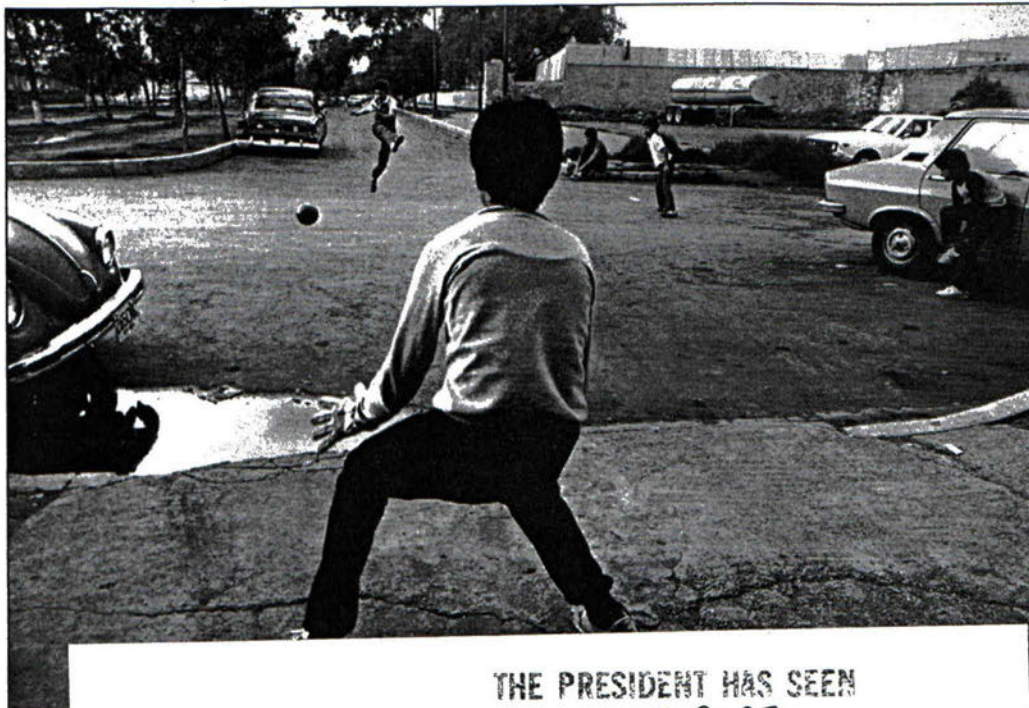


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BUSINESS IN LATIN AMERICA



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...in the United States only since last January. They are traded on the New York Stock Exchange in the form of American Depositary Receipts, or ADRs (which confer ownership of shares deposited in a bank, normally in the issuer's home country). Mavesa may be small, but it is part of a new Latin American corporate elite that is growing fast. It was one of 40 companies from the region that gave presentations to this year's annual Latin American equities conference organised by J.P. Morgan, an American investment bank. When the conference was first held four years ago, it attracted only 15 companies and 40 investors. This year the number of investors attending had risen to 400.

In 1991 Cemex, a Mexican cement company, became the first Latin American firm to issue ADRs. Since then, more than 150 others have followed, raising a total of more than \$40 billion through new share issues in international markets (see chart next page). The path has not been smooth; foreign

this autumn, the region as a whole will return its best economic performance for a generation this year, with growth of around 4.5% and inflation below 10%. True, it may not last. Growth in Brazil will slow sharply next year as the government has had to face the facts of an overvalued currency and a large and persistent fiscal deficit—still worryingly familiar maladies in Latin America. Elsewhere in the region, economic prospects depend partly on the continued availability of cheap finance. Yet such problems appear more manageable than those now facing South-East Asia.

A decade of liberal reform in Latin America has delivered healthier economic fundamentals and speeded up the underlying rate of economic growth by two percentage points, according to research by the Inter-American Development Bank. Inflation has been tamed by broadly sound fiscal and monetary policies; protectionist barriers to imports have been largely dismantled; economic nationalism

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BUSINESS IN LATIN AMERICA

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Back on the pitch

IN A smart hotel in mid-town Manhattan, Ruben Morales, a manager from Mavesa, a Venezuelan consumer-goods maker, is talking to 50 Wall Street analysts. His company, he explains, wants to buy some food businesses in the Andean countries, and is stepping up its exports to Colombia and Peru. The firm's margarine, mayonnaise and laundry-soap brands already dominate their home market. Mavesa is hardly a Unilever. Its sales last year were below \$300m, and profits were disappointing. Yet the analysts are listening attentively.

Not long ago this scene would have been unthinkable. Mavesa's shares have been available to retail investors in the United States only since last January. They are traded on the New York Stock Exchange in the form of American Depositary Receipts, or ADRs (which confer ownership of shares deposited in a bank, normally in the issuer's home country). Mavesa may be small, but it is part of a new Latin American corporate elite that is growing fast. It was one of 40 companies from the region that gave presentations to this year's annual Latin American equities conference organised by J.P. Morgan, an American investment bank. When the conference was first held four years ago, it attracted only 15 companies and 40 investors. This year the number of investors attending had risen to 400.

In 1991 Cemex, a Mexican cement company, became the first Latin American firm to issue ADRs. Since then, more than 150 others have followed, raising a total of more than \$40 billion through new share issues in international markets (see chart next page). The path has not been smooth; foreign

investors briefly retreated from Latin America after Mexico's currency collapse three years ago, and recent stockmarket wobbles have caused several planned issues to be postponed. But such setbacks seem likely to be temporary. Carlos Hernandez, head of investment banking for Latin America at J.P. Morgan, reckons that new share issues by the region's firms will total about \$6 billion next year and over \$8 billion in 1999.

Reaping the fruits of reform

That partly reflects the strength of Latin America's economies. Despite the bout of Asian flu it caught this autumn, the region as a whole will return its best economic performance for a generation this year, with growth of around 4.5% and inflation below 10%. True, it may not last. Growth in Brazil will slow sharply next year as the government has had to face the facts of an overvalued currency and a large and persistent fiscal deficit—still worryingly familiar maladies in Latin America. Elsewhere in the region, economic prospects depend partly on the continued availability of cheap finance. Yet such problems appear more manageable than those now facing South-East Asia.

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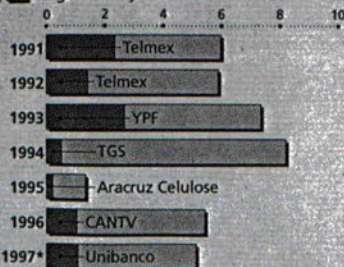
A decade of liberal reform has brought great improvements in Latin America's economies, notwithstanding the current jitters. But, asks Michael Reid, are the region's firms ready to take on the world?

SURVEY BUSINESS IN LATIN AMERICA

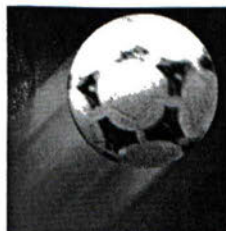
To market

International share issues by Latin American firms, \$bn

■ largest each year



Source: J.P. Morgan *To September (Full-year estimate: \$6.2bn)



Argentina, Mexico and Peru. More recently, they have gathered pace in Brazil, but moved more slowly in Colombia and Venezuela. In a huge and diverse region with 470m people and an annual income of around \$1.7 trillion, the reforms are only one factor among many that are shaping companies' behaviour. For example, Brazilian firms, with a domestic market amounting to two-fifths of the entire Latin American economy, have different worries from their counterparts in much smaller Chile, which rely heavily on exports. Mexico, with the United States as a next-door neighbour, and as a member of the North American Free Trade Agreement (NAFTA), is in a different class.

In the 1970s and 1980s, a combination of high inflation and protected markets produced perverse incentives for companies in Latin America. Costs or quality mattered less than the speed with which firms got goods into the shops and invested the revenue in financial markets. A deeply unequal income distribution inhibited the growth of consumer markets, so firms had little incentive to develop branding and marketing skills. Profits had much more to do with government regulation than with business efficiency. Closeness to government officials—who often determined prices, wages, tariffs and interest rates as well as access to imported inputs and credit—was far more important than closeness to the customer. Inflation meant the most important sort of engineering was financial. "If the industrial director proposed a project that would cut costs by 14% in two years he wasn't listened to, because the finance director would say that if his

has been replaced by enthusiasm for foreign investment; and hundreds of state-owned companies have been wound up or sold to the private sector. A web of regional trade agreements, such as Mercosur (made up of Argentina, Brazil, Paraguay and Uruguay, with Chile and Bolivia as associate members) has prompted a sharp increase in trade within the region, especially in manufactured goods.

However, those liberal reforms are neither uniform nor complete. Among the larger economies, they have gone furthest in Chile, Argentina,

scheme wasn't adopted the firm would lose its capital in six months," says Antonio Barros de Castro, of Brazil's Federal University of Rio de Janeiro.

As a result, many Latin American firms made shoddy, expensive goods, and could export only with the help of government subsidies or undervalued currencies. In a study of four industries in the five largest Latin American economies, published in 1994, McKinsey, a management consultancy found that labour productivity was well below that in developed countries. For example, in telecommunications it was only 60% of the level in the United States, and in steel, processed food and retail banking it was less than 40%. However, the study also found that where industries had been privatised or deregulated, as in steel, Latin American productivity was rising much faster than in, say, retail banking, which remained protected. McKinsey concluded that the main reason for low productivity was poor management and organisation rather than skills shortages.

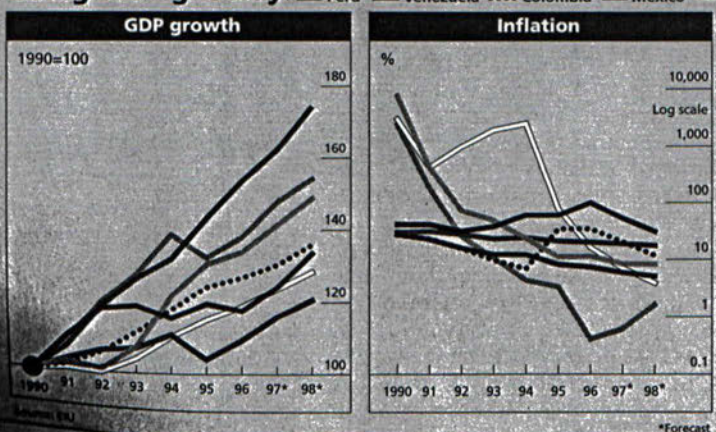
The hurricane of competition

Thanks to the reforms, for the first time in a generation most Latin American firms are operating in a business environment which could be described as normal. For many firms, that has turned out to be a chastening experience. Freer trade, foreign investment and market deregulation have exposed them to the kind of competition that their counterparts in rich countries take for granted. The effect has been magnified because Latin America's reform have coincided with a period of rapid technological change and of globalisation—a steep increase in international flows of goods and money. Multinational companies have decided that a reformer Latin America may offer the kind of swift market growth they had previously associated with Asia, and have rushed to invest in the region.

All these changes have sent a hurricane howling through locally owned businesses. Many of the weaker firms have been forced to shut down or sell out to foreign rivals. All have struggled to overcome competitive disadvantages, especially inflated costs and outdated technology. Many of the region's firms, especially the larger ones, have responded to competition by restructuring. That is bearing fruit in the shape of bigger profits. Despite Brazil's slowdown, earnings per share of publicly quoted Latin American firms will grow by at least 15% next year, in dollar terms, reckons Robert Pelosky of Morgan Stanley Dean Witter Discover, a stockbroker.

In many countries, labour productivity is rising sharply. In Brazil, for example, it has almost doubled since 1990 after standing still for the previous five years. Some of this reflects outsourcing of non-essential activities. But the first effect of restructuring has often been higher unemployment: in São Paulo, Latin America's largest industrial centre, manufacturing employment has fallen by 14% (around 300,000) since June 1994, when a new currency tamed Brazil's chronic inflation. Many of those laid off lack skills. They drift into service businesses, which are less exposed to competition, into the low-productivity "informal economy" of unregistered businesses, joining the one in three Latin Americans officially classed as living in poverty, and underlining the need for faster growth.

Going the right way



Plenty of things could still go wrong. Because many Latin Americans have yet to feel much benefit from free-market reform, there is a question-mark over its political sustainability. Its pace is slowing even though much remains undone. In many countries, tax systems, labour laws and commercial codes remain archaic. In some places violence and security fears are becoming a big obstacle to doing business, especially for foreigners. Colombia is the worst case, but not the only one. Kidnapping is an ever-present risk.

More immediately, the turbulence in the region's stockmarkets in recent months, and the doubling of short-term interest rates in Brazil in late October, are reminders that economic stability cannot be taken for granted. If nothing else, these events will push up the cost of capital for Latin American firms for a while.

Because of the region's long history of financial volatility, only three Latin American countries (Chile, Colombia and Uruguay) have an "investment grade" (low-risk) international credit rating. But for much of the past two years, Latin American firms have enjoyed the luxury of a world awash with capital and indifferent to risk. Many have taken advantage of this either to issue equity or, more often, to raise debt. Latin American firms raised \$11 billion in bonds in 1996 and a further \$10.3 billion in the first half of 1997. During those 18 months they also raised \$25.4 billion through syndicated loans from international banks, according to Anne Milne, of the New York office of ING Barings, an investment bank.

In good times, Latin America's blue-chip borrowers pay only slightly more (say 1-3% a year) in the capital markets than their rich-country rivals, a cost they should be able to offset by cheaper labour or other competitive advantages. But there are two problems. First, Latin American firms cannot escape their countries' volatility. At the peak in 1995, yields on Latin American corporate bonds rose to 15 percentage points more than the rate on United States Treasury bonds. Second, and even more serious, only larger firms can tap international capital markets. The mass of medium-sized firms are stuck with expensive and underdeveloped financial mar-

kets in which bank loans, if they are available at all, can cost 50% or more, as they currently do in Brazil.

All of this makes life more difficult for Latin American businesses. Yet the biggest problem of all for the region's managers and entrepreneurs, this survey will argue, is that they are now having to measure themselves against the world's best. That is so even if they do not leave home, though many will. Relying on obscure niches in a protected domestic market that were once profitable is no longer an option.

Small and wizened

To understand why Latin American business now needs a global outlook, start by considering the following paradox. Capitalism has a much longer history in Latin America than in many parts of Asia. Yet whereas the largest Asian firms have grown swiftly to become household names across the world, their Latin American counterparts have remained almost unknown outside their own region, or even their own country. Only seven Latin American firms appeared in this year's list of the world's 500 largest companies published by *Fortune* magazine, and none of these was a non-financial firm in the private sector.

The reason why Latin American firms are generally small is not that they are young. Paul Holden, of the Enterprise Research Institute for Latin America, a think-tank based in Washington, DC, points out that in Mexico the average age of firms is 30 years and in Uruguay 35 years, compared with only about 15 years in the United States. Luciano Martins, a Brazilian sociologist, found that six of Brazil's 20 largest private business groups perished between 1988 and 1990, a period in which the country was hit successively by hyperinflation, sequestration of bank deposits by the government, and an abrupt dismantling of import controls. But all of the survivors were still there in 1995. Starting new businesses in Latin America is hard, but once established, firms prove extraordinarily resilient.

What, then, is stunting their growth? The first place to look for explanations is that archetypal Latin American business, the loose, family-owned conglomerate.



Inside story

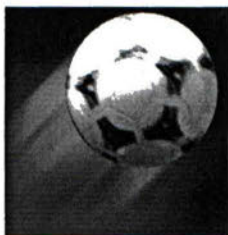
DESPITE all the changes of the past decade, family-controlled conglomerates continue to dominate Latin America's private sector. They account for more than two-thirds of the 33 largest private business groups in Brazil, according to Mr Martins's study. The biggest business groups in Mexico, Argentina and Colombia, too, are diverse family-owned empires. More surprisingly, perhaps, the same is true in Chile, where a much-touted private pension system has created a large domestic capital market, and ownership of some of the country's privatised businesses is widely dispersed. But two Chilean family groups—the Luksic family's, and Anacleto Angelini's—continue to outstrip such companies in size as well as diversity.

Family businesses in Latin America are strong

partly because the extended family itself is strong. "There is no clear-cut separation between family interest and business interest, or between the person of the owner and the legal personality of the firm," argue Larissa Adler Lomnitz and Marisol Perez Lizaure, two anthropologists, in a vivid account of a prominent Mexican business dynasty*. But family duty and social status may clash with the aim of maximising profits. Thus, the "Gomez" family, as the authors called their subject, lost its position in the top echelon of Mexican business in the 1970s because it refused to consolidate its firms in a professionally managed holding company, and failed

Family firms still rule

* "A Mexican Elite Family 1820-1980", by Larissa Adler Lomnitz and Marisol Perez Lizaure. Princeton University Press, 1987



to seek foreign allies: "Foreign businessmen are rarely flexible on matters such as providing jobs for relatives, handling expense accounts, arranging for convenient work schedules, allowing for cash withdrawals and safeguarding personal prestige."

Such entrepreneurs were willing collaborators in the development of protectionist and interventionist states in Latin America from the 1930s onwards. Reluctant to stump up large sums of capital themselves, they were happy for the state to invest in capital-intensive industries such as steel, and to become a source of subsidised credit for local private businesses. It was only when debt and inflation became overwhelming and the private sector started being crowded out of the credit market that many Latin American entrepreneurs became grudging converts to economic liberalism.

The logic of the family business and of protectionism combined to discourage growth through specialisation, which might have led such firms to conquer foreign markets and become multinationals in their own right. Instead, family firms typically diversified, both horizontally and vertically. That eased the succession problems which strike such firms every generation or so. Diversification was also a response to foreign-exchange controls or import barriers which made breaking out of the home market difficult or impossible; and it provided a defence against the region's extreme economic and political volatility.

In such an environment, family businesses have great advantages over publicly owned companies. They can take decisions more quickly and be more flexible. But even they cannot escape the effects of volatility, which hinders the company's growth and development by encouraging the systematic avoidance of risk. Winston Fritsch, of the Rio de Janeiro office of Dresdner Kleinwort Benson, an investment bank, points out that Brazilian firms tend to have very low levels of debt in relation to their capital because spells of high interest rates have winnowed out most companies with high gearing.

To live outside the law you must be honest

But there is another reason for the strength of the family business, and the corresponding lack of large public companies in Latin America: the weakness of the legal framework. On gaining independence, Latin American countries adopted the French system of civil law, then recently codified by Napoleon. Research by a group of economists from the universities of Harvard and Chicago* has shown that this French civil-law tradition provides markedly less protection for outside minority shareholders and for creditors than either Anglo-Saxon common law or the civil-law systems of Germany and Scandinavia.

This weakness of the legal system has had two main consequences. The first has been to inhibit the development of capital markets in Latin America. For all their ebullience until recently, Latin America's stockmarkets remain small in relation to the size of the region's economies. They also lack

depth: many of the companies listed on the exchanges are unattractive to investors because few of their shares are traded. For example, in the São Paulo stock exchange, the region's largest, trade in the shares of just three companies accounts for up to 75% of the total market.

This creates a vicious circle in which many entrepreneurs prefer not to issue public equity because they think the market will undervalue their firms. That could be about to change—unless equity markets go on crashing. In Brazil, says Claudio Haddad of Banco Garantia, a local investment bank, companies are starting to see the stockmarket as a source of capital. Argentina has around 50 mid-sized companies that have done well in recent years, and might decide to go to the market to finance expansion abroad, according to Daniel Tassan-Din, of the Buenos Aires office of Deutsche Morgan Grenfell, an investment bank. Something similar has already happened in Chile.

Family trust

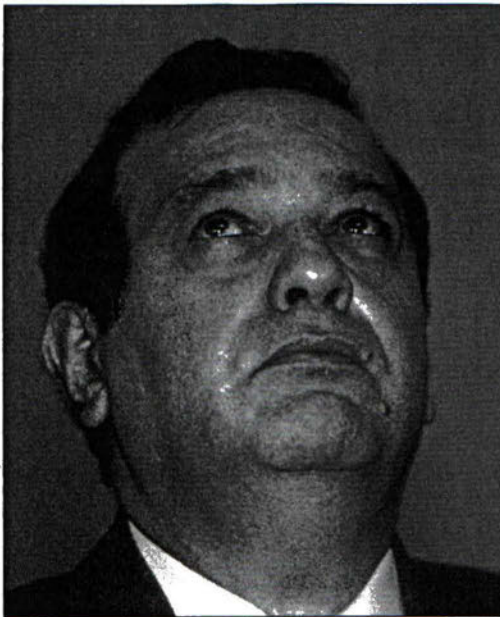
The second consequence of an ineffective legal system is that firms dislike dealing with outsiders because they fear they will not be able to enforce contracts. It is safer to rely on relatives or close friends in whom they can have *confianza*, or trust. This, too, has encouraged diversification and vertical integration in family business empires.

Bosses of Latin American family firms will invariably assert that nowadays their business has professional managers, and they will often be right. This is one of the main ways in which Latin American firms have changed in response to competitive pressures over the past decade or so. For example, Alfa, one of Mexico's largest and most efficient family-controlled conglomerates, has a "strict policy" of obliging family members to demonstrate management competence, says Alfonso Gonzalez, the group's finance director (who is not a family member). When the family patriarch recently retired as chairman, he chose his nephew—who has degrees from Harvard and Stanford—as his successor in preference to his son.

There are some signs that hitherto shapeless family conglomerates are shaping up. One example is Bunge & Born, a group originating in Argentina, based in Brazil and registered in Bermuda, which with sales of \$11 billion last year can claim to be Latin America's largest private-sector firm. In 1991 it called in management consultants and set about transforming itself. It has withdrawn from Europe, got rid of paint, textile, construction and insurance businesses worth a total of \$2 billion, and spent an equal amount on acquiring food businesses. Now it is buying Ceval, a big Brazilian soya and grain firm, in line with its new strategy of specialising in food and agribusiness in the Americas and Asia.

Another example is Grupo Carso, a conglomerate run by Carlos Slim, a buccaneering Mexican stockbroker with good political connections who has specialised in buying undervalued or undermanaged businesses. In a dizzying series of deals over the past two years, Carso has split itself in three: a telecoms outfit with ambitions in multimedia; a retail company to be partially floated; and the rump of the old company with interests ranging from tobacco to mining.

*"Law and Finance", NBER Working Paper 5661, and "Legal Determinants of External Finance", NBER Working Paper 5879, both by Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer and Robert W. Vishny



Lean look for Slim

Yet old habits die hard. The typical Latin American firm remains a hierarchical dictatorship in which information is closely guarded and outsiders regarded with suspicion. Take Chile's Luksic group, part of which is publicly quoted. Its Antofagasta Holdings subsidiary, whose shares are listed in London, has mining and railway businesses, and Quiñenco, listed in Santiago, bundles together banking, beer, telecommunications and spaghetti manufacturing. When your correspondent began an interview with Guillermo Luksic, who runs Quiñenco, by asking about the business logic behind such diversity, he was politely shown the door.

Such secrecy can have serious consequences. Cemex startled the stockmarket when it used the money raised in its first ADR issue to buy a Spanish firm: its prospectus had made no mention of such plans. Other Latin American entrepreneurs have

chosen to raise capital in international equity markets by listing a subsidiary and offering only a minority of its shares. That way they can be sure of keeping control, as well as of protecting the family holding company from the rigours of US GAAP, the accounting standard required by the United States' Securities and Exchange Commission.

