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The Roots of China's Crisis

by Nien Cheng

Both my late husband and I went to the London School of Economics in the 1930s, and we became very liberal, or left-wing. When I read a book on the Soviet Union by Sidney and Beatrice Webb, I thought, "How wonderful and idealistic socialism sounds." However, I was shocked by Stalin's show trials in 1937, so I never joined the British Communist party.

My late husband was a diplomat in the Nationalist government. At the end of 1948, after serving in Australia during World War II, we returned to China. Conditions there were very bad. During China's eight years of waging a war of resistance against Japanese aggression, 1937 to 1945, 20 million Chinese people had lost their lives. Millions more were impoverished. The economy was in a terrible state, with runaway inflation and shortages of daily necessities. We thought the Kuomintang would never be able to pull China together.

Nien Cheng, the author of *Life and Death in Shanghai,* came to the United States in 1980. This article is based on her remarks at a recent Cato Institute luncheon.

The Communist underground was actively circulating propaganda materials. One of them was an essay by Mao Zedong, "On the United Front Government," in which he advocated democracy and the unity of every sector of Chinese society in order to rebuild China. It greatly appealed to us and to our friends, many of whom were professors with Ph.D.s from universities in the United States, Britain, Germany, France—Western democratic countries. We all decided to stay in China.

At the London School of Economics we had learned about socialism, the planned economy, and state ownership, which to young people sounded very equitable and fair. But there was no mention of class struggle, which was the most important thing to Mao and the Chinese Communist party, so we were unprepared for the realities of Communist rule.

In This Issue

Repression in China

After the recent crackdown in Tiananmen Square Stanley Karnow called me and asked me what I thought of it. I said, "Stanley, what do *you* think of it?" He said, "Well, it is not the worst, but it is the worst that has been *seen.*" I think that is a very good way of summing it up.

Between 1949 and the end of the Cultural Revolution Mao launched no fewer than nine major political movements as well as several minor ones. And during each political movement a large number of Chinese people were wrongfully accused of crimes and thrown into prison. I was one of them. In 1966, at the beginning of the Cultural Revolution, I was accused of being a spy. I could not have become a spy even if I had wanted to; I had no access to confidential government information. Many innocent people were thrown into prison or labor camps, and many lost their lives.

Periodically the Communists would encourage people to express their opinions. The biggest fiasco was the Hun-

(Cont. on p. 10)

Founders of the Alliance of Chinese Patriots, an organization composed of Chinese students at American colleges, met with Cato senior fellow Roger Pilon (at end of table) for advice on drawing up their Declaration of Principles.

Let the Boat People In

Chairman's Message

Around 50,000 Vietnamese people who fled their homeland in small boats are now confined to hovels in Hong Kong, awaiting deportation. The British government has reportedly offered the oppressive Communist government of Vietnam a bribe of $1,000 for each refugee who is forcibly returned. The U.S. government has ignored the situation, presumably on the grounds that it is a British problem. And the boat people, who risked their lives to flee Vietnam, have been given no choice in the matter.

In the larger pattern of 20th-century oppression, Britain's shabby treatment of the Vietnamese boat people may seem to be only a minor offense. And that offense is overwhelmed by Britain's refusal to allow even the most productive Chinese residents of Hong Kong to immigrate. Britain's policy toward the immigration of Asians, including those who bear restricted British passports, explains its treatment of the Vietnamese boat people, but its conduct is no less shabby as a consequence.

Nor does the U.S. government have an excuse for refusing to allow the boat people to immigrate. We are a nation of immigrants. After the first generation, foreign-born Americans have generally been more productive than native-born Americans. Vietnamese immigrants have been especially productive. Since the first substantial wave of Vietnamese immigration less than 20 years ago, they have established a large number of small businesses, and their children are honor students.

Moreover, the United States, not Britain, has a moral obligation to the Vietnamese. Our involvement in the Vietnam War was born more of innocence than of imperial ambition. But after the loss of 50,000 American lives and several hundred billion dollars, we left Vietnam to chaos and oppression, with the last Americans scrambling into helicopters on the roof of the U.S. embassy.

We once tried to help Vietnamese people by means of a war. We now have an opportunity to help Vietnamese people by means of an act of mercy. The United States can permit the boat people to immigrate as temporary workers or political refugees without changing the law. But it must do so before the British government forcibly returns them to Vietnam. A U.S. decision to welcome the boat people might also embarrass Britain into permitting increased immigration of Hong Kong residents, who are subject to oppression by the Communist government of China.

Maybe we cannot open America's borders to all the oppressed people who would prefer to move here. Maybe we should do more for homeless Americans. For important reasons, we should maintain good relations with Britain. And permitting the Vietnamese boat people to immigrate would not erase the mistakes that led to our involvement in the Vietnam War or the failings in our execution of that war. None of those considerations, however, is a sufficient basis for looking the other way while the boat people are forcibly repatriated.

I pray that the U.S. government will be generous enough and act quickly enough to permit the boat people to immigrate. The moral character of a nation is determined by its response to the oppression of individuals, not by the sophisticated rationalizations that pass for geopolitics.

—William A. Niskanen

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First Issue Out in January

Cato Acquires *Regulation* Magazine from AEI; Niskanen, England, Tripoli Will Be Editors

The Cato Institute will begin publishing *Regulation* magazine in January 1990. Founded by the American Enterprise Institute, *Regulation* has played an especially important role by presenting new scholarly work on the potential benefits of economic deregulation in a lively, readable manner. Moreover, it helped to shape the political climate that led to the deregulation proposals of the Carter and Reagan administrations.

AEI had planned to fold its three regular publications, including *Regulation*, into one new magazine. "When we heard of those plans," said Cato president Edward H. Crane, "we approached Chris DeMuth, president of AEI, with a request for the right to publish *Regulation*."

Crane is pleased with the "friendly takeover" and expects it to benefit Cato considerably. "The acquisition was made because *Regulation* will complement our existing programs perfectly," he said. Moreover, *Regulation* will serve as another means for Cato to "involve the business community with regulatory issues."

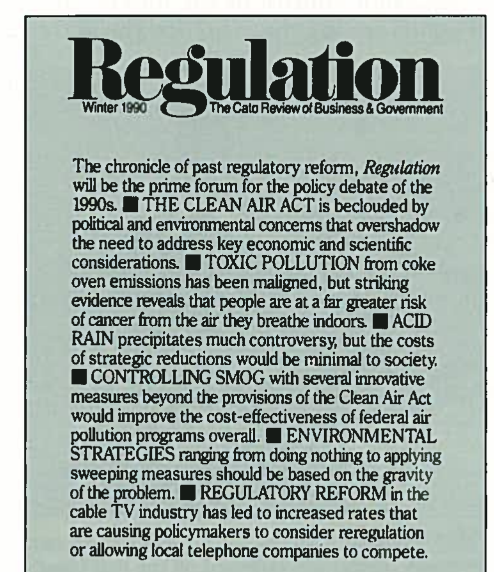
The Institute plans to publish three issues of *Regulation* a year. Under a controlled-circulation system, five thousand copies of each issue will be distributed to policymakers, important members of the media, and representatives of trade associations and corporations.

