suffering. One by one, he sweeps away the dangerous fallacies of liberalism and socialism.

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SPEAKING FREELY ABOUT ELECTION LAW

Federal election laws that regulate political contributions and spending seriously threaten both free speech and the robustness of the American political system, concludes a recent study by the Cato Institute, a Washington, D.C.-based think tank. Over the years, some observers have criticized various aspects of these laws. But the Cato study now provides a comprehensive, detailed critique of the election laws that should spark serious debate in public-policy circles.

Journalist Mary Meehan, author of the study, detailed ways in which the post-Watergate Federal Election Campaign Act (FECA) of 1974 and the Federal Election Commission (FEC), created by the act in 1975, restrict First Amendment rights and discriminate particularly against "the underdogs of American politics." For example, by limiting the amount an individual can contribute to a federal political campaign (\$1,000 per primary and \$1,000 per general election to each candidate), the law prevents "many candidates from raising the money they need for communications with the public," thereby restricting candidates' exercise of free speech. Such restrictions, of course, are more likely to affect less-well-funded minority-party candidates than those of the two major parties.

Moreover, observed Meehan, the FEC, by imposing various reporting requirements and spending restrictions on politically active groups, "has a chilling—if not freezing—effect on the speech of grass-roots, issue-oriented groups." In 1978, for example, the FEC ruled that Massachusetts Citizens for Life, a non-profit antiabortion organization, violated federal election law by distributing a special issue of its newsletter reporting candidates' views and voting records on abortion. Though the group's challenge of the ruling was vindicated by a federal judge—*six years later*—the FEC appealed the court's decision, forcing the group into another legal battle. After winning the first court contest, Meehan reported, the group's newsletter editor declared: "I can testify that there has been a chilling effect on our ability to communicate with proliferers."

Through FEC regulations on "independent spending"—spending that is not

directed, coordinated, or overseen by a candidate or his campaign—this "chilling effect" also extends to citizens' right of free association. Though the Supreme Court has ruled that independent spending cannot be limited, groups spending more than \$250 in a year must report this to the FEC and swear that it was in fact independent. In order, then, to avoid having their independent spending construed as contributions, citizens cannot consult with candidates. Their "only safe course of action," Meehan observed, "is to avoid all contact with the candidate they support, trying to learn of his themes and plans through the news media."

Meehan criticized several other aspects of the FECA, including the way in which "a law reputedly designed to ensure honest politics has encouraged a great amount of fudging, concealment, and deceit." Moreover, she documented the discriminatory fashion in which the FEC enforces election laws. For example, in the first quarter of 1979 the commission investigated only 2 senators and 6 representatives among incumbent candidates for noncompliance with election laws; while it probed 8 Senate and 52 House *nonincumbent* candidates during the same period.

The 1974 election law and the FEC should be abolished, concluded the Cato study. We already have the best campaign law ever passed, the study reminds us—it's called the First Amendment.

DEREGULATION TRAVELS WELL

Transportation deregulation got off the ground during the Carter administration, so it's been around long enough to make a mark. Its bracing effects are evident both with intercity buses and with airlines.

Bus deregulation was discussed recently by someone with an acute interest in the subject—William McCracken, a senior vice-president of Greyhound Lines and a former transportation regulator with the Interstate Commerce Commission (ICC). In a presentation at the US Army Transportation School, McCracken pointed out that before the changes, "regulation virtually assured an operator a profit if he played by the rules. When costs increased, they

were passed on to the customer."

The effect on the bus companies, however, was hardly salutary. "There was a decided absence of imaginative, aggressive marketing people in a regulated enterprise," McCracken observed. "Regulation was an excuse for not being imaginative and for not really working hard to find some new way to sell or to carve out a new market niche... Without exception, every bus company fit this pattern."

Deregulation completely transformed the industry. A "phenomenal" number of new companies entered the intercity bus market—some 2,169 in a 13-month period. And the ICC received applications from companies to serve 55,000 new route miles, 20 percent more than were served previously.

With competition where before there had been protected routes, bus companies searched for ways to cut costs. Before deregulation, McCracken noted, "Greyhound was the high cost operator" in an industry whose labor costs overall were already greater than for any other comparable industry.

But when it came time to negotiate a union contract that expired in October 1983, Greyhound asked the union for concessions. A long and bitter strike followed before the union agreed to a settlement: a 13 percent wage reduction for employees already on Greyhound's payroll, and an additional 15 percent reduction in the wages of new employees.

Bus companies are doing more to sell their services, too. "Long range planning is foreign to a regulated business," but now Greyhound, for example, is investing in research, devising marketing strategies for various customers, and renovating bus terminals.