In many companies personal and corporate interests are still intertwined. To reassure outside shareholders, Emilio Azcarraga Jean, aged 29, who earlier this year inherited the top job at Televisa, Mexico's media giant, quickly sold his late father's fleet of corporate jets. Their shares may be quoted in New York, and their finance directors may allow Wall Street analysts to pore over the books, but Latin American firms still inhabit a different world from that of the British or American public company. The family patriarch will combine the jobs of chairman and chief executive, which is becoming less common elsewhere.

Partly because they are under-leveraged by world standards, Latin American firms still prefer to raise capital in the form of debt rather than equity. When they do issue equity, it is usually in the form of non-voting preference shares, which do not threaten family control. In Brazil, for example, company law allows a firm to issue two-thirds of its capital in that form. Traditionalists would rather keep outsiders away altogether. In a recent interview with *Veja*, a Brazilian magazine, Antonio Emirio de Moraes, chairman of Votorantim, the country's largest private business empire, said he was contemplating listing his group's shares, but added wistfully: "It's complicated because it means opening up the group's big decisions to shareholders."

If Mr Emirio de Moraes is prepared to consider this horrific possibility, it is because firms such as his need more capital to take advantage of Brazil's privatisation programme. Since October, Votorantim (with partners) has paid a total of \$4.2 billion for two electricity distributors in southern Brazil. Clearly privatisation is changing the priorities of many Latin American businesses.

A very big deal

THE third big change in Latin America's business environment, along with the taming of inflation and the liberalisation of trade, has been the dismantling of the proprietorial state. Latin America has privatised with remarkable speed and on a vast scale. By one count, over the past ten years 279 companies have been sold for a total of \$90 billion in the seven largest Latin American countries (see table 3, next page). Between 1990 and 1995, Latin America accounted for more than half (by value) of all privatisations in the developing world, including Central and Eastern Europe.

And there is more to come. As with other reforms, privatisation's progress around the region has been uneven. Chile and Mexico were the pioneers, followed by Argentina and Peru in the early 1990s. Now Brazil's huge privatisation programme has shifted up several gears. Between 1990 and '96, Brazil sold 73 companies for a total of \$14.9

billion. This year alone, Brazilian officials expect to sell assets worth \$20 billion, including the sale last May of Companhia Vale do Rio Doce (CVRD), the world's largest iron-ore producer, and chunks of the electricity system. Next year privatisation sales could run to \$30 billion (including Telebras, the federal telecommunications holding company).

Most Latin American privatisations were inspired by the need to improve the government's accounts rather than by ideological zeal. The earlier growth in state ownership in Latin America from the 1940s onwards had owed more to Mussolini than to Marx. It was supported by private business (which saw state companies as a source of padded contracts or cheap raw materials) and by the armed forces (which favoured it for reasons of national security), as well as by trade unions and the left. But by the 1980s, inefficient management, political manipulation and, in some cases, corruption had

Privatisation has changed the region's business for good

Adding up

Privatisation sales

	1988		1989		1990		1991		1992		1993		1994		1995		1996		1997		Total	
	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn	No	Value \$bn
Argentina	-	-	-	-	3	1.88	3	1.09	22	6.5	8	4.83	4	0.75	4	0.99	6	0.55	5	4.32	55	20.91
Brazil	1	0.05	1	0.01	1	0.04	4	1.62	15	2.44	7	2.59	22	1.96	8	1.00	16	5.28	21	12.42	96	27.41
Chile	1	0.17	1	0.06	-	-	-	-	-	-	-	-	4	0.19	1	-	2	0.52	-	-	9	0.94
Colombia	-	-	-	-	-	-	1	0.05	-	-	-	-	2	0.67	-	-	3	1.21	2	2.72	8	4.65
Mexico	4	1.92	1	0.14	3	2.31	12	10.91	10	6.39	2	1.22	1	0.55	-	-	1	1.40	1	0.43	35	25.27
Peru	-	-	-	-	-	-	-	-	10	0.21	10	0.34	14	3.08	7	1.04	8	2.16	4	0.22	53	7.05
Venezuela	-	-	-	-	-	-	4	2.06	7	0.01	2	0.03	1	-	3	0.05	5	1.50	1	0.06	23	3.71

Source: Privatisation International

turned many a state enterprise into a liability.

In Argentina, for example, where state-owned companies even at the mid-1980s peak accounted for a relatively small 6.2% of GDP, they managed the improbable feat of making annual losses averaging 5.6% of GDP between 1983 and 1988, according to a study by Andrea Goldstein, an economist at the OECD. In Mexico, at their 1982 peak, 1,155 state companies received transfers and subsidies from the central government equal to 12.7% of GDP, according to Jacques Rogozinski, who as a finance official was involved in privatising many of them during the presidency of Carlos Salinas. As well as huge oil and steel firms, which were symbols of national pride or industrial aspiration, governments also had some less glorious businesses: for two decades Peru's government owned one of Lima's more successful pornographic cinemas, which it had taken over along with an insolvent banking empire.

As might be expected, privatisation has made the private sector bigger, sometimes substantially so. Chile, for example, in its two bouts of privatisation in the mid-1970s and mid-1980s privatised firms with sales equal to more than 13% of GDP. Peru since 1991 has privatised firms with sales equivalent to 11% of GDP.

As a rule, the new owners have turned out to be much better managers than the state. The main exceptions have been in Mexico, where two airlines went into receivership after ill-judged expansion plans went awry, and where 12 of 18 commercial banks sold by the government in 1991-92 had to be taken back. Though most of the blame lay with the collapse of the peso, poor management and fraud by some of the banks' buyers also played a part. But other Mexican firms performed far better in private hands than the state's.

The same has been true in other countries. Consider Brazil's Embraer, the only manufacturer of jet aircraft in Latin America. Founded under a military regime in 1969, it developed a reputation for sound engineering. But nobody much cared about costs or customers, which proved the firm's undoing once a civilian government started to question Embraer's bills. In 1994 Embraer made a loss of \$310m on sales of \$253m. After privatisation in December of that year it started to fight its way back, and should break even this year. Its payroll, having plummeted from a peak of 12,700 in 1990 to a post-privatisation low of 3,600, is swelling again: the company is recruiting 1,100 new workers.

In less sophisticated industries, the increase in productivity after privatisation has come more eas-

ily. Take Brazil's formerly state-owned steel industry, which between 1991 and 1993 was sold as six separate companies, raising a total of \$8.2 billion. In 1990 the industry employed 115,000 people and produced 22.6m tonnes of steel. Last year 65,000 employees produced 25.2m tonnes. The quality and value of production has increased too, thanks to investment in better equipment.

In public utilities, such as telecommunications and electricity companies, the potential benefits of privatisation for both businesses and consumers are even greater. Yet utilities are natural monopolies that require tough, independent and technically sophisticated state regulation if the full benefits of privatisation are to be felt. That is one of the biggest challenges now facing Latin American governments. In their anxiety to extract the largest possible revenues, many of them have sold utilities on terms that favoured investors over consumers.

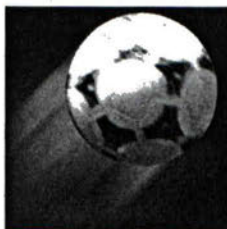
Digital dilemmas

If you take the lift to the top floor of the new headquarters of Chile's CTC telephone company, you not only rise above the Santiago smog and get a heartstopping view of the snow-capped sweep of the Andean cordillera; you also get a sense of what can be achieved by aiming telecoms privatisation and regulation at promoting competition rather than plugging the fiscal deficit.

CTC's origins are in local telephony, where it still has 91% of the Chilean market. But unlike many of its privatised counterparts elsewhere, CTC (in which Spain's Telefonica has a 43.5% stake) has no monopoly. Since 1994 it has been allowed to compete in the market for long-distance calls, where it is now the second-largest operator. But it must give its long-distance competitors access to its local network on equal terms.

Competition in the long-distance market is fierce, and choice easily exercised: customers can select their carrier for any particular call simply by punching in a prefix before dialling. Prices have plummeted, and CTC claims to have become Latin America's most efficient telecoms firm. According to Claudio Garcia, the company's chief executive, it now has 350 lines per employee, compared with 77 when it was privatised in 1987. The Baby Bells in the United States have around 400.

Chile's local telephony charges are fixed by a government regulator every five years, giving telecoms operators a big incentive to cut costs. When charges were last set, in 1994, the price of installing a line was cut by 20%. There are drawbacks



Seismic shifts?

THE three largest companies in Latin America have two things in common: they are all state-owned (despite so much privatisation), and they are all oil companies. Obvious, perhaps. Since the days of the Spanish *conquistadores*, the average Latin American has believed that the ultimate source of wealth is in the ground—and that covetous outsiders are forever conspiring to steal it. Even Chile's Chicago Boys were unable to sell ENAP, the country's monopoly oil trader, or Codelco, its much larger state-owned copper producer. So will state-run oil companies, the ultimate icon of Latin American nationalist pride, remain forever untouchable?

Probably not. Remarkably, in the past few years three of the region's state oil companies have been privatised (in Argentina, Bolivia and, partially, Peru). But even the larger and more venerated firms are having to change to keep pace with rapidly rising domestic demand for energy.

Venezuela's PDVSA, Latin America's largest company, with sales of \$34 billion last year, is streamlining itself by

merging three separate exploration and production businesses. It is planning to double oil output over the ten years to 2006, relying heavily on investment and expertise provided by multinational oil firms. In June it auctioned licences to operate 18 mature and profitable oilfields. Privatisation is not yet on the agenda. But Luis Giusti, PDVSA's modernising chief executive, has suggested floating part of the firm on the stockmarket, and has backed proposals to end its monopoly of petrol retailing and to sell its petrochemical division.

Number three in the hierarchy of Latin American companies is Brazil's Petrobras. It, too, faces change. Petrobras lost its monopoly of production and refining this year. It expects its production nearly to double (to 1.5m barrels per day) by 2000, and plans to sign up to 80 joint ventures with private firms. Private operators could soon be allowed to explore in Brazil, and if President Cardoso is re-elected next year, Petrobras might even be sold some time in the next five years.

That leaves Pemex—number two, with sales of \$29 billion in 1996—as

Latin America's last remaining big oil monopolist. Juan Manuel Romero, Pemex's finance director, justifies this status by explaining that production costs in the shallow waters of the Gulf of Mexico are among the world's lowest (\$2.50 per barrel), so private firms would reap excessive profits. However, such lavish profits could easily be taxed away. Pemex, too, is increasing its capital investment (from \$2.5 billion in 1995 to \$5.2 billion this year) to boost production from 2.7m barrels per day in 1994 to 3.7m barrels per day by 2000.

But even Pemex is more humble than it used to be. It is turning to the private sector to finance up to 30% of its investment spending; and it now admits that its proven reserves are only 43 billion barrels, rather than the 66 billion it used to claim. It also concedes that being a national symbol costs money. "We have identified activities that in other situations wouldn't be part of an oil company," says Mr Romero, referring to Pemex's 10,000-strong medical service and its telecoms system. They reflect "other priorities", he says. Translation: Pemex's managers might prefer to run a much leaner firm, but politicians and public opinion will not let them.

to this system: CTC has no legal obligation to install a line in a given time, and in remote areas can take months over it. However, the spread of mobile phones has made this less of a problem. And CTC has a strong interest in increasing the number of lines in service: according to Pyramid Research, a telecoms consultancy (and part of The Economist Group), line growth in Chile has matched that elsewhere in Latin America (see chart 4).

Across the Andes, Argentina offers a less happy example of telecoms privatisation. The country was divided up between two firms, Telecom (in which Italy's Stet, France Télécom, and Argentina's Perez Companac all have large stakes) and Telefonica (which is operated by the Spanish firm of the same name). Each was granted a six-year monopoly in its area, renewable for three years, as well as joint control of long-distance telephony and the right to operate mobile-phone services. The two firms have made a reasonable job of upgrading Argentina's phone system, which was perhaps the worst in Latin America: businesses used to employ staff solely to hold a telephone handset for hours on end to get a dialling tone. Telecom has invested \$5 billion since 1991. Its network is now 100% digital and includes 4,700 kilometres of fibre-optic cable. But all these improvements come at a price. Although charges have been rising by 2% less than inflation each year, they remain much higher than in countries with more effective competition, particularly for international calls (which are used to subsidise local ones).

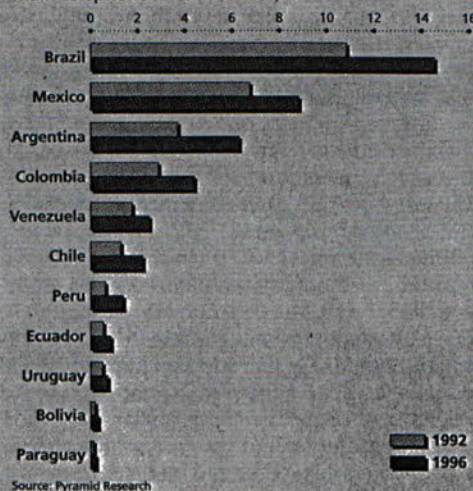
Mexico too granted Telmex's new owners a six-year monopoly when they took over in 1990. Since

January, however, two new entrants—Alestra, run by Alfa and AT&T, and Avantel, made up of MCI and Banamex, a Mexican bank—have won around 25% of the long-distance business in customer ballots held in Mexico's 60 largest cities. That will prompt Telmex to reduce its charges and improve its service. It faces "an enormous cultural change", says Adolfo Cerezo, its finance manager. "A monopoly thinks of the company. A company in a competitive market has to think of the customer."

Brazil looks set to apply some of these lessons. It plans to carve up the state-owned network into a

Keep talking

Main telephone lines in service, m



long-distance company and three local telephony firms, each with its own large geographical area. After their sale, due next year, all these companies will face competition from potential new entrants, and particularly from privately run mobile-telephone services, which will start up in January. With a huge backlog in phone demand, Brazil is already one of the world's fastest-growing cellular-phone markets: the number of subscribers more than quadrupled between 1994 and 1996, and is likely to grow at a compound annual rate of 40% between now and 2001, reckons Pyramid Research.

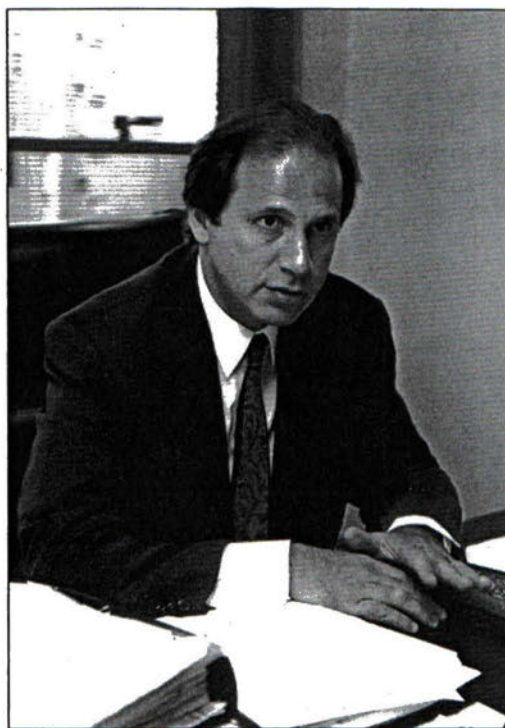
The privatisation of Brazil's telecoms system should reduce the costs of consumer-goods firms by 1-2%, and those of retail banks by 4-5%, reckons Maurizio Mauro, of the São Paulo office of Booz, Allen & Hamilton, a management consultancy. Other parts of the region's infrastructure also need radical overhaul. The World Bank reckons that to grow by 5% a year, Latin America must spend an annual \$60 billion on new infrastructure (leaving to one side the repair bill to keep existing facilities from falling apart). Governments are increasingly turning to private firms to upgrade and manage ports, railways and trunk roads, and in many countries private firms are now running the electricity system. In Brazil, these changes are starting to have a dramatic effect: excluding telecoms, infrastructure projects worth \$190 billion are either already in progress or planned between now and 2000, according to Jose Augusto Marques, of the country's capital-goods industry association. Between 1993 and 1996, spending on such projects was just \$10 billion, he says.

Get rich quick

Despite its benefits, privatisation is not widely popular in Latin America. That is partly because its victims, be they workers who lose their jobs or suppliers who lose padded contracts, are clearly identifiable, whereas its benefits are less immediate and tangible. In Latin America, where governments are rarely trusted and corruption is rife, this unease is aggravated by suspicions, normally unfounded, that privatisations have been rigged to benefit cronies. In deeply unequal societies, privatisation has been seen as a quick way of making the rich even richer by selling precious public assets.

Damagingly, in 1994 *Forbes* magazine disclosed that Mexico had no fewer than 24 dollar billionaires, at least half of whom had benefited either from privatisations or from government concessions under President Salinas. But that wealth was often inflated by a booming stockmarket and an overvalued currency. Three years and a peso devaluation later, their numbers had been thinned to seven (of whom only three run privatised or government-licensed businesses).

Privatisation has more often than not been introduced by authoritarian rulers—not just Chile's General Pinochet, but also Mexico's Mr Salinas, Peru's Alberto Fujimori and even Argentina's Carlos Menem. Both Mr Menem and Mr Fujimori were re-elected for a second term. Perhaps that was why Brazil's President Fernando Henrique Cardoso, who is not an authoritarian, but who is also trying for reelection, seems to have few qualms about privatisation. However, on the only occasion when voters in



Steinbruch thought big

a Latin American country were asked specifically about privatisation—in a referendum on the sale of Uruguay's phone company in 1992—they voted overwhelmingly against. Perhaps they should have thought more carefully. Certainly privatisation has delivered palpable benefits: private management usually succeeds in squeezing costs and improving quality or service in even the best-run state-owned businesses.

Foreign multinationals have come to see privatisations as a way into Latin America, often in alliance with local firms. And the bolder local entrepreneurs have piled in, conscious that this kind of opportunity may never come their way again. Take Benjamin Steinbruch, whose family owns Vicunha, a São Paulo textile firm. Five years ago few people even in Brazil had heard of him. Now, thanks to privatisation, Mr Steinbruch has become his country's most powerful businessman. In 1992, when CSN, Brazil's largest steel maker, was privatised, Vicunha bought 9.1% of the shares. By forming alliances with other investors, such as Brazil's pension funds, Mr Steinbruch became CSN's chairman. In subsequent privatisations, CSN has bought stakes in Light, Rio de Janeiro's electricity distributor, as well as in two railway companies.

But Mr Steinbruch's biggest coup was to assemble an alliance that outbid Mr Emílio de Moraes, of Votorantim, in an auction for CVRD, the Brazilian government's most prized asset. To do so, Mr Steinbruch was prepared to borrow, which his more cautious rival was not. CVRD—which has a cornucopia of mining and industrial interests alongside its core iron-ore and transport businesses—was the only firm in Brazil with the scale to be a global competitor, Mr Steinbruch explains. Size may not be everything, but its lack has been the undoing of many Latin American firms.

Buy, buy, buy

METAL LEVE, a maker of pistons, pins and bearings founded in São Paulo in the 1950s, was in many ways a model of old-fashioned Brazilian industry at its best. At its peak in the 1980s, it employed 7,000 people in three factories and had a return on equity of over 20%. But it owed its profits to Brazil's closed economy, which obliged the car makers to buy their parts locally. When that rule was scrapped in 1990, Brazil's car factories began to buy components worldwide.

Metal Leve's owners had tried hard to anticipate change. They had been exporting to the United States since the 1960s, and in 1989 had invested more than \$25m in building a factory in South Carolina to be able to supply their customers "just-in-time". They had experimented with joint ventures with German partners to gain technology. And they had cut costs, shedding half the workforce.

All to no avail. Sales halved from their peak, to just \$303m in 1995, and Metal Leve began to make heavy losses. "We were efficient, but not efficient enough to compete with huge, volume producers," says Roberto Faldini, a member of one of the six families who owned the firm. To compete, Metal Leve needed to invest \$100m a year, which was beyond its owners' resources. Last year they sold the firm for \$300m to a consortium including Mahle, a big German piston maker with annual sales of \$3 billion, and Cofap, another Brazilian car-parts firm. Less than a year later, Cofap's ageing owner sold a majority stake in his firm to Magneti Marelli, the parts division of Italy's Fiat.

Can't go on like this

The sale of Metal Leve was just one of several hundred takeovers in Brazil last year. And although Brazil has a much larger complement of family-owned, medium-sized manufacturers than other Latin American countries, takeovers are booming throughout the region. The reasons are manifold. Sometimes companies are sold because of succession struggles. Sometimes the current owners are

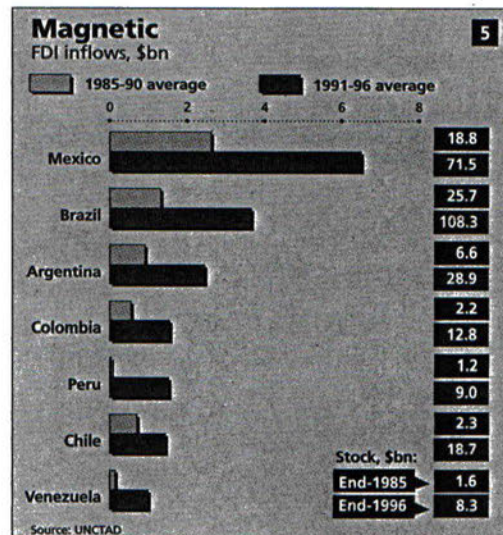
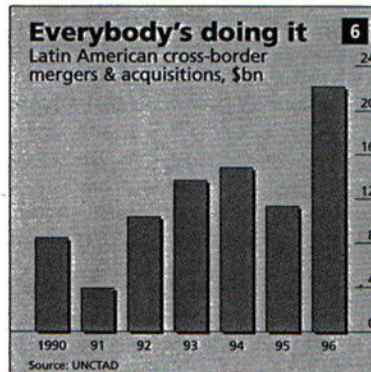
made an offer they cannot refuse. But more often owners sell because they lack the technology or the capital to compete in a more open market.

Increasingly the buyers are foreign, as multinationals decide to enter Latin America or to expand their presence there. Foreign direct investment has boomed, first in Mexico, as outsiders rushed in to take advantage of NAFTA, and then in Argentina and, above all, Brazil, as these countries conquered inflation, and as Mercosur helped to expand the size of the market. Some of this investment is in Latin America's traditional extractive industries, in response to new mining codes in countries such as Peru, Bolivia and Argentina. South America is now the world's single most important region for mining investment, heading for \$14.3 billion this year, more than double the 1995 figure. In manufacturing, it is the prospect of fast-growing domestic markets that attracts incomers. In many industries, acquisition is the easiest way to enter the market: it removes a competitor and offers instant access to a distribution network, local know-how and good connections.

Unlike China or Eastern Europe, Latin America is familiar territory for many multinationals, which have been operating there for up to a century. Until recently they behaved much like their local counterparts, taking advantage of closed markets by charging high prices for goods of poorer quality or more old-fashioned design than they could sell at home. But as trade barriers have fallen, especially in intra-regional trade, many multinationals have brought Latin America into their worldwide strategy. For example, Unilever, as part of its drive to dominate the global ice-cream industry, in October bought Kibon, Brazil's largest ice-cream maker, for \$930m.