William A. Niskanen, chairman of the Cato Institute and a former member of the President's Council of Economic Advisers, will be editor of *Regulation*. Catherine England, Cato's director of regulatory studies, will be senior editor. Cato has hired Leigh Tripoli, who was managing editor of the *Rand Journal of Economics*, as managing editor of *Regulation*.

"The deregulation revolution of the 1970s and the 1980s was incomplete," Niskanen said, "and that has caused problems that many observers have incorrectly attributed to deregulation. For better or for worse, the 1990s will prove to be an active decade for regulation, antitrust, and trade policies, and *Regulation* can play an important role in shaping the perspectives of the policy audience."

The new editors of *Regulation: The Cato Review of Business & Government*: Catherine England, senior editor; Leigh Tripoli, managing editor; and William A. Niskanen, editor. Cato's first issue of *Regulation* will appear in January 1990.

England said, "Our political system is likely to respond to health, safety, and environmental issues by demanding more regulation, even though many forms of regulation are grossly inefficient, in part because regulations are manipulated to serve special interests."



Regulation
Winter 1990 The Cato Review of Business & Government

The chronicle of past regulatory reform, *Regulation* will be the prime forum for the policy debate of the 1990s. ■ THE CLEAN AIR ACT is beclouded by political and environmental concerns that overshadow the need to address key economic and scientific considerations. ■ TOXIC POLLUTION from coke oven emissions has been maligned, but striking evidence reveals that people are at a far greater risk of cancer from the air they breathe indoors. ■ ACID RAIN precipitates much controversy, but the costs of strategic reductions would be minimal to society. ■ CONTROLLING SMOG with several innovative measures beyond the provisions of the Clean Air Act would improve the cost-effectiveness of federal air pollution programs overall. ■ ENVIRONMENTAL STRATEGIES ranging from doing nothing to applying sweeping measures should be based on the gravity of the problem. ■ REGULATORY REFORM in the cable TV industry has led to increased rates that are causing policymakers to consider reregulation or allowing local telephone companies to compete.

"The debates on regulation are far from resolved," said Crane. "Cato will need to make a special effort to seek out the younger scholars and persuade them to use *Regulation* as their primary forum for reaching the policy audience."

Each issue of *Regulation* will focus on a theme, to which most of the articles will be devoted, as well as examining other topics of particular concern. The first issue will address the revision of the Clean Air Act. Subsequent issues will spotlight mandated benefits, trade policy, and the Sherman Antitrust Act.

Regular features of *Regulation* will include short essays by members of an advisory board composed of 15 distinguished scholars, reports on recent developments in the regulatory community, book reviews, and letters to the editor.

As a complement to *Regulation*, Cato plans to hold an annual conference on regulation, antitrust, and trade issues. A conference assessing the Sherman Antitrust Act on its 100th anniversary is scheduled for April 1990. ■

Cato Hosts Discussion of Political Change in Hungary

Cato Events

June 8: **"Is Your Private Life in the Public Eye?"** David F. Linowes, author of *Privacy in America,* warned that sensitive information on individuals is routinely collected by the private and public sectors. According to Linowes, information assumed to be confidential is widely shared by U.S. corporations, and the disclosures are often inaccurate or out of context. That practice, he said, has had disastrous consequences for employment seekers. Linowes argued that although businesses have been aware of the problem for 10 years, they have not made reforms. Having noted that other countries have privacy laws, he contended that the United States should introduce similar legislation.

June 12: **"Freeing the Baby Bells to Compete."** At a Cato forum held in the Rayburn House Office Building, Philip D. Mink of Citizens for a Sound Economy argued that allowing the Regional Bell Operating Companies to compete in the telecommunications marketplace would improve America's standing in the race to develop information-age technology. Daniel Kelley, director of regulatory policy at MCI, maintained that because the RBOCs would engage in discriminatory practices and cross-subsidization, their entry into the telecommunications industry would reduce domestic competition and have no offsetting trade benefits. Mink countered that FCC supervision would protect competitors and users from cross-subsidization.

Judy Shelton discusses the economic crisis facing the Soviet Union.

Philip Mink of Citizens for a Sound Economy discusses regulations imposed on the Bell Operating Companies as Daniel Kelley of MCI listens.

June 15: **"Constitutional Change in Hungary."** In keeping with its interest in constitutionalism worldwide, Cato's Center for Constitutional Studies hosted a luncheon address by Jozsef Szajer, a professor of law at Eotvos Lorand University in Budapest and cofounder of Fidesz, a liberal opposition youth group. Szajer discussed the goals and methods of the movement for constitutional change in Hungary, noting the historical connection between political and economic liberty as well as the role of private property in a free society.

June 20: David Glasner, an economist at the Federal Trade Commission and the author of ***Free Banking and Monetary Reform,*** asserted that the time is ripe to revisit the issue of privatizing money. He argued that financial innovations are undermining federal regulations and the Federal Reserve System's control of the money supply. Glasner described the history of private money, observing that until the Depression brought about a radical reduction of competition among banks, there was a fairly competitive environment. For the next 40 years, however, the government maintained tight control of the money supply, thus setting the stage for the activist monetary policy that brought about the "great inflation" of the 1970s.

June 22: James Bovard, author of ***The Farm Fiasco,*** advocated abolishing all agricultural subsidies. Bovard argued that the federal government, through a maze of regulations, has waged a 60-year war on agricultural markets, causing some farmers to go bankrupt while doling out $20 billion a year in subsidies. Bovard said that the average American farmer is a rich landowner and that such government programs hurt taxpayers more than they benefit farmers. Furthermore, he maintained, most farm products are unsubsidized, and the allocation of federal subsidies largely reflects which lobbies have influenced politicians. Benny Bunting, president of the National Family Farm Coalition, countered that the dumping practices of certain countries prevent American wheat farmers from competing in the world market.

July 1–8: **Summer Seminar in Political Economy.** The Institute's 11th annual summer seminar, held once again at Dartmouth College, featured as speakers Charles Murray, Earl Ravenal, Ralph Raico, David Kelley, Leonard Liggio, Mario Rizzo, Edward H. Crane, Catherine England, Ted Galen Carpenter, David Boaz, and George H. Smith. The 75 participants came from as far away as Iceland, New Zealand, and Peru and ranged in age from 16 to 60.

July 10: **"Decade of Revolution: The Dismantling of the State under Thatcherism."** During a round-table luncheon discussion held at Cato, Douglas Mason, a domestic policy adviser at the Adam Smith Institute, discussed the achievements of Prime Minister Margaret Thatcher's privatization movement and strategies for further reform.

July 12: **"The Coming Soviet Crash."** Judy Shelton, a research fellow at the Hoover Institution and author of *The Coming Soviet Crash,* asserted that more Western aid to the Soviet Union would impede the economic and political changes the West seeks. Because the expansion of the Soviet Union's money

Jozsef Szajer of Eotvos Lorand University discusses constitutional change in Hungary with Walter Friedenberg of Scripps Howard.

supply has outpaced its productivity, Mikhail Gorbachev faces a Catch-22: to ease domestic unrest, more consumer goods must be produced; yet the traditional incentive to increase productivity—increasing wages—would only make the country's economic problems worse. Thus, Gorbachev desperately needs Western goods and technology, which explains his efforts to woo the West. Shelton claimed that if the West withheld aid, Gorbachev would be forced to make such major changes as transferring funds from the military sector to productive sectors.

