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THE CHALLENGES OF THE NEW DECADE

by

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I had occasion in the last week of 1979 to be walking one delightful evening down the streets of Paris with a very old French friend and in thinking about the dawning decade, we started to consider which decades in the Twentieth Century began under equally difficult circumstances. Our conclusion was that -- apart from 1930, when the Great Crash had already occurred, and 1940, when World War II had begun -- 1980 announces the most awesome, uncertain, treacherous, bewildering and troublesome decade.

It is troublesome for a number of reasons, but one seems particularly thereatening -- a lack of shared national values. As John Gardner once explained:

"A nation is held together by shared values enabling them to rise above conflicts and divisions. This is what gives a nation its tone, its fiber, its moral style, its capacity to endure. And in a sense, it is that absence of shared values that is probably the most critical issue facing our society."

All of the institutions and forces in our society -- whether they be rich, whether they be poor, whatever be their color, whatever be their motivation -- have similar societal responsibilities. First, they have an obligation to participate in shaping the values of the society. Secondly, they have the duty to act consistently with these values. However, today's society lacks such a consensus on values, and even more basically, it lacks the trust in our institutions necessary to

the process of reaching a consensus. As a result, the increasing tendency is for people to hold on to what they have -- for indeed, as many perceive it, they have nothing to be for.

In this context, the traditional principle of "let us reason together" has become critically more important. This Nation needs institutions which are mutually independent, resourceful and effective. Each must contribute towards establishing the common values necessary to building a societal consensus, which in turn is a prerequisite to building our Nation's future together.

So long as the economy of this Country was growing, there was enough growth individually and institutionally, so that -- perhaps in our largess -- we could share a portion of it with others. We could, in effect, feed, fuel and support the fight for social justice and other worthwhile causes that make this society different and separate from others in the world. We could not only fund social programs, but we could encourage, inflame and enhance social expectations and social aspirations.

Now we cannot economically afford that approach. We lack the economic growth that makes it possible. Rather, at the present time, we tend to focus on what we can afford among government programs. To a degree, we cannibalize some social

programs to maintain others. But, again, we are hampered by the lack of consensus, i.e., the lack of agreement about how to make the trade-off judgments necessary in a society dealing with scarce resources. We need to build a consensus that makes such decisionmaking acceptable to all facets of society.

Even if we had an effective process by which to reason together and decide the allocation of resources among public purposes, that would not, in itself, resolve our present societal dilemma. A threshold question must be faced regarding how much we can allocate towards fulfilling the social purposes of our society at this point in time. How much do we need, as a society, to reinvest in the economic underpinnings of the society to assure that it continues in the future to provide that same wellspring? My conclusion, at this point, is that we are eating our seed corn -- we are not reinvesting enough in the future of the economy of this Country to assure the future social aspirations that we could achieve.

In principle, it is not government that creates wealth. Rather, it is the business community that produces the economic wealth which creates the jobs and provides the other resources that then make so much else possible. We must recognize that an essential tension must exist between, on the

one side, the private sector's economic efficiency -- with all the good and bad connotations of that term -- and, on the other side, our national ideals of equality, equity and egalitarianism. The tension of these two forces creates the uniqueness of this Country and this society. Both are valid. Both have their place. Both must be healthy. Both must be mutually supportive of each other and yet mutually independent of each other to thrive. But, this traditional equilibrium is threatened because this Nation is unconsciously moving from being a political economy to being an economic polity. My thesis tonight is that this process should proceed only by conscious judgment rather than inadvertence.

My favorite speech of John Gardner discusses the need for society to have loving critics. That is an interesting juxtaposition. It has a good feeling because that is what is missing so much from contemporary society -- not merely criticism, not merely blind defense and love, but balanced, loving criticism. Tonight, I am going to talk to you in relation both to business and government -- not as a defender of either. I have been outspoken and critical of both. But they both have their virtues as well.