Often, the first thing multinationals do to modernise their Latin American operations is knock down the walls that divided identical but separate operations in each country. Switzerland's Nestlé, for example, is spending \$380m on reorganising its food factories throughout Mercosur, siting them where the raw materials are cheapest. Two years ago Royal Dutch/Shell created a new management post in London to co-ordinate purchasing by its operating units throughout Latin America. Over the past three years, IBM "has completely reshaped" the way it operates in Latin America, making each business activity rather than each country a profit centre, according to Elio Catania, the firm's general manager for Latin America. That has meant regionalising many of its activities: for example, the boss of public-sector programmes for Latin America is based in Brazil, the manager for telecoms business in Chile, the education specialist in Mexico city and the banking-systems manager in New York. IBM has also fused 16 back-office operations, one for each country, into a single one for the region.

Foreign companies are on a takeover spree





A dollop of global ice-cream strategy

The most spectacular example of how foreign businesses in Latin America have reshaped themselves has been the car industry. Thanks to NAFTA, Mexico's car industry is now an integral part of that in the United States. Until recently, car makers in South America were selling small volumes of a large range of antiquated, poor-quality and high-priced models. But as the market revived (see chart 7), investment poured in. According to a study by the Economist Intelligence Unit (a sister company of *The Economist*), between 1990 and 1995 foreign car makers invested \$12 billion in Latin America. Between 1995 and 2000, says the study, that figure will rise to \$23.3 billion, of which more than half will be spent in Brazil.

At a crossroads

Or at least that was the plan before Brazil's fiscal squeeze, which includes an increase in the tax on new cars. This will hit the industry hard. Sales will slump next year, and the pace of expansion and modernisation may slow. But much has already been achieved. The recent investment falls into three categories. The first involves new entrants (or returnees) to the market: Renault is building a \$1 billion factory for Mercosur in southern Brazil; Honda has opened a plant in São Paulo state; and Mercedes-Benz will open a car factory (only its second outside Germany) in Brazil next year.

The second kind of investment involves modernising existing plants to bring them closer to world standards. Thus Fiat last year used its Brazilian factory to launch the Palio, a small car with which it plans to break into emerging markets in Asia and Eastern Europe. Ford has re-equipped its plant at São Bernardo, near São Paulo, to make its Fiesta and Ka small cars to European specifications. Volkswagen is using its Mexican factory to launch its new Beetle, a souped-up model adapted from its best-selling Golf and aimed exclusively at the United States market. Last year Volkswagen opened a "modular" truck factory at Resende, near Rio de Janeiro. Originally touted as the most advanced in the world, this plant has been plagued by problems, and a senior company official now dismisses it as "an experiment".

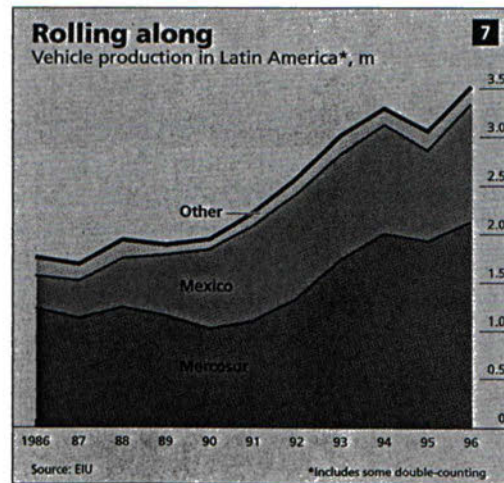


Thirdly, the market leaders are expanding capacity to keep up with demand. For example, General Motors, which runs second to Volkswagen in Latin America, has announced plans for a third assembly plant and two parts factories in Brazil.

The long-term prospects remain bright. Car ownership in Latin America is low, with just one car for every 9.7 people. But the slowdown in Brazil's economy has reinforced fears about overcapacity in Mercosur. Some economists argue that high tariffs (of up to 62%) on imported cars will stimulate over-investment. Whether that happens will depend partly on how quickly those barriers fall, and on whether Mercosur's car plants can raise quality and efficiency enough to develop their export trade. Mexico has already done so through NAFTA: when domestic demand for cars collapsed in 1995, the car makers exported a solid 84% of their output, almost all to the United States.

As the car makers outsource more of their supplies, quality and cost increasingly depend on parts manufacturers. In Brazil, which has Latin America's largest car-parts industry, the squeeze on component makers has been acute. The parts market has been thrown wide open, and the assemblers have introduced new models with worldwide supply contracts. Between 1990 and 1995, employment in Brazil's components industry fell by a quarter, to 214,000, while sales almost doubled. Metal Leve was only one of 18 parts makers to be sold in 1995-96. One of the buyers was Britain's BTR, which is now among Brazil's biggest makers of plastic parts, such as bumpers and dashboards.

This kind of consolidation led by multinationals is becoming the norm in Latin America, in industries from food to retailing to banking. Once it starts, it often proceeds at great speed. In Brazil's white-goods industry, for example, within just two years all three local firms sold out to foreigners which had begun as technological partners with minority shareholdings—Sweden's Electrolux, Germany's Bosch and America's Whirlpool. In some industries, local firms that rebuffed foreign takeover offers ended up accepting them on worse terms a year later, says Alfredo Gutierrez, the head of J.P. Morgan's Brazil office. But at the same time a new breed of local firms is starting to turn international contacts to its own advantage.



Making it in Monterrey

ONLY a hundred miles or so from the Texas border, Monterrey has always considered itself more up-to-date than the rest of Mexico, to say nothing of the rest of Latin America. That was true back in 1890, when Cerveceria Cuauhtemoc opened as one of the region's first modern breweries, and it is true today: NAFTA has forced a city already known for its entrepreneurial drive to prove it all over again, ahead of the rest of Latin America.

But in 1992 Femsa, as the Monterrey brewery is now called, seemed to have gone to sleep, content to be the junior partner in Mexico's cosy beer duopoly behind Modelo, the brewers of Corona. Yet Femsa had unwittingly become a successful exporter. Nimble foreign distributors in Britain and the United States of its Dos Equis and Sol brands recognised their international appeal, and begged the brewery to send them more of the stuff.

Five years later, an unremarkable shed just over the road from the original brewery contains one of Latin America's most efficient manufacturing plants. Computer-controlled presses and stamping machines turn out millions of precision-engineered aluminium can tops and crown corks for beer bottles. A handful of workers, dressed in jeans and green T-shirts, wander around checking the machines; they have no supervisors. A store-room full of \$5m-worth of supplies and spare parts is unlocked and untended; any worker takes anything the job requires, logging the details on a computer.

More with less

In the old days, workers would receive a small bonus simply for turning up on time; now a quarter of their pay is linked to productivity and quality targets. Production has almost doubled since 1991 and quality has improved sharply, while the workforce has fallen from 920 to 385.

Jose Antonio Fernandez, Femsa's chief executive since 1995, has also introduced the firm to economic value added (EVA), a fashionable nostrum developed by Stern Stuart, a management consultancy. According to this, everything a firm does should provide a return at least equal to the cost of capital employed in doing it. Femsa was not measuring up. In 1996, when its cost of capital was 12%, it was making a return of less than half that. Mr Fernandez hopes that next year the return will reach 11%, and has tied managers' salaries to that target.

Femsa's improvement owes much to the company's international contacts. Labatt, a Canadian brewer (now owned by Belgium's Interbrew), bought a 22% stake in Femsa's beer division in 1994, and has taken an active interest in its purchase. Femsa is also one of only two Coca-Cola "anchor bottlers" in Latin America, with franchises for Mexico city and Buenos Aires. Mr Fernandez says Coca-Cola provided him with much informal advice on applying EVA.

But if brewers such as Femsa are thriving, that may be partly thanks to powerful defences against incomers. Laura Meizler, a drinks analyst at Salomon Brothers, an investment bank, points out that

Latin American brewers, unusually, have big soft-drink businesses that strengthen their hold over distribution channels. In the same way, cement firms are protected from foreign competition by the sheer bulk of their product, which makes long-distance transport uneconomic. Mexico's Cemex, another Monterrey firm, has used the cash flow from its dominance of the home market to become a Latin American multinational, with plants in Colombia, Venezuela, Spain and the Philippines.

But Cemex is less of a rarity than it was. Increasingly, Latin American firms are realising that in business, as in Brazilian football, the best form of defence is attack. That usually begins by invading neighbouring markets. Firms that become regional rather than purely domestic learn a lot, especially about making their management more sophisticated and capable, argues Heinz-Peter Elstrodt, of the São Paulo office of McKinsey. "If you want to compete with multinationals, you need to know what it feels like to be one," he says.

The boldest firms have sought to grow internationally through acquisitions. Perhaps the most dramatic example is the oil company YPF, Argentina's largest firm. Between 1982 and 1991, when still state-owned, YPF had made losses totalling \$6 billion. By the time it was privatised in 1993, YPF had been transformed: it had cut its payroll from 51,000 to 6,000, and disposed of assets worth \$2 billion as part of the deregulation of Argentina's oil industry. Yet after privatisation it was still a medium-sized and parochial firm. In 1995 it paid \$750m for Maxxus, a Dallas-based oil and gas firm laden with debt that owned fields in Indonesia, the United States and South America. At the time analysts thought the move was risky, but it paid off. "YPF needed to get out of Argentina to continue growing," says Roberto Monti, who became the firm's chief executive earlier this year.

The purchase has been important both in turning YPF into a regional competitor (although Argen-

The perils of parochialism



Femsa's miracle draught

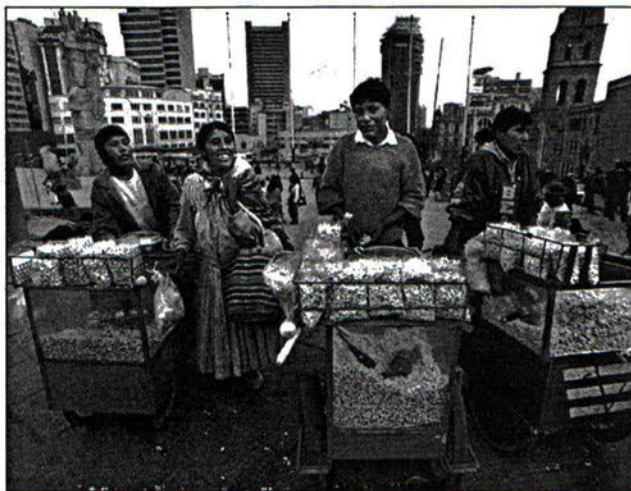
Small is difficult

IN A dreary suburb of Mexico city a young entrepreneur (call him Mr Diaz) sits at a desk full of unpaid bills in an office above an empty garment factory. Mr Diaz's father founded the firm in 1969, with three sewing machines. By 1981, their number had risen to 120, the staff to 200, the annual sales to \$6m, and the business had become Mexico's largest in its line of clothing.

Then began 15 years of turmoil, culminating in the 1994-95 peso devaluation. Mr Diaz has spent the past two-and-a-half years coping with creditors. Now he reckons the worst is behind him. "My company has gone from a medium-sized business to a small one, but it's growing again and it's profitable." He has improved quality, cut product lines and begun exports to the United States. A new, leaner firm is emerging from the ruins of the old one: sales will be \$2m this year, the staff is down to 60, and a move to a smaller factory nearby is imminent.

Across the city, in a modern office in Santa Fe, a gleaming new business district, Enrique Altamirano tells a straightforward success story. Six

years ago, he and a friend began a business with \$2,000 in borrowed capital and an idea: greeting cards featuring a group of cartoon characters designed to appeal to young Mexicans. Their firm, Altcecard, now has 155 workers, exports to 18 countries and expects sales of \$4.5m and a pre-tax profit margin of 20% this year. Altcecard too became an exporter through necessity, when cash-strapped Mexican shops started delaying payment. Mr Altamirano and his partner have management degrees from ITAM, Mexico's leading business school; their firm began as a course project. He



We're working on our management skills

admits that this pedigree helped with lining up both credit and customers.

Latin America's future depends in large part on the fate of small firms like these. Many of them are admirably entrepreneurial. Among the million or more small businesses in the Brazilian state of São Paulo are exporters of chemicals, shoes, software, grapes, car parts and packaging, according to the local office of Sebrae, the government's small-business advisory service. But right at the bottom of Latin America's corporate pyramid, life remains tough for a huge number of micro-enterprises and an army of precariously self-employed people. This so-called informal sector made up 54% of Latin America's non-agricultural workforce in

1992, compared with only 40% in 1980, according to a study by the International Labour Organisation.

What is stopping these people from becoming established small businessmen? Just excessive regulation by a bureaucratic state, say those who see them as a reservoir of frustrated entrepreneurs. Perhaps. But even where such rules have been eased, as in Bolivia and Peru, small enterprises continue to struggle. Without capital, technology and management skills, most of them always will.

tina last year still accounted for 56% of YPF's sales of \$5.9 billion) and in bringing an international perspective to the company's management. That was urgently needed. "They had a culture of worrying the whole time about the toilets in the service station in Ushuaia," says Christopher Eccleston, of Interacciones, a brokerage. Mr Monti himself, though an Argentine, had worked for more than 20 years at Schlumberger, a French oil-services giant.

If YPF had to import an international management culture, Argentina's Grupo Techint has successfully exported one. It was founded by Agostino Rocca, who had managed Italy's steelworks for Mussolini before emigrating to Argentina, where he set up Siderca, a maker of seamless steel tubes for the oil industry. Although Siderca formed part of the *patria contratista*, as Argentines call firms that make money from supply contracts with the state (in this case YPF), it was careful to maintain international standards of quality and cost. In the 1980s Siderca invested heavily in technology, and developed export markets by opening sales offices around the world.

More recently it has applied these skills to acquisitions. First it turned round Tamsa, a loss-making Mexican producer of steel tubes, and then Siderar, Argentina's formerly state-owned flat-steel

maker. Lastly, in a nice historical irony, the firm bought Dalminé, a privatised Italian steel-pipe maker once managed by the late Mr Rocca. Techint, with total sales of \$5.5 billion, is now the world's largest manufacturer of seamless steel tubes, with around 25% of the global market. Its success is due mostly to the care it has taken over training managers, a rarity in Latin America.

Expansion through foreign acquisitions has not always worked for Latin American firms. Vitro, a Monterrey glass giant, is still struggling to recover from its disastrous 1989 purchase (for \$900m) of Anchor Glass, a Florida-based glass-bottle maker. Vitro has spent the past two years trying to deal with debt that peaked at \$2.4 billion in mid-1996. It has had to take some tough decisions, including a distress sale of Anchor and the disposal of a 49% stake in Cydsa, a lacklustre petrochemical firm run by the chairman's cousins. But its enthusiasm for foreign markets remains undimmed: almost half its sales are outside Mexico, and it has made a more successful foray into the United States with vvr, which installs windows in skyscrapers and makes car mirrors.

The more common route to international status is through exports. The conglomerate Alfa, Vitro's neighbour in the verdant Monterrey suburb of



Garza Garcia, weathered the peso crash by doubling its exports in 1995. This year sales abroad should reach around 25% of the group's total. NAFTA helped, but the group would have got nowhere without an earlier radical overhaul after it almost went bankrupt in 1982. Alfa shed businesses in tourism and electronics, and cut costs in its big steel and petrochemical units.

Further south too, many firms have found that if they want to go on growing, they need to break out of the domestic market. Chilean firms, constrained by a small home market, have known this for some time; a score or more have become small-scale regional multinationals. In Argentina, Arcor, a family company, wants to be the regional leader in chocolates and sweets by 2004. It already has factories in six South American countries. It has recently computerised its distribution system, and is beefing up its marketing. It has some tough competitors, such as Philip Morris and France's Danone, but Luis Pagani, its chief executive, reckons he has both the technology and the market knowledge to keep ahead of them.

T-shirts around the globe

In a country as big as Brazil, a company can become internationally competitive without going beyond its home market. Coteminas claims to be the world's most efficient manufacturer of T-shirts, able to produce a 2-pack for just 75 cents. Admittedly, labour is cheap in its factories in Brazil's north-east, but that is not its main advantage. Its T-shirts take only two minutes each to cut and sew, so the labour

element is small, according to Josue Gomes da Silva, the firm's chief executive. What has given the firm its cost advantage is an investment of \$450m over the past six years in the most modern machinery available.

That has enabled Coteminas, which used to make yarn and grey (unfinished) fabric, to increase its production capacity sixfold, and to add more value by making finished consumer goods. Up to now it has mainly produced private-label goods for supermarkets, such as the Brazilian stores of Carrefour and Wal-Mart; but now it is starting to market its own brands of socks, towels and bed-linen. For the moment, its priority is dominance in the domestic market. Brazilians buy 750m T-shirts in an ordinary year, and Mr da Silva hopes that they may splash out on 850m next year, to get them through their elections and the football World Cup. His factories will be making 144m of them. After that, Coteminas has its sights set on a factory in Mexico from which to tackle the United States.

What unites many of these firms has been an ability to respond quickly to change. For many Mexican and Argentine companies, the first wave of cost-cutting is over. To grow further, they will need to buy companies across Latin America. But for all of them, investment in training and in management will become ever more important. Even where there is strong leadership from the top, when the market changes radically, the risk is that firms end up with 150 middle managers who will not know what to do, says Hernando Madero, of Booz, Allen & Hamilton's Mexico city office.



Join the world

SOMETHING revolutionary happened in Chile in October. Jose Yuraszek, chief executive of Enersis, Latin America's largest private-sector electricity firm, was forced to resign after a revolt by shareholders. They objected to Mr Yuraszek's scheme to merge his firm with Endesa, a Spanish utility now being privatised. This merger, under which Endesa has so far acquired 29% of Enersis for around \$1.4 billion, sensibly aimed at creating a firm with the scale and financial muscle to play a part in future electricity privatisations in Latin America. But some shareholders reckoned that the terms favoured Mr Yuraszek and his senior colleagues at their expense.

Such an exercise of shareholder power is unprecedented in Latin America. They do things differently there: for example, hostile takeovers conducted through the stockmarket are almost unheard of. This is unlikely to change just because foreign institutional investors now own larger chunks of Latin American firms; indeed, the foreigners seem quite happy with the present arrangements. Non-voting shares usually cost more than voting ones because they are more actively traded. Investors seem to attach more importance to liquidity than to control over owner-managers.

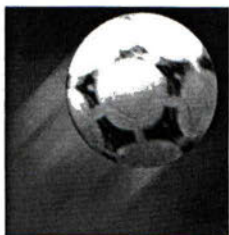
Equally against the trend in rich countries, the shares of conglomerates in Latin America trade at a premium to the market. That is partly because in

economies still undergoing rapid change, such large and diversified groups may be better placed to take advantage of new opportunities; because they have more capital (and can raise more, more cheaply); and because they may have a better supply of skilled managers than smaller rivals.

Moreover, foreign investors tend to see groups such as Mexico's Alfa or Grupo Carso, or Chile's Luksic firms, as "country funds", whose diversity offers comfort in markets that are still relatively risky. That may change, but only slowly. A handful of Latin American firms have come to resemble their counterparts in the Anglo-Saxon world, being majority-owned by institutional investors rather than by family patriarchs. Apart from the Chilean electricity firms, such exceptions include YPF and Perdigão, a Brazilian chicken exporter which has staged an impressive recovery after being taken over by a group of local pension funds in 1994. Brazilian privatisation may yet produce a few more such companies.

Yet Brazil, rather than adopt the Anglo-Saxon model, is more likely to copy French firms that combine several family-based groups under complex shareholder agreements to achieve sufficient scale, argues Persio Arida, of Opportunity, an investment company. That may become the norm elsewhere in Latin America as well. Wouter Rosingsh, of Booz, Allen & Hamilton, thinks that Latin American firms

Latin American business must, in its own way, play the global game



may often form alliances with foreign partners rather than simply sell out.

Who is to say that such arrangements will not work perfectly well? As this survey has shown, Latin Americans are great adapters. And families can be demanding shareholders. As he hurries off to the annual meeting of Grupo Techint, Javier Tizado, Siderar's chief executive, says he must satisfy the "brothers, sisters, nephews, widows and orphans" of the group's founder. A bunch of fund managers might well seem an easier alternative.

But will this gradual evolution in a more competitive environment ensure prosperity? There are several doubts. The first is whether enough Latin American firms will go for new export markets. It is not safe to rely on multinationals to do the job: in contrast to Asia, much of their investment in Latin America (except perhaps in Mexico) is aimed at the domestic market. But without more exports, the region's economic growth will be held back.

A few signs point in the right direction. Fundacion Chile, a not-for-profit but market-minded technology transfer-centre, has had some success in developing wholly new industries, such as salmon farming (where Chile is now the world's second-largest producer), berry growing and furniture making. Now it is working on sturgeon and hake farming and goat's cheese production. In Argentina, Cresud, an investment firm, is buying farms and improving their yields. Now that the United States has lifted restrictions on Argentine beef imports, the company is looking at beef processing and marketing. There is enormous potential throughout Latin America for ventures to add value to primary products and develop new markets for them.

Another worry is that Latin Americans, inspired improvisers though they may be, have a poor record as innovators. That partly reflects past volatility, leading to risk avoidance, but partly also the near-impossibility for young would-be entrepreneurs of getting start-up capital. One consequence is that

Latin American firms spend little on research and development. Brazil's R&D spending this year will amount to only 1.1% of GDP, compared with 2.5% in the United States. A second result is that Latin America plays little part in new industries.

Again, there are some exceptions. Pay-television is growing fast in many countries in the region, creating opportunities for locally developed programming in Spanish and Portuguese. Telecoms privatisation is spawning some local technology firms. Guadalajara in Mexico is one of several areas with ambitions to become an information-technology "cluster". IBM rates its factory there as one of its five most efficient plants in the world.

Costa Rica—which alone among Latin American countries has signed the World Trade Organisation agreement eliminating barriers to trade in information technology—has similar pretensions. Last year Intel, a United States technology firm, chose Costa Rica for a \$300m silicon-chip factory, in preference to Ireland or Malaysia.

An optimist might argue that Latin America's past backwardness in information technology gives it the scope to leapfrog rivals by adopting the newest systems, such as network computing, fibre-optic cable and wireless communication. But there is only fragmentary evidence that it is doing so. That may be because the slowest thing to change is managers' attitudes. Such basic things as brand-building, marketing, offering good service and trying to please the customer still rate as novelties in many Latin American firms and are often badly done, especially in Brazil.

No hiding place

Hierarchical and inward-looking family conglomerates traditionally considered training for their managers and workers a waste of time and money. Remarkably, it was only in 1993 that Brazil's Fundação Getulio Vargas, which vies with Mexico's ITAM for the title of Latin America's top business school, set up an MBA course along North American lines to train high-flying managers; and only now are top Mexican firms systematically trawling the business schools of the United States for suitable Spanish-speaking graduates.

Protectionism, inflation and instability meant that in the 1970s and 1980s Latin American business fell a long way behind its competitors in other parts of the world. Yet there is no intrinsic reason why the region's family-based firms should not produce world-class managers and products (just look at their counterparts in northern Italy). Many Latin American businesses are now starting to catch up. How quickly they can get there depends partly on continuing macroeconomic stability. Since the problems of risk measurement and uncertainty in engineering are similar to those in economics, Brazilian production engineers have in the past often ended up as bond traders, Mr Arida points out. An extended period of low inflation should make production engineering much more attractive.