Established firms such as Greyhound are facing competition not only from upstart bus companies but from discount airlines (see "Fly Me—I'm Deregulation," Trends, Jan.). But as *Aviation Week* recently noted, Greyhound is beginning new service to deliver passengers to low-cost People Express flights at five major airports.

The beneficial effects of transportation deregulation are also evident in the case of Hawaii's interisland airlines. When regulation was in full force, Hawaii and Alaska were the only states whose intrastate air fares were regulated by the Civil Aeronautics Board—so when the 1978 Deregulation Act took effect and the fed-

TRENDS

eral government ended all of its fare regulation, Alaskans and Hawaiians were doubly affected.

The biggest change in Hawaii was the emergence of a new airline, MidPacific Air (MidPac). Two established airlines, Hawaiian Air and Aloha Airlines, had dominated the interisland market in the past, but MidPac has now shattered that near-duopoly with the time-honored tool of competition—low prices. Where Hawaiian and Aloha were charging \$50 for interisland fares, MidPac swooped into the market with \$25 fares and, at one point during price wars, \$10.95 standby fares. How? The upstart shuns expensive downtown offices, hires non-union employees, and buys aircraft that are small and old (but quite adequate).

The formula has worked. Last summer, when MidPac was three years old, it enjoyed 20 percent of the interisland traffic and "has been turning large and regular profits."

PUBLIC POLICE SINGING THE BLUES

Just a few years ago, only "wild-eyed" laissez-fairists took seriously the idea of privatizing police and other functions of the criminal-justice system. Today, the idea is no longer considered bizarre. In fact, it's actually happening.

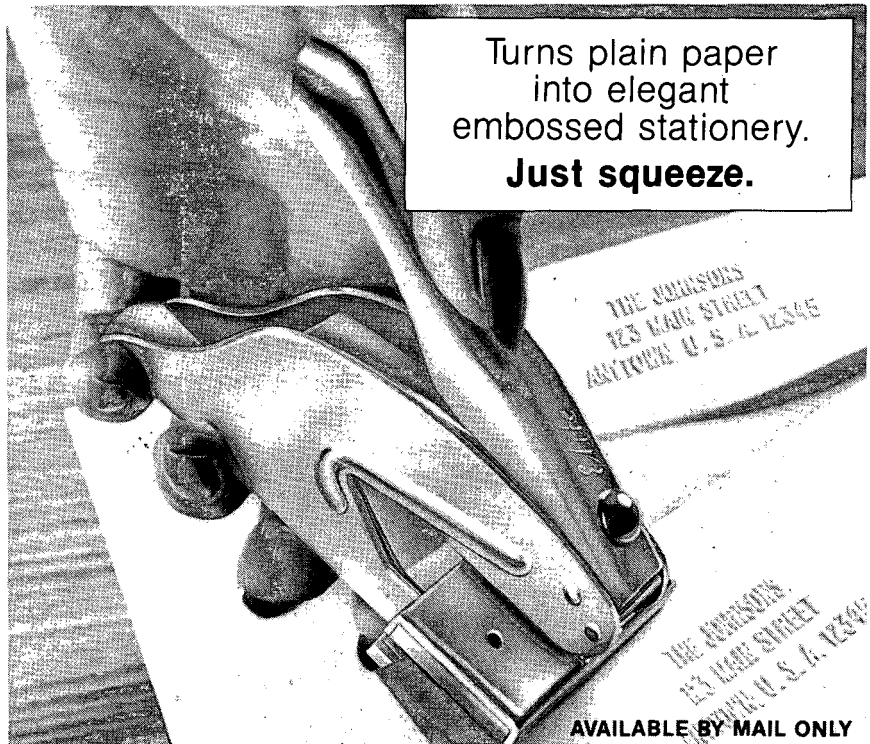
That police privatization is becoming a live possibility was evident in a recent warning to the boys in blue that they could become "an endangered species" by 1994 if citizens aren't satisfied with public police services. The warning came in a recent speech by Edward J. Tully. Tully is not some Charles Darwin gone mad, nor is he associated with the privatization-oriented Local Government Center. Rather, he is the head gumshoe of the education department at the FBI National Academy, and he made these predictions in a talk at the recent annual meeting of the International Association of Chiefs of Police.

"I know of nothing in any state law," Tully observed pointedly, "that prevents IBM from providing law enforcement services." Already, he noted, private security services are 50 percent larger than public law enforcement agencies.

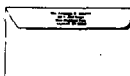
Tully noted that when citizens fail to get the police services they need, they are willing to go elsewhere. "People are reinventing government," he said, pointing to such self-help groups as Neighborhood Watch and Mothers Against Drunk

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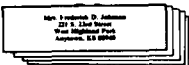
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TRENDS

Drivers. Tully didn't mention one of the most successful competitors with public cops—the Guardian Angels, dedicated young people who voluntarily patrol on foot the worst sections of some cities and provide real protection to the poor.

Perhaps a harbinger of the future in the United States is the recent replacement in Britain of the official British Transport Police (who have guarded British ports since the 1820s) with private security firms. Associated British Ports announced the decision as a cost-saving measure. According to one press report, the port authority said that the

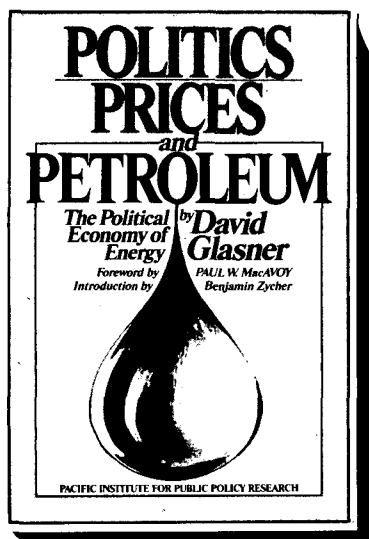
switch to private security firms "would not mean any reduction in security cover for our customers."

But even Prime Minister Margaret Thatcher, the guiding light of privatization in Britain, would probably be surprised by the privatization now occurring in certain parts of the criminal-justice system here. As noted in a recent *60 Minutes* feature titled "Crime Pays," dynamic firms such as the Nashville-based Corrections Corporation of America and Behavioral Systems Southwest in the Los Angeles area are already operating a number of minimum- and medium-

security detention and correctional facilities. Other reports indicate that the nation's largest independent private-security firm, the giant Wackenhut Corporation of Coral Gables, Florida, is talking to several states about building and operating prisons and jails. And it now looks as if a small independent company, Buckingham Security of Lewisburg, Pennsylvania, will actually build and operate the nation's first private maximum-security prison, due to open its gates in Pennsylvania in early 1986.

So what was a few years ago unthinkable—the privatization of criminal-justice functions—is now an emerging reality as private self-help groups, security firms, and even prison companies are confronting the government monopoly with real free-market competition.

BUREAUCRACY vs. ENVIRONMENT



POLITICS, PRICES, AND PETROLEUM
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By DAVID GLASNER
Foreword by PAUL W. MacAVOY

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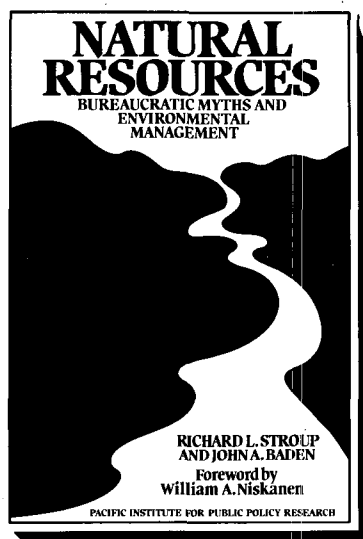
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By RICHARD L. STROUP AND JOHN A. BADEN
Foreword by WILLIAM A. NISKANEN

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MAY THE CAB R.I.P.

It was a death worth celebrating: on December 31, the Civil Aeronautics Board passed into history. Created in the '30s to regulate the nascent US airline industry, the CAB was legislated out of existence by the 1978 Airline Deregulation Act.

The CAB's demise marks another milestone in airline-industry decontrol. In December 1981 came the first major step: deregulation of entry and routes—anybody could start an airline, and any airline could start up or stop service on any route. Then, one year later, air fares were decontrolled.

The CAB functions that remain—primarily involving consumer affairs, anti-trust rules, international agreements, and enforcement of operating rules—have been transferred to the Department of Transportation (DOT). About this development, William Gregory commented in an editorial in *Aviation Week & Space Technology*, "In practice, the airlines are likely to operate pretty much as they please, something that is all for the best."

One aspect of airline operations that might, in fact, do better under DOT control is the allocation of landing and take-off rights ("slots") at airports. In contrast to the present allocation system, in which airline committees distribute the slots, the Transportation Department has proposed a market arrangement, in which slots would be bought and sold.

Various problems with the present allocation-by-committee system were recently dramatized. The nation's six busiest airports are experiencing

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troublesome delays caused in part by crowding of flights at "peak hours" when there is much demand (9:00 A.M., for example). Airlines that operate flights at these airports were given anti-trust immunity last fall to mutually arrange rescheduling of their flights to ease peak-hour crowding.

The "solution," however, was not universally greeted with open arms. Several airlines criticized the agreement as anti-competitive, as did the Federal Trade Commission and the President's Council of Economic Advisers. Even the CAB, which approved the plan in October, conceded its anticompetitive effects.

American Airlines president Robert L.

Crandall warned that the airlines should not be regulated in response to the delay problem and blamed the Federal Aviation Administration's inadequate air traffic control system for the situation. "If slots must therefore be allocated in one way or another," Crandall said, "we should allow the marketplace to allocate them according to price."

And even Michael Kinsley, a senior editor at the left-liberal *New Republic* magazine, called the airlines' agreement "a virtual cartel." "The correct capitalist solution to airport overcrowding," instructed Kinsley, "would be to auction off desirable takeoff and landing slots."

Indeed. And with the demise of the

CAB, such market-like solutions to aviation problems may be more likely to evolve. CAB, R.I.P.

FOREIGN-AID ENTREPRENEURS AID ENTREPRENEURS

Washington regularly wastes billions of dollars on aid to Third World governments, yet vast numbers of these governments' subjects remain destitute and hungry. Meanwhile, entrepreneurship continues to bring wealth to countless individuals in developed countries. It

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seems obvious that encouraging entrepreneurship in developing nations would be worthwhile. And that's what former United Nations official Glen Leet and his wife, Mildred, set out to do six years ago, when they used \$1,000 of their own money to begin a private foreign-aid program for Third World entrepreneurs.

It's called Trickle Up Program, Inc. As of last November, it had disbursed \$114,000 worth of \$100 grants to entrepreneurs in 61 developing nations. "There are foreign-aid programs for helping entrepreneurs in the Third World," Glen Leet recently told REASON, "but I don't know of any others that do it

on the level of \$100 grants." Grant recipients have included a Cameroonian family who invested their grant in a sewing machine, fabrics, and a marketplace booth; some Solomon Islanders who purchased pineapples and mangoes to make fruit jam; and a group of Dominican women who bought ginger plants so they

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PERU'S ROADS TO THE MARKET

LIMA, PERU—Latin American cities are often depicted in popular literature as huge "pueblos jóvenes," new neighborhoods where people suffer from enormous material want and spiritual frustration. But this conventional image is very different from reality. The fact is that a thriving free-market economy exists in much of Latin America, and it provides a framework for Latin Americans to devise creative solutions to a wide range of problems. Lima's streets are an interesting example of this.

Lima is a city with five million inhabitants, 47 percent of whom live as settlers on land that they have obtained, made habitable, and developed outside of the framework of Peruvian law. They accomplish this by invasion and spontaneous organization and construction.

In theory, the state is supposed to provide at least some assistance to the settlers because they are officially poor. But in fact, they themselves are the ones who provide for themselves despite the state's regulations. For example, the settlers construct their own streets and sidewalks—developing several mechanisms to obtain public goods for themselves and avoid the "free-rider" problem.

The system as it has evolved in many areas shows how such mechanisms can work. Sidewalks and streets are paid for by the owners of lots adjoining the streets. If a settler does not pay his share for street construction, he won't have a street in front of his house. And if a settler pays his share but his neighbor across the street does not, then only half of the street will be built—the half in front of

the lot belonging to the settler who has paid. So in areas where nobody pays, there are no streets or sidewalks.

This is typical of how people in the "pueblos jóvenes" provide for their own public services—without public officials, public monopolies, and public bribes. In a sense, it is a spontaneous privatization of one of the Peruvian state's ostensible functions.

Although a large number of Lima's streets have been constructed this way, there is still a need for many more. Unfortunately, many settlers lack incentives to pay for streets and sidewalks in front of their homes because they lack title deeds to their homes. Indeed, the state has granted such deeds to only about 10 percent of the settlers, and it never grants title deeds for the roads themselves.

Yet it is striking that many settlers are still building streets and sidewalks, sometimes even though they don't have the title deeds to their homes. It's persuasive proof of the workability of market-like mechanisms, privately arrived at.

—ENRIQUE GHERSI

SOMETIMES ON SUNDAY

GREAT BRITAIN—Retailing here has long been a nest of regulatory nonsense. An example is the group of regulations called the Shops Acts, a series of laws that cover hours of trading, Sunday opening, and the employment of staff.

These bizarre laws institutionalize such anomalies as allowing consumers on Sundays to buy pornographic magazines but not Bibles, whiskey but not baby food, and partly cooked tripe but not fish and chips.