There are aspects of the business world that need improving and I have addressed myself to many of them. Business needs

to be more accountable. Business needs to be timely in terms of tracking, assessing and understanding where the needs, desires and aspirations of this Country and its social values are taking it. Business needs to recognize better than it does that, as a general proposition, our society does not understand economics and never will; and that it does not understand our economic system and will not understand any other. Thus, business cannot deal with its current challenges by defending itself in terms of economic systems. Rather, it must face them on the meeting ground of moral values. However, business is, as I said last night, becoming increasingly sensitive to these problems. I am concerned that we not destroy the business sector in the process of trying to improve it. We should not try to ideologically purify it because that will not be achieved in business any more than it will anyplace else. Competition in the business sector is to be encouraged as in all walks. I recognize that the thin line between competition and greed will be overstepped in the business community as it is sometimes overstepped in other aspects of our society. However, a greed-free society cannot exist. If society destroys greed, in the process it cannot avoid destroying the competition necessary for venturesomeness. Therefore, the characterization of business as having a quality of greed is acceptable. And, to the extent that tolerating a greedy

fringe element is necessary to make our system work, I will defend that tolerance. It is the price we pay in each of our institutions for those positive things it brings to us.

In my judgment, from the business standpoint, America's economic vitality is its greatest asset. It is the product of the creative spirit of a free and industrious people and of an economic system that gives opportunity for private initiative. I consider it the foundation of our prosperity. I am convinced that our economic and political freedoms are not coincident -- they are inexorably intertwined. As Justice William O. Douglas, in his book "Go East, Young Man," said of his views in the 1930s, when he was at the SEC:

"Preservation of free enterprise seemed to me to be the best . . . Free enterprise is not guaranteed by the Constitution as are free speech and free press. But the First Amendment and free enterprise seemed to me to go hand-in-hand in a practical way."

However, no activity can flourish if the public takes a dim view of it over the longer term, and no activity can continue unaltered if either public apathy or distrust become active antagonism. That is a problem that business faces today. If government and business are adversaries, then the future of business is in doubt, for government, as the only social institution that can legally enforce its will, must win any struggle if the issue is reduced to one of power. Dan Yankelovich reminded us last night of the erosion of confidence

in business and of the public skepticism over whether business strikes a fair balance between profits and the public interest. Business can take little comfort from the fact that other institutions in our society are also losing public support.

Yet, looking at the contemporary political, social and economic environment, institutions, in order to be effective -- whether they be in business or government -- have to have a measure of authority. To do their jobs, they need a measure of public deference -- including the leeway to make mistakes. Without it, they cannot function. Without it, they spend all of their time protecting themselves. If the institution is in business, that means losing operating efficiency and, thus, the economy becomes less competitive. That is the environment that we are creating, and if we want it, we need to be prepared to pay the price. But there is no moral law or public law that can prevent institutions from making mistakes, although we sometimes behave as though the opposite is true. The result is that we are so complicating decision-making, both in the public sector and the private sector, that an administered society is gradually -- but certainly -- coming to pass without a conscious choice on our part that that is the way we want it to be.

I think the problems of the difficulty of decisionmaking in the private sector is clear. The difficulty of decisionmaking in the public sector may be less clear. Some laudable purposes -- such as John Gardner's goal of opening up government -- have had the collateral consequence of making it increasingly more difficult for government to engage in effective and timely decisionmaking. For example, we have effectively bureaucratized and delayed the decisionmaking process -- and decisionmaking courage -- of both the private and the public sectors by allowing an increasingly litigious society, and by the other risks that we have imposed upon decisionmaking.

In the 1930s, Adolph Berle wrote his book entitled "Power Without Property." At that time, he pointed out -- in an analysis that still stands the test of time -- the separation that has developed between corporate ownership and corporate management. In effect, he made the points that corporate ownership now was neutralized, sterilized and separated from corporate management; and that corporate management had power without property, and, in a sense, without responsibility to anyone. This is a theme that continues to recur, and indeed a theme that I have been addressing under the rubric of "corporate accountability" for some two years. However, Berle, in his book written in 1954 entitled "The Twentieth Century Capitalist Revolution" characterized large American

corporations as "essentially revolutionary instruments in Twentieth Century capitalism." He called their development ". . . a revolution calling for risk-taking, dreambuilding and bold ventures into new technologies." Berle, of course, was talking about the inventors, marketers, production geniuses and financial managers who together created the most dynamic, economic instrument in the history of the world out of the needs of the marketplace.

As Dan Yankelovich tells us, the populus began to believe in the New Society and in what was being built by the economic and business communities in the '50s and '60s. They became convinced that a totally new and totally unprecedented economy had been achieved upon which we could all depend and build. But not only did the public believe in this vision, but business also believed in it. Many of those in the business community became convinced that they had found the ultimate wisdom, that they could do no wrong, that all their ventures would always turn out well. For example, we had portfolio managers in their thirties -- who had not experienced the Depression -- who were convinced that they had all the wisdom in the world in terms of picking securities for investment. We all learned to ride bikes without using our hands. The ease of the process went to our heads and the assumption that

it would continue caused many to throw caution and good judgment to the wind and to make moves that were later regretted.

Politicians believed in this vision too. And, in the '60s, they expected to provide us with both guns and butter. Economists, obviously, believed it because they thought that they were the ones who had solved the economic cycle. Of course, as Dan Yankelovich pointed out, society believed it too.

Then came the collapse of the late '60s. My view of that collapse, and the hostility towards business that it generated, is that it reflects an anger at the tender of the well just at the time when we were beginning to depend on the well and all of its wonderful life-giving qualities.

Let me suggest to you, however, that the period of the '50s and '60s was not the norm, but the sport -- that the period of the '70s, '80s, and beyond will be much more similar to the periods we knew before World War II. Heretofore, we were enjoying the honeymoon period of post-World War II, where we experienced the uniqueness of having geared ourselves up through all of the inventiveness and all that we brought forth by World War II. This included the transistor, nuclear power, the jet engine and all those things which we could then convert to civilian uses; the buying power that was pent up during World War II; and, indeed, the opportunity that we had to rebuild the Free World. With the benefit of hindsight, it

seems clear that those forces were spent by the middle or late '60s.

At the same time that this was going on until sometime in the late 1950s, the regulatory process of the federal government focused on markets and on rates -- on what one might call "regulatory guidelines" and "traffic rules." Then we began to move into the new regulatory mode which was interventionist in affecting the conditions under which goods and services are produced and the physical characteristics of goods. I use the term "interventionist" in a neutral manner. I just say it is different. But, it does impact much more directly on the way companies are run and the way products are produced; and, in many ways, it has a much more direct impact on the economy of the Country.

In recent years, we have begun to talk about a third form of regulation which is even more directly interventional. This regulation is exemplified by OSHA, ERISA, equal employment opportunity, truth-in-packaging, and truth-in-lending. I think this new regulation springs from two concepts. One is a concern for the accountability of the corporation -- the accountability for its power, either real or perceived. Second, there is a sense that, rather than individually addressing each way in which the American corporate community is perceived

as not living up to the changing values and mores of our society, we should determine who sits on boards of directors and thus directly impact the process by which American business is run. Advocates of this process believe that we can then catch particular problems embryonically before they occur; because, obviously, directors who are more sympathetic to the values of the society would prevent the problems from becoming significant in the first place. My own sense is that we have never learned how to legislate morality, and we would not be able to do so in this vein either.

I have a very real concern about a federal presence in determining the composition or standards of performance in American board rooms. I think the American board today -- indeed, the business community -- is already too conservative and too risk-averse. I do not think we need to create even more risk aversion. Rather, I think we need to reestablish a greater opportunity for risk-taking, and a greater tolerance for mistakes than we are now prepared to accept.

The dynamic that we are creating -- if we can analogize it to a concept in the scientific field -- is a concept loosely called entropy, which refers to a situation where complexity is carried to such lengths that all the forces and counterforces are checked and balanced into a state of equilibrium, and, thus,

nothing happens. I would say to you that the proportion of the energy and resources of this society that are now being devoted to maintaining a kind of social homeostasis is growing exponentially and that we are neutralizing ourselves.

If I put all these together and I extrapolate from it, I -- although a bureaucrat -- would say to you that the urge to pass new, corrective laws and to erect new administrative procedures is one that never subsides by itself. No matter how many legislative policies are developed, even more will be produced. That is the nature of man -- whether he is in government, in the private sector, or in the academy. Man is productive. In government as elsewhere, we do not -- sometimes unfortunately -- reward people for doing nothing. So, entropy advances while confidence recedes, and an increasing frustration with government cultivates the demogoguery which is the greatest danger for a democratic society.

What do we need today for business to deal with this problem? I would say for business, government and society as a whole, we need a new level of understanding about their respective roles. And, just as business must recognize that it exerts its substantial economic, sociological, physical, political and psychological impact on society and must involve -- and be accountable to -- many facets of the public, government must recognize that business is the wealth-producing

mechanism of the society which gives viability to social aspirations and achievements. Additionally, business needs an environment which is supportive and conducive to delivering its contribution. While it is abundantly clear that what is good for General Motors is not necessarily good for the Country, over the long term, what is good for business and the society are inexorably intertwined and interdependent.

I think a basic thing business needs, even though I am not optimistic that it will occur, is a better understanding of profits. To me, "profit" is a misnomer. When you look at it in strict accounting terms, it ought to have one more factor subtracted from it: "profit-by-definition." Profit needs to be reduced by what is paid to suppliers of capital in the forms of dividends -- for it is as important and legitimate an expense to pay dividends to attract and retain capital as it is, for example, to pay wages to attract and retain labor.

Profit is the return for the risk that is taken, and investment is a product of the assessment of risk. Profit is that resource available to be reinvested in a business to replace obsolete plants, to enhance productivity, to invest in research and development, to develop new products, to create new jobs and to improve the quality of life in this society. By any measure, looking at industry in general,

although recognizing that particular exceptions exist, the profit being retained after payment of dividends to shareholders -- dividends which are not at all out of context or inappropriate in today's inflationary society -- is inadequate to do the job that American industry needs to do.

Again, I say to you, we are eating the seed corn of our economic system. Possibly, that is the course society wants to take. But, let's make that a conscious, societal decision, so that we might all be prepared for its consequences. My major concern is we do not know the ramifications of our actions, and in many cases, we do not seem to care. But, I still have great confidence in the American people to make intelligent decisions if they know the facts.

What are business' concerns today? Business is concerned with inflation. It is concerned with regulation, but not only with the extent to which regulation itself is a cost which consumes capital. Much more importantly, it is concerned with the extent to which regulation itself provides a form of uncertainty, i.e., the uncertainty of how regulation is going to be changed next and the difficulty in meeting its new requirements. Business is concerned, and I think appropriately, with a degree of distrust that is manifested and articulated in fashions that are, in my judgment, more unbecoming to the

articulator than to the object of the criticism. For example, I am concerned with the pejorative of the "three martini lunch." I have worked in the business community for 25 years, and, during that time, only once did I have lunch with a person who had three martinis. Now, maybe my experience is exceptional, but the three martini lunch is not a sufficiently general enough phenomenon to be considered a business characteristic -- particularly by political leadership.

It is this attitude which, if I were in the business community today, would contribute to my reluctance to invest. Given the unpredictability of regulatory and political actions, I would not be able to predict with any degree of certainty the kind of return that I would need to justify my investment. And as a result, the return I would have to project would be an unachievable return -- particularly when one considers the cost of money today.

Although I understand the reluctance to invest that presently characterizes American business, this reluctance leads to practices of which I am critical. I do not endorse the takeover movement and its rearranging of corporate assets. I would much rather see business invest dollars in a new plant. Nevertheless, I fully understand why they are doing it that way -- because it is more certain and cheaper to acquire than to build,

because of the unpredictability of regulatory requirements and litigation, and the increasing cost of money.

At the same time, the business community's own attitudes exacerbate these problems. For example, it focuses too much on short-term performance. It rewards short-term performance in too many ways -- in terms of incentive compensation, in terms of stock options, in terms of how quarter-to-quarter earnings performance is compared. It puts too much of an incentive on otherwise responsible businessmen to cut corners on the belief -- which is not without merit -- that, if an executive does not produce this year's earnings, he may not be here next year to be able to worry about some of the longer-term business concerns. Certainly, we saw some ramifications of this pressure in the sensitive payments area which the Commission investigated at great length. I think part of that uncertainty and part of the focus on the short term is also the responsibility of the boards of directors who should be more focused on the longer-term issues. However, I recognize that it is difficult to maintain a long-term perspective absent the kind of confidence in the future that, in my judgment, the business community needs.

Another troubling aspect which I believe has to be changed if the role of government is to be changed, is that

the business community does not have effective ways to address, resolve and discipline conflicts within its own ranks. I believe that the business community needs to do more in providing its own sense of leadership and its own sense of discipline. There are many individuals who have been involved in major corporate acts of malfeasance who should be drummed out of the executive core -- but who are not. Business does not clean its own house. It does not criticize itself. Indeed, if we are to avoid the necessity for government to preempt many of these areas of concern, the only effective way to do it is through a more effective system of self-regulation. It is a system that can be effective. Many of the aspects of the SEC's activities are based on self-regulatory principles with governmental oversight.

Now let's turn to the roles and responsibilities of government. I think the most important responsibility of government is its obligation to consider the problem that it, itself, is creating. But the discipline for government to engage in this process is not compelling. Government is disorganized and lacks coordinative leadership. It really has no effective check and balance. Rather, it engages in what I call "action stopping" -- not "action generating" -- which often reminds me of Will Rogers' famous comment: "Be thankful

that you are not getting all the government that you are paying for." Government has poor performance measures, even less oversight and accountability than does business, and the vested interests in its system are much more difficult -- in fact, may well be impossible -- to reach.

What should the role of government be? I believe that there must be a greater degree of self-regulation and an ability on the part of the government to recognize that there is a distinction between, on the one hand, things that should change, and on the other, things that government should try to change by regulation or law. That is a distinction that neither Congress, nor the White House, nor the administrative agencies generally make. So, while I would say that government should do less, in some respects, government has to do a lot more. Government has to, at least, lead us in the dialogue and in the process by which we set priorities and allocate our limited resources. And it must do this not only in terms of allocating governmental resources, but also in allocating between the private sector and government. That includes not only the federal budget, but increasingly also the new mechanisms by which government imposes costs on the private sector that do not appear in the federal budget. You cannot look at the federal budget and say that it is \$600 billion and determine

that to be the cost of the federal government. Increasingly, these costs are costs which do not appear in the federal budget, such as direct costs imposed on the private sector and off-budget financing with government guarantees.

At the same time that I talk about limiting the government's role, these are pressing problems that must be faced. And, they raise basic questions of priorities and allocations. For example, we need money for mass transit. However, an attractive mass transit system will draw traffic away from the railroads that are already marginal in their economics. So we will cut out rail lines. Do we need railroads as a national priority? Do we need a rail system to move coal as well as other freight? I happen to think that we do -- but how do we achieve these seemingly conflicting goals?

The automobile industry is another example. I can explain how Chrysler made its own bed and how General Motors said for years that they just sell the public what it wants -- while the public was out buying Volkswagons and Datsuns. But what is the societal significance? We have an auto industry. Do we need an auto industry in this Country? How do we determine that? How do we do something about it? There is a role of government in this problem, which is not something that can be addressed by a public consensus.

Energy is another example. After seven years, we still do not have an energy policy. I am concerned.

We are concerned about inflation. We are beginning to hear advocacy for protectionism. Can trade-dependent economies avoid falling into protectionism? Protectionism is superficially attractive. It will bring business and government together as do other survival-oriented stress situations such as war and post-war reconstruction. Who would support a politician who opposes protectionism? What are the arguments against it? In our political process, who are the advocates? Where do the rewards come from for a politician who opposes protectionism? It is almost like being for triage.

Nonetheless, I work with an agency that I think is one of the best in the federal government. And, I must say that I am getting very disturbed, with all my concern about the federal government, with much of the attitude that I hear coming from opportunistic politicians and self-appointed wisemen about the federal government -- and, indeed, the federal bureaucrat.

If we continue to bad-mouth the public service and make it a more difficult career -- that means economically, socially and in prestige -- if we hound it, if we show only contempt for it -- we will break the spirit of people who, in their way, are trying very hard to do a competent and conscientious job. All we will succeed in doing is to drive out the best of our young

people from the public service with the result, not of less government, but with third-rate quality government.

It is nonsense to talk glibly about simplifying government as evidenced by the patchwork solutions in a number of current "regulatory reform" proposals -- without looking more fundamentally at what we expect of government -- and particularly at the role of Congress in enacting legislation and in conducting responsible oversight. Unless we look fundamentally at that, we are talking nonsense. The policies and the decisionmaking of government will have to be very good if we are to get through this century in an increasingly interdependent world.

We no longer hold all the high cards, and we are vulnerable. Government and the public service are not the whole answer, but they are part of it. Instead of demeaning it, we ought to look to its strengths, sort out its weaknesses, assess what we expect of it, and above all, enhance its legitimacy and its pride of service.

Thank you.