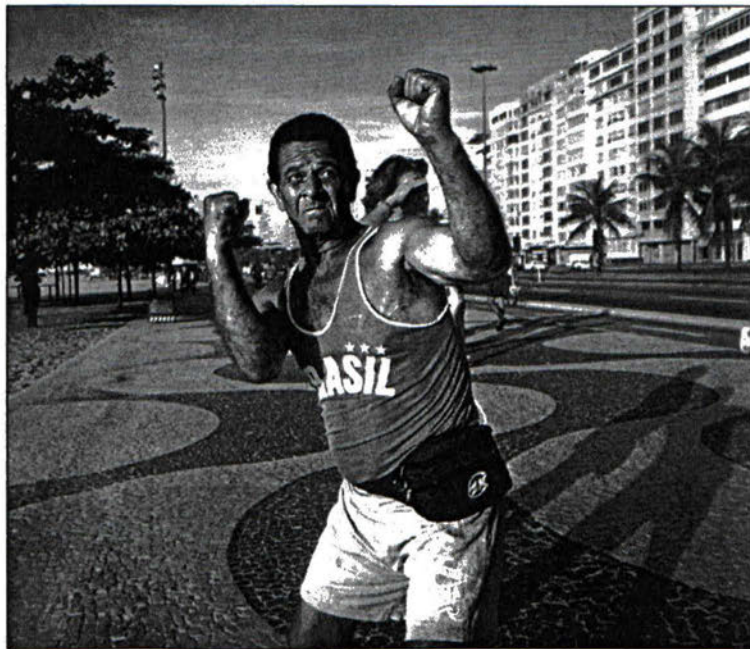
To catch up with their rivals, Latin America's firms must achieve much higher standards in everything from cost control to new-product development and marketing. In short, they must compete at the same game as the rest of the world.

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Tony Blair's big idea

The government is about to launch new plans to help the "socially excluded". But can New Labour do better than the Tories?

IT IS, says Tony Blair, the "defining difference" between his government and its Tory predecessors. Mr Blair argues that the Conservatives adopted a laissez-faire attitude to the growth of a British underclass; his government will tackle the problem head on. On December 8th, a special "Social Exclusion Unit", based at 10 Downing Street, will be launched to deal with the problem.

Social exclusion means different things to different people. The term was invented in France, originally referring to people who dropped through the social-security net. From France, it was picked up by the European Commission, which is now responsible for fretting on a European-wide basis about the "socially excluded". But the phrase is a newcomer to Britain. Although it now peppers ministers' speeches almost as often as the words "modern" and "people", it was not mentioned at all in Labour's election manifesto.

The craze for talking about "social exclusion" contains hazards for policymakers. Gather together the speeches of ministers and you might conclude that the disabled, lone mothers, the unemployed and many pensioners are all, in different ways, socially excluded. Some commentators estimate that the total number of "socially excluded" people could amount to over 10m, or around 20% of the population. Refining the problem will be one of the tasks of Mr Blair's new Downing Street unit, which is headed by Moira Wallace, a feisty Treasury official and former aide to John Major when he was prime minister.

The government sees "social exclusion" as something different from poverty, although related to it. As Mr Blair himself put it, the socially excluded are "people who do

not have the means, material and otherwise, to participate in social, economic, political and cultural life." They are likely to be cut off from the activities that define normal life for most Britons: work, school, family life. They may lack transport, secure housing, even a telephone.

Encouragingly, the social-exclusion unit has decided to focus on three specific problems: poor housing estates; the prob-

when you take a closer look at the three areas identified by the social-exclusion unit.

The most visible sign of social exclusion is people sleeping rough on city streets. Their growing visibility in the 1980s and 1990s contributed to the widespread feeling that Britain had become a rougher, as well as a richer, society under the Tories. The street sleepers include, among others, young people leaving care, ex-prisoners, drug users and the mentally ill.

As it happens, the problem has been getting better in recent years. Estimates circulating in Downing Street suggest that the number of rough sleepers in London has fallen from perhaps 2,000 in the late 1980s to below 300 today. In private, some of Mr Blair's advisers acknowledge that Conservative initiatives to get the homeless and mentally ill into shelters had begun to work.

Although the problem of people sleeping rough on the streets may be easing, the social pathologies of big public housing estates remain entrenched. Nearly half of all crimes take place in just a tenth of neighbourhoods. Gangs, drugs and prostitution proliferate in certain estates and seem impervious to police action. At present the British papers are full of stories about an estate in Rotherhithe in south-east London, where the police have been unable to investigate a gang murder because local tenants are terrified to testify. Deprived estates have twice as many unemployed and lone parents, and 50% more invalids than the national average.

But once again it seems likely that the government's rhetorical distance from its Tory predecessor will mask considerable continuities in

policy. Anne Power, an academic, has examined the approach of five different countries in her recent book "Estates on the Edge" (Macmillan, £57.50). She points to some success stories from previously problematic British estates like Broadwater Farm in north London, where there were serious riots in the 1980s. There, a co-ordinated approach involving housing, local-authority services, schools and police has improved matters, reducing crime and truancy.

Ms Power also highlights the success of



Spot the socially excluded

lems of children who are expelled from school or who are persistently truant; and street homelessness. But in taking on these problems, the Blair government has eschewed the weapons that the Labour Party would traditionally have reached for. Mr Blair's "New Labour" says it no longer believes in "throwing money at problems", or sharply increased taxes on the rich. This may be good for the economy. But it does suggest that Mr Blair will struggle to define the difference between his approach and that of the Tories. That impression grows

BRITAIN

tenant-management organisations on some estates. And she thinks that the Conservative policy of devolving budgetary responsibility to individual schools could prove a model for building strong institutions at the estate level. Public-housing estates, she argues, should be seen as a resource more than as a problem: making estates more attractive places to live by getting local people involved in their management would not only improve tenants' lives but would remove the cost of housing them elsewhere.

When it comes to education, the government revealed plans this week for special "education action zones". These will be encouraged to get businesses and parents involved in schools and to set up extra child-care and "homework clubs". The government is concentrating on housing, homelessness and truancy but it acknowledges that the problem goes rather deeper than that. For although it draws a distinction between social exclusion and both poverty and unemployment, they are obviously closely correlated phenomena.

John Hills, head of the new centre for the analysis of social exclusion at the London School of Economics, says that the challenge is to understand why people move in and out of low incomes, rather than just considering snapshots at any one time. The most recent analysis of this data, by Stephen Jenkins of Essex University, shows evidence of considerable income mobility: only 7% of the population remain in the bottom 20% of incomes for four consecutive years.

Clearly the best route to higher income is through work. The policy unit says that Labour's "new deal" for the unemployed is central to tackling social exclusion. But parts of the deal—subsidising employers to take on young people and the long-term unemployed—are similar to old policies sponsored by the Tories. And other proposals—the minimum wage and increased trade-union rights—are likely to benefit current workers at the expense of those looking for work. If social exclusion really is the government's priority, then the interests of the unemployed should come first.

Lone parents provide another example of the "hard choices" Mr Blair is so fond of talking about. In the bottom fifth of the income distribution there are now more lone parents than any other type of family. Lone-parent poverty can be tackled in three main ways. The Tories were convinced that the benefit system offered perverse incentives to people to become single parents. Cutting benefits, and so removing their advantages over married couples, was one approach. A second approach is to get lone parents into work; a third would be to provide more public money to lone parents at home. The "Parent Plus" scheme pioneered by the Tories offered job advice to lone parents. The

Blair government's "new deal" for lone parents is essentially a repackaging of this policy, with extra cash for child-care.

Before they left office, the Tories were also planning to "align" benefits for new lone parents with those for couples—by cutting the amount of public money going to single mothers. In opposition, the Labour Party decried this approach; in government, they are going ahead with the cuts.

Not surprisingly, traditional Labour supporters have noticed and protested. This week Harriet Harman, Labour's hapless social-security secretary, faced wide-

spread criticism from Labour MPs over her plan to press ahead with the Conservative cuts in lone-parent benefit. The government is arguing that its decision is driven largely by its desire to keep within the budgetary limits imposed by the previous government. But given that it has been able to find emergency money for other priorities, it seems likely that the Blair government privately accepts that the benefit system is providing perverse incentives to single motherhood. So far, however, this is too difficult an argument for most Labour politicians to make in public.



Mad cows

For whom the bell tolls

ANOTHER shiver of fear swept across Britain this week. On December 3rd, Jack Cunningham, the minister of agriculture, announced plans for a ban on the sale of beef bones because of the possibility that they could pass mad-cow disease (BSE) to humans. Within hours of the news, supermarkets around the country had begun to take oxtail, T-bone steak and beef ribs off their shelves.

The announcement added to the woes of Britain's already mutinous beef-farmers. Even before Mr Cunningham made his unexpected announcement Welsh farmers, hit by falling beef prices and the continuing European Union ban on British beef exports, had been blockading ports and hurling imports of Irish beef into the sea. But for most British people, the future of beef prices is the least of their worries. The government announcement has raised new questions about the safety of beef, and raised again the nightmare scenario of a wide-scale epidemic of new variant

Creutzfeldt-Jakob disease (nvCJD), the human equivalent of BSE. Obvious questions are again being asked. Is any beef safe to eat? Is milk safe to drink? And how much do we now know about the chances of an epidemic of nvCJD?

The difficulties in answering these questions are threefold. First, prion diseases—comprising BSE, all forms of CJD, scrapie (the sheep equivalent) and some others—are among the most mysterious diseases known to science. It is not even clear what causes them, let alone anything else. Second, as there is still no test to tell whether animals are infected, experiments to find out whether or not beef is safe take ages. The best experimental model is the mouse, but infected mice may take two years to show signs and symptoms of prion diseases. And third, nvCJD is so new that it is impossible to make any reliable predictions about the potential for an epidemic. Crucial variables for such forecasts, like the average time from infection to disease in

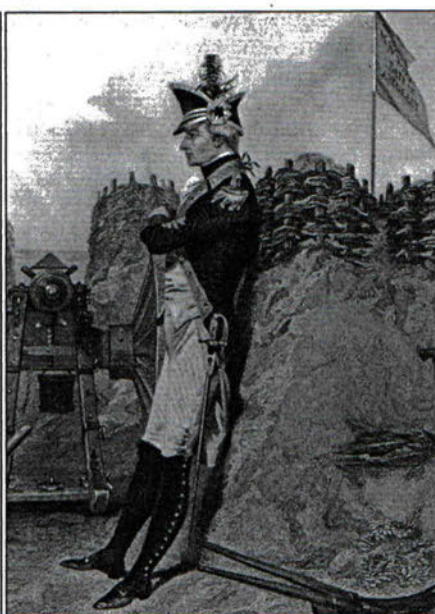
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THE PRESIDENT HAS SEEN
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A war of myth and memory

WASHINGTON, DC

Eclipsed for a century by Thomas Jefferson, Alexander Hamilton is making a comeback

FOR much of this century, America's history buffs have been fascinated most of all by Thomas Jefferson, author of the Declaration of Independence, secretary of state in George Washington's administration, and America's third president. Of all the founding fathers, Jefferson was the staunchest advocate of freedom. He disliked concentrations of power, both political and economic; he wanted a republic with a weak central government, its tone set by independent farmers rather than by industry. His suspicion of authority made him leery of standing armies, and of the invasive taxation that goes with them; his instincts on America's foreign policy were isolationist, except when it came to supporting fellow partisans of liberty in revolutionary France.

Jefferson's passion for freedom has endeared him to politicians in this century, who have used his name as a prayer to summon idealism from men's souls. Admirers of Woodrow Wilson's democracy-boosting foreign policy liked to invoke Jefferson's idealism. Franklin Roosevelt made Jefferson

the patron saint of the New Deal. The Declaration's assertion that "all men are created equal" made Jefferson a hero of the civil-rights movement. Ronald Reagan suggested that Americans "pluck a flower from Thomas Jefferson's life and wear it in our soul forever." In 1990, George Will, a conservative columnist, named Jefferson the "Per-

THE LONG AFFAIR: THOMAS JEFFERSON AND THE FRENCH REVOLUTION, 1785-1800. By Conor Cruise O'Brien. University of Chicago Press; 367 pages; \$29.95.

AMERICAN SPHINX: THE CHARACTER OF THOMAS JEFFERSON. By Joseph Ellis. Knopf; 400 pages; \$26.

AMERICAN SCRIPTURE: MAKING THE DECLARATION OF INDEPENDENCE. By Pauline Maier. Knopf; 352 pages; \$27.50.

HAMILTON'S BLESSING. By John Steele Gordon. Walker; 224 pages; \$21.

HAMILTON'S REPUBLIC: READINGS IN THE AMERICAN DEMOCRATIC NATIONALIST TRADITION. Edited by Michael Lind. Free Press; 345 pages; \$25.

son of the Millennium", no less.

This fascination with Jefferson continues: in the past year or so, he has been the subject of a television series and two new biographies. His admirers on the left cite the agrarian Jefferson as an early critic of big business. His admirers on the right cite the devolutionist Jefferson as a prescient critic of big government. But there is something new about the most recent attention that Jefferson has been receiving. After a century or so of praise, interrupted only by quiet academic criticism, Jefferson has come in for a clobbering.

The first of the two recent biographies, by Conor Cruise O'Brien, an Irish polemicist, is a hatchet job: it portrays Jefferson as a racial hypocrite, a blood-thirsty extremist, even as a precursor of Pol Pot, the butcher of Cambodia. The second, by Joseph Ellis, an academic at Mount Holyoke College, is more measured, but is critical nonetheless.

Jefferson's life affords ample scope for criticism. He proclaimed freedom yet owned hundreds of slaves and refused to side with contemporaries who favoured abolition. He was critical of power yet refused at times to criticise France's revolutionary terror. Having originally denounced political parties as a divisive threat to the young republic, Jefferson became the first American politician to organise and lead one. Having denounced the national debt as a scheme to aggrandise central government, he borrowed a large sum to pay for the Louisiana Purchase.

Editing Jefferson

It is not just biographers who assail Jefferson. In "American Scripture", a book published last summer about the Declaration of Independence, Pauline Maier, a historian at the Massachusetts Institute of Technology, added to Jefferson's humbling. The Declaration is usually remembered as a monument to his genius. Actually, Jefferson copied much of it from George Mason's preliminary draft of Virginia's Declaration of Human Rights, including the ringing statement that "all men are created equal". Moreover, Jefferson's draft was wordy; the elegance of the final version owed much to editing done in Congress, where a quarter of the text was cut. Far from being the Declaration's sole author, Jefferson turns out to have played a role akin to the constantly reworked script-writers of Hollywood.

The new vogue for bashing Jefferson is prompting a curious reversal in the fortunes of his most bitter rival, Alexander Hamilton. While Jefferson was the principal author of the Declaration of Independence,

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Builders of Richard Meier's Getty Centre in Los Angeles, which opens next week. They appear in "Making Architecture" (Thames and Hudson; £29.95. The Getty Trust; \$50)



dence, emphasising liberty, Hamilton was the organiser and main writer of the Federalist Papers, which made the case for a stronger union among the 13 states.

Hamilton believed in a powerful federal government, robust enough to promote American interests abroad and American industry at home. Appalled by these ideas, Jefferson accused Hamilton of "machinations against the liberty of his country"; Hamilton called Jefferson a "contemptible hypocrite". At his home in Monticello, Jefferson placed a bust of Hamilton opposite a portrait of himself, ensuring that the two of them would be "opposed in death as in life."

In the aftermath of the civil war, Hamilton seemed to be winning this posthumous competition. The Unionist victory over slavery was in part a triumph for Jeffersonian freedom, and Lincoln alluded to the Declaration of Independence in his address at Gettysburg. But the civil war was really more a triumph for Hamilton, partly because he had been an early advocate of abolition, and partly because he had always upheld federal authority against southerners' assertion of states' rights. In the decades that followed, Hamiltonian industrialisation defeated Jeffersonian agrarianism. For a while, Hamilton was second only to Washington in the pantheon of national heroes. His reputation declined, most markedly during the Depression, as he came to be seen as a hard-hearted, hard-money ideologue.

Now two pro-Hamilton broadsides have appeared this year, hoping to restore Hamilton to the pantheon. The first, by John Steele Gordon of *American Heritage*

magazine, celebrates Hamilton's success as the first secretary of the treasury: he saved the young republic from bankruptcy by institutionalising the national debt. The second, published this month, is an anthology by Michael Lind which seeks to establish Hamilton as the "source of most of what is sensible and sound in American foreign policy, constitutional law, and economic policy." And a sympathetic biography of Hamilton by Richard Brookhiser of the *National Review* is in the works.

Mr Lind argues, rather persuasively, that America today is Jefferson's in rhetoric but Hamilton's in practice. It was Hamilton who put in place many of the institutions that give America its modern form: a federal government with extensive powers, judicial review, a central bank. Over the past two centuries, the central power that Hamilton stood up for has strengthened in response to wars, moral crises like slavery, or economic ones such as the Depression. Federal highways criss-cross the land; federal agencies regulate everything from the environment to food; federal bureaucrats run America's mighty military machine.

And yet it is hard to feel sorry for the comparatively neglected Hamilton, or to regret America's infatuation with an idealised Jefferson of myth. For the memory of this passionate lover of freedom serves to put hurdles in the way of authoritarian schemes in America, even if it cannot stifle all of them. Since governments everywhere are forever trying to expand their reach and authority, this is no bad thing.

History of slavery

Middle passage

THE SLAVE TRADE: THE HISTORY OF THE ATLANTIC SLAVE TRADE, 1440-1870. By Hugh Thomas. Picador; 925 pages; £25. Simon & Schuster; \$37.50

HUGH THOMAS, an adept of the broad sweep-of-history school, has tackled his latest subject, the human commerce between Africa and the Americas, brokered by Europeans, with assiduity. His archival knowledge of the Spanish empire, expanded by his earlier blockbusters on the Spanish civil war, Cuba and the conquest of Mexico, has stood him in good stead.

The Iberian initiative was critical in the development of one of Europe's most gruesome contributions to history. Lord Thomas takes his readers back to the 15th-century origins of the trade, the period when Prince Henry the Navi-

gator (of whom there is a magnificent thumbnail sketch) and his successors made the first fateful explorations down the West African coast. Lord Thomas observes caustically, "they were looking for gold, but finding little of it, made do with men and women." Nonetheless, the great period of growth for the slave trade came when the Spanish hijacked it in the 16th century.

The Portuguese brought their slaves to markets in Spain and Italy. It was Ferdinand of Aragon and Emperor Charles V early in the 16th century who authorised the shipment of slaves to the newly discovered Americas. They have thus been marked out as the true progenitors of the trade, which entailed such added cruelties as branding (see illustration). Not until the end of that century did the French, the Dutch and the British muscle in on the action, just as they tried to crash into the Spanish trade in gold and silver.

The whole saga is traced with great detail by Lord Thomas. His surefootedness does not desert him as he moves through to the serious and methodical way the British in particular used slaves to develop plantation economies in sugar and in cotton in the Caribbean and in North America. "No nation has plunged so deeply into this guilt as Great Britain," observed Pitt the Younger in 1792; and it was in Britain that the celebrated conscience of the non-conformists (who had previously helped engineer a capitalist system) triggered the movement for abolition that achieved success in the early part of the 19th century. But Lord Thomas's bold assertion that Britain's abolitionism "surely compensated for the country's previous dedication to the trade" is surely questionable.

He handles his vast canvas with expertise, offering a wealth of information not just on the slaving countries and their New World extensions, but on the complex and sophisticated history of West Africa, where his father served in the colonial service in the Gold Coast (now Ghana). He is right to stress that slavery was prevalent and accepted everywhere in the medieval world, in both Christian and Islamic lands, and was even reinforced during the Renaissance by the cult of Antiquity, some of whose adherents felt that the leisure provided by slaves to an elite allowed civilisation to flower.

As well as fingering some arch enthusiasts for slavery over the centuries, including a number of British monarchs, he also records the acceptance of slavery in Africa itself as applied to enemies or even neighbours. But he rightly laments that the slaves themselves are "silent voices", prior to the 18th century and the eloquent testimony of Olaudah



FINANCE AND ECONOMICS

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Dealing for dollars

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GENEVA

Freer trade in financial services is once again within reach. It is up to the United States to grasp it

IN THE early 1990s, trade officials from rich countries were often asked not to write the word "Services" on the spines of their office files, lest it upset negotiators from the developing world who were having a torrid enough time liberalising their goods markets. Free trade in services is no longer such a taboo. Many countries have opened their markets under their own steam, and earlier this year the World Trade Organisation's 130 members sealed pacts on freeing telecommunications and information technology. That leaves one gaping hole in the fabric of global agreements on trade: financial services.

Fixing that depends on whether negotiators from the rich world find the new batch of market-opening offers from developing countries enticing enough by December 12th, the deadline for a WTO-sponsored agreement on banking, insurance and other financial services. A deal that improves access to many markets is within reach, but its success depends on Washington. America has pushed harder than any other country to prise open the world's financial markets. But with expectations that many consider unrealistic, it is also the biggest potential obstacle to an agreement.

America has been obstructive once before. A financial-services deal seemed near in 1995, but the Americans, egged on by big banks and insurers, walked away at the last

minute, complaining of inadequate offers from several Asian countries. The EU was left to cobble together a stop-gap agreement, which expires this month. This temporary measure helped maintain momentum, encouraging countries such as India to grant more licences to western banks. Since 1995, large developing countries, such as Turkey and South Africa, have sent improved offers to the WTO, along with Japan, the EU and America. Several big countries, including India and Brazil, promise to submit offers next week.

Perhaps the biggest benefit of a new agreement would be to make these offers binding. At the moment, a country that has allowed foreign banks to run majority-owned subsidiaries is free to reverse that decision. But a WTO pact would give its commitment legal force. If the government changed its mind, it would be answerable to a dispute-settlement panel with sweeping powers. This multilateral approach soothes investors and makes policies more predictable.

A good number of countries which once cloistered their financial sectors, such as Mexico and Hungary, now welcome foreign investment in banking and insurance. But many governments still coddle their home-grown institutions. The worst culprits are in Asia, where countries such as Malaysia and South Korea have sharply re-

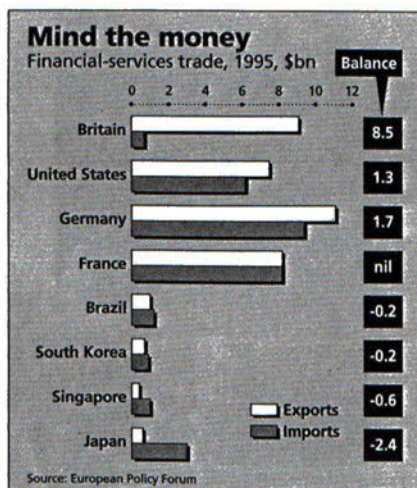
stricted the activities of foreign banks, stockbrokers, fund managers and insurers. Protective instincts are not confined to emerging markets. Canada, for instance, still discriminates against foreign banks by limiting the size of their branch networks.

In many cases, the lack of foreign competition in these markets has made financial companies bloated and inefficient. American and European bankers and insurers, whose own home markets are relatively open, see huge opportunities in emerging economies if the barriers are swept away, which is why they pressed for a financial-services pact in the first place. This is also why many emerging countries have resisted an agreement: if efficient foreigners come in, many local institutions will suffer. That consumers would benefit does not seem to count.

Excuses, excuses

Some Asian countries are using the region's financial crisis as an excuse to offer less liberalisation than they might have. More competition, the argument goes, could exacerbate the problems of weak banks and insurers, requiring costlier government bail-outs. A WTO deal would also limit governments' ability to induce sick banks to restructure by offering shelter from foreign competition. All of this is true, but it misses the point. The problems of Asia's financial firms are due not to too much competition, but to over-protection and cronyism, which have encouraged shoddy lending and poor cost-control. The entry of foreigners is the easiest way to provide the discipline that is lacking. It is significant that financial institutions in Hong Kong and Singapore, both of which are wide open to foreign financial companies, have been able to withstand the region's turmoil.

Yet even among nationalistic Asians, at-



itudes are changing, if for no other reason than the desperate need for foreign capital to rebuild banking systems. "We realise we must compete for such capital, not run from it," says one Asian negotiator. To encourage this new view, rich countries have shown an increased willingness to let poorer ones open their financial markets over time rather than all at once.

As the talks' deadline nears, the outcome may well hinge on relations between America and two of its more tendentious trading partners, India and Malaysia. India has been a leader among countries sceptical of financial liberalisation. Its offer, due next week, will probably fall short of a commitment to letting in foreign insurance companies. Even more worrying is a stand-off between America and Malaysia over insurance. The Malaysians' latest offer includes a promise to let foreigners own up to 51% of insurance firms, but does not protect the interests of foreigners now holding stakes greater than 51%. As it happens, one of the few foreign companies affected is American International Group, a huge insurer whose boss, Maurice Greenberg, knows how to pull strings in Washington.

The Malaysian insurance issue has divided America and the EU. While European negotiators agree with America on principle, they say it is not worth risking the entire negotiation over a relatively small dispute. "No individual firms should be allowed to wreck the talks," insists Andrew Buxton, chairman of Barclays Bank and co-head of an industry group advising negotiators, in a pointed reference to Mr Greenberg. The Americans must weigh the merits of rejecting a pact that lacks a better Malaysian offer against the costs—most notably, the compounding of suspicions that America, once a forceful advocate for trade liberalisation, is no longer interested in it.

There is room for compromise yet. But the signs are ominous. Some American officials have hinted that they would prefer to stall until 2000; at that point, a new round of talks might take in other sectors as well as

financial services, providing more scope for trade-offs. While the EU's negotiators consider the offers already tabled as sufficient basis for a deal, the Americans "say they want much more, even in private", according to one European official. If America walks away, the EU would probably try to patch together another interim agreement, but it might find the task more difficult second time around.

Whatever the outcome, it seems certain to be decided once again in Washington. American officials are right to say that no deal is better than a terrible one, but the agreement on offer looks far from terrible. The consequences of a break-up in the talks, on the other hand, might well be.

Russia's economy

Russian roulette

MOSCOW

INTEREST rates spiked above 50%, the rouble tottered, and the central bank's reserves were falling fast. Russia's fledgling financial markets were on the brink of crisis this week, though they held back from a final plunge. Foreign investors were leaving with cash earmarked for withdrawal a month earlier, when markets slumped around the world. More Russians were trading in roubles for dollars. And the government, having failed to respond to problems visible well in advance, was struggling to convince the public that economic policy had not collapsed into incoherence.

The central bank's reputation has already fallen victim to market turmoil. On December 3rd, its governor, Sergei Dubinin, said reserves had fallen to about \$18 billion, down from \$21.5 billion on November 21st. That was the price of a futile attempt the preceding week to hold down

interest rates and prop up the rouble at the same time. Only this week did Mr Dubinin stop trying to dictate prices to the government-securities market, allowing some yields to rise from 30% to more than 40%. The market's response was grudging: traders said the interest-rate rise (see chart on next page) was ten points too little and two weeks too late. At a conference for institutional investors Mr Dubinin had no useful answer when asked why he had not raised rates sharply much earlier.

One explanation may have been that the central bank was supporting the market while some Russian banks reduced their positions. Foreigners withdrawing from the market for government bonds, known as GKOS, are required to give 30 days' notice. This allows domestic bondholders to escape before foreign withdrawals knock bond prices down. By keeping prices high, the central bank may have helped banks holding large amounts of government debt to avoid booking big losses.

Mr Dubinin was also constrained by the need to build a consensus within the government favouring sharply higher rates. That would have taken some work. The government still asserts that the economy will grow next year after nine years of shrinkage. A sustained rise in interest rates, which will divert money away from industrial investment and into government securities, would all but preclude that possibility.

Foreign investors have been pulling out of Russian markets mainly because they fear for the rouble. They also fear for the banking sector and the scale of its unhedged dollar liabilities. Analysts estimate these borrowings are between \$5 billion and \$15 billion—money that the banks have lent out in roubles but which they will need to repay in dollars. A collapse of the rouble would make these debts much more expensive to repay, probably driving some banks under. Small wonder the central bank has been focusing this week on a single message to the markets: the rouble will not be allowed to collapse.

The big question is whether that message is believed by Russian households. Average Russians are increasingly reluctant to hold the currency. On December 1st the central bank widened the "corridor" within which it manages the rouble-dollar exchange rate, to prevent the rouble breaching its lower limit. On December 2nd moneychangers began advertising for the first time a rate exceeding 6,000 roubles to the dollar. With many Russians also wary of hanging on to roubles until after the planned redenomination on January 1st, which will relaunch the currency at 6.1 to the dollar, the central bank will be hard-pressed to hold the line until then.

In part Russia is sharing the problems of emerging markets around the world. But weak fiscal management has exacerbated



Every dollar helps

THE AMERICAS

THE PRESIDENT HAS SEEN

12-9-97

Sunny
Fyl - su alto
Meerom / Relabille

Castro turns to Rome

HAVANA

In Cuba, the government's acceptance of a visit by the pope next month marks a startling change. In Mexico too (next article), the church is speaking up

OPEN-AIR masses, held regularly across Cuba, are attracting hundreds of people. Many churches—some opening their doors for the first time in years—are holding daily services for packed congregations. For the first time since the 1959 revolution, Cuba's revered patron saint, the Virgin of Charity of Cobre, is on a tour of all the island's churches, in a "pilgrimage of blessing" attended by thousands of weeping Catholics bearing flowers and candles. And President Fidel Castro, in a nine-hour meeting with Protestant and Jewish leaders, has asked them too to pray for the island, to help solve its problems. Cubans wonder what is going on.

The short answer is that Pope John Paul is due to visit the island in late January. But is that all? He is indeed, and Cuba did indeed in 1992 drop the commitment to atheism written into its constitution. Yet the sudden and general loosening of restrictions on religious worship has taken most Cubans by surprise. Could it be that Mr Castro had a Damascene conversion when he recently met the pope in Rome?

"I could never have believed it, if I hadn't seen it with my own eyes," says a devout Catholic who used to attend secret masses in the home of a priest. "He seemed so deeply moved by his meeting. One has to believe it was sincere." Another, however, a regular churchgoer, says many Catholics are angry at the meeting. "For years we had to hide our faith. We couldn't attend mass because he closed the churches and drove away the priests. If we were known to be Catholics, our children would have had a rough time at school, we might have lost our jobs, all kinds of things. And now he meets el Papa. Of course he's impressed. Now he says it's OK to attend mass. He gives us his permission to worship God!"

Certainly the government actively sought the papal visit. Mr Castro, once a pupil of the Jesuits, described his audience with the pope as a "miracle", telling John Paul that he would be treated "like a king" in Cuba. He will go to greet the pope on his arrival, and will attend a mass. The government, having already authorised the cur-

rent open-air masses, will lay on public transport to and from papal gatherings. The church has even been promised limited access to the media. Religious matters are rarely covered by the official (and only) news services. Religious groups require permission to distribute information; most are not even allowed to own a photocopier.

Time will show how real these concessions are. Even so, many Cubans wonder why Mr Castro accepted the visit. He may be trying to enlist the church in his battle with the Americans, but has he not bitten off more than he can chew? "What will happen if some people try to cause trouble during the papal masses?" asks one Catholic. "Are the police going to stamp on them there in front of the pope and all those foreign television cameras? What will Fidel do if the pope says something he doesn't like?"

The official line, in the version set out by the newspaper of the Communist Youth, *Juventud Rebelde*, is that the visit

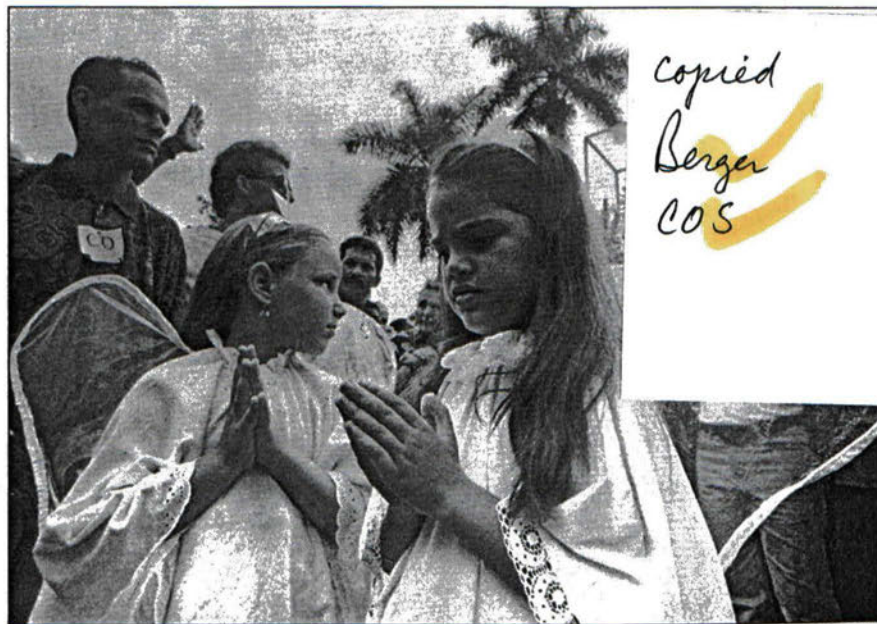
tends to be interpreted as sympathy for Cuba and condemnation for the American block-

ade... The pope, in numerous interventions, has taken the same view as Cuba does of capitalism and its neo-liberal packages. The visit will show that a society with firm attitudes against drugs, child prostitution and other social evils shares many of the ethical principles enunciated by the pope.

The Communist Party is not quite so sure. Caridad Diego, head of its religious-affairs department, thinking of the papal masses, has said that the government wishes to "prevent public acts that could be politically motivated." No tourist visas are being granted for January, and foreign journalists will be barred, unless they are coming specifically to cover the papal visit.

The government debated long and hard before giving permission for an American cruise ship carrying 1,000 Catholics, many of them Cuban-American exiles, to call during the visit. "There are too many people who want to come here from Miami," says a staunch Communist in Havana. "I'm pretty certain many of them are not coming to see the pope, but to cause trouble and embarrass us at a time when all the world's press will be here."

But it will not really be such people who can cause embarrassment. It will be the pope. For the first time in 38 years, Fidel Castro, on his own doorstep, will have to deal with a man more powerful and respected than himself, and one who will speak his own mind to hundreds of thousands of people normally permitted to listen only to what comes out of Mr Castro's.



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Berger
CO S

The Virgin of Charity rides again

THE WHITE HOUSE

WAS

THE PRESIDENT HAS SEEN

12-9-97

December 8, 1997

cc via letter
to Sec. Albright
Fgs

Mr. Billy B. Goldber
Suite 500
6100 Corporate Drive
Houston, Texas 7703

Dear Billy:

I'm grateful for you
on the Middle East p
that you received my October 21 reply to
your previous letter. I have made clear
my belief that the issues between Israelis
and Palestinians need to be solved at the
negotiating table. I continue to urge the
parties to resume their negotiations, and
I will do everything I can to support them.

Thanks for your birthday wishes for Hillary.
She and I hope you and Rosalie are well.

Sincerely,

Bill Clinton

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copied
incoming only
to Secretary
Albright

Billy —
your ideas are
interesting and I will discuss them
with our folks. I want badly to work
through this. — Bill

THE WHITE HOUSE

WASHINGTON

December 8, 1997

Mr. Billy B. Goldberg
Suite 500
6100 Corporate Drive
Houston, Texas 77036

Dear Billy:

I'm grateful for your additional comments on the Middle East peace process and hope that you received my October 27 reply to your previous letter. I have made clear my belief that the issues between Israelis and Palestinians need to be solved at the negotiating table. I continue to urge the parties to resume their negotiations, and I will do everything I can to support them.

Thanks for your birthday wishes for Hillary. She and I hope you and Rosalie are well.

Sincerely,

Bill Clinton

Billy —
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them out. Thanks — Bill

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incoming on
to Secretary
Albright

Today SEC
PC 340
Billy B. Goldberg

11-21-97

11-25-97

To Dan Bunkhardt for reply?

November 5, 1997

Yes ☒ *No* ☐

President Bill Clinton
Washington, DC 20500

Coordinate with NSC?
Yes ☒ *No* ☐

Dear Mr. President:

Before the '67 war, the Golan Heights belonged to Syria, and part of Jerusalem, the West Bank and Gaza, belonged to Jordan. After these areas were liberated in the war, the United Nations passed two resolutions calling for a "return" of land for peace. Those resolutions never contemplated returning the land to the Palestinians because they had never owned it. Now we find Israel negotiating with several terrorist groups that are still committed to the destruction of Israel as a nation.

I believe the direct negotiations now going on will never reach an agreement on two of the major issues -- Jerusalem and statehood. Neither side can give in. When this conclusion is reached, I suggest that you convene a conference of nations of the Middle East for negotiations for peace and democracy. I suggest it be held in Egypt and recommend to you that the Vice-President be assigned to preside over the meetings.

Here are the desirable results that I believe are obtainable under this process:

1. Golan Heights - Israel should be required to de-annex the area and that it become an autonomous territory, not a state. External security shall be provided by Syria, Israel and the United States. It shall be governed by a territorial council elected in a democratic process with women and men having equal rights. No person or family shall be barred from the territory because of their religious beliefs.

President Bill Clinton
November 5, 1997
Page 2

2. Lebanon - Over a six-month period, Israeli groups shall return from south Lebanon and Syrian troops over that same period shall be withdrawn from Lebanon. I suggest a foreign aid grant of \$25 million, taken from the funds currently going to Israel, be sent to Lebanon with their commitment to use these funds to establish a militia that will protect the borders and prevent bombings by terrorist groups.
3. West Bank and Gaza - These areas shall also constitute an autonomous territory. External security shall be provided by Israel, Jordan and the United States. The territorial assembly and municipal councils shall be established through democratic process. No one should be barred from this territory because of their religion. The territory shall be known as Palestine. It will have no capitol. It can maintain a liaison office in Jerusalem, Amman and Washington.
4. Jerusalem - Jerusalem shall remain the undivided capitol of Israel and shall belong to the Jewish people of the world. It will continue to be a democracy and recognize the property and rights of other religious groups.

I believe the nations of the Middle East will agree that the Palestinian territory cannot be a separate independent state. With no army or air force, it will be in a position like Kuwait, who didn't last 24 hours when attacked. This arrangement would not bar the Palestinian territory from someday becoming an independent nation. Over 80 percent of the West Bank is unoccupied by anyone and as an autonomous territory can encourage construction of settlements for peoples of all faiths.

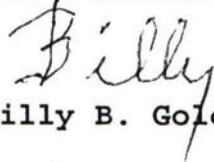
Mr. President, I have known you for a long time and I am very pleased with the support you have given to

President Bill Clinton
November 5, 1997
Page 3

✓ (Israel over many years, especially since you became President. The time has come for you and the United States to bring about a fair and democratic solution. Perhaps the final result can be for the United States and our friendly nations in the Middle East to sign a treaty comparable to NATO, which has certainly been a success.

Thank you for considering my suggestions. Rosalie joins me in sending our best wishes to Hillary on her 50th birthday. In providing strength, stability and democracy to the world, you and Hillary are just starting.

Yours sincerely,



Billy B. Goldberg

BBG/bs

INTERNATIONAL

PRESIDENT HAS SEEN

12-9-97

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International criminals, beware

If there is to be an international criminal court, how free will it be to pursue, catch and try the world's villains?

IF POL POT were ever handed over to international justice by the Khmers Rouges, the world would have a problem. Cambodia's legal system, like most of its other institutions, is in ruins. The government is no friend of the Khmers Rouges. He could not get a fair trial in Cambodia. Nor would it be easy to find a court elsewhere that would try him with even a semblance of impartiality. In leading a government that murdered perhaps 2m people, Pol Pot broke umpteen international laws, but there is not much prospect that he, or his lieutenants, will ever be brought to trial.

This week, representatives of more than 100 countries are meeting at the United Nations in New York in an effort to remedy this failure. From now until December 12th, they will be negotiating the details of a proposed new international criminal court. This would be a permanent version of the current ad hoc tribunals, set up to try people accused of atrocities in former Yugoslavia and Rwanda.

The lack of such a court has been the most glaring omission in the system of international institutions established after the second world war. It is now, say most participants at this week's talks, almost certain to be set up.

The current meeting comes after three years of negotiation. It will be followed by another get-together in March, before a conference convenes in Rome in June to agree on the final text of a treaty setting up the court. The United States and other big countries have thrown their weight behind the idea. Bill Clinton has said that he wants to see it up and running before 2000 (ie, before he leaves office).

Human-rights groups are excited at the prospect. "The court's very existence will send an important signal," argues Christopher Hall, a legal adviser with Amnesty International. "People planning truly terrible crimes will know that the international

community will eventually hold them to account." Amnesty, along with dozens of other non-governmental organisations, has been taking part in the discussions on a consultative basis.

Whether the court lives up to the high hopes of its advocates depends on how much independence, and power, it is given. About this, there is little agreement. The court's jurisdiction, procedures and relations with national courts all have to be

independent the international government Council. At one and Japan argue the examine a case only governments involve as combatants, victims accused. At the other many, most of Scandinavia and many developing countries argue that the court should be free to examine conflicts referred to it by any concerned government, thus giving it virtual independence.

The court's relationship with the Security Council could be even harder to resolve. Although America enthusiastically backs the idea of the court, it wants to exclude it from investigating crimes committed in any conflict with which the council is involved as peacekeeper. It would be "odd", argues David Scheffer, who leads the American delegation, for the court to start indicting people in a conflict which the council was trying to settle through negotiations (this, indeed, was the problem in Bosnia). Moreover, the court may have to rely on the council to enforce its decisions.

Others point out that the Security Council becomes involved in most major conflicts. The American proposal, they argue,



Sincerely

* I need a copy of this

Are we going to get this?
Should I make a public
Statement? —

Be

THE PRESIDENT HAS SEEN

12-9-97

with no more than the three "core" crimes: genocide, war crimes and crimes against humanity, all of which are defined in existing treaties. And there is general agreement that the accused will not be tried in absentia (too much like a show trial), or face the death penalty.

The most contentious points are how

interest in Singapore suggests could be the first to break ranks and sign up to it. Even America seems willing to listen. "The merit of the Singapore proposal is that it recognises the legitimate role of the Security Council," says Mr Scheffer. That sounds like an invitation to deal.

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Whether the court lives up to the high hopes of its advocates depends on how much independence, and power, it is given. About this, there is little agreement. The court's jurisdiction, procedures and relations with national courts all have to be



worked out. Germany and Italy want the crime of planning or waging aggressive war to be included in its remit; Caribbean countries want drug-trafficking included; Turkey and Tunisia want terrorism.

But a consensus seems to be emerging that, at least at first, the court should deal with no more than the three "core" crimes: genocide, war crimes and crimes against humanity, all of which are defined in existing treaties. And there is general agreement that the accused will not be tried *in absentia* (too much like a show trial), or face the death penalty.

The most contentious points are how

independent the court will be of either national governments or the UN Security Council. At one extreme, France, Russia and Japan argue that it should be able to examine a case only with the agreement of governments involved in some way, either as combatants, victims or custodians of the accused. At the other extreme, Canada, Germany, most of Scandinavia and many developing countries argue that the court should be free to examine conflicts referred to it by any concerned government, thus giving it virtual independence.

The court's relationship with the Security Council could be even harder to resolve. Although America enthusiastically backs the idea of the court, it wants to exclude it from investigating crimes committed in any conflict with which the council is involved as peacekeeper. It would be "odd", argues David Scheffer, who leads the American delegation, for the court to start indicting people in a conflict which the council was trying to settle through negotiations (this, indeed, was the problem in Bosnia). Moreover, the court may have to rely on the council to enforce its decisions.

Others point out that the Security Council becomes involved in most major conflicts. The American proposal, they argue, would give any one of the council's five permanent members a veto over the court's actions. Without independence, the court could be a mere handmaiden to the great powers, too politicised for its impartiality to be believed.

Singapore has proposed a compromise: the court would have the power to investigate any case, but would stay out of situations if the Security Council told it to. This is a much stiffer test, requiring all five permanent members to agree to tell the court to back off. Canada has suggested an amendment to the Singapore proposal under which a council command would automatically expire after 12 months unless it were unanimously renewed.

Some council members have expressed interest in Singapore's suggestion. Britain could be the first to break ranks and sign up to it. Even America seems willing to listen. "The merit of the Singapore proposal is that it recognises the legitimate role of the Security Council," says Mr Scheffer. That sounds like an invitation to deal.

ing to reject a casino application, Bruce Babbitt, the secretary for the interior, favoured Indian tribes who had contributed to the Democratic Party over some who had not. Miss Reno has until mid-February to decide whether or not to appoint an independent counsel for Mr Babbitt's case. She notes that she has already referred investigations to such outsiders six times, and "will not hesitate to do so again if the facts and the law justify it."

Similarly, it is premature to dismiss the House's investigations into campaign financing just because the Senate's eventu-

ally came to naught. Mr Burton and his colleagues may fail to engage the American electorate, but the drip-drip effect of their hearings and of the Justice Department's investigations must surely erode Democratic support before next year's congressional elections.

A more lasting danger, however, is that it will erode support for the political process. The Democrats charge that the Republicans play the same campaign-financing tunes, and that the congressional hearings are cynical attempts to keep a Republican hold on Congress during a popular Demo-

cratic presidency. Many Americans will agree with that analysis, which implies an electoral plague on both political houses.

Moreover, the institution of the independent counsel, which comes up for review in 1999, could also come into jeopardy. What seemed so sensible two decades ago now looks like an open-ended invitation to indulge in limitless investigation. Kenneth Starr, the Whitewater independent counsel, has now spent three years and over \$25m in a quest that still leaves the president and his wife in a limbo of uncertainty; David Barrett has spent two and a half years trying to determine whether the former housing secretary, Henry Cisneros, lied to the FBI about payments to his mistress. No wonder many legal luminaries, including Archibald Cox, are calling time limits, perhaps of one year, for independent-counsel investigations and a rowing of the crimes and people within their scope.

In the meantime, perhaps ever should appoint Richard Nixon as scapegoat for today's ills, real or alleged. After all, it was Watergate that led to the independent counsel act, and it was Watergate that led to the present rules on campaign financing. If those rules did not tempt sensible politicians to seek a loophole, would be far less for independent counsel to investigate.

THE PRESIDENT HAS SEEN

12-9-97

Drug abuse

Young, white and middle-class

PLANO, TEXAS

FEW towns are as aptly named as Plano. The eerily identical streets of this north Dallas suburb bring to mind the "ticky-tacky" houses of Pete Seeger's song. In the 1980s Plano had a lot of child suicides; now its young people have developed a fatal taste for heroin. In the past year 12 Plano youngsters from apparently stable middle-class families have died from heroin overdoses. One victim was black, two were Latino; the rest were white. The youngest was 14.

The heroin they are ingesting comes in a new form. Dealers call it chiva. Black-tar heroin is mixed with ordinary sleeping pills, and is sold in capsules that users break open and snort. A handsome hit costs around \$15 on the streets of Plano; smaller doses can be had for \$5. Quality varies alarmingly. "The kids are playing Russian roulette when they sniff chiva," says Bruce Glasscock, Plano's chief of police. "They have no idea how pure their powder is, or how it will affect them." Drug experts say that chiva appeals to teenagers who

In Louisiana, the chips fall

NEW ORLEANS

WHEN Louisiana legalised gambling five years ago, investors came from far and wide, expecting easy money in a state with easy morals. But involvement in Louisiana gaming seems a bit like playing craps: sooner or later, the odds will catch up with you.

The latest casualty is Edward DeBartolo Jr, owner of the San Francisco 49ers. Mr DeBartolo announced this week that he would give up his management duties with the team to concentrate on defending himself in court. His legal troubles stem from an extracurricular venture: a riverboat casino he once co-owned in Bossier City, Louisiana. Mr DeBartolo was one of six men to receive a "target letter" this week from a Louisiana grand jury, saying that federal indictments are likely to follow.

A former governor of Louisiana, Edwin Edwards, got one too; both men fiercely deny any wrongdoing. But observers believe that Mr DeBartolo's abrupt announcement is a sign that the charges are serious indeed.

The investigation appears to focus on \$400,000 in cash, which federal agents seized from Mr Edwards in April. Mr Edwards, a famous high-roller, has said the money was gambling winnings. But according to the *Times-Picayune*, prosecutors believe it was a payoff from Mr DeBartolo, in exchange for a coveted casino licence. Although Mr Edwards was out of office when the licence was won, he racked up piles of political favours in his 16 years as governor; opponents say he is still cashing in.

Louisiana gambling was born under shady circumstances. The 1992 vote for gambling in the state legislature had, some complained, been manipulated. Lucrative casino licences seemed to go to those best connected with Mr Edwards. Rumours spread about ties to organised crime. This summer, a video poker oper-



Scene of woe

ator and a former state senator were convicted of racketeering.

Perhaps partly because of this grubbiness, gambling never realised its economic promise. Casinos are successful in two New Orleans suburbs and in a few cities close to the Texas border. But New Orleans itself has proved a disappointment. Several riverboat casinos sailed away for financial reasons, and took jobs with them. A temporary land-based casino went bankrupt; the permanent version is mired in bankruptcy court.

As a result, Louisiana has become a nationwide joke in gambling circles, says C.B. Forgotston, a New Orleans anti-gambling activist. Mr Forgotston sees every trip-up as good news: fuel to kill gambling in Louisiana and stunt the industry nationwide. But others doubt that Louisiana gambling will die so easily. The industry still enjoys hefty influence and is still flush with cash; and what else could put so much easy money into the eager mitts of politicians?

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have eschewed shooting up heroin for fear of dirty needles. But most inject their chiva anyway, to get an immediate high.

The convenience of chiva is one reason for heroin's return. The other is economic. Colombian cartels have turned to heroin to claw their way back into a market flooded with cheap Mexican cocaine. Although most heroin in Texas comes from Mexico (whose drug lords offer free heroin with a purchase of cocaine to get users hooked), the Drug Enforcement Administration (DEA) says that Colombians own 60% of the American market, including almost all of the market on the east coast. Heroin is also easier to smuggle, more profitable and more addictive than cocaine. And farmers like to grow it. They can earn \$14,000 a year from a three-acre plot of opium poppies, compared with only \$4,000 for a similar-sized crop of coca leaves.

To combat chiva, Mr Glasscock has doubled his narcotics taskforce and brought in federal experts. He hopes that aggressive action will force the dealers off his turf. But, even if it does, the return of heroin is a national problem. Heroin-overdose cases in emergency rooms have nearly tripled since 1990. In Texas, the cities of Austin and San Antonio have each seen 30 heroin deaths this year. The DEA says that today's heroin, which is about 40% pure—as against 5% in the 1970s—packs a particularly dangerous punch.

The Plano deaths also highlight the rising number of young drug abusers. A University of Michigan study has found that the proportion of 13- and 14-year-olds taking drugs has risen from 11% in 1991 to 24% in 1997. A smaller Texas A&M University study found that 31% of 13-year-olds in Dallas are now dabbling in drugs.

This is depressing news for those involved in drug-education programmes. The largest such programme—Drug Abuse Resistance Education (DARE)—has taken most of the blame. DARE was developed by the Los Angeles Police Department in 1983 and is now used in 70% of America's schools. Its detractors say the programme relies too heavily on lectures from police officers, and does not teach children to say no to their peers. DARE's defenders, such as Mr Glasscock, say the problem lies not with the programmes but with lazy parents and a corrupt popular culture. When rock stars (such as members of the bands "Hole", "Sublime" and "Blind Melon") die from heroin overdoses, the effect is often merely to glamorise their addiction.

In Texas, at least, intolerance of drugs may also have a political effect. Politicians in Dallas have begun calling NAFTA the "North American Free-Trafficking Agreement". Simplification though that is, the deaths in Plano may yet cause a backlash against an open border with Mexico.

Florida politics

The second son also rises

MIAMI

IN MEDIEVAL times, primogeniture in Europe dictated that the eldest son inherited the estate and the second son went into royal service, thereby avoiding probate fights. The descendants of George Bush, a former president, are finding a different way to pass on the political mantle: the first-born son gets Texas, while the next in line tries Florida—again.

John Ellis Bush, 44 years old and known since boyhood as "Jeb", formally announced last month that he would try a second time to become the governor of Florida, the state where he has lived since 1980. He came maddeningly close to winning it four years ago when he challenged the incumbent governor, Lawton Chiles, a veteran Democrat: in his first try at public office, he came within a percentage point of victory.

His near miss was all the more disappointing because Florida, a state generally friendly to Republicans, was alone among the ten most populous states in electing a Democrat as governor that year. Mr Bush has confessed that it was "the worst hurt I have ever felt in my life." But he has shown few signs of brooding on his wounds. He returned to his successful business ventures, including the management of a professional football team, to replenish the family's funds; and with at least equal pas-

sion he took on several civic and political duties. This had the effect, intended or not, of keeping his name in the forefront of Republican contenders.

The younger Bush has copied his father by establishing a public-service organisation—the Foundation for Florida's Future—that operates on the edge of government: not a think-tank, he insists, but a "do tank". He has also become a star money-raiser for other Republicans, thereby earning their gratitude for his future endeavours. He headed Bob Dole's campaign operation in Florida last year (not a high point, as Mr Dole became the first Republican presidential candidate to lose the state since 1976) and collected more than \$40m for his father's library at Texas A&M University. Best of all, however, Mr Bush studied the election returns from his losing race as an accident expert might examine the details of a aeroplane crash. He has vowed that he will not repeat his mistakes.

The trap he fell into in 1994 (albeit of his own making) was in enabling his Democratic opponents to portray him as an ultra-conservative, in part because he chose as a running-mate a man who had been a champion of the right-wing Christian Coalition. It also hurt that he was seen as a dilettante, born to wealth and privilege and thus insensitive to the concerns of ordinary voters. This time Mr Bush is more likely to be found campaigning in Democratic strongholds—South Florida condominiums, factories and inner cities—than in comfortable suburbs or at country clubs.

He concedes his blue-blooded pedigree, but also tells interviewers that, unlike his brother, he graduated from a public college (the University of Texas) and came to Florida to earn his own way without the benefit of a trust fund. More important still, for many voters, is the fact that Mr Bush married a woman he met in Mexico as a teenager and has become a fluent Spanish-speaker, a huge asset in Miami.

He may also have softened the feminist vote by choosing as a running-mate Florida's secretary of state, Sandra Mortham, who favours choice on abortion. But most revealing of the "new" Jeb Bush may be his relations with blacks. Among the projects started by his foundation was an experimental school in one of Miami's poorest districts. Its enrolment is entirely black. Mr Bush joined the Miami Urban League, a black-led organisation, to finance and run the school in the belief that its emphasis on basic learning and discipline would make it a model for the state. So far, the experiment is working, and has drawn many other blacks to his cause.

Several opinion polls show Mr Bush to be the early front-runner. His task may be made easier by Mr Chiles's retirement. The leading Democrat is Kenneth "Buddy" MacKay, the lieutenant-governor, a well-re-



No mistakes this time

TO VP - Fgn
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LEXINGTON

THE PRESIDENT HAS SEEN
12-9-97

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In praise of preaching

FOUR years ago Christine Varney, White House staffer and proud mum, took her small son to eat in the office canteen. A hamburger later, his face smothered in ketchup, the three-year-old encountered the vice-president. Bravely risking a large dry-cleaning bill, the Veep bent down and picked up the youngster, and carried him upstairs to his office. There, seated on America's second-most powerful lap, Ms Varney's child had his first taste of computing.

That, at least, is the story as Ms Varney told it this week, in front of 500 cyber-activists. Ms Varney was introducing Vice-President Gore at her conference on children and the Internet. The audience also heard from three cabinet ministers, as well as the *illuminati* of the cyberworld; but it was easy to see why Mr Gore would choose to show up also. Here, on the very same day that the attorney-general let him off the hook for dodgy fund-raising phone calls, was his chance to appear before the cameras as a child-loving techno-saint.

But Mr Gore had other reasons for appearing, besides Ms Varney's flattering anecdote. For a conference on children and the Internet combines three things that he and President Clinton find irresistible. You can sound optimistic, futuristic, even (given America's dominance of cyber-industries) subtly nationalistic, just by uttering the word "online". You can sound sensitive and righteously tough by discussing the challenge of raising children in a dangerous world. And, most intriguingly, conferences have a special appeal to Messrs Clinton and Gore. Indeed, they have become the signature of this administration.

There is a view that lawmakers exist to make laws, and that the executive exists to execute them. This is charmingly old-fashioned. Most of the initiatives of Mr Clinton's second term do not involve legislation at all; they involve preaching. On education, the administration dares not impose national tests by law; so it urges states to adopt school tests voluntarily. On welfare reform, the administration cannot control the rate at which the indigent find work, so it challenges business executives to hire welfare mothers. On crime, the administration has no part in getting murder rates down; but Mr Clinton goes to Boston to showcase the city's success in fighting juvenile delinquency. On race, the administration cannot erase the distaste for affirmative action that dominates the Supreme Court; so it convenes a dialogue on the subject, hoping, as Mr Clinton said on December 3rd, that its effects will "spread across America like ripples from a pebble in a pond." Having held a White House summit on the early development of the brain in May, Mr and Mrs Clinton implored parents to read more bedtime stories.

Up to a point, preaching is a way of sticking a Clinton-Gore tag on things that voters approve of. Up to a point, it is a way to make the best of limited power, given a conservative judiciary, a Republican Congress, and 32 Republican governors. But it is not just that. The Clintonites sensibly recognise that many big things

in life, such as economic globalisation and technological advance, cannot be resisted by laws or other means, so they might as well be welcomed. At the same time, the Clintonites are not totally *laissez-faire*: they want to "empower" citizens, to "help people to help themselves", so that everyone is equipped to deal with inevitable transitions.

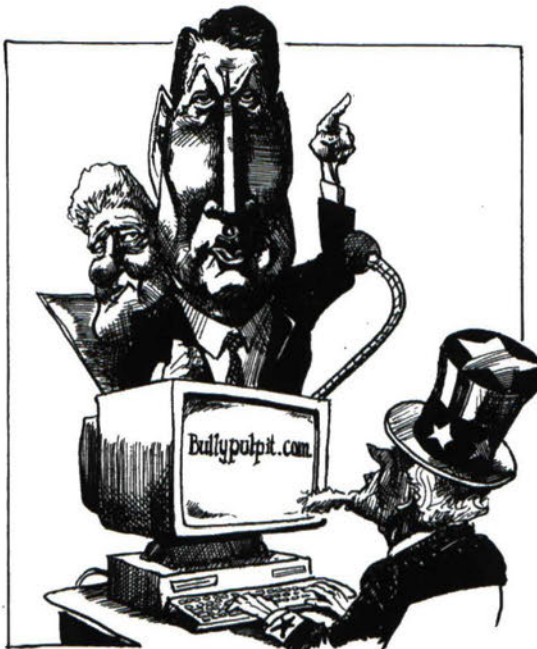
This is politically astute. Acceptance of change sets the administration apart from left-wing Democrats, who vest naive hope in laws raising the minimum wage or mandating better foreign labour practices. Meanwhile, a determination to help people face change marks the administration off from most Republicans, who show minimal concern for the losers in a market system. Having staked out this middle ground, the administration manages to be optimistic about the world, but at the same time justifies its existence by promising to improve it.

And so, in this week's speech on children and the Internet, Mr Gore waxed lyrical about the advent of the cyber age. ("The Internet allows our civilisation to take a quantum leap forward", he said, betraying his customary originality.) But good things can be improved; so Mr Gore promised a campaign to help parents introduce children to the cyberworld, while shielding them from pornography and paedophiles. The campaign has a nifty slogan ("Think, then Link"); it will involve "teach-ins" and "town-hall meetings"; it will provide parents with a "toolkit" of information. It will, in short, be a fine example of government by preaching.

As well as empowering parents, the administration challenges the cyber-industry. Back in June the Supreme Court struck down the Communications Decency Act, a law that criminalised Internet pornography. So Mr Gore now seeks to protect children by other means: he calls on software firms to produce tools that will allow parents to block off violent or pornographic sites. Since two senators are touting bills to regulate Internet indecency, the industry knows that, if it does not listen to Mr Gore, something bad might happen.

At this week's conference, companies promised a variety of tricks to help parents keep children out of cybertrouble. A new website, www.smartparent.com, offers a crash course for parents about the Net's dangerous side. The American Library Association has created an easy way for children to visit 700 tasteful websites. A throng of programmers offers filtering devices: Cybersitter, marketed by a Christian group, is said to screen out all references to sex and gays; others, with names like Net Nanny Pro and Cybersnoop, are slightly more inclusive.

Hand it to Mr Gore: this is quite impressive. The Communications Decency Act gave the job of defining decency to courts, a bad idea since decency is so subjective. The filtering software, on the other hand, places this responsibility where it ought to be in a pluralistic society, namely with parents. And so, despite its hokey side, government by conference can boast of a considerable achievement.



12-9-97

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The charitable reading of the prime minister's intentions sees last month's offer as little more than a postponement of the inevitable showdown inside the cabinet when the firm withdrawal plans, however modest, are eventually submitted. The opposition leader, Ehud Barak, has indicated that his Labour Party would provide the prime minister with the votes in the Knesset required to carry a redeployment motion against a hardline rebellion in coalition ranks, even though it fell far short of Labour's own peace policies.

Perhaps it is this prospect that has prompted America to respond less dismissively than Israeli peaceniks to the offer. Madeleine Albright, the secretary of state, was due to meet Mr Netanyahu in Paris on December 10. The Israeli prime minister has also sent envoys around the world to tell people that his government will need to

sugar—with lesser amounts spent on medicine and other humanitarian goods. In the northern (Kurdish) zone, the UN is in full charge of distribution. Elsewhere, the Iraqi government hands out the food, along with normal rations, under the eye of 140 UN observers. According to these observers, the distribution is fair and they can inspect what they want. The problem, they say, is the late and erratic arrival of the goods, the poor quality of some of it and the continuing shortage of non-food supplies.

Mr Annan calls for "a systematic review of the whole process of contracting, processing of applications, approvals, procurement and shipment and distribution". The current procedure is laborious, riddled with political pot-holes. Once the oil is sold, Iraq has to draw up contracts with foreign suppliers for the goods it needs. These con-

do it while the row about weapons goes on. The chances are that it will do so after a further report by Mr Annan in February.

On December 3rd a council statement called on Iraq to allow its weapons inspectors unimpeded access to all sites. The statement also encouraged the inspectors to "intensify" their efforts to close the files on Iraq's weapons of mass destruction. It did not set a timetable. The matter is now in abeyance until Richard Butler, the top inspector, goes to Iraq on December 13th.

Bahrain

Sheikhly fall-out

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Iraq

Still hungry

SANCTIONS after seven years on Iraqi oil sales, only uncrushed ganga part, are imposed by UNIC children under be chronically to alleviate suffering, while keeping sanctions in place, the Security Council invented, and the Iraqi regime eventually accepted, an oil-for-food deal under which Iraq sells \$2 billion-worth of oil over six months and receives food and medicine in return. This week, after sharp altercations with Iraq, the council was on the point of agreeing to a third six-month period, on the same terms. Is the scheme working?

Up to a point. The deal, unprecedented and complex, has taken a long time to get off the ground. Some of the goods from the first six-month phase have still to reach Iraq; the Iraqis claim that they have so far received only 5% of goods ordered in the second phase. In his report on the first year of operations, Kofi Annan, the UN secretary-general, admits that, as yet, the scheme has made little noticeable difference: infant mortality is still high, food rations inadequate, drugs desperately short and safe water beyond many people's reach.

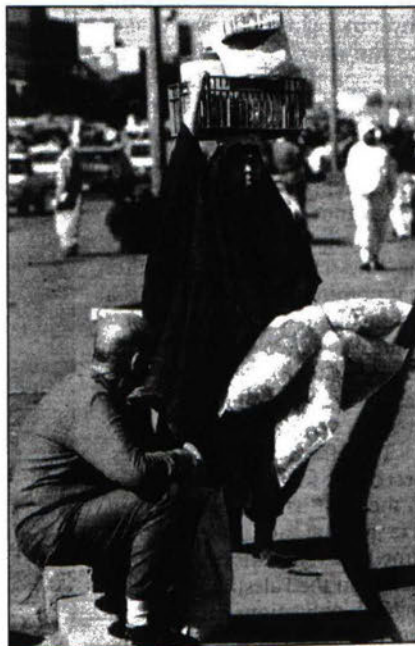
A proportion of the oil money goes into a compensation fund for Iraq's victims in the Gulf war. The bulk of it goes on food—wheat, rice, pulses, vegetable oil and

THE PRESIDENT HAS SEEN

12-9-97

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Short rations for the family

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The crown prince and the UAE's ruler share many interests, including camel racing and Arab verse. So Sheikh Hamid was disposed to listen when Sheikh Zayed urged reconciliation with the London-based Bahrain Freedom Movement—and offered, if this happened, to help Bahrain's impoverished countryside.

Before Iraq disgraced itself by invading Kuwait, Sheikh Khalifa tended to look to Saddam Hussein as model. Sheikh Hamid, fearing that his uncle's hard line will radicalise the opposition's still relatively restrained call for political rights, prefers to look for example to Jordan's King Hussein. But mounting international criticism, most recently by the European Parliament, of the regime's repressive methods has small effect on a government that banks on support from America (Bahrain is host to the Fifth Fleet) and Saudi Arabia, itself anxious about Shia radicalism.

12-9-97

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Perhaps it is this prospect that has prompted America to respond less dismissively than Israeli peaceniks to the offer. Madeleine Albright, the secretary of state, was due to meet Mr Netanyahu in Paris on December 5th. Israel's prime minister has also arranged to meet Germany's chancellor and France's president, and has sent envoys around the world to persuade people that his peacemaking zeal is sincere. They'll need silver tongues.

Iraq

Still hungry

SANCTIONS are a crude instrument. After seven years of a United Nations ban on Iraqi oil sales, Saddam Hussein is brazenly uncashed but his people, his own gang apart, are in a bad way. A survey, sponsored by UNICEF, shows one-third of all children under five, nearly 1m of them, to be chronically malnourished. In an effort to alleviate suffering, while keeping sanctions in place, the Security Council invented, and the Iraqi regime eventually accepted, an oil-for-food deal under which Iraq sells \$2 billion-worth of oil over six months and receives food and medicine in return. This week, after sharp altercations with Iraq, the council was on the point of agreeing to a third six-month period, on the same terms. Is the scheme working?

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Mr Annan calls for "a systematic review of the whole process of contracting, processing of applications, approvals, procurement and shipment and distribution". The current procedure is laborious, riddled with political pot-holes. Once the oil is sold, Iraq has to draw up contracts with foreign suppliers for the goods it needs. These contracts are then examined by the Sanctions Committee, which has the same country membership as the Security Council. Approval has to be ultra-careful because Iraq, up to tricks as always, sneaks in items that could, at best, have a dual use.

The troubles continue when the goods reach Iraq, largely because everything there is so run down. Transport, or rather the lack of it, turns out to be a major problem. And the collapse of basic facilities often undermines the purpose of the scheme: what use, for instance, is it to send chlorine to purify water if the pipes the water has to flow through are poisonously polluting?

Even if the supplies arrived on time, says Mr Annan in his report, they would be insufficient "to address, even as a temporary measure, all the humanitarian needs of the Iraqi people." The Security Council agrees, in principle, that the size of the deal should be increased but is not prepared to



Short rations for the family

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Bahrain

Sheikhly fall-out

MANAMA

BY ORDERING the trial of eight leading Shia Muslim activists, Bahrain's prime minister, Sheikh Khalifa al-Khalifa, may have put paid to any early hope that the country's four-year-old troubles can be settled peacefully. At the end of last month, a state security court sentenced the eight *in absentia* (five of them live in London) to prison terms of five to 15 years. The charges were that they had spied for an unnamed foreign country (meaning Iran) and wanted to see the Sunni rule of the al-Khalifa family overthrown. Such charges are hard to refute. In any event, the eight were denied legal representation.

Sheikh Khalifa in effect runs Bahrain, although his elder brother, Isa al-Khalifa, has been ruler since 1961. He may have decided on the trial to undermine his nephew, Sheikh Hamid al-Khalifa, who is the ruler's heir. Sheikh Hamid, who hopes to inherit a less troubled little island-state, had been encouraged towards a political settlement by Sheikh Zayed, the president of the United Arab Emirates.

The crown prince and the UAE's ruler share many interests, including camel racing and Arab verse. So Sheikh Hamid was disposed to listen when Sheikh Zayed urged reconciliation with the London-based Bahrain Freedom Movement—and offered, if this happened, to help Bahrain's impoverished countryside.

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Mr. President has left
12-9-97

For the former Governor of Alabama July 30, 1997

Wintley Phipps' proposal

If prisoners get a college education recidivism drops from 60 per cent to less than 15 per cent. The most likely prisoners of the future are the children of prisoners. We can educate the former and identify the latter.

We need a commitment to engage the historically black colleges and universities in distance learning to bring education to every prisoner and then bring a job opportunity to every educated prisoner. (A virtual black university that would also have tremendous potential for helping in sub-Saharan Africa.)

We need an on-line faith-based academy for the at risk children and in particular for the children of prisoners. Angeltree can identify today one million children of prisoners who could be helped.

The key is to combine four building blocks:

1. Faith
2. Parenting or Mentoring
3. Learner-focused Information age technologies in their homes
4. Incentives and a belief their future can be better

Part of this project has to be private (faith-based) but much could be public.

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we need to disassemble
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up the prison system/patterns
of imprisonment in the shape
they're in now
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THE PRESIDENT WAS SEEN
12-8-97

THE WHITE HOUSE
WASHINGTON

December 1, 1997

MEMORANDUM TO THE PRESIDENT
FROM RAHM EMANUEL
SUBJECT CRIME SPEECH

Attached are two memos that Mark Kleiman prepared on crime and drugs. As I mentioned in my weekly report last week, I believe that you should deliver a speech outlining our efforts on the issues of crime and drugs. The speech would not put forth specific initiatives or policies but mark your overall philosophy based on what we have learned fighting these issues over the past five years. I think that the speech should be intentionally controversial. It should attack both the left and the right and should be written to create a debate on the issues of crime and drugs.

If you agree I can begin to work on getting a date on the schedule for such a speech.

[Handwritten signature]

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Emanuel

THE PRESIDENT WAS SEEN
12-9-97

To VP - There are
worth leading
[Signature]

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(310) 206-3234 Voice
(310) 206-0337 Fax
kleiman@ucla.edu

To: Rahm Emmanuel
From : Mark Kleiman
Re: Targeted Zero Tolerance and Crime Control
Date: November 6, 1997

Central point:

Using only existing knowledge and resources, the country could have a much smaller crime problem three years from now than it has now.

The important new idea is "targeted zero tolerance," also known as "getting deterrence right." It can work at the neighborhood level, focused on the petty crimes that create the atmosphere for major crimes (e.g., some of Bill Bratton's initiatives in New York), or at the level of the individual offender or offender group (e.g., the Boston Youth Gun Project and coerced abstinence for drug-involved offenders).

Either way, the three keys are focus, communication, and follow-through.

Focus means picking specific behaviors for zero tolerance and, where possible, identifying the individuals or groups most likely to engage in them. Communication means telling those people precisely what won't be tolerated and precisely what will happen to them if the lines are crossed. Follow-through means delivering the promised sanction every time. This requires using the resources and powers of all the elements of the criminal-justice system: not just police, but probation, parole, prosecutors, courts, juvenile authorities as well; not just the locals or the feds, but everyone together.

Key organizing ideas:

Disorder makes neighborhoods vulnerable to serious crime. Controlling disorder prevents serious crime.

Most serious offenses are committed by a small number of people. Controlling their behavior is therefore essential. It is also feasible, precisely because they are so active and thus so vulnerable to enforcement focus. Multi-offending and

probation/parole status make high-rate serious offenders manageable, if the system works in a coordinated fashion to use those handles. That rarely happens now.

Deterrent threats need to be communicated to the people they are intended to deter, on an individual, "This Means You" basis where possible. The threat needs to be specific about what behavior will trigger a response and what the response will be. Arrests and sentences are very poor communications channels. Don't strike the rock, talk to the rock.

Most offenders are reckless and impulsive. Low-probability deferred threats of serious punishment sometime in the future bounce off them (otherwise they wouldn't be offenders). We need high-probability threats of immediate punishment; if we can deliver on those, behavior will change even if the punishments aren't severe.

The resources of the police and the rest of the criminal justice system can't deliver sanctions for every violation of every law by every person. But they can deliver effective zero tolerance for specified violations by specified people.

Controlling group offending (as represented by youth gangs) requires group-level accountability. Tell the whole group that if any member commits a specified act (such as shooting someone) the whole group will become a zero-tolerance target with respect to any offense, no matter how petty. Then let the groups control their own members.

A convincing threat can deter much more behavior than could actually be punished. How does the mythical Texas Ranger face down an angry mob when he has only one bullet left in his gun? By letting everyone know that the first one who steps forward will get shot. No one wants to go first.

Neighborhood version:

Crime is going down for many reasons: more cops on the street, more high-rate serious offenders in prison, good people in high-crime neighborhoods getting together to stop the carnage.

We're also getting smarter about controlling crime. Community-based, problem-oriented policing has penetrated more and more deeply into the daily life of police departments around the country, thanks in part to the community policing requirement attached to the COPS grants but in greater part to the growing understanding among police officers and the leadership of police departments that community policing is the best way to do the job of crime control.

One of the key ideas behind community policing is "fixing broken windows." By refusing to tolerate low-level acts of disorder (vandalism, graffiti, public drunkenness, retail drug dealing) and by cleaning up physical signs of decay, we can send a signal to all potential violators that this block, this corner, this neighborhood are not places where "anything goes." That turns out to have a powerful effect on serious crime.

But simply announcing a blanket zero-tolerance policy is an empty gesture, and all the offenders know it even if the pundits don't. There's no way any police department could make an arrest every time some local ordinance is violated, and if they tried the result would be to gridlock the courts. What Bill Bratton's troops did in New York was to focus on a few specific kinds of disorderly activity: some city-wide, like "squeegeeing," but most on a precinct-by-precinct basis. The choice of behaviors for local zero tolerance was made by precinct management, in consultation with neighborhood residents and business owners. In every case, the target behaviors were well-publicized in advance. The goal was not to maximize the number of arrests (that's the idea behind "sweeps") but to get the level of the targeted activity as close as possible to zero as quickly as possible, using the minimum number of arrests necessary.

This variety of targeted zero tolerance makes neighborhoods more crime-resistant. Learning how to make it happen is a central element of doing community policing well.

Offender/group version:

Most serious crime is done by a relatively small number of offenders. Most of them are active in a wide array of crimes, large and small, and many of them are on probation or parole when not in prison. Multi-offending and conditional release give the criminal justice system potential handles that can be used to suppress the serious stuff, but traditionally those handles haven't been used very well; the fact that the police think that a particular probationer is behind a string of robberies tends not to influence how his probation officer handles him. Just recently, practitioners have learned how to use them in a different version of targeted zero tolerance, and the results have been spectacular.

The Boston Youth Gun Project identified about 1300 juveniles and young adults in 60-70 gangs as being responsible for virtually all of the youth gun homicides in Boston. The gangs were called in, one-by one, as groups, for meetings involving the gang unit, the drug unit, the Department of Youth Services, probation, the District Attorney, the State Attorney General, the U.S. Attorney, and the DEA and BATF.

Each gang was given the following message:

1. We know who you are.
2. We know what you're doing, and most of it is illegal. You're playing hooky, you're violating your probation curfews, you're stealing, you're selling marijuana, you're drinking out of open containers, you're driving unregistered cars, whatever.
3. We can't stop all of you all the time.
4. We can stop any of you anytime we want. If all of us work together to enforce all of the laws and probation conditions you guys violate, you won't be able to function for a day. This doesn't mean we're going to violate your rights or harass you; it just means that every time one of you does something illegal he's going to pay for it. You won't have any fun or make any money.
5. Here are the rules: Nobody gets shot. Nobody gets stabbed.
6. If you violate the rules, we'll know. We know who is feuding with whom, and if someone from the Elm Street gang show up with a hole in him we'll know it was one of you Beech Street guys.
7. At that point, we're all over you like a cheap suit, and we won't let up until you say "uncle" and turn in all your guns.
8. There's no deal here: just a threat. As long as you keep doing illegal stuff, you're vulnerable to arrest or other sanctions, and we're not giving you a pass. But if you break the rules, we promise you'll pay for it.

After this series of meetings, there were two shootings (neither fatal). In each case the gang involved was identified and targeted. In each case, they eventually gave in and handed in their guns. The task force then went to all the adjacent gangs, explained that Gang X had broken the rules, been spanked, and had now knuckled under, and explained further that any act of aggression against Gang X would subject the gang responsible to the same treatment. This was perhaps the key move: making it safe to disarm.

One especially violent outfit that made it clear they didn't intend to comply was taken out by a DEA undercover operation that will have all its key players doing long federal sentences, except for the ones who wind up doing even longer state murder sentences based on one another's testimony.

There hasn't been a youth gun homicide; over that period, the expected number would have been more than thirty. Everyone is breathing easier; not only juveniles, but adults, are less prone to carry guns now that the gangs are no longer shooting up the town.

A similar program in Minneapolis, started this summer, has had similar results. At the individual-offender level, Lowell, Mass., targeted the sixty people most active in committing aggravated assaults, and the rate of that crime fell by two-thirds. An earlier, less formal project brought homicides in

the Chicago's Cabrini-Green housing project down from more than 100 per year to fewer than five. This isn't just a cute idea anymore; it works, and we know how to do it.

This approach is not an alternative to community policing. It assumes that the police have detailed knowledge of who is doing what to whom, a focus on problem-solving rather than arrest-maximizing, and a broad definition of their mission and their potential allies. All of these are characteristic of community-policing departments.

Coerced Abstinence for Drug-Involved Offenders

Reducing drug use and crime by drug-involved offenders on probation and parole by requiring abstinence from illicit drug use, frequent drug tests, and immediate sanctions for violations relies on the same logic as other targeted deterrence programs: specifying behavior to suppress, singling out a group to be forced to comply, and using certainty and swiftness rather than severity to control their behavior.

Administration role:

These programs don't usually need much outside money or manpower; the idea is to focus the resources already present. They do need, or at least benefit from, cooperation by the U.S. Attorneys and federal enforcement agencies, but that has been forthcoming. (Boston started out as a Treasury Enforcement initiative.) DC would be a good testbed, but not until it has a functioning police department.

It would be useful to have some funding for conferences, training, and, most of all, technical assistance. Small dollars, big impact.

But the real opportunity is to put the concept in the public eye, with everybody leading the cheers: the President, the AG, the VP, Louis Frech (maybe), Ray Kelly. "Getting deterrence right" puts some meat on the bones of being smart rather than just tough. Or rather, it shows how to be tough intelligently and compassionately, and elides the distinction between "enforcement" and "crime prevention" by using enforcement to prevent crime.

Lots of outside people would happily sing in the choir: Bratton himself, who would love some opportunities to get back into the national media, Paul Evans, the Boston Police Commissioner, other police chiefs and prosecutors, mayors like Rendell in Philadelphia and Goldsmith in Indianapolis, academics such as Blumstein, Wilson, and DiIulio. This stuff, especially the Boston story, makes great press and could generate lots of columns, talk shows, etc., if the Administration helps give it a high profile. Jeremy Travis at NIJ would gladly help on the research.

and research-promotion end. (I've got a panel on the topic at the American Society for Criminology meetings in San Diego two weeks from now, and can help lay the groundwork.)

1/11/98 [A very ambitious version of this could involve a White House Conference on Crime Control where the new gospel would be preached. The point would be to say that crime control is no longer something that would be nice if we could get it; it's now available if we just do what we know how to do. One result would be to leave the pure lock-'em-up types on the Hill looking shrill and irrelevant.

Given that crime control is possible, it gets to be the centerpiece of any serious assault on urban poverty. Of all public services, protection from serious crime is the most unequally distributed by race and class, and the level of crime risk in urban poverty areas is one major reason why jobs there have been disappearing for a generation. As long as there wasn't anything sensible to do about it, there was no point explaining how nice crime control would be if we knew how to do it. But now we know.

Declining crime numbers make a good context for this, but we shouldn't bank too heavily on them. What goes down may come back up, and the demographics over the next decade are strongly against us. The best use of the good news is to make some political space for really intelligent crime control policy.

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A THIRD WAY IN DRUG ABUSE CONTROL

Mark A.R. Kleiman

Much of the damage now done by drug abuse, drug dealing, and drug control efforts in the United States is avoidable. Using only existing knowledge and resources, the nation could have a much smaller drug problem five years from now than it now has. That conviction stands behind a new effort mounted by the Federation of American Scientists and endorsed by some forty experts in drug research, drug policy analysis, and law enforcement. Its first effort was the publication of a set of fourteen "Principles for Practical Control Policies." [See box for excerpts and a list of signers.]

Along with Robert MacCoun of the Graduate School of Public Policy at Berkley and Charles R. Schuster of the Wayne State University Medical School, I helped organize the group and draft its first statement. We plan to organize a number of working groups to prepare detailed policy statements on a number of specific topics, including sentencing, retail law enforcement, treatment, and alcohol regulation.

This essay reflects some of the thinking behind that project. However, while the Principles statement was so thoroughly collaborative an effort that it is no longer possible to assign individual authorship to its sections (the penultimate draft bore the heading "Draft S" and a date almost nine months later than the date of "Draft A"), what follows is very much an individual statement and is the responsibility of its author alone.

"Hawks," "Doves," and the Struggle over Drug Policy

The major barrier to more effective drug control policies is that effectiveness - measured in terms of damage control - is not at the center of policy-making in this arena. Discussion has instead been dominated by a strongly ideological polarization about how to deal with the subset of abusable, addictive, and/or intoxicating substances that also are illegal (or restricted to medical uses alone). At one pole are the advocates of stricter controls, increased enforcement, harsher punishment, and school-based and mass-media efforts to "denormalize" non-medical consumption of those substances: advocates, in the unavoidable jargon phrase, of a "war on drugs." At the other pole are those who are more afraid of anti-drug efforts than of drugs, who therefore favor relaxed controls. In the logical extreme, this tendency

points toward repeal of the controlled substances laws themselves, that is, "legalization."

The stylized combat between "warriors" and "legalizers" is convenient, both for journalists and office-seekers and for the partisans at the two polar extremes. For journalists, it provides an easy set of categories and a source of battling quotations or dueling experts. For office-seekers, it sets up a no-lose situation. Since support for legalization, even of cannabis, remains safely below the 25% mark, if the only options are "drug war" or "legalization" the choice isn't a hard one. For the partisans, the actual horrors of the current situation serve as a firm rhetorical basis from which to attack the other side: as testimony to how much evil would be averted by repeal or, from the other viewpoint, as a both reminder that half-measures are inadequate (there is no substitute for victory) and a faint indication of the extent of the damage illicit drugs would inflict if made even more widely available by legalization.

Against these conveniences of the warrior/legalizer analysis of drug policy must be set some disadvantages. By focusing on the currently illicit substances, it removes from the debate over "drug policy" the question of what to do about alcohol, which entraps several times as many addicts and accounts for considerably more crime, disease, fetal damage, and death than all the illicit drugs combined, and about nicotine in cigarette form, which while not intoxicating is astonishingly addictive and roughly doubles the mortality rate of its addicted users at any given age. Excluding them from the debate makes it possible to be strongly against "drugs" without supporting higher taxes on beer or cigarettes. But thinking about drugs while excluding alcohol and nicotine is a little like thinking about oceans while ignoring the Atlantic and the Pacific. For each of these licit substances, control measures (not the same ones) well short of those now applied to the "controlled substances," and not requiring even a fraction as much enforcement effort, could prevent enormous suffering among users and non-users alike.

The warrior/legalizer polarization also conceals the reality that neither an unreflective tightening nor an unreflective loosening in current measures aimed at the illicit drugs is likely to improve matters. The shape of the function relating total social damage to the overall tightness of drug controls remains not merely an unexplored question but an unasked one. In particular, how it slopes near the current level is quite unknown. In the abstract, there is no reason to think either that doing more of the same will produce a radically better result or that, where a fairly heroic dose has failed to cure, a homeopathic dose will succeed. But there is every reason to think that a variety of changes, some in the direction of tightening and others in the direction of loosening, would markedly improve the overall situation.

The metaphor of "drug war" has, perhaps inevitably, generated "hawks" and "doves" as an alternative set of labels for the two poles. These labels have stuck in part because this version of the struggle over drug policy is conducted along substantially the cultural and ideological fault lines that characterized the anti-war movement. The pro-war/short-hair/jock world view and sensibility are as recognizable at meetings of drug-war "hawks" as the anti-war/long-hair/hippie world view and sensibility are at gatherings of those who call themselves "drug policy reformers." (Even back then, someone suggested that at least the on-campus aspect of the Vietnam issue had less to do with "hawks" and "doves" than with "jocks" and "freaks.")

In this instance, however, the hawks have had very much the better of the political confrontation. While discontent with the performance of the anti-drug effort is quite widespread, the legalization option has consistently failed to catch the public imagination other than as a bogey-man. Legalization advocates draw some comfort from the widespread support they enjoy among some elites, noticeably academic economists and law professors, and the unmeasured but substantial "underground" legalization constituency among judges, prosecutors, and police; they can also reflect that support for the Eighteenth Amendment remained strong until almost the end, and hope for a comparable turnaround as a result of a major scandal or the sudden accession of a few very prominent leaders to their cause. In the meantime, however, the public doesn't seem to be at all receptive. The political sociology and psychology of why this should be so is a fascinating question, but the situation stands, with no current hint of any substantial change.

Moreover, the drug-war doves have consistently failed to come up with any coherent description of post-prohibition control regimes or any plausible predictions of the extent of drug abuse and drug-related damage under alternative policy scenarios. They tend to assume new regimes with the magical property of exerting all the consumption-reducing powers of the drug war with none of its costs. Their speeches and publications tend to be long on horror stories about the present and future if prohibitions are maintained, but short on the details of the "taxes," "regulations," "educational campaigns," and programs to abolish poverty and racism that are to replace those prohibitions. To unsympathetic ears, they sound like nothing so much as Marxists asked what practical arrangements are to replace capitalism or libertarians asked how, precisely, the minimal state is to handle air pollution and the maintenance of city streets or keep the improvident and unfortunate from starving. In particular, the drug policy reformers, like their drug-warrior opponents, have been virtually silent about how to control the carnage and other suffering associated with the currently legal drugs.

Thomas Szasz continues to say what he has always said - that an unregulated market in psychoactive drugs would lead to a substantial increase in the number of people who severely damage themselves with such drugs, and that such an increase is a price worth paying for freedom - but he remains cheerfully marginal, with few drug-war doves capable of matching his clear-mindedness or willing to copy his apparent hard-heartedness.

Harm reduction as slogan and policy

With the legalization campaign largely bankrupt both politically and intellectually, the anti-prohibition forces have fallen back on a strategy of piecemeal attacks on current policies, under the general rubric of "harm reduction." As a result, this innocent-sounding label has become highly ideologically charged.

To understand how it is that someone could be against "harm reduction" requires a little simple algebra.

Let us imagine that the total damage done by drugs and drug control efforts under a given set of policies and surrounding social conditions could be measured as a single quantity. Call that quantity D , for (total) "Damage"; it might be measured in lives, or dollars. Imagine also a single number measuring the extent of drug use; it might be the total number of dosage units consumed, or the total number of users, or some more complicated measure. Call that quantity U , for "Use." Dividing D by U , we have the ratio of damage to use, which we can think of as a measure of the tendency of drugs, under those policies and social conditions, to create damage; call that H , for "Harmfulness."

Concretely, imagine society X in which the use of alcohol is widespread, and society Y in which it is rare; if the total damage D associated with alcohol in the two societies were equal, we would say that alcohol is more harmful in Y than in X , because the ratio of aggregate damage to use is higher. Prohibition of alcohol, for example, would be expected to reduce use but increase the rate of harmfulness in a variety of ways, from creating illicit markets to weakening informal social controls of moderation in drinking. To a lesser extent, so would heavy taxation, which would shrink consumption by increasing price but at the same time make any given level of drinking that much more difficult economically for low-income heavy drinkers. Conversely, lower taxes, or the repeal of prohibitions, would be expected to increase use but reduce harmfulness. In each case, much would depend on the details of policy and of user behavior; more than abstract theorizing is required to determine whether a particular policy would push aggregate damage up or down.

To favor drug control policies that minimize total damage is merely to apply to the drug problem the general rule of policy analysis dictating that policies be judged by their (likely) results. Holding use constant, anything that reduces harmfulness ought to be welcome, since if U is fixed and H falls, $D = U \times H$ must fall in proportion.

But that is precisely the fly in the "harm reduction" ointment. There is no reason to think that drug use, however measured, is a fixed quantity in the face of policy changes. In general, if those who use drugs are at all rational, one would expect that any reduction in the harmfulness of drug-taking to them would lead, all else equal, to an increase in the level of use. So it will not in general be true that reducing harmfulness will reduce aggregate damage; that will be true only if a given reduction in H does not lead to a more-than-proportionate increase in U .

Of course, any given program to reduce harmfulness (what MacCoun has called "micro harm reduction") may in practice contribute to reducing aggregate damage ("macro harm reduction"), even if it were to increase use somewhat. I can think of several good candidates, including the familiar "designated driver" campaign (which aims to reduce not drinking, or drunkenness, but only the probability that a given drinking incident will lead to a car crash) or changes in law and police practice designed to reduce the extent of needle-sharing among injection drug users. Many "doves" believe, sincerely and not unreasonably, that current policies tend to over-emphasize reductions in drug use at the expense of opportunities to reduce harmfulness. But those who interpret "harm reduction" in terms of micro harm reduction alone reject out of hand any policy that would reduce aggregate harm by reducing use, and it is hard to believe that no such opportunities exist. This has fueled suspicion among drug war "hawks" that the "doves" are merely trying to seize a fine-sounding slogan, especially in light of the indiscreet statement by the head of a prominent "drug reform" group that "Harm reduction is what we're calling legalization now." Those who favor macro harm reduction - minimization of aggregate damage - are left with an unpleasant choice between abandoning a useful term to the harmfulness-minimizing extremists or using it and risking being confused with them.

But the fury with which the drug warriors have attacked "harm reduction" as an idea is not entirely attributable to this suspicion, or to the perhaps justified concern that measures intended to reduce harm without increasing use will go awry. Just as many of the micro-oriented "harm reduction" advocates oppose attempts to reduce aggregate damage by reducing use, many "use reduction" advocates oppose attempts to reduce aggregate damage by reducing harmfulness. Psychologically, there is no great distance between thinking that drug use is a dangerous practice and ought to be discouraged in order to avert harm and feeling

that drug use is an evil practice whose practitioners deserve all the harm that can be made to come to them. The generational and cultural baggage which the drug issue carries merely adds to the tendency for disapproval of drug use to shade over into hatred of drug users and dealers.

The political controversy over needle exchange programs illustrates this phenomenon. Several careful studies have found that exchange programs not only reduce HIV transmission but increase the rate at which participants enter treatment, and there is no evidence whatever that needle exchange does anything to increase the rate of needle initiation or the consumption rate among those who do inject. Yet the Congressional ban on funding such programs remains, and the relevant officials remain unwilling to provide the certification of benignity that would clear the way for such funding.

It is possible to be unenthusiastic about publicly-supported needle exchange efforts on pragmatic grounds. There are several reasons to think that small-scale, voluntary efforts might outperform large-scale publicly funded ones. Other means of outreach to injection drug users might be equally effective in changing behavior while creating much smaller political problems. Changes in police practice independent of needle exchange - especially the cessation of arrests for possession of injection equipment - might have comparable potential for changing sharing behavior. Even the scientific evidence, while unanimous, is not quite conclusive.

But it is not on these grounds that the Helms Amendment rests. The Archangel Gabriel could appear on the Senate floor with a scroll written in letters of fire attesting to the fact that needle exchange reduces drug abuse as well as disease transmission without noticeably changing the politics of the situation. It is the sense that needle exchange represents a compromise with heroin addiction, rather than any actual undesirable side-effects it might have, that keeps it controversial. It would be unkind, but not unfair, to say that the continuing opposition to needle exchange programs expresses a preference that injection drug users who cannot or will not quit should die, as painfully as possible.

Only by liberating ourselves from the illusions of "harm reduction" in its harmfulness-fixated "micro" sense and "use reduction" as preached by those who still pretend to believe that America could become "drug free" can we develop practical policies to shrink the total damage drug abuse, drug dealing, and drug control measures do to individuals and institutions.

Prevalence Measurement as a Policy Trap

The dominance of the "use reduction" viewpoint is both illustrated and reinforced by the extent to which measures of prevalence, especially the prevalence of self-reported illicit drug use among adolescents, as measured by the annual Monitoring the Future surveys, dominate public discussions of the effectiveness of drug control policies. That dominance is unfortunate for at least three separate reasons, even putting aside concerns about the accuracy of self-reports not verified by any chemical test:

- Prevalence in the use of any drug is a poor proxy measure for aggregate damage. Most users of most drugs (cigarettes and heroin are the prominent exceptions) are occasional users, suffering little damage, doing little damage to others, and contributing little - even in the aggregate - to the illicit markets. The highly skewed distribution of drug consumption means that a relatively small number of individuals on the right tail of the distribution account for most of the activity and most of the damage. If the shape of the distribution were fixed, reducing the total number of users would reduce the size of the right tail proportionately, but there is neither theory nor evidence to suggest such a fixed relationship. Thus, for example, the dramatic decrease in the prevalence of cocaine use since 1986 has not been accompanied by any detectable shrinkage in volume consumed or aggregate damage: rather, volume and damage continued to rise until about 1989, even as prevalence fell, and at best have fallen slightly since despite sharp continuing declines in prevalence.
- Illicit-drug prevalence numbers, especially among adolescents, are dominated by those who use marijuana only, and relatively modest amounts of that. While the damage associated with heavy, chronic marijuana use is far from negligible, aggregate marijuana-related damage represents a small proportion of the total illicit-drug problem. Again, if there were a fixed proportion between cannabis use and the use of more dangerous drugs, as postulated by the strong form of the "gateway hypothesis," or even if there were some weaker tendency for marijuana use to increase vulnerability to the use of harder drugs, shrinking the number of adolescent cannabis users would be a powerful way to reduce total drug-related damage; but again, there is no convincing theory nor evidence to suggest that the observed correlation between marijuana use and the use of other drugs has any causal significance.
- Like other fashions among adolescents, the use of various psychoactive substances varies wildly over time, for reasons very imperfectly understood and in patterns not easily manipulated. Even as apparently substantial an intervention as the decriminalization of marijuana by several states in the 1970s seems to have left very little measurable trace on rates of adolescent marijuana

use in those states. The relationships between current policies, especially at the national level, and prevalence rates are probably even weaker, and in any case entirely obscure. Thus using the Monitoring the Future numbers as scorecards for the performance of the current national Administration is utterly inappropriate.

The Means of Drug Abuse Control

Conceptually, the elements of explicit drug abuse control policies can be listed under five headings:

Legal restrictions on supply and consumption (regulation, taxation, prohibition);

Law enforcement to give effect to those restrictions;

School-based, community-based, and mass-media efforts to persuade potential drug users not to start (called, conventionally but not quite accurately, "prevention"); and

Efforts to persuade, help, and coerce current users to cut down or quit (conventionally but again inaccurately, "treatment").

To this catalogue must be added an often-omitted fifth category: policies not aimed directly at explicitly at drug abuse control, but whose operation serves to reduce drug-taking or its unwanted consequences. (One way to reduce drunk-driving fatalities is to build safer cars and highways; better job opportunities, or stronger conventional values - if we knew how to provide either one - might reduce drug dealing among poor adolescent males.)

Understanding the roles and limits of these elements in reducing drug damage is the meat of drug policy analysis as a practical enterprise. That understanding is made difficult by a combination of genuine complexity, ideological preoccupation, and organization and professional self-seeking.

While the oversimplified categories of "licit" and "illicit" break down under close examination - sufficiently high taxes or tight regulations are not practically distinguishable from prohibitions - laws restricting availability and increasing price are nonetheless of great importance. Relatively modest changes in price levels brought about by taxation have measurable impacts on consumption of alcohol and nicotine, and especially on initiation rates among the young. Prohibition, even in the absence of aggressive enforcement, tends to suppress consumption not merely

by increasing prices but by decreasing the ease of access, especially for new users. These effects - what Peter Reuter has called "the structural consequences of product illegality" - are illustrated both by American alcohol prohibition and by Dutch cannabis policy, where despite the *de facto* legalization of the retail trade the price of a gram of cannabis is not markedly lower than in the United States.

Once a drug is prohibited, and that prohibition is enforced sufficiently to prevent flagrant retail distribution, the potential contribution of additional enforcement to reducing its consumption may not be very large. That potential is greatest for drugs which have not yet achieved mass-market status and in "border" zones between areas where more or less open illicit distribution flourishes and areas where such distribution is absent. In general, however, the phenomenon of market replacement - new dealers entering the trade or current dealers expanding their business to fill the market niches left by dealers deterred by enforcement or incapacitated by imprisonment - puts strict limits on the value of enforcement as a means of drug abuse prevention.

~~X~~ What well-designed and competently-executed enforcement can do, however, is greatly reduce the neighborhood impacts of illicit markets, by creating pressure on dealing organizations to deal discreetly and to avoid the employment of adolescents and the use of violence. Careful economic and operational analysis can identify specific tactics to put identified open markets out of business. Enforcement aimed at maximizing the number of arrests or the number of felony convictions, and sentences based largely on drug quantities and such irrelevancies as being within some given distance a school, sacrifice these opportunities. For example, there is a federal statute creating an enhanced sentence for a dealer who employs a minor, but the quantity-based mandatory sentences are so harsh that the enhancement is very rarely pursued, leaving dealers with no effective incentive to avoid minors as employees.

The anti-drug persuasion effort (usually referred to as "prevention," as if the laws and their enforcement did not serve to prevent drug abuse) is virtually everyone's conceptual favorite. The problem is learning how to do it, actually implementing programs that successfully replicate proven prototypes, and finding out whether the effort worked. The first two would be enormously difficult in any event, but that difficulty is multiplied by the enormous complexity of the last. Since severe substance abuse disorder (especially involving illicit drugs) is a rare outcome, and one that typically develops several years later than the ages at which school-based programs typically work, outcome evaluation represents a huge challenge.

The easily-measured outcomes, since they involve common and early occurrences, are the rates and ages of initiation for alcohol, nicotine, and marijuana,

but there is no strong reason to believe that all, or only, programs that succeed on these measures will succeed in reducing the incidence of serious drug problems. For example, the popular and widely-implemented DARE program, which brings police officers into fifth-grade classrooms for thirteen hours of instruction focused largely on the social skill of refusal, has consistently failed to show benefits in delaying the onset of drug use, but one recent study shows that DARE students are less likely than matched controls to take up the use of cocaine or inhalants several years later.

Even if more were known about how to deliver anti-drug messages in classrooms, actually getting it done with actual school personnel would represent an daunting challenge. (Recall that the "New Math," as delivered by highly skilled and highly motivated pilot-program staff, was a well-documented and successful program.) As to mass-media efforts, their proven efficacy in reinforcing anti-drug sentiments among adults who do not themselves use illicit drugs has not been matched by any demonstration that they influence the behavior of current or potential drug users.

Some anti-drug persuasion efforts almost certainly produce measurable benefits, and benefits well in excess of their costs. But the hope that any feasible persuasion effort can produce age cohorts with markedly less propensity to get into trouble with drugs than current cohorts seems unjustified. There may be a good case for aiming more effort at earlier ages and addressing the broader problem of impulse control and health-risk avoidance rather than drug abuse specifically.

The transition away from frequent, high dose use of psychoactive drugs is often a difficult one; that's what the term "addiction" means. External assistance, in the form of help, advice, exhortation, medication, and pressure, can increase both the number of attempts to quit and their success rate. For many of those who have had severe drug abuse problems, the recovery process will involve more than learning how not to abuse drugs; they also need to reintegrate themselves into the entire fabric of family, living space, neighborhood, and workplace relationships that they have been neglecting, and in some cases to catch up on pieces of education and maturation that were omitted in an alcoholic or otherwise drug-induced haze. It is conventional, but far too simple, to speak in terms of "drug treatment;" while it is true that formal treatment can help in the recovery process, it is also true that most people who have, for some substantial period, smoked cigarettes or used intoxicants on a more-than-daily basis, no longer do so, and that only a minority of those ex-abusers have had any formal drug treatment.

While long-term cessation is a highly desirable goal, and for most ex-drug abusers probably represents the only stable healthy state, imperfectly successful quit

attempts also have benefits, in the form of reduced drug consumption and drug-related harm during the attempt and for some time following it. The conventional evaluation of treatment efforts in terms of the percentage of their graduates who remain entirely abstinent a year later misses this important class of benefits. Worse, it gives program managers a strong incentive to seek out and serve low-cost, high-recovery-probability clients rather than concentrating on those whose problems are causing the most damage. Far better to evaluate programs in terms of their ability to reduce the absolute level of drug-related damage to those they treat and to surrounding individuals and institutions.

XX (Evaluated as a crime-control measure alone, providing drug treatment for criminally-active addicts is strikingly cost-effective. Yet publicly-funded drug treatment remains scarce, and is frequently of poor quality. The lack of effective political pressure to remedy the situation has many causes, including some internal to the treatment programs themselves and the public agencies which manage them, but reluctance to do anything for the hated class of drug abusers surely accounts for a substantial part of the problem. The focus on prevalence as the single measure of drug control success also plays a role; because they concentrate on the minority of problem users, treatment and related activities have little impact on the total number of drug users even when they dramatically reduce total damage.

XX (Expanding drug treatment and making sure that it is available to the right people is one way to shrink drug-related harm on the right tail of the distribution. Another is to use the coercive pressure of the criminal justice system to induce reductions in drug use and drug-related crime among probationers and parolees. With heavy users accounting for about 80% of cocaine and heroin volumes, and last year's arrestees including about 75% of heavy heroin and cocaine users, it seems probable that as much as 60% of the cocaine and heroin sold in this country goes to people who are nominally under criminal-justice supervision. Drug courts and drug-diversion programs are useful efforts in this direction, but limited in scope and scale. It is possible that making frequent drug testing - with immediate and predictable, even if mild, sanctions for each missed or "dirty" test - part of routine supervision for drug-involved probationers and parolees could make a major dent in the illicit markets and in drug-related crime. Here again, the problem is to take an attractive concept that seems to work well in pilot programs and operate it at a scale big enough to matter.

Current Drug Control Efforts

(Drug law enforcement, including prison cells to hold convicted drug offenders, accounts for something like three-quarters of the estimated \$35 billion in annual public-sector drug abuse control expenditures. At any given moment,

* approximately 400,000 Americans are behind bars for drug law violations, and in the poverty areas of many big cities noticeable fractions of all the young men are, or have recently been, so confined. If one could, by some heroic feat of measurement, weigh the total suffering caused by illicit drug abuse against the total suffering caused by incarceration for drug-law violations, it is not at all clear which side would be heavier. While most of those imprisoned for drug offenses also commit non-drug offenses, it appears that on average they do so at only about half the rate of those locked up for "predatory" crimes. Consequently, the expansion of drug-related imprisonment has probably had the tendency to increase crime by reducing the incapacitative effectiveness of the average prison cell.

There is a shocking lack of evidence that this very substantial expenditure of resources and infliction of pain is matched by any proportionate impact on drug abuse or drug-related harm. The price of cocaine is substantially lower now than it was fifteen years ago, even though the number of cocaine dealers imprisoned has increased by an order of magnitude over that period. Even more shocking is the lack of curiosity about the effectiveness of enforcement; it is as if the punitive process needed no external justification.

In a pale reflection of the hawk-and-dove battle over legalization, there is a long-standing quarrel over the appropriate shares of the drug abuse control budget. Here the "dovish" camp - by no means restricted to those who favor wholesale revision of the drug laws - favors expanding the share of treatment at the expense of enforcement. (Everybody talks about prevention, but nobody does much of anything about it in budgetary terms.)

There is a good case to be made for expanding drug treatment, and another good case to be made for shrinking (and, more importantly in my view, redirecting) drug law enforcement. But the conclusion often drawn - that drug law enforcement dollars ought to be redirected to treatment - does not follow from these premises and is probably incorrect.

The "drug budget" is an artifact of measurement. No one actually has a fund of \$35 billion to allocate to among drug law enforcement, drug prevention, and drug treatment. Rather, spending for drug abuse control comes out of appropriations to law enforcement agencies, schools, and a variety of health-care and social-service agencies, including the state departments of alcohol and drug dependency which in turn buy services from private, largely non-profit, treatment providers.

The total national health-care effort totals about \$1 trillion. Between public programs such as Medicare and Medicaid and the tax subsidy to employer-paid health insurance, about half of those dollars come from the public fisc. If drug

treatment is under-funded, that is because it gets a tiny share of a colossal "health budget." By contrast, the national law enforcement and criminal justice effort totals about \$125 billion. If drug law enforcement is over-funded, that is because it gets a generous share of a much smaller "law enforcement budget." On this analysis, the case for moving money from drug enforcement to drug treatment seems quite weak. If more resources are needed for drug treatment - as I believe they are - why should they not come out of the health care sector? If resources can be saved by reducing drug law enforcement, why should they not be redirected to, say, reducing the proportion of homicides which go unsolved from the current 35% to the less than 10% which was the national average a generation ago?

Thus cutting drug law enforcement is neither a necessary nor a sufficient condition for increasing drug treatment; even if one wanted to redirect drug law enforcement spending into drug treatment, the budgetary mechanisms are simply not there to make the transaction work. Getting health care providers and their financing mechanisms to pay appropriate attention to substance abuse - including the large proportion of substance abuse that occurs in relatively mild forms among those who are not socially dispossessed, and that can be substantially reduced if primary-care physicians are trained and induced to make appropriate early and brief interventions - will require a mammoth effort. That effort must embrace changes in medical education and certification, the management of health insurance programs and health maintenance organizations, policies of public providers of health services or health insurance, and the health-coverage purchasing behavior of employers and their labor unions. The sooner we stop playing budgetary games instead, the sooner we can get to work.

The Licit Drugs

The political transformation of the tobacco issue over the past generation, but more strikingly in the past five years, has created conditions under which it may be possible to make a serious run at reducing the level of tobacco-related disease. But how far we are from treating even the least popular of the licit addictive substances as if it were a "drug" is illustrated by the proviso in the proposed "global tobacco settlement" that conditions the FDA's authority to regulate nicotine content on a certification that any such regulation would not create any "substantial market in contraband."

In any case, it seems likely that significantly higher cigarette prices are on their way, perhaps along with subsidies for smoking-cessation programs. (Amazingly, most health insurers will not pay for the nicotine patch; the turnover in their subscriber pools, and their reluctance to offer benefits that might attract smokers onto their rolls, makes it financially imprudent for them to do so, despite

evidence that the patch roughly doubles the success rate of unassisted efforts to quit smoking.) Whether anything else will be done for the large population of strongly addicted smokers, especially the elderly poor remains to be seen. Some sort of exemption from higher cigarette taxes for smokers over a certain age and under a certain income level would be easy to justify, but the most likely outcome, as reflected in the proposed settlement, is that they will be allowed to add impoverishment to the other harms they inflict on themselves by continuing to smoke. Even a licit-drug addict, it seems, gets little sympathy or help.

Part of the reason anti-smoking sentiment may be expressed in legislation is that most smokers are addicted and hate both the fact that they smoke and the companies that supply them. (In this, smokers resemble heroin addicts.) Efforts of the tobacco companies to create a "smokers' rights" movement have proven signally unsuccessful. By contrast, most people who drink alcohol (like most people who smoke cannabis) are controlled users and satisfied customers, much easier to mobilize against any increase in price or decrease in availability for their favorite mind-altering chemical. That makes the prospects for higher taxes on alcohol much dimmer. Bolder measures, such as public service advertisements directed against drunkenness (as opposed to drunken driving or underage drinking) or an effective ban on the sale of alcohol to those convicted of drunken driving or drunken assault seem even more remote. On the other hand, the widely violated ban on sales to, or use by, minors, and the definition of the age of majority for that purpose as 21, remain sacred cows.

Conclusion

Anyone who expresses real optimism about the prospects for significant drug policy improvements in the short run might reasonably be asked what he has been smoking (or drinking). The forces that support the current unsatisfactory set of policies and outcomes cannot be wished out of existence.

Yet the gap between actual performance and optimal performance - between what we now do and what we know how to do - is too wide to tolerate. Elite and mass dissatisfaction with the situation, albeit unfocused, may be too widespread to ignore. Many officials, given adequate cover against the dreaded charge of being "soft on drugs," might be willing to try something new. Under these conditions, pointing out a "third way" between the warriors and the legalizers seems worth a try. Even where optimism seems unjustified, hope remains a virtue.

THE WHITE HOUSE
WASHINGTON

'97 DEC 8 PM3:1

December 8, 1997

MEMORANDUM TO THE PRESIDENT

FROM: ANN LEWIS *ALW*
SUBJECT: ABIGAIL THERNSTROM

I have spoken with Abigail Thernstrom several times since the Akron Town Hall. She wanted to be sure you knew that she appreciated the opportunity to be part of the discussion; does not feel that she was "picked on"; and has told the press that she thinks what you are doing - encouraging discussion about race - is very important. When the Boston Globe misquoted her in a way that was negative to you, she called the editor and insisted on a correction.

She very much agrees with the emphasis on education and with the kind of school reforms underway in Chicago. (Abigail is a member of the K-12 Education Board in Massachusetts.) She and Stephen are looking forward to the conservatives meeting.

I thought you would be interested in her column this week in Newsweek which makes many of these points.

*Thernstrom
is these
Thy's in mind to be*

*copied
Lewis
COS
Mathews*

Going Toe to Toe With Bill

The conservative who sparred with Clinton over race on what she didn't get a chance to say about affirmative action. BY ABIGAIL THERNSTROM

IT WAS NOT A ROUTINE DAY FOR ME. I AM A SCHOLAR AND A writer; I spend most of my time working at my desk. But last Wednesday I found myself going head to head with the president of the United States. I was on a stage in Akron, Ohio, discussing race in America at a televised "town meeting" moderated by Bill Clinton. (I had been invited because I am the coauthor of a new book, "America in Black and White," which chronicles black progress over the last half century and argues against the use of racial preferences.) As part of a yearlong initiative, the president has asked for open talk on race—and last week he got it. At the end of the two-hour meeting, Clinton turned to the audience in a University of Akron auditorium and asked, "How many of you believe in continuing affirmative action in higher education?"

With perhaps too much chutzpah, I shouted, "The issue, Mr. President, is not affirmative action but *racial preferences*." I didn't have the microphone in my hand at the moment, but the president heard me and wheeled around. "Abigail," he asked, "do you favor the United States Army abolishing the affirmative-action program that produced Colin Powell? Yes or no?"

This is not a question that can be answered with a yes or a no, and the discussion of race requires thoughtfulness, not theater. Most Americans believe in affirmative action as it was originally conceived: as outreach—a nondiscriminatory search for the best possible person regardless of race. But the overwhelming majority of Americans are opposed to racial preferences—numerical quotas, goals or timetables that lead to double standards. They do not think America has solved its racial problems. Few are so naive as to believe that the country has miraculously become colorblind. But most do not like policies that view people first and foremost as members of racial groups. They also know that in a society already too conscious of race, double standards in contracting, employment and admissions (that is, when less is expected of blacks and Hispanics than of whites and Asians) widen the racial divide, heightening rather than reducing race consciousness and racial tension.

The Colin Powell example is instructive. When the president turned to me, I told him that I do not think racial preferences made Powell. And I went on to note that the army does something very right: it prepares recruits to compete on a level playing field. But our short exchange ended there.

Preferences ignore and disguise the real problem: a racial gap in cognitive skills, a crisis the military understands and addresses.

The armed forces are an equal-opportunity program—or at least as close to one as we can get in an imperfect world. Minorities do well in the services because they are, by and large, treated equally, and rise or fall according to their merits, not their race. And most of the time, the best go far.

At one point in his career, Powell did benefit from the proper kind of affirmative action—not a quota but a widening of the net. The question was promotion to brigadier general. A list of candidates had been

sent to the secretary of the army, Clifford Alexander, and it included no blacks. Alexander sent it back saying, in effect, look again. Powell, who, among other accomplishments, had graduated second in his class from Command and General Staff School, was added. The rest, as they say, was history.

That approach to affirmative action—in the military, in universities, in the corporate world—is right; racial preferences are wrong. The debate often centers on higher education, and I believe that admissions should be colorblind. When, for example, the University of California, Berkeley, admitted black and Hispanic students with SAT scores 300 points on average below those of whites and Asians (and with similarly lower grade-point averages), that is a preference. In the short run, abolishing racial factors in admissions will mean fewer non-Asian minorities in top colleges, and that is painful.

But in the long run, there is only one genuine solution to the nation's continuing inequality: close the appalling, unacceptable racial gap in educational performance in the K-12 years. Today, on average, a black 12th grader reads almost four years behind the average white student. And there are similar disparities in other subjects. Shame on us that we set any of our kids up for

failure in a world in which only the highly skilled do well. We can do better—and we were doing better just a decade ago, when the gap between whites and blacks in educational performance was closing.

Thankfully, there is emerging agreement on this crucial point. "The era of dual standards is over," Hugh Price, president of the National Urban League, said recently. "We have got to get our kids clearly and unquestionably qualified." Precisely. Real equality of opportunity is the key to minority advancement, not double standards. Let's abandon the latter, and get to work on creating the former. That would be real progress.

TERNSTROM is the author, with Stephan Thernstrom, of "America in Black and White: One Nation, Indivisible."



Pointed exchange: Clinton with Thernstrom (far left)



ONE AMERICA IN THE 21ST CENTURY

The President's Initiative on

THE PRESIDENT HAS SEEN
12-9-97

'97 DEC 8 PM3:5

12-9-97

The New Exec
Washington, D
202/395-1010

November 30, 1997

President William J. Clinton
The White House
Washington, DC 20503

Dear Mr. President:

Since our appointments, your Advisory Board members have received many reports containing information about discrimination and racial disparities in several key areas including education, housing, employment, health and in the administration of justice. You may recall that on September 30, 1997, the Advisory Board discussed and reviewed research about the nature, extent and manifestation of contemporary racism. On November 10th, a number of Advisory Board members participated in the White House Hate Crimes Conference and discussed major shortcomings in hate crimes data collection and enforcement of civil rights laws related to hate crimes prosecution.

More recently, the Initiative staff provided, at my request, a summary of key racial discrimination and civil rights enforcement research material. This material formed part of the Advisory Board meeting held on November 19, 1997 at the University of Maryland. While there is much more that we need to know and discuss about race and national origin discrimination, there are several areas upon which the Board would like to provide recommendations to you.

The data we have received and reviewed indicate that actionable illegal discrimination on the basis of race and national origin is still active and the source of harmful consequences to men, women, and children who are the targets of this discrimination. Such discrimination in education, housing, and employment contribute to growing isolation and feelings of alienation. They further impede our ability to live, work, and grow together as One America, free from prejudicial, stereotypical thinking and discriminatory behavior.

Information we have received also make clear that for the last two decades, civil rights enforcement agencies have had their budgets and staffing reduced while many of their responsibilities have been increased. While there have been some increases in funding in recent years, often the funding level has not kept pace with the increasing volume of cases or the need for careful compliance investigations.

The increasing demands on civil rights enforcement agencies make it particