Readings
of particular interest

More on Campaign Spending

"The Economic Theory of Regulation and Public Financing of Presidential Elections" by Burton A. Abrams and Russell F. Settle, in *Journal of Political Economy*, vol. 86 (April 1978), pp. 245-257.

Did public financing alter the outcome of the 1976 presidential election? Professors Burton Abrams and Russell Settle of the University of Delaware argue that it did.

The authors begin by presenting two hypotheses on the purpose of regulation—that regulation is supplied in response to public demand to correct "inefficient or inequitable market practices" (the public-interest theory), or that it is sought by individuals, groups, or industries as a means of serving their own interests (the economic theory). They apply these two theories to the Federal Election Campaign Act Amendments of 1974 that provided for optional public financing of presidential campaigns. The public-interest theory is rejected because it attributes the inauguration of public financing to the belief that presidential campaigns are becoming more and more expensive (and increasingly susceptible to corruption), whereas "relative campaign expenditures have, for the most part, declined during the last 70 or 80 years." Turning to the economic theory, they attempt to demonstrate that it is a more reasonable explanation for this important regulatory change. Their thesis is that a Congress controlled by the Democratic party could be expected to produce a campaign-financing law that would benefit the Democratic party.

The authors point out that Republican candidates for the presidency have historically outspent Democratic candidates (except in 1912 and 1948). Their quantitative analysis shows that, holding all other factors equal, spending is positively correlated with the number of votes received. They then note, for example, that the 1974 campaign act amendments were favored in the Senate by more than 80 percent of the Democrats but only 42 percent of the Republicans and in the House by 98.6 percent of the Democrats but only 75.1 percent of the Republicans.

Inasmuch as Republican spending for presidential campaigns in the period 1900–1972 averaged 63.5 percent of total spending on these campaigns, and inasmuch as spending and the number of votes received are correlated, the public funding requirement of equal expenditures by Democratic and Republican nominees leads Abrams and Settle to conclude not only that the law was passed by Democrats to benefit Democrats, but that that goal was fulfilled. They attribute Carter's victory in 1976 to the amendments to the Federal Election Campaign Act, observing "that a Republican president signed into law legislation which seemingly led to his own party's defeat. . . ."

Predatory Pricing: A Redefinition

"Predatory Pricing: A Strategic and Welfare Analysis" by Oliver E. Williamson, in *Yale Law Journal*, December 1977, pp. 284-340.

Predatory pricing—an attempt to monopolize —is forbidden by three federal laws. Oliver E. Williamson of the University of Pennsylvania here argues that since the concept of predatory pricing involves current behavior to achieve a future purpose, it is unsuited to static economic models because they do not take into account those aspects. He notes, however, "a remarkable degree of consensus" in recent court opinions in favor of using cost to determine when pricing is predatory, probably a result of the works of Philip Areeda-Donald Turner and of Richard Posner. Both use static economic analysis (which assumes no basic changes over time in the system studied). Indeed, the Department

of Justice has recently dropped two antitrust cases on the grounds that predatory pricing—which it defined as pricing below marginal or average variable costs (the Areeda-Turner definition)—could not be proved.

"Allegations of predatory pricing are easy to level but difficult to evaluate," Williamson writes, in part because predatory pricing may be directed at discouraging prospective rivals. Moreover, workable criteria are needed for distinguishing between predatory pricing and merely competitive pricing which will eliminate inefficiency. "An appreciation for the long-run efficiency benefits of competition is essential if the uncertainty that surrounds the law on predatory pricing is to be removed and useful rules are to be developed," says the author. Marginal cost pricing is advocated by Areeda-Turner and Posner because it promotes efficiency. Their analysis is criticized by Williamson on the grounds that, unlike his proposed rules, it fails to take account of temporary marginal cost pricing for strategic purposes.

His analysis is limited to those firms that have an incentive to exclude or eliminate existing or potential rivals (which leaves out firms in highly competitive industries), and concentrates in particular on the response of dominant firms and collusive oligopoly industries to new entrants. Williamson defines dominant firms as those with 60 percent of a market that is difficult to enter, and collusive oligopolies as a market in which firms "are able to maintain an effective concurrence of market action."