July 20: **"Government-Sponsored Enterprises."** Thomas H. Stanton, a Washington attorney and former associate general counsel for the Federal National Mortgage Association (Fannie Mae), argued that although government-sponsored enterprises have a legitimate role, the government has badly mismanaged their affairs. The seven GSEs, all multibillion-dollar operations, have been allowed to act like national banks, issuing federally backed loans under few constraints. GSE managers have taken excessively large risks, knowing that "heads, we win; tails, the taxpayers lose." Charles O. Sethness, director of capital markets at the International Finance Corporation of the World Bank, asserted that GSEs are unnecessary but conceded that their elimination is unlikely. Because GSEs are backed by powerful lobbies and interest groups, he said, it is almost impossible to supervise their financial risks. ■

CATO INSTITUTE CALENDAR

America's Housing Policy
Grand Hyatt Hotel • Washington
October 6, 1989
Speakers will include Al DelliBovi, Peter Ferrara, John Weicher, William Tucker, Irving Welfeld, Stuart Butler, Robert Woodson, Martha Burt, and Cassandra Moore.

RICO, Rights, and the Constitution
Grand Hyatt Hotel • Washington
October 18, 1989
Speakers will include David B. Sentelle, Roger Pilon, G. Robert Blakey, Joseph diGenova, Gerard Lynch, Nat Hentoff, Theodore B. Olson, Gordon Crovitz, and Gerald Lefcourt.

Education and the Inner City
Sheraton Carlton Hotel • Washington
November 2, 1989
Speakers will include Lynne V. Cheney, Pete du Pont, Seymour Fliegel, Robert Peterkin, Lawrence G. Patrick, Jr., John Chubb, Myron Lieberman, Bonita Brodt, Joan Davis Ratteray, William A. Niskanen, and John Coons.

Freedom and Technology: Prospects for Progress in the '90s
Fairmont Hotel • San Francisco
November 16, 1989
Speakers will include Milton Friedman and George Gilder.

Organizing for Change in China
A Conference for Chinese Student Leaders
Cosponsored with the Alliance of Chinese Patriots
Quality Inn • Washington
January 5–7, 1990

Second Annual Benefactor Summit
St. Thomas, Virgin Islands
January 25–28, 1990
Speakers will include Frederick W. Smith, Charles Murray, and George Gilder.

Global Monetary Order: 1992 and Beyond
Eighth Annual Monetary Conference
Cosponsored with the Institute of Economic Affairs
Queen Elizabeth II Conference Centre • London
February 22–23, 1990
Speakers will include Manuel H. Johnson, W. Lee Hoskins, Yoshio Suzuki, Antonio Martino, Pascal Salin, Anna J. Schwartz, Jerry L. Jordan, Georg Rich, Lawrence H. White, and Allan H. Meltzer.

100 Years of Antitrust
Sheraton Carlton Hotel • Washington
April 5–6, 1990

Twelfth Annual Summer Seminar in Political Economy
Dartmouth College • Hanover, N.H.
June 30–July 7, 1990

Will Government Lenders' Defaults Be the Next S&L Crisis?

Policy Forum

The Cato Institute regularly sponsors a Policy Forum at its Washington headquarters, where distinguished analysts present their views to an audience drawn from government, the media, and the public policy community. A recent forum featured Thomas H. Stanton, a Washington attorney and former associate general counsel for the Federal National Mortgage Association. Commenting on Stanton's remarks was Charles O. Sethness, director of capital markets at the International Finance Corporation and former assistant treasury secretary for domestic finance.

Thomas H. Stanton: The federal government uses government-sponsored enterprises to encourage the flow of credit to borrowers in special sectors of the economy—home buyers, students, and farmers, among others—who are considered not quite capable of obtaining credit on favorable terms.

Today there are seven GSEs: the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), the Farm Credit System, the Federal Home Loan Bank System, the Student Loan Marketing Association (Sallie Mae), the Federal Agricultural Mortgage Corporation (Farmer Mac), and the Financing Corporation (FICO) of the Federal Home Loan Bank System.

Fannie Mae and Freddie Mac provide a secondary market for residential mortgages. The Farm Credit System provides agricultural loans. The Federal Home Loan Bank System lends to thrift institutions. Sallie Mae provides education-related funding. Farmer Mac, which is technically part of the Farm Credit System, provides a secondary market for agricultural mortgages. FICO is helping to fund the insolvent FSLIC. The Bush administration has proposed that yet another GSE, the Resolution Funding Corporation (FICO II), be established to provide an additional $50 billion in off-budget financing.

GSEs can be huge, and they tend to grow quickly. At year end 1988 Fannie Mae had assets and mortgage-backed securities totaling $290 billion—an increase of $47 billion over year end 1987. Freddie Mac was a $260 billion financial institution. The Federal Home Loan Bank System's total was approximately $175 billion. Sallie Mae grew by 25 percent last year. In 1979 Sallie Mae was a $1.2 billion enterprise; today it is a $30 billion enterprise.

GSEs share other characteristics as well. First, they are privately owned, which has several implications: They're not included in the federal budget. They're not subject to the typical controls for government programs, such as civil service and federal procurement regulations. They are free to set up PACs, and at least two of them have done so. There are no limitations to their freedom to participate in the political or legislative process.

Thomas H. Stanton: "There is no free lunch in federal credit programs."

Another characteristic of GSEs is that they issue debt obligations and, in some cases, mortgage-backed securities that carry implicit federal guarantees. The implicit federal guarantee is an ingenious device. Essentially, it permits GSE obligations to mimic the characteristics of Treasury securities so that they can trade with Treasury securities in the federal agency credit markets. GSE obligations are eligible as collateral for Fed open-market transactions—they're bought and sold on the books of the Federal Reserve System. No limits are placed on their being held by national banks, federally chartered thrifts, pension and trust funds, and so forth. They are generally exempt from SEC registration requirements.

Because GSE obligations mimic the characteristics of Treasury securities, the market infers a guarantee. The government wouldn't exempt securities from such basic investor safeguards as SEC registration and limits on bank investments unless it believed that they were very safe. So investors tend to treat GSE obligations as being very close to Treasury securities—even when the guarantee is expressly disclaimed. The disclaimer itself is a clue to the existence of an implicit guarantee. General Motors doesn't need to go around disclaiming that the U.S. government stands behind its debt obligations.

Even though implicit, the federal guarantee is very powerful. My favorite example is an offering circular from FICO, which was created in 1987 to recapitalize the FSLIC. It discloses to anybody who wants to read the balance sheet that at year end 1988 FICO had a negative net worth of $5.3 billion (assets of $663 million and liabilities of $6 billion). Yet FICO was able, in that offering circular, to issue 30-year bonds at 9.7 percent interest. The disclaimer is right on the cover—"The bonds and interest payable on the bonds are not obligations of, or guaranteed as to principal or interest by, the U.S. government." But the market doesn't read balance sheets or disclaimers. Because of the implicit guarantee, the market treats GSE obligations as if they were in fact backed by the federal government.

The Farm Credit System lost a total of $4.6 billion in 1985 and 1986. Yet in 1987, thanks to the federal guarantee, Standard & Poor's was able to issue a report stating that Farm Credit System obligations were eligible as collateral for AAA-rated bond transactions.