It's a typical regulatory fiasco created by allowing producer interests to override consumer sovereignty. There have been 18 attempts to amend or repeal the Shops Acts (in particular, the restrictions on Sunday trading) since 1956, all of which have failed. Now, though, a much more powerful force for abandoning the laws has appeared in the form of consumers stating their preferences in the marketplace.

Strangely, this force has come from a combination of the British love for tidy homes and gardens, and some of the biggest retailing businesses in the land, the food supermarket chains. In an effort to extend their businesses, major food chains have been opening giant home-improvement stores selling everything from garden sheds to door chimes. These stores run on the pre-packed, self-service, multiple-checkout, easy-parking basis that we've all used for years to buy our food. What day do most of us repair our back doors or paint the bedroom? Well, Sunday, of course, and are those new stores convenient for getting a bag of nails or a pot of paint. Consumers love them and they are doing great business. The result is that all over Britain, home-improvement stores are being built—in the clear knowledge that by trading on Sunday they will be breaking the law.

It may be hard to believe, but some zealous local authorities take the local store management to court on a regular basis, fine them a paltry sum, and send them back to their stores to get on with their business. It is an odd way of keeping up appearances.

If you're thinking that maybe the government would do something about all this, you are half right. In February 1983 a bill originated in the

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could distill and bottle the roots for wine.

Trickle Up's structure is simple. It is financed completely by private contributions, and it functions with the help of 275 volunteer coordinators around the world, many from agencies such as the Peace Corps, the Catholic Relief Service, and the United Nations. To qualify for a Trickle Up grant, applicants have to assemble at least five people, devote at least 1,000 hours to the business during its first three months, and agree to reinvest 20 percent of their profits in the business.

Mildred Leet told REASON that the application form for a grant is only one page. "We ask on it, What are you going to market? Where are you going to market it? and How much profit will you make?" They ask these questions, she noted, because "the people who want to start the business have to sit down and figure these things out."

Once the project is off the ground, though, "they're on their own to make a success of it," she recently told *Venture* magazine. Her husband told the magazine that the Trickle Up projects have been quite successful, with each business averaging \$358 in profits after their first three months of operation. But Mildred Leet suggested to REASON that there are other measures of success—"when a banana-chip business in Dominica expanded and moved into larger quarters, and when the number of children going to school grew because their parents can now afford school uniforms."

Trickle Up is hardly on the scale of the World Bank or the gargantuan aid programs that regularly flow out of Washington, and it's certainly on a scale far smaller than the problems it addresses. Yet it's a useful example of the good that can be accomplished by giving entrepreneurship a fighting chance. (Trickle Up's offices are at 54 Riverside Drive, New York, NY 10024.)

INTERSTATE BANKING WAITS FOR NO CONGRESS

It was in 1927, during the Coolidge administration, that the federal government first prohibited interstate banking with the McFadden Act. Bad habits (especially the government's) die hard, and the prohibition was left basically intact for decades. But change is in the air. In the last few years, interstate banking

has steadily inched closer to reality—not because of a change of legislative heart but because of a legal loophole.

When federal banking law was amended in 1970, a bank was defined as an institution that both takes checking deposits *and* makes commercial loans. Such institutions are subject to the interstate taboo. But suppose an institution offers *only* checking accounts but not commercial loans, or vice versa? It was a moot issue until interest rates were deregulated starting in the 1970s, but once that happened bank competition set in. And in 1980 the first "non-bank bank" slipped into existence through the regulatory loophole.

Other non-bank banks were soon established by major banks and financial service companies. But Congress, pressured by the small-bank lobby and various federal officials (such as at the government's central bank, the Federal Reserve), objected to the new interstate bank branching, charging that it violates the legislature's intention. Congress asked the comptroller of the currency to withhold approval of any more non-bank banks while it figured out how to close the loophole.

The moratorium on approving new applications lasted 18 months, and still Congress hadn't acted. The legislature recessed in November without passing any interstate-banking reform legislation. And when Congress left town, C. Todd Conover, comptroller of the currency and an advocate of banking deregulation, announced that he would grant 13 bank holding companies preliminary permission to operate 29 non-bank banks outside of their home states.

Who would object? Primarily, small banks that don't want any competition from their larger brethren in New York and Chicago. As the *New York Times* noted, "Politically, this is the heart of the interstate banking issue—the fears of so-called independent banks in non-money center states that they would find themselves competing with Goliaths." And Federal Deposit Insurance Corporation economist Alan McCall explained to REASON, "When entry into a market is restricted, your business is worth more, and the small banks know that. When those barriers come down, the value of the business declines. In the longer term, geographic deregulation will have a negative effect on the small banks."

The chairmen of the Senate and House banking committees—Sen. Jake Garn (R) of Utah and Rep. Fernand St Germain (D) of Rhode Island—have vowed to stop

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up the loophole—retroactively. “If people want to go ahead [and start non-bank banks],” St Germain solemnly warned late last year, “they will be required to divest, no matter what the cost. There’s no way I can bend or give.”

But such fiery pronouncements are not standing in the way of major institutions intent on offering diverse financial services nationwide. In late November, a Conover aide told REASON that the Comptroller’s office had received some 340 applications to start non-bank banks, and

Conover is intent on processing them in accordance with the law, loophole and all—unless and until Garn and St Germain can make good on their threats.

What will interstate banking mean? “We will get the Citicorp equivalent of a McDonald’s on every other corner,” small-bank lobbyist Kenneth Guenther moaned in a *Business Week* interview. But “locally limited borrowers” (individuals and small businesses) stand to benefit considerably. “Without geographic deregulation, locally limited bor-

rowers are pretty much handcuffed to local institutions,” FDIC economist McCall noted. That would no longer be the case. Last year, he testified before a House committee that the increase of competition between financial services will make it easier for small businesses to obtain loans. Other benefits of deregulation pointed out by proponents are higher interest rates for consumer deposits and lower rates for loans, as well as “neighborhood banks” with the range of services and expertise of a ma-

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(Continued from p. 16)

House of Lords (who needs elected representatives for good ideas?), but it succumbed in the faint-hearted House of Commons to a lobby of trade unionists, the Lord’s Day Observance Society, and a consortium of retailers. A “committee of inquiry” was set up—a traditional British parliamentary device that really means, “I wish the issue would go away.”

Well, maybe it will. Cracks are appearing all over the place. Some home-improvement stores are seeing small specialist stores nearby cashing in on the demand on Sundays and opening, too. There’s also an entire industrial sector being revitalized by the rise in the dollar. Myriads of American tourists came to Britain last year and wherever they go, stores open on Sundays, catering to consumer preferences for tripe, fish and chips, or whatever junk food that visitors from Cincinnati want.

When the power of the market blows silly regulations away, there’s hope for us yet. My bet is that Britain’s Shops Acts will be quietly repealed sometime over the next decade. Slow progress perhaps, but then the first prohibition on Sunday Trading was the Fairs and Markets Act, passed in, ahem, 1448! Some things take time.

—EBEN WILSON

THE ROAD TO DENATIONALIZATION

MEXICO—A few days after the state appropriation of Mexico’s private banks in 1982, the government announced that those businesses which had been owned or con-

trolled by the banks but were not directly connected to their financial operations—but which had also been taken over as part of the banks’ assets—would be sold back to the private sector “in the very near future.” Until last fall, many suspected that the Mexican authorities had decided to forget their promise.

Last September, however, the government announced the sale of many of the firms involved. These companies, numbering nearly 100, all rank among the most important in Mexico. They represent virtually every sector of the economy—mining, retail sales, tourism, insurance, securities exchange, real estate, and heavy industry. Many of these have quickly found enthusiastic new owners, some of whom turned out to be the former bankers themselves.

The news has been welcomed by almost everyone. The prominent Mexican economist and author Luis Pazos has written, “It would be ideal if the government took other similar measures. Even though this decision will not, by itself, solve Mexico’s troubles, it is a step in the right direction.” And financial analyst Isse Nunez, in his daily newspaper column, observed, “It is simply an act of justice...and its psychological value is very important. At present, only private enterprise can foreseeably provide the necessary boost to bring Mexico out of its crisis.”

Such opinions are becoming quite widespread among other economists, since under government ownership, the now-denationalized went through their worst economic period ever. Their market value declined, production was at a standstill, there were no new investments, and thousands of workers were laid off.

This was the case, for example, of

Minera Frisco, one of the nation’s leading mining companies. Until the day of the expropriation, it was one of the best options on the Mexican stock exchange. A year later, production plummeted and its stock had to be temporarily withdrawn from the market. Other enterprises suffered similar fates. The multi-million-dollar projects Hotel Plaza Reforma and Hotel Mediterranee, which were to be, respectively, the country’s tallest building and most luxurious hotel, were suspended a few days after they became government property. They now stand as abandoned construction sites in the heart of Mexico City, attesting to the government’s inability to continue the work. Perhaps the new owners, with far superior managerial capabilities, will once again guide all of these ventures onto a productive path.

The government’s decision to fulfill its two-year-old promise came at a crucial time for Mexico. After enduring 30 months of belt-tightening policies, an average of 100-percent annual inflation, large increases in unemployment, zero economic growth, a three-fold increment in taxes, and a 1,000-percent devaluation of the national currency, the people of Mexico have grown increasingly skeptical—to say the least—about their one-party state’s attempts to expand its powers in the economic sphere. As of August 1984, the government controlled well over four-fifths of the economy. The return of these firms to private hands has seemingly dampened this rapid advance toward socialization. Moreover, it has perhaps averted the ever-present threat of violence, stemming from popular unrest, from materializing. If so, this is the happiest news that Mexicans could hope for at present.

—JULIO A. MARQUEZ

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for financial institution.

It's a little ironic that interstate banking appears to be on the horizon not because of deregulation's inherent advantages but because of a minor loophole that was virtually ignored for years.

HOW TO SPELL RELIEF? I-N-D-E-X

As America's taxpayers were cheerfully singing "Auld Lang Syne" on New Year's Eve, they had more reason to celebrate than they may have realized. That's because tax-bracket indexing made its debut with the new year—and despite nasty rumors to the contrary, it's special cause for celebration by those at lower income levels.

Tax-bracket indexing means that federal income tax personal exemptions, the zero bracket amount, and all marginal tax rate brackets are now indexed to inflation, so the percentage of your income that you must send to the IRS will increase only when the actual value of your income goes up. "Bracket creep"—

people creeping against their will into higher tax brackets even though their real income stays the same—is a thing of the past. Legislators must now raise taxes explicitly if that's what they're wont to do. That's why *Los Angeles Times* editorial writer Ernest Conine calls indexing "one of the most important tax reforms in the history of the Republic."

Even though Congress passed and President Reagan signed the legislation that provides for indexing, a number of Washington officials are not as pleased with the reform as is Conine. It's been charged that indexing is a scam to help rich people evade taxes while their poorer neighbors don't benefit at all. But a recent study for the National Center for Policy Analysis by David Henderson, formerly a staff economist with the Reagan administration's Council of Economic Advisers, found that the opposite is the case.

"For families who already are in the highest tax bracket (50 percent), 'bracket creep' has a very small effect on taxes," Henderson explained. "For families who are in low tax brackets, however, the

Reagan indexing scheme turns out to be extremely important."

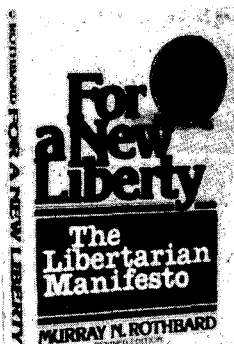
To see why, it's worthwhile to note what would happen by 1988 if indexing were eliminated. Relying on calculations done by Harvard University economist Lawrence B. Lindsey, Henderson pointed out that a family with a \$10,000-15,000 annual income would pay 15 percent more taxes without indexing; and a family with less than \$5,000 in income would pay a staggering 74 percent more taxes by 1988. And the wealthy? Eliminating indexing would make little difference for them. Their taxes would increase only two percent without it.

No one with a speck of humanity could oppose the reduction of poor people's tax burdens that indexing will evidently bring about. Or so it might seem. But the fact is that all their rhetoric notwithstanding, Washington pols of both major parties yearn for all the tax revenue that bracket creep used to bring them, so they're feeling rather nervous about indexing. During his campaign last year, Walter Mondale proposed that indexing be eliminated for brackets over \$25,000 unless the annual inflation rate exceeded

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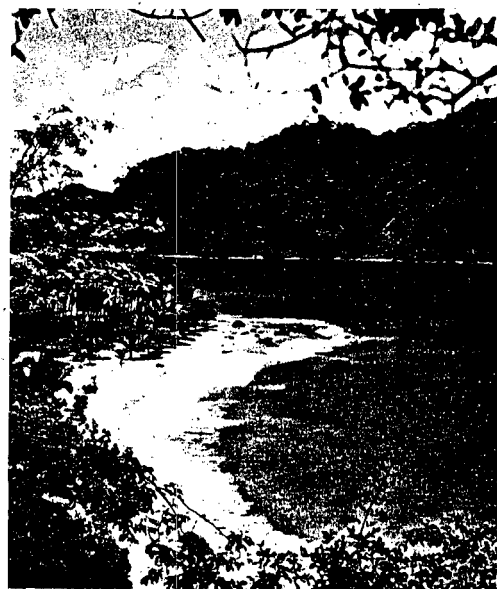
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four percent. In a *Los Angeles Times* op-ed piece, Ernest Conine pointed out that House Ways and Means chairman Dan Rostenkowski (D-Ill.) is already on record for repeal of indexing. And Conine suggests that with the memory of 1984 campaign promises quickly fading, President Reagan might fudge his vocal pro-indexing position.

Time will tell. The anti-indexing forces may well mobilize as the year goes on, and they'll probably revive their old canard about how indexing is just a sop for the rich. When they do, don't believe it. As the Henderson study shows, indexing is welcome tax relief, especially for people who can use the relief the most. And it forces the powers that be to play straight with taxpayers.

PAY PHONE PERMISSIVENESS

When the average consumer is counting his or her blessings these days, what belongs at the top of the list? Ralph Nader? Product-safety legislation? Tony the Tiger commercials? Hardly. Three far more plausible candidates are new technology, deregulation, and competition. Already, these three—often working in tandem—have made any number of consumer products and services more affordable and pleasant, and before long, yet another example will be coming down the pike. It is the humble pay phone.

Virtually every pay phone in the country is now owned by local telephone companies, but that monopoly is fated to go the way of hula hoops and the New Deal. Last June the Federal Communications Commission (FCC) voted to give private parties the choice of installing their own pay phones instead of renting them from Ma Bell's progeny and cousins.

The FCC action is important, but as a recent article in *Regulation* magazine pointed out, the advent of private pay phones "owes as much to advances in telephone technology as to the trend toward deregulation." The recent state of the pay-phone art was such that equipment in telephone companies' central offices had to verify coin deposits, return the coins whenever there was a busy signal or no answer, and more. No longer. There are now "smart" pay phones that, by virtue of internal circuitry, can accept coins, time calls, and so on—all using regular phone lines and

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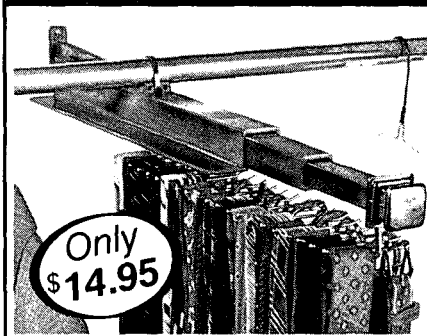
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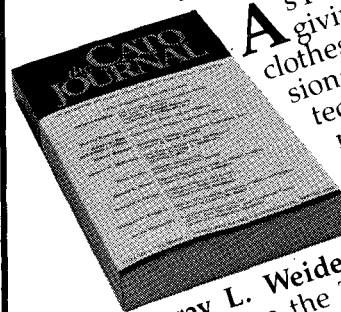
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The FCC didn't go as far as it might have, however. Instead of mandating full deregulation of pay phones, the commission is permitting state regulators to decide the rules for private pay phones and set their rates. This may create problems, though, since state public-utility commissions hostile to deregulation may have the opportunity to make mischief. In Minnesota, for example, instead of letting the parties work out their own arrangement, regulators have set a monthly fee that a business with a private pay phone must pay to the phone company for use of a line, as well as a fee for each call after the first 200 calls every month. It is not yet clear how much state regulation of this kind the FCC will permit, but *Regulation* noted that at least "some degree of nationwide deregulation is assured."

How will this new competition between the phone company's pay phones and the new private pay phones affect the consumer? *Regulation* predicted a wide variety of new pay phones will be available. Some will take calls for across the city, others for across the state or country. Some will take different credit cards. And perhaps most important, there should be new price competition where there is none currently.

So if it is not thwarted by overzealous state regulators, this one small deregulatory reform, along with the new technology that makes it widely feasible, should improve the lot of consumers more than a hundred Ralph Nader harangues and a thousand new bills in Congress ever would.

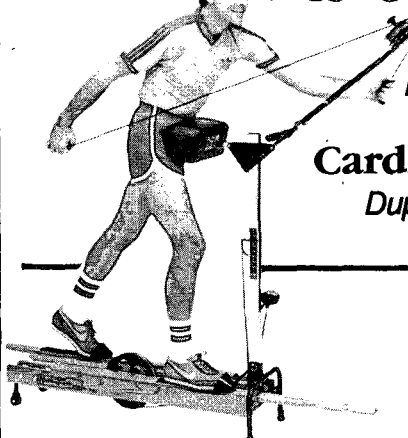
MILESTONES

• *Animal liberation.* A management audit of the Los Angeles Recreation and Parks Department has called the city zoo's management inadequate and declared that the city should consider turning the zoo's management and operation over to the private Greater Los Angeles Zoo Association.

• *Sollicitous opinion.* The New York Court of Appeals, the state's highest court, recently ruled that lawyers may use direct mail to solicit accident victims as clients. State laws throughout the country have prohibited lawyers from such solicitation.

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