In this study, three possible rules for restraining dominant firm behavior after a new rival firm enters a market are tested. The first, the "output restriction rule" (favored by Williamson), says that after entry the dominant firm cannot increase output above the trend-adjusted pre-entry level. The "marginal cost rule" (favored by Areeda-Turner) allows the dominant firm to increase output after the entry of a new firm if the price does not fall below short-run marginal cost, and the "average cost rule" permits output to increase if the price exceeds short-run average cost. The author argues that an output rule would be easier to enforce than a marginal cost rule because of the great difficulty in measuring short-run marginal cost: indeed, "a marginal cost test would be a defendant's paradise."

The three predatory pricing rules are next evaluated for their effect on social welfare before and after entry, with the author concluding that both the short-run marginal cost and short-run average cost rules are inferior to the output restriction rule in pre-entry welfare. Total post-entry supply is identical under all three rules, which means that post-entry welfare differences turn on cost differences. The entrant's costs of supply are identical under all three rules, which means that cost differentials depend on the costs of supply for the dominant firm. These turn out to be less for the output restriction rule than for the others. Williamson also argues that it is easier for potential entrants to predict dominant firm behavior with the output restriction rule than with the cost-based rules, because the latter allow greater latitude and, therefore, greater uncertainty.

There may also be predatory pricing among established rivals. Price-cutting can occur (1) in loose oligopolies, (2) in industries still in the early stages of development, and (3) by firms attempting to enter a new market, and in *each* of these situations, these are special problems. For the first, output restriction rules are irrelevant because firms have little incentive to use strategic behavior, so Williamson suggests an average total cost test, except for the special case of declining industries where the Areeda-Turner test (an average variable cost test) is suitable. (This is the "only case for which the Areeda and Turner tests and those proposed here" agree.) For the second, he proposes a double test—that the price-cutting firm be required to show that its prices cover prospective costs for the short-run future and that, in order to bring a case, the competing firm demonstate its ability to achieve the cost levels of the price-cutting firm. For the third ("promotional pricing"), Williamson suggests a very limited short-run exemption from predatory pricing rules, because new entrants can in fact be engaged in predatory pricing.

The article concludes with a critique of the predatory pricing rules proposed by Areeda and Turner. Williamson points out that their rules do not distinguish between predatory pricing in response to new entry and among established firms. Further, the rules rely on marginal cost pricing tests, admittedly difficult to estimate. He urges, instead, his output restriction rules for dominant firms facing new entry. Such firms should be governed over the short- and

intermediate-run by the "business as usual" rule that quantity produced by the dominant firm after new entry cannot exceed the trend-adjusted pre-entry quantity and that in the long run (after the rule has expired) prices must recover full (total) costs. Williamson argues that his "output restriction rule provides a practicable way to sort out meritorious from protectionist claims of predatory behavior."

The FTC: Competition and Stability

Economic Regulation and the Public Interest: The Federal Trade Commission in Theory and Practice by Alan Stone (Ithaca, N.Y.: Cornell University Press, 1977), 314 pp.

Professor Alan Stone, a political scientist at the University of Houston, begins this study of the Federal Trade Commission with the thesis that the agency's actions, as well as its successes and failures, stem mainly from "a central contradiction" in the conduct of both business and government under capitalism—"the fundamental contradiction between stability and competition." Because of this conflict, the impact of economic regulation is often nullified or, if the regulation is strictly enforced, its cost to the public is often too great.

In Part One, Stone (who served as an attorney with the FTC from 1960 to 1968) reviews the legislative history of each statute administered by the FTC and considers how effectively these statutes have been enforced. Beginning with the Federal Trade Commission Act and the Clayton Antitrust Act, he uses case studies to illustrate the contradictory content of the FTC Act's proscription against "unfair" competition and to trace the way the agency has both promoted and restricted competition in entering its "cease and desist" orders against individual transgressors. In Stone's view, the cease and desist order itself is an ineffective enforcement tool, reflecting as it does "an uneasy compromise" between the need for stability and the need to compete. Its use has led to pressures for more efficient sanctions and, therefore, to increased resistance by business. The FTC, says Stone, will always be subject to criticism so long as its major sanction continues to be the cease and desist order, under which "a transgressor is entitled to a free bite of the apple before the courts can impose any meaningful monetary penalty; so deterrence is minimal." Nor is he optimistic about the efficacy of recent enforcement powers granted to the FTC.

In Part Two, Stone continues his consideration of how the FTC has both promoted and restricted competition, focusing on issues dealing with exclusionary and collusive practices. He examines two periods—1956–1964 and 1973–1975—the first having been described by agency critics as typical of the FTC's bad performance, the second as a time when the agency sought to reform itself and became more public interest oriented. In both periods, says Stone, the cases reflect (1) "the fundamental contradiction between competition and stability inherent in the statute" and (2) the FTC's dependence, in most cases, upon the business community for information about possible violations.

The most important amendment to the Clayton Act was the Robinson-Patman Act of 1936, which, says Stone, "stands unambiguously on the side of stability and against vigorous competition." The fact that the FTC, which tried hard for many years to enforce Robinson-Patman, has—because of considerable criticism—virtually ceased to enforce it prompts Stone to conclude two things. The first is that the statute's impact on the U.S. economy has been almost nil. (This is also the conclusion of his examination of FTC antimerger policy.) The second is that, if the statute is to be abrogated, this should not be done by "administrative whim" and that the future will probably bring another period of vigorous enforcement.

The FTC's growing role in the area of consumer protection is detailed in Part Three. Included are analyses of the way the commission uses its original mandate to prevent unfair competition in fighting deceptive advertising and of the Wheeler-Lea Act of 1938 (which applied criminal provisions to the advertising of drugs that could lead to bodily harm). Other sections deal with the four labeling acts: The Wool Act of 1939, the Fur Act of 1951, the Flammable Fabrics Act of 1953, and the Fiber Act of 1958. Characterizing these statutes as attempts to lessen competition by imposing standards that would help consumers, Stone argues that they have also aided producers. The FTC's administration of all but the Flammable Fabrics Act

has had little impact on consumers' buying habits, and the same is generally true of three newer laws passed in response to the growing consumer movement: the Fair Packaging Act, the Consumer Credit Protection Act, and the Magnuson-Moss Warranty FTC Improvement Act. These laws marginally aid consumers, he says, but fall short of consumerists' goals. Moreover, each "inhibits unacceptable forms of competition, yet is sufficiently flexible to permit some competition to remain in the problem area." This leads Stone to wonder, in pondering the possibility of there being a defect in the nature of regulation, whether the notion that regulation will help consumers is equivalent, in Milton Friedman's image, "to an expectation that cats will bark."

The FTC has failed to satisfy anyone, says Stone, the reasons for this being built-in delay, inadequate money expended, the use of the private litigation system as a model, and ineffective sanctions. Moreover, on the whole, regulation often leads to market distortions very costly to the consumer. Thus, this kind of regulation, although a response to serious problems created by the market, is not and cannot be an "effective instrument for promotion of public values." This leads Stone to conclude that public ownership of industry within a democratic framework deserves serious study.

The Value of a Life

"How Much Should We Spend to Save a Life?" by Steven Rhoads, in *The Public Interest*, Spring 1978, pp. 74-92.

Professor Steven Rhoads of the University of Virginia asks, "Can't we think sensibly about lifesaving programs without trying to put a dollar value on human life?" The article first surveys benefit-cost approaches to valuing life, concentrating on "willingness-to-pay" (WTP) and "discounted-future-earnings" (DFE) and their applications. "The victory of the DFE approach within the government has been . . . complete." This approach means that one starts with the average age at which death or disease occurs and calculates what future income would have been, given a normal life term. This figure is then discounted (a dollar today is worth more than a future dollar because the former can be invested), and the result is the value of life for the average member of the group in question. The Department of Health, Education and Welfare, the Federal Aviation Administration, and the Office of Science and Technology have used this straight DFE method. Among the problems of DFE are the facts that it yields a much higher figure for men's lives than for women's (men earn so much more) and that it seems to represent a "crude materialism" devoid of such considerations as pain and grief.

The WTP approach tries to determine preferences based on the willingness of individuals to pay for reduction in risk. WTP is calculated by obtaining a figure that represents the amount those who are affected by a government program are willing to pay for this benefit. The aggregate figure is then divided by the number of lives saved, and this amount is assumed to be what could justifiably be spent to save a life under the program. The difficulty lies, Rhoads points out, in making the original calculation. Three serious studies have used polling or job market decisions as their basis, with conflicting results. Still when these results are compared with the value of life figures obtained by DFE, it appears that the latter (ranging from $100,000 to over $400,000) are much too low.

Are the principles of benefit-cost analysis a "sufficient guide for public policy on life-saving programs?" A different approach is to ask, Who should benefit from scarce exotic lifesaving therapy? The answer has been either that preference should be given to the most deserving (defined to consider age, number of dependents, and future potential, among other criteria) or that all should be treated equally. Rhoads urges the use of economic analysis along with "political judgment," which includes a willingness to distinguish "between things that some people desire and things that are truly important."

The article concludes with a prediction that we will never see value-of-life issues debated openly as are other kinds of public policy issues. This is a good thing, in Rhoads's opinion, because society should never publicly place a "value on human life." Rather, legislators should affirm the pricelessness of human life, by saving a whole category of people (such as those suffering from kidney failure), because

those values that depend on the sanctity of life are constantly being undermined.

The Other Side of Advertising

The Political Economy of Advertising, edited by David G. Tuerck (Washington, D.C.: American Enterprise Institute, 1978), 217 pp.

"Political" or "public" advertising can refer to advertising by governments and political parties. It can also refer to advertising by private organizations in response to government requirements and incentives or for the purpose of deterring additional government regulation. This volume brings together eight papers from an AEI conference that examined the growing political role of advertising in public policy.

—Charles Clotfelter of the University of Maryland provides a classification of public advertising, describes the functions performed by such advertising, and estimates its total cost at $650 million in 1974.

—Murray L. Weidenbaum and Linda L. Rockwood of Washington University (St. Louis) take a broader view of public advertising, one that includes private-sector advertising in response to government promotion or subsidy. They examine the effects on private decision-making of a number of government activities, specifically, government procurement programs, revenue-sharing requirements, election campaign subsidies, affirmative action policies, postal subsidies, and tax laws. The "carrot and stick" nature of much government funding of the private sector may have, they conclude, adverse effects on the freedom to disseminate information.

—David Tuerck, editor of the volume and former director of AEI's Center for Research on Advertising, explores existing economic theories to see if they can identify which advertisements should be provided by government and which should be regulated. Tuerck asks whether economic theory can provide a set of standards for this purpose, concludes that such a use of economic theory is inappropriate, and cautions against attempting to apply it to public policy areas it is ill-equipped to consider.

—Richard Wagner of Virginia Polytechnic Institute analyzes political advertising according to two theories of democratic government. One theory, which stresses similarities between government and the market, views political advertising (like private-sector advertising) as a cost-effective means of disseminating information about candidates and programs (products and services) so that voters (consumers) can choose intelligently. The other, which stresses the monopolistic nature of democratic government, views political advertising as a means of promoting voter approval of the current majority and thus further expanding the public sector. Wagner notes that publicly supported political advertising fits in with the second theory.

—Allen M. Wyse and David G. Davies of Duke University analyze the function of advertising by government bureaucracies. The bureaucrat can attempt to influence the "consumer-voter's" expectations by providing information about the bureaucratic policy. Wyse and Davies find that bureaucracies produce information beyond the point at which marginal benefits equal marginal costs. The availability of free "public service" media time to the bureaucrat distorts relative prices in such a way as to discourage the use of "scientific/product" information and to encourage the use of less reliable "exposure" information.

—Robert J. Staaf of VPI examines the subsidies and restrictions that have been applied to political campaign financing in the post-Watergate era, and analyzes campaign contributions as payments for political favors. Agreeing with Wagner that the role of information is fundamentally different in political decision-making from what it is in commercial decision-making, he notes that the voter, unlike the consumer, "receives no benefit from possessing unique information since decisions are not made at the margin, but rather according to majority rule." In Staaf's view, campaign financing laws have replaced individual decisions with collective decisions and therefore represent a loss of individual freedom.

—Albert J. Martin of Florida International University discusses the cost-effectiveness of public advertising for recruiting military personnel. For this purpose he describes a Defense Department study that finds paid radio advertising likely to be useful in recruitment efforts.

—James H. S. Pierson, an economist at AT&T, analyzes sales-related and institutional

advertising by public utilities, showing how public utility advertising is affected by regulators' decisions to disallow advertising expenditures for rate-making purposes. He concludes by raising some of the difficult questions about the role of regulation in changing or maintaining public attitudes: for example, should the public pay (via utility rates) for advertising designed to alter its own views? Should regulators be making these kinds of decisions?

Does Freight Rate Regulation Really Matter?

"Allocation in Surface Freight Transportation: Does Rate Regulation Matter?" by Richard C. Levin, in *Bell Journal of Economics*, vol. 9 (Spring 1978), pp. 18-45.

The prevailing view of economists that rate deregulation would improve surface freight transportation is reflected in both the Railroad Revitalization Reform Act of 1976 and the administration's transportation policy. But Yale economist Richard Levin doubts that the savings would be as large as claimed. He argues here that, for two reasons, economists seriously overestimate social costs of freight regulation (including the misallocation of traffic from rail to truck). In making their calculations they concentrate on differences in shipment size and average transit time, and they assume "that all shippers have identical preferences" for the various features of freight transport.

Levin constructs a model to measure the effects of certain characteristics of shippers, shipments, and kinds of transport chosen on the market shares of truck, boxcar, and piggyback (trailer on flatcar) transport. His study is limited to shipments of manufactured commodities and uses data for forty-two such commodities.

Taking reported revenues for boxcar and piggyback traffic, Levin calculates the average rates for both and, since equivalent data are not available for trucks, he assumes that truck rates are competitive. Calculations of transit time are based on a 1968 study which uses Defense Department data showing that truck transport is faster up to a distance of 915 miles, piggyback faster than truck beyond 915 miles, and rail faster than truck beyond 2,430 miles. Though the variation in transport time is less for trucks than for rail, the differences are not so great as had previously been thought. Finally, in order to compute the welfare loss from rate regulation, it is necessary to use the ICC cost formulas (although they have been criticized for employing inappropriate techniques to divide railroad costs into fixed and variable components).

Based on these data, Levin finds that a 2 to 7 percent increase in market share results for any of the three kinds of transport when transit time is reduced by one day. This compares to the increase in market share of only 2.5 to 3.5 percent that results from a drop in freight rates of $1.00/ton. Levin concludes that time is considerably more important to shippers than price. Other advantages of truck service not measured in this study (including such things as a better loss-and-damage record, faster pickup, and greater flexibility in meeting shippers' needs) are large enough so that truck rates could be 12 percent higher than boxcar rates before trucks and boxcars would split the market evenly.

One problem with his model, Professor Levin notes, is that it assumes, contrary to fact, that shipment size is determined prior to a shipper's choosing whether to use rail, piggyback, or truck. But the data are not available to measure how the choice of transport influences shipment size.

With all this in hand, Levin substitutes marginal costs for current boxcar and piggyback rates in the regression equations of his model of shippers' preferences, in order to calculate the loss to society stemming from regulation of surface freight rates. This yields the market share that would correspond to an efficient allocation in each transport market.

For the commodities in his sample, his estimates of the overall cost of rate regulation range from 0.3 to 0.75 percent of total freight revenue—which, assuming these commodities are representative, works out to $53 million to $135 million for 1972. This figure compares with widely cited previous estimates by other economists ranging from $1 to $3 billion.

Professor Levin points out that his results clearly indicate that the benefits to be expected from deregulation of freight rates are small.

But he suggests some reasons for caution before concluding that rate deregulation is undesirable. For example, his estimates apply only to manufactured products, and the case may be quite different for agricultural products. Also the indirect social costs of rate regulation may be much greater than the costs he measures. Therefore, if rate regulation leads to excess service competition and "limits the diffusion of new low cost technology," it causes higher transportation costs.

Levin urges that policy-makers, instead of expecting the largest social costs to disappear with rate deregulation, should adopt measures aimed directly at cost reduction—eliminating operating restrictions and allowing mergers. He expresses the hope that this study will show other economists that they should not focus narrowly on rate distortion as the "principal ailment of the transportation system."

ICC Regulation of Household Movers

"The Monopoly Value of Household-Goods Carrier Operating Certificates" by Denis A. Breen, in *Journal of Law and Economics*, April 1977, pp. 153-185.

Denis A. Breen of Washington State University applies the "producer-protection" theory of regulation to the household-goods carrier industry, in order to determine the value to the carriers of ICC regulation. According to this theory, if regulation creates monopoly profits by protecting producers from competition, those profits should be reflected in the sale value of operating certificates. (For this argument as applied generally to common-carrier trucking, see the article by Milton Kafoglis in *Regulation*, September/October 1977.)

In 1971 the household-goods moving industry included 2,400 carriers involved in interstate commerce and therefore subject to ICC regulation. Twenty-five nationwide movers accounted for about two-thirds of the industry's revenues of $910 million. The rest of the industry was composed of 120 regional movers and about 2,200 small local movers.

One outstanding characteristic of the market behavior of the industry is its pricing policy. Almost all firms are members of either the Household Goods Carriers Bureau or the Movers and Warehousemen's Association of America. These rate bureaus, operating with antitrust immunity, publish moving rates for their members, the result being a complete uniformity of rates in any given market area.

Since 1935 the trucking industry, including the household-goods movers, has been subject to regulation by the ICC. In addition to controlling entry into the industry, the ICC sets minimum rates ("the commission workload is dominated by minimum as opposed to maximum rates cases"), prohibits "discriminatory" rates, and often suspends rate cuts pending ICC review.

In spite of the generally protective nature of ICC regulation, certain recent developments limit the extent of monopoly profits in the household-goods carriers industry. For example, consumer pressure has led to reforms such as "interlining" (transferring shipments from one carrier to another, a practice that allows movers with limited operating authority to compete with those holding long-haul authority) and prohibition of peak and off-peak pricing (movers must charge the same rate the year round, rather than charging higher rates for busier periods). Nevertheless, Breen argues, the effect of ICC regulation is to create monopoly gains for the industry and these gains are "capitalized into the market value of transferable operating certificates."

Using actual sales prices between 1970 and 1973 for seventy-one radial certificates (which authorize operations from a fixed base or hub to points within a prescribed area), Professor Breen constructs a model, using multiple regression analysis, to estimate the sale value of similar certificates. His results show that certificate prices are positively related to population and the length of haul, and negatively related to competition. In other words, much of the extreme variation in value among smaller radial certificates (a range of about $500 to $26,000) is due to these three factors.

On the theory that the bulk of the monopoly profits that regulation creates for household movers would be reflected in the value of the largest certificates—nationwide nonradial (operating rights between any two points in a prescribed area)—Breen estimates the sale value of such certificates. Using the amount

spent by carriers to acquire enough existing certificates to achieve nationwide status, he arrives at a preliminary figure of $361,857 for the average sum actually paid by a sample of seven nationwide carriers. Because none of the carriers has ever purchased complete nonradial rights to operate in the continental United States, this figure understates the true value. Breen adjusts for this by simulating the purchase of authority to operate in the Western states (more expensive, and in most cases, incomplete in the existing authority of the seven), arriving at a figure of $728,857. This is then assumed to be the value of each of the fourteen nationwide nonradial certificates that actually authorize service in all forty-eight states.

Based on these figures, the total monopoly value for the industry would be $39.4 million (the fourteen nonradial plus the 2,807 other certificates). But a further correction is necessary because, although the fourteen nationwide movers alone account for 52 percent of industry revenue, in these computations they only represent 26.9 percent of the monopoly value. The corrected estimate of the monopoly value of operating certificates for the entire industry is thus $60.8 million.

Breen recommends that "serious consideration" be given to deregulating household-goods carriers. Abolishing entry controls, rate regulations, and antitrust immunity would probably result in lower rates (because of increased competition or potential entry into the industry), while ending discriminatory rates and eliminating inefficient firms.

Public Disclosure at the Fed

Federal Reserve Policies and Public Disclosure edited by Richard D. Erb (Washington, D.C.: American Enterprise Institute, 1978), 108 pp.

In February 1977 AEI sponsored a conference on the impact of more open decision-making within the Federal Reserve System. This volume includes three conference papers (plus commentaries) covering the effects of public policy disclosure on (1) domestic monetary policy, (2) international monetary policy, and (3) bank supervision and regulation. In addition, an introduction by editor Richard Erb, AEI resident fellow, reviews the effect upon the Federal Reserve System's traditional independence of "government in the sunshine" and "freedom of information" legislation, coupled with more aggressive congressional oversight.

In Part One, Benjamin M. Friedman of Harvard University argues that the economic arguments for and against greater disclosure of the Open Market Committee's monetary policy deliberations "are relatively weak on either side, especially if the Committee were to be permitted some limited discretion to withhold potentially damaging specific items of information." The disclosure issue is primarily political, he says, and, because it is, revelations about the committee's objectives, forecasts, and fiscal policy views would probably fuel public debate and greatly increase the Federal Reserve's political vulnerability. In comments on the paper, Sherman J. Maisel, a former governor of the Federal Reserve, suggests that public disclosure of the Open Market Committee's discussions would produce weaker committee decisions and greater rigidity within the system; Robert Z. Aliber of the University of Chicago, on the other hand, believes that the case for complete disclosure on monetary policy is "compelling."

In Part Two, economist A. James Meigs at Claremont Men's College points out that the boundary between domestic and international monetary policy is unclear because responsibility for the latter is distributed among so many diverse government agencies and is so poorly defined. Meigs argues for an "announced steady-money-growth rule" along with floating exchange rates in order to reduce uncertainty about domestic monetary policies and thereby help to stabilize foreign exchange rates. The problem of stabilizing exchange rates, he says, "is that market expectations are strongly influenced by changes in the U.S. money supply." Commenting on Meigs's paper, William Poole of Brown University and Roger E. Shields, deputy assistant secretary of the Treasury for research, argue that Meigs did not draw an adequate distinction between disclosure per se and other policies designed to produce exchange rate stability.

In Part Three, Neil B. Murphy of the University of Maine notes that, as a result of requirements for increased disclosure by individual banks, "there is not much information

about a bank's financial condition . . . that is not currently available." He reports that the Securities and Exchange Commission has now become a major bank regulator through monitoring the accounting methods employed, but that empirical studies have shown little adverse effect of disclosure thus far. In their comments, Lewis Mandell of the Comptroller of the Currency's Analysis Office and Dudley D. Johnson, vice president of Citibank, agree that one unstated reason for increased reporting requirements is the desire to attain social goals.

In the opinion of the book's editor, Richard Erb, Murphy's paper and Mandell's and Johnson's commentaries suggest that as a result of greater disclosure of individual bank data, the investment community is better able to evaluate the performance of individual banks and thus to discipline errant bank managements by influencing stock values. Therefore, we may eventually discover that one consequence of greater disclosure will be a reduction in the supervisory requirements of the bank regulators.

Burdening the Democratic Process

Proposals for Government Credit Allocation by Leland B. Yeager, with a foreword by Yale Brozen (Washington, D.C.: American Enterprise Institute, 1977), 75 pp.

Yale Brozen of the University of Chicago points out in his foreword to this study that federal borrowing and federally assisted borrowing claim a growing proportion of available credit —36 percent today compared to 13 percent in 1960. Increased federal activity in the credit markets has made funds scarcer for other borrowers, forcing up interest rates and leading to demands for more government assistance. "Thus, credit-allocation programs beget more such programs."

In this analysis, one of a series of AEI evaluative studies in economic policy, Professor Leland Yeager of the University of Virginia examines the proposals and arguments for selective credit controls, the effectiveness of the controls, and their costs (potential and actual) to the U.S. economic system. He concludes that enactment of government credit allocation programs to the extent favored by their proponents would place a burden on the democratic process that would threaten to overwhelm it.

As credit tightens and interest rates rise, pressures increase for government allocation of credit to assist what are perceived to be high-priority social programs affecting small business, farming, housing, and state and local governments. According to Yeager, there is as yet "no systematic and coherent case" for the efficaciousness of credit controls as an instrument of public policy. Nevertheless, he points out, the ambitious intent of such proposals is clear: "to steer credit toward some uses and users and away from others by issuing commands and prohibitions or offering positive and negative inducements to lenders and perhaps to borrowers also."

In appraising this central idea, Yeager criticizes such arguments for controls as their use to eliminate discrimination against the poor, to help perfect the free market system of credit allocation, to further consumption of "merit wants," or to help redistribute income. Noting that credit controls have proliferated in part through the extensive use of various loopholes to circumvent them, he argues that the evasion of "negative" controls is assisted by the "fungibility" of money and credit. This enables individuals and corporations to shift funds ostensibly borrowed for one purpose to a completely different purpose. Loopholes, in turn, lead to additional controls, causing costs to mount in an effort to force compliance. Selective credit controls, therefore, "tend to undercut the profit orientation and market character of financial markets and of the whole economic system. . . . They nudge the economy in the direction of central planning."

Yeager believes that the ultimate consequences of this would be to overburden the democratic process, "for effective economic planning cannot be accomplished democratically." Furthermore, increased government credit allocation would foster a vast multiplication of government activities that would defy monitoring either by the people's elected representatives or by the people themselves. Among the dangers he foresees are broader grounds for lawsuits and a wider scope for court decisions creating unexpected legal precedents.