A GSE can issue billions of dollars' worth of obligations on the basis of a one-page term sheet that says, "This is what we're offering, so make your bid." A 1989 term sheet from the Federal Home Loan Bank System said, "By the way, we have some financial statements from October 1988 if you want to look at them." In contrast, ordinary borrowers in the private market have their balance sheets scrutinized by everybody and therefore face significant market discipline if they take risks.

The implicit guarantee of GSE obligations is even better than federal deposit insurance. GSEs, unlike banks and thrifts, don't have a $100,000-per-account limit, and the implicit guarantee even applies to their subordinated obligations.

A GSE can be considered a special kind of national bank. Like national banks, GSEs are federally chartered and privately owned. Like national banks that have federal deposit insurance, GSEs use federal credit support to lower their borrowing costs. Indeed, given the targeted nature of their lending, GSEs might more properly be likened to thrift institutions, which are also specialized in terms of assets and lending functions.

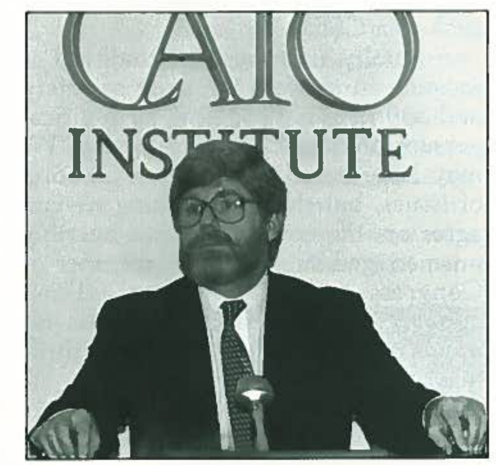
Like thrifts, GSEs have market risk. The Farm Credit System was seriously affected when the agricultural economy, to which it is limited, suffered a severe decline in the early 1980s. What will happen to Fannie Mae and Freddie Mac—and the credit quality of their loans—if we find out that the baby-boom generation has been housed and we have a decline in housing demand and housing values during the next few years instead of the steady appreciation we've been enjoying during the past few years?

GSEs have other kinds of risks as well: credit risk, interest-rate risk, operations risk, and management risk. Like institutions with federally insured deposits, they lose a significant amount of market discipline because of the federal guarantee.

In a regular private company, debt holders get paid before shareholders, so they'll say, "I want a capital cushion. I want you, the manager of this institution, to have something of your own at stake when you are engaging in lending because I want you to act prudently. If your money is there, you will have first loss." But in a GSE, where the investor is looking at the implicit guarantee instead of the balance sheet, that kind of constraint on risk-taking doesn't exist.

When the Farm Credit System declared that it could not meet its obligations without federal assistance, its loans still traded at rates considerably below normal corporate rates. Yes, the rates increased—there is still some residual market discipline—but not significantly. GSE managers have an opportunity to take extra risks to seek extra returns. To paraphrase Ed Gray of the FSLIC, "Heads, they win; tails, the taxpayers pay for the big mistake." If we accept the analogy to banks and thrifts, the significant missing ingredient is effective federal oversight of GSEs' safety and soundness.

Until the Farm Credit System hit the wall in 1985, it essentially dominated its regulator. The Farm Credit System had been taking substantial interest-rate risk and credit risk as well as some management risk. The new regulator has many of the enforcement powers of the federal bank regulators.



Charles O. Sethness: "Government-sponsored enterprises distort credit allocation."

The Department of Housing and Urban Development has been weakened as a financial regulator since Fannie Mae got into trouble in the late 1970s. Fannie Mae essentially served as a large thrift in the secondary market. It was lending long on a portfolio of long-term mortgages and borrowing short—the same squeeze that caught thrift institutions.

HUD, which has never had a clear conception of its mandate to ensure safety and soundness, has provoked Fannie Mae with various housing policy directives. In the late 1970s, for example, HUD launched a four-year effort to force Fannie Mae to invest in inner-city mortgages, even though that was not an element of Fannie Mae's corporate charter. It doesn't excuse the Fannie Mae management team of that era, but I suspect that a four-year feud with its regulator concerning everything but safety and soundness could have helped to cause Fannie Mae to take its eye off the ball, which at the time was interest rates.

The savings and loan bill currently going through Congress further weakens HUD's supervisory powers. It essentially eviscerates HUD's authority to set conditions that apply when Fannie Mae and Freddie Mac enter new lines of business. The bill also transfers regulatory authority over Freddie Mac from the Federal Home Loan Bank Board to HUD, which is likely to be overwhelmed by having responsibility for two institutions whose assets and mortgage-backed securities total over half a trillion dollars. Unlike the bank and thrift regulators, HUD doesn't have the power to build up a core of trained examiners who can go in and assess the quality of transactions. To the best of my knowledge, not once in 19 years has HUD used its authority to examine Fannie Mae's books. I'm not sure that its examiners would know what to do when they got there.

With some exceptions, GSEs tend to have less capital than commercial banks. Fannie Mae, a $290 billion institution, has shareholder equity of $2.3 billion; Freddie Mac, a $260 billion institution, has shareholder equity of $1.6 billion—in each case well under 1 percent.

Remember, capital is the deductible on the federal insurance policy. If, heaven forbid, something goes wrong with a GSE, that problem, be it an external one such as a change in a market or an internal one such as the failure of an operations system, has the potential to permeate the whole range of that GSE's portfolio. Bank portfolios contain agricultural loans, commercial loans, consumer loans, international loans—all different kinds of loans. Those loans have risks, but the risks are different for each category of loan. But because GSEs are specialized lenders, their risks line up, so problems with interest-rate risk, credit risk, and management risk can hit them all at once.

Problems can hit specialized lenders very quickly. I met with a group of Farm Credit System representatives in

(Cont. on p. 8)

Lenders' Defaults (Cont. from p. 7)

1983, when they were trying to fend off the Reagan administration's efforts to privatize the system. They were proud of its being the premier GSE; its obligations traded at the tightest spreads over Treasury securities. But in 1984 the Farm Credit System regulator's report said, "We have a problem with loan losses, but don't worry." In 1985 it said, "Folks, we can't make it." By the end of 1986 the Farm Credit System had booked losses of $4.6 billion in two years.

I consider GSEs legitimate instruments of federal policy, but I find FICO to be an absolute outrage, a total budgetary subterfuge. Basically, FICO is a way for the government to saddle our kids and grandkids with our obligations. It's a way to issue 30-year loans that everybody knows FICO—or FICO II, as the case may be—could never repay on its own. That is not, to my mind, a legitimate use of a government-sponsored enterprise.

As for the other GSEs, the benefits of their activities should exceed the costs. The failure of the FSLIC shows that there is no free lunch in federal credit programs. We can't keep extending an open-ended guarantee; we must insist on accountability. If GSEs are comparable to national banks, then we should establish a regulator of safety and soundness comparable to the Comptroller of the Currency or, even better, comparable to the FDIC, an independent agency.

That is a modest proposal, but winning support for it will not be easy, even with the lessons of the FSLIC before us. A provision in the House-passed S&L bill, section 1404, illustrates the difficulty of getting the federal government to put its house in order. The House Ways and Means Committee added section 1404. It's not a regulatory provision but asks only that the federal government annually assess the risks it incurs from the implicit guarantee extended to each of the GSEs. A senior Senate conferee has strenuously objected to that provision, which, as far as I'm concerned, is a classic case of political hardball versus good government. I advise you to take a close look at how the contest comes out.

At least one Wall Street firm has already told us how the contest is going to come out. A *First Boston Investor Advisory* said, "The probability of Fannie Mae facing higher capital requirements or any type of user fee compares with the likelihood that Congress will convert the Lincoln Memorial to a discotheque. We see no reason, based on political factors, to alter our buy recommendation on Fannie Mae." Wall Street exerts grueling pressure on companies to shorten their time horizons, pay attention to their quarterly returns, try to intermediate their yield curves, and get a little more kick out of their portfolios, lending long and borrowing short or vice versa, in the interest of upping their short-term attractiveness to shareholders. There can be real costs to a short-term perspective for a long-term institution in a specialized sector, such as a GSE.

A totally unorganized coalition is forming to address the issue of safety and soundness. People of all political persuasions are beginning to say, "We may have our differences on all sorts of issues, but there's one thing we can agree on: the government has horribly mismanaged its affairs." A member of Congress said, "You know, talking about GSE safety and soundness reminds me of trying to warn about thrift institutions in 1980."

Charles O. Sethness: I spent three years at the Treasury Department watching those implicit guarantees become explicit and trying to figure out what to do about it. I believe that government-sponsored enterprises distort credit allocation and are therefore costly and, given a market-based allocation of resources, unnecessary. They also tend to freeze out private initiatives. For those reasons, if we can't abolish GSEs, we should at least be very careful about how they get set up, how they get managed and administered, and how the taxpayer gets protected from their effects.

In discussing GSEs, any definition one picks causes problems, and part of Tom's outrage about FICO may stem from its falling into the category of GSEs that were not in fact set up to do the kinds of things that Fannie Mae, Freddie Mac, Sallie Mae, and the Farm Credit System do and Farmer Mac is intended to do. FICO and the Farm Credit System Assistance Corporation were set up to help institutions that were facing insolvency. The only way to get congressional approval for that was to do it through off-budget enterprises.

Those of us who believed that an implicit federal guarantee was in force whether we wanted one or not were very worried that the first time the government dishonored the implicit guarantee, it would find itself with somewhere between $100 billion and $500 billion worth of securities that were about to drop sharply in value. That sharp decline in value would probably wipe out the remaining money-center banks, even those that weren't already in deep trouble, because it would diminish the value of their securities portfolios as well.

We knew that the ripple effects from defaults among the Farm Credit System banks or the S&Ls would be very bad, so we had to do something. It wasn't practical to provide on-budget funding to the Farm Credit System or the FSLIC, so we created some useful quasi-fictions—FICO and the Farm Credit System Assistance Corporation. Those two GSEs and FICO II, the Bush administration's proposed S&L bailout mechanism, all have the same basic pattern and the same basic purpose. I think they were designed in such a way that they would not create moral hazard. Their activities are very narrowly defined, and their dollar limits are capped. There are no hidden agendas. They can do only the damage that Congress was told they were going to do when they were designed.

I think that Tom's FICO balance sheet argument is a little misleading. FICO's assets, which supposedly amount to much less than its liabilities, are all held in zero-coupon bonds whose value at maturity will be identical to the value of the liabilities at maturity. FICO's liabilities are defeased in principal terms. The risk to the bondholder is that there will not be a premium stream from the FSLIC sufficient to cover the interest on the bonds.

I couldn't agree more that capital-adequacy standards should be established and that a mechanism for reasonably close supervision of GSE activities, with a particular focus on the financial risk that the taxpayer is taking, should be put in place. Under the present system, however, it is next to impossible to accomplish those things. Each GSE goes through its own committee and reflects its own constituents' interests. Each piece of legislation is custom-cut for that GSE. The only reason a GSE comes into existence is that somebody—and eventually a majority of the legislators in both bodies—wants preferred credit to be allocated to a class of borrowers that would not otherwise get loans, at least not on such favorable terms.

The next step, it's argued, is to make that credit as cheap, easy, and flexible as possible. Well, the way to do that is to eliminate all lending constraints, reduce capital requirements to a minimum, and make GSE obligations as much like Treasury securities as possible. It's then argued that there's no need to go through the relatively expensive and cumbersome process of registering with the SEC and so on. As long as legislators take those matters up one at a time in a single-committee context, they're going to end up with something that has moral hazard. That's because it's impossible to enforce enough discipline at the committee level to take the broader view that the taxpayers' interests ought to be protected. ■

Cato adjunct scholars Walter E. Williams and Paul Craig Roberts at a Cato Policy Forum.

Friedman Highlights *Cato Journal* Issue on Economic Reform in China

Nobel laureate Milton Friedman discusses the role of the market as a vehicle for China's economic and social development in the latest issue of the *Cato Journal* (vol. 8, no. 3). He argues that the best way to promote rapid progress toward a market economy for China is to "give government-owned enterprises to the citizens" and that the best way to avoid corruption is to leave economic decisions to private groups and individuals.

The special *Journal* issue also features essays by such noted scholars as Pu Shan, director of the Institute of World Economics and Politics at the Chinese Academy of Social Sciences; He Weiling, a senior fellow at the National Economic System Reform Institute of China; Steven N. S. Cheung, a professor of economics at the University of Hong Kong; Alvin Rabushka, a senior fellow at the Hoover Institution; and author George Gilder.

The papers in the *Journal* issue were presented at the September 1988 conference "Economic Reform in China," held in Shanghai. The conference, cosponsored by the Cato Institute and Fudan University, was directed by James A. Dorn, vice president for academic affairs of the Institute and editor of the *Cato Journal*. It was the first time an American think tank was able to carry on such far-ranging and frank discussions of economic reform with prominent Chinese scholars and economic planning officials.

The corruption that is currently splitting China at the seams "stems from the ruling elite's vast power over economic and personal freedom," Dorn writes in his introduction to the *Journal* issue. "As long as a Chinese wall surrounds the ruling elite—preventing the free flow of market information and the free expression of ideas—the quest for economic and social stability will fail to be realized."

A complete set of conference papers will be published in English by the University of Chicago Press, and a publisher is being sought for a Chinese edition.

"Corruption and inflation, which are inevitable results of China's refusal to move away from piecemeal reform and toward thoroughgoing price and ownership reform, helped lead to the demonstrations for freedom and democracy in Tiananmen Square," Dorn said. "The articles in this issue seek to explain the economic forces underlying the events in Tiananmen Square and describe the steps that must be taken to bring freedom and prosperity to China."

A one-year subscription to the *Cato Journal* costs $21.00; single issues cost $7.00. ■

Milton Friedman and Pu Shan listen as *Cato Journal* editor James A. Dorn introduces a panel at the Shanghai conference.

China's Crisis (Cont. from p. 1)

dred Flowers campaign in 1956, during which everyone was urged to offer constructive comments about the shortcomings of the Communist party. The following year all the people who had said anything were seized and punished. Most of the victims were educated people—intellectuals. After that there was almost complete silence in China, and all cultural activities stagnated.

Now once again there has been a crackdown on the student movement. This episode has to be viewed on two levels: as a power struggle within the party leadership and as a spontaneous expression of discontent on the part of the Chinese people.

Early in 1989 there were hints of an impending power struggle that might result in the ouster of Zhao Ziyang, who had been China's prime minister at the beginning of the economic reforms. When Hu Yaobang was ousted as general secretary of the Communist party because he had refused to repress the December 1986 student demonstrations, Zhao Ziyang became general secretary and Li Peng became prime minister.

Deng Xiaoping had entrusted both Hu and Zhao with carrying out the economic reforms. Contrary to the general understanding outside China, Deng never intended China to go the whole way and adopt a market economy—that is, abandon socialism. He wanted to preserve the socialist sector—government-owned factories and so on—and have only a small capitalist sector to supplement it. Of course, that's an unworkable idea.

The reason Deng wanted to apply market economies' methods to the management of the socialist sector is that at the end of the Cultural Revolution China's productivity was at an extremely low point, and the prestige of the Communist party was at an all-time low. Deng wanted to improve the people's standard of living a little and pull China together economically.

Half Controlled, Half Free

But in the course of implementing Deng Xiaoping's policy, Zhao Ziyang and Hu Yaobang both realized that it was impossible to keep half of China's

> "Zhao Ziyang and Hu Yaobang both realized that it was impossible to keep half of China's economy under state planning and half of it free."

economy under state planning and half of it free. For one thing, the state-owned enterprises got their raw materials from government agencies at very low subsidized prices, and side by side with that arrangement was a free market for the same materials at prices five to eight times as high.

In such a situation, the opportunity for corruption is tremendous. Anyone who had access to government-supplied raw materials could sell them on the free market. Some of the factories could afford to pay their workers without producing anything at all. Everything was based on personal relations. Factory managers without connections were obliged to buy raw materials on the free market. Of course, the children and associates of senior government officials were at a great advantage because they had connections. There was a great deal of corruption, and the economy was in a constant state of confusion.

Zhao Ziyang and Hu Yaobang realized that China must go the whole way and adopt capitalism. On the other hand, the old guard, leaders who are now in their eighties, would not give up socialism. But neither could they oppose Deng Xiaoping; he is too strong and has too much personal prestige in the party. So what they hoped to do is destroy the men who implement the economic reforms. First they got rid of Hu Yaobang, and this year they turned on Zhao Ziyang. Naturally, because of his position, Zhao had a great deal of power. Deng Xiaoping felt that Zhao was too ambitious and independent, so he sided with the old guard.

As Simon Leys, who is a great writer on China, noted in a recent article, whether a Chinese leader is a hero or a scoundrel from the point of view of the people depends on whether he has been ousted or is in power. Hu Yaobang was not very popular when he was in power, but when he died, having been ousted, the students all turned out to eulogize him. Their pro-Hu demonstration on April 15 was also a typically Chinese way of making a statement. The demonstrators were not only paying tribute to Hu but saying "We support Zhao Ziyang," because Hu and Zhao represented the same viewpoint. Of course,

Nien Cheng talks with *New Republic* editor Hendrik Hertzberg at a Cato luncheon.

> "The main reason for the Chinese people's discontent is not that they cannot exercise the freedom of speech or assembly; it is basically economic."

later Zhao refused to be a party to the decision to suppress the student demonstrations by force. That is the background of the power struggle.

Popular Discontent

As for the Chinese people's discontent, consider what happened when Poland relaxed its price controls: all the basic necessities became much more expensive. The same thing happened when Zhao released a few items from price control. People on fixed salaries, such as professors, had a hard time making ends meet. The official figure for inflation in China is 26 percent, but the unofficial estimate puts it at over 40 percent.

The main reason for the Chinese people's discontent is not that they cannot exercise the freedom of speech or assembly, criticize the government, or choose alternative candidates for the People's Congress. The reason for their discontent is basically economic—their living standard has declined. The discontent is not confined to urban areas. Because the government doesn't have enough money to pay the peasants for their grain and other products, they are being given IOUs. With the inflation rate so high, in no time at all an IOU is worth nothing.

When the students first demonstrated in Tiananmen Square, all they meant by "democracy" was freedom of the press, a student union that was freely elected, not controlled by the government, and an end to corruption and nepotism. Of course, they also wanted more control over their lives. Young people in China know that when they graduate from college, it's the government that will give them jobs. They know that if the government gives them jobs in, say, Tibet, that's where they'll have to go. They are not free to make such basic choices as where to work, where to live, and how many children to have. The government intrudes in people's lives to a great extent.

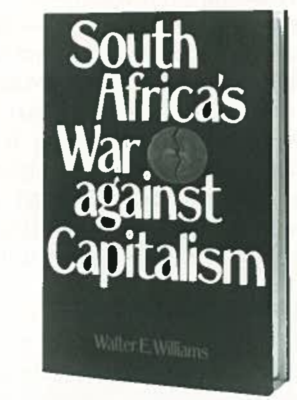
If the general population hadn't participated in the protests in Tiananmen Square, the government probably wouldn't have sent out the troops. But when workers and ordinary citizens joined the students, the government got really frightened. ■

Cato president Edward H. Crane listens as Nien Cheng discusses China's current crisis.

Williams Indicts Apartheid

South Africa Needs Capitalism

Apartheid is the result of anticapitalistic efforts to subvert the operation of market forces, charges Walter E. Williams in *South Africa's War against Capitalism*. "Indeed, it is the free play of market forces—with no intervention by political forces—that has always been seen as the enemy of white privilege and that apartheid ideology has always sought to defeat."



Market forces have eroded adherence to the extensive body of regulations designed to keep nonwhites from holding certain jobs, Williams argues. "Many of the socioeconomic advances made by blacks, coloreds, and Asians in South Africa have been due to the market forces that produce this search for mutually advantageous exchange." Moreover, he notes, an overwhelming majority of South Africa's blacks are against disinvestment and trade sanctions because they view foreign business as a way to break down apartheid and as the source of some of the best jobs.

Aided by market forces, nonwhites have made significant inroads into such industries as mining, textile manufacturing, and postal work. The Federated Chamber of Industries estimated that 47 percent of the industries in the Pretoria, Witwatersrand, and Vereeniging areas have hired more blacks than the legal quota. Williams argues that white employers have "constantly sought special exemptions and evaded, contravened, and violated [apartheid laws] in order to hire blacks."

Williams also argues that when property rights are restricted and profit motives constrained, there is an increase in discrimination of all forms. "This suggests that—contrary to popular wisdom—constrained profit motives do not serve the interests of less preferred groups." That conclusion "requires no judgment on or even acknowledgment of the personality traits of managers in for-profit organizations versus those in not-for-profit organizations. It requires only the acknowledgment that people's decisions are influenced by cost."

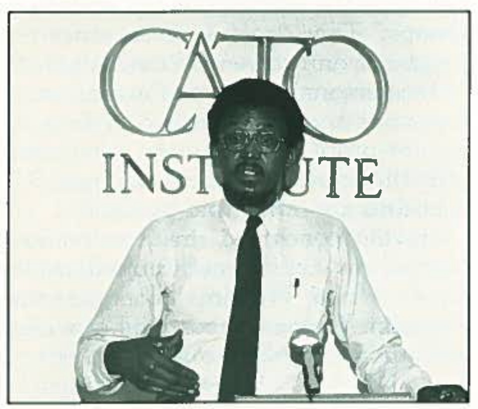
Having concluded that free-market capitalism would benefit nonwhites in South Africa, Williams notes that the economic illogic of apartheid provides an important lesson on the inefficacy and unfairness of government regula-

(Cont. on p. 12)

South Africa (Cont. from p. 11)

tion in any society. "The evidence marshaled in this book strongly suggests that whatever strengthens market forces and weakens government power will best serve the interests of South Africa's nonwhite population," he writes. Such a proposition applies to any group of people that "can be characterized as low skilled, unpopular, and discriminated against"; it is "not unique to South Africa."

The book has been hailed by prominent South Africans, including KwaZulu chief minister Mangosuthu G. Buthelezi, who writes, "When people call South Africa a capitalist country, I don't know whether to laugh or cry. Apartheid—a system that tells people where they can live, forbids them to own land, restricts the businesses they can enter, and controls the prices of goods and services—is the opposite of free-market capitalism. Walter Williams



Walter E. Williams attacks the notion that South Africa is a capitalist country.

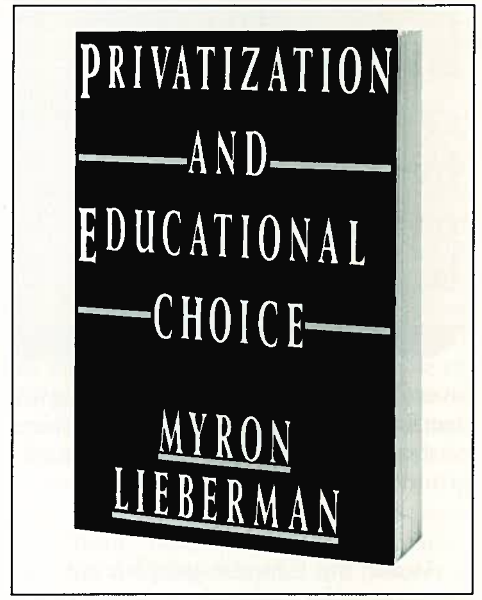
is right: privileged groups in South Africa set up apartheid to protect themselves from competitive capitalism, and what we need now is to replace apartheid with free enterprise."

Development economist Peter Bauer says, "The discussion of the role of market forces in eroding apartheid is both illuminating and highly pertinent to American public policy and business conduct toward South Africa. The book is Walter Williams at his best, which is saying no little."

A clothbound edition of *South Africa's War against Capitalism*, published by Praeger, is available from the Cato Institute for $19.95. ■

Education Reform Will Fail, Book Says, without For-Profit Schools

In *Privatization and Educational Choice* Myron Lieberman argues that the only ways to achieve lasting improvements in American education are to "foster private schools that compete with public schools and among themselves and [to] foster for-profit competition among service providers within the public school system."



Conventional approaches to educational reform will ultimately fail, Lieberman asserts, because of the bureaucratic structure of the public schools and the interest groups that block reform.

According to Lieberman, parents, not government agencies, should be empowered to make choices that compel schools to maintain high standards. Furthermore, there would be great benefits to having parents pay for educational services, just as they pay for medical care, transportation, and so on.

"Unfortunately, public education has severed the connection between the payor and the consumer, to the point where the latter lacks adequate incentives to monitor the services provided," Lieberman writes. "The evidence that higher levels of effort and achievement would result from education paid from personal instead of public funds is overwhelming."

James S. Coleman of the University of Chicago says that Lieberman's book is "a guide toward realization of the educational potential of the movement for choice."

Lieberman analyzes such modes of privatization as education vouchers, contracting out instruction, franchises and subsidies (including tax credits) for providers of educational services, and load shedding, or the government's withdrawal from the funding as well as the delivery of such services.

Privatization and choice would lead to competition and increased efficiency, Lieberman says, and for-profit schools would have a strong incentive to provide the educational quality that parents seek while holding costs down through innovative techniques.

Today high school diplomas are "symbols of time serving, not of significant educational achievement," Lieberman argues. "In many cases, staying in school retards rather than fosters the skills, attitudes, and habits required for civic, social, and economic competence."

Lieberman identifies trends that could lead to greater support for privatization and choice in education, including parents' dissatisfaction with public schools. He argues that one of the changes in attitudes toward children—the increasingly widespread view that they are "the outcome of deliberate 'consumer' decisions whose economic costs should be borne by those who make the decisions"—is "irreversible" and "certain to weaken support for public education."

The demand for specialized educational services outside regular schools is also increasing, Lieberman notes. "In view of the expansion of choice in religion, politics, marriage, higher education, occupation, spouse, residence, and lifestyle, in addition to the enormous increase in choice of products and services, the absence of educational choice below the college level may be simply an anachronism."

Privatization and Educational Choice, published by St. Martin's Press, is available from the Cato Institute, in cloth for $35.00 and in paper for $12.95. ■

Let the Marketplace Experiment

Government Should Not Subsidize HDTV, Moore Says

The government should treat the advent of high-definition television with benign indifference, according to a new study from the Cato Institute.

Thomas Gale Moore, a senior fellow at the Hoover Institution who was a member of the President's Council of Economic Advisers from 1985 to May 1989, warns that "while the HDTV industry looks like a winner, it could be the turkey of all time." Thus, given that "the government is singularly bad at picking winners and losers," it should "stay out of the private sector. Its incentives are wrong, its information is inadequate, and its biases are all wrong."

Moore contends that because of technological and regulatory problems, including the possibility of different production and transmission standards in the United States, Japan, and Europe, "the introduction of HDTV is likely to be evolutionary rather than revolutionary."

The marketplace, Moore observes, will allow "experimentation with various systems until consumers make a clear choice," whereas "a government-imposed standard may easily be wrong, but there is no way even after the fact to be certain of whether the right decision was made."

The development, production, assembly, and installation of electronic components often take place in different countries; "world trade is based on specialization." Thus, "no [HDTV] system should be ruled out or discriminated against simply because it has been developed primarily in another country. If the Japanese system is the best, it should be chosen."

Moore argues that there is no basis for the fear that if the United States loses the HDTV market to Japan, U.S. firms will lose other markets to Japanese firms as well. "A country's dominance of one market implies nothing about its potential to dominate others."

The Defense Advanced Research Project Agency plans to invest $30 million in HDTV. DARPA claims that HDTV would have important military applications, but according to Moore, its reluctance to award R&D contracts to U.S.-based, foreign-owned firms shows that "the hidden agenda is to foster a domestically owned HDTV production base."

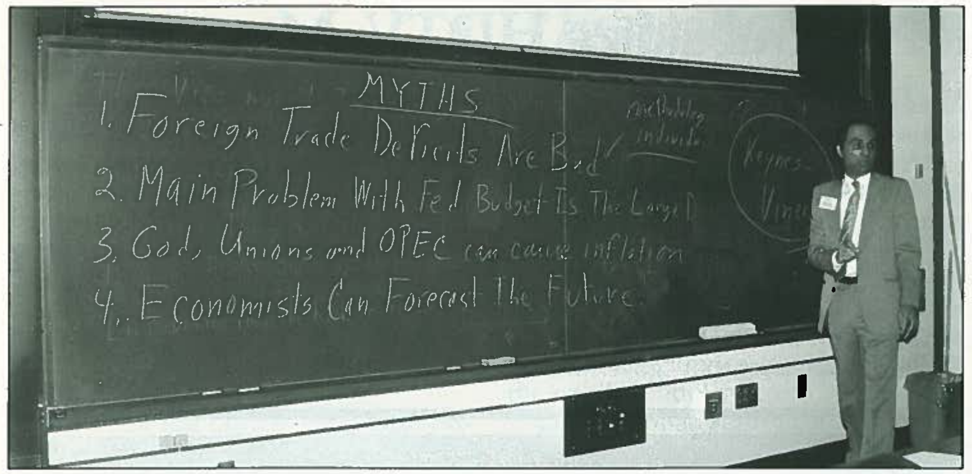
Pending legislation calls for a $500 million subsidy for HDTV development. "A major drawback to fostering HDTV artificially," Moore notes, "is that the resources . . . would have to be diverted from elsewhere because engineering talent is scarce and valuable."

Moore also notes that "governments often base investment and spending decisions on political considerations." They choose investments that would preserve or create jobs, not investments that would be profitable.

"The Promise of High-Definition Television: The Hype and the Reality" is no. 123 in the Cato Institute's Policy Analysis series. It is available from the Institute for $2.00. ■

The Cato Institute's interns for summer 1989: Iain Smedley, Cambridge University; Scott Bullock, University of Pittsburgh; Denise Wolf, University of Pennsylvania; Lance Alarcon, Yale University; Channing Rouse, University of North Carolina; Tim Lukens, Colgate University; and Matt Reid, Oberlin College.

Cato president Edward H. Crane talks with David Gergen of *U.S. News & World Report* at a Cato luncheon.



Mario J. Rizzo of New York University discusses myths about economic policy at the Cato Institute's 11th annual Summer Seminar in Political Economy, held once again at Dartmouth College. Other speakers included Ralph Raico, Leonard Liggio, David Kelley, George Smith, David Boaz, Catherine England, Ted Galen Carpenter, and Earl Ravenal.

The summer seminar's 75 participants came from all over the United States and from as far away as New Zealand, Chile, Iceland, and France. Pictured here are Beverly Jenkins of Glendale, Arizona; Phillipa Szekeres of Holmdel, New Jersey; and John Bechtel of Columbus, Ohio.

One of the high points of the summer seminar is the opportunity to converse with the lecturers throughout the week. Here John Juergensen of the University of Chicago talks with Charles Murray.

FmHA Subsidies Hook Farmers

Loans from the Farmers Home Administration "have helped wreck thousands of subsidized farmers' lives and created unfair competition for unsubsidized farmers," according to a new study from the Cato Institute.

In the study, which is based on a chapter in his new book, *The Farm Fiasco*, Cato associate policy analyst James Bovard argues that in responding to the farm credit crisis, policymakers "avoided fundamental structural reform and instead simply injected cash and vastly expanded taxpayers' liability."

Since the 1880s, when "many farmers borrowed money at justifiably high interest rates to buy land and plant crops, the remedy prescribed for every farm crisis has been more credit on easier terms," Bovard writes. "Between 1975 and 1984 FmHA's loan portfolio increased from $5 billion to $27 billion. Its 1979 loan volume was 50 times as large as its 1960 loan volume."

FmHA's records indicate that the most frequent cause of farm bankruptcy is poor agricultural practices, but "FmHA's records also indicate that almost one-quarter of the bankruptcies among its borrowers were largely due to their having received too many loans."

A 1986 General Accounting Office report estimated that half of FmHA's $28 billion loan portfolio was held by farmers who would default on their loans. According to Bovard, "the federal government's farm credit policy is one of the clearest refutations of the notion that politicians can manage the economy better than private citizens."

FmHA loans penalize farmers who do not receive them, Bovard contends. "Congress has created two classes of farmers: welfare farmers and self-reliant farmers," he writes. "Every dollar of aid the government gives to welfare farmers makes it more difficult for self-reliant farmers to survive."

"The Farm Credit Quagmire," no. 122 in the Policy Analysis series, is available from the Cato Institute for $2.00. ■

"To be governed..."

Britain needs bureaucrats, not entrepreneurs

An all-party committee of the House of Commons [approved] a policy that would provide a haven [in Britain] for only a few thousand of [Hong Kong's] residents. . . .

The committee called for "assurances" to be given to "a significant number" of "key people in the Hong Kong civil service, the police or . . . any area of public life" that they will be admitted to [Britain].

—*Washington Post*, July 1, 1989

It's worked so well up till now

The Soviet legislature . . . approved in principle the plans of . . . Lithuania and Estonia to develop market-oriented economies independent of the central plan that now governs almost every aspect of Soviet business. . . .

The Baltic plan encountered bitter opposition from central planners, who complain that it would complicate their work.

—*New York Times*, July 28, 1989

Reflections of a Public Man: The Sequel

[Former Speaker of the House Jim] Wright said he has made no immediate plans, though he said he is looking forward to having more time to write.

—*Washington Post*, June 6, 1989

It's always something

"How's your hand?" [Voter Revolt's Harvey] Rosenfield asks. [Ralph] Nader looks at the hand he scalded in a sink a few days back in Sacramento.

"Better," Nader says. "That hot water was almost boiling. The government hasn't set temperature limits in Sacramento, so that's what happens."

—*Washington Post*, July 23, 1989

At last we've found the right job for him

[Jimmy] Carter, as he has been demonstrating quietly for years and has just demonstrated spectacularly in Panama, is the class of the field—the most imaginative, the most exemplary, the most useful to his country, in short the most presidential of the ex-presidents.

—Hendrik Hertzberg in the *New Republic*, June 5, 1989

They're good enough for the taxpayers

Officers [of the U.S. Mission to the United Nations], almost all of whom live in New York City, receive no allowance for their children's schooling, meaning many must send their children to the city's decrepit public schools.

—*Washington Post*, June 19, 1989

Action ideas for taxpayers

Ordinary working Chinese undermine [the Communist party's] authority, sometimes with an extra dash of daring, or even cruelty—people like Lei Xiding. A small-town peddler, Mr. Lei had tax evasion rather than rebellion on his mind when he took on the Government. Four officials went to his village to make him pay taxes on 46 pigs he had purchased, but Mr. Lei and his family tore up the men's legal papers, robbed them of their watches and locked them in cages with the pigs. Then, according to China's official press, Mr. Lei and his relatives beat the tax collectors for five hours, urinated on them and paraded them blindfolded through the streets.

Eventually, the four men were released, alive—which makes them luckier than some of their colleagues. Since 1985, according to the *People's Daily*, 13 tax collectors have been murdered, 27 crippled and 6,400 beaten up.

—*New York Times*, June 4, 1989

Not quite getting it

[The *People's Daily*] asserted that "opening to the outside world" and "economic reform" must remain China's policies, but it said they could succeed only if the [Communist] party strictly enforced its own monopolies on political power and right-thinking.

—*Baltimore Sun*, June 17, 1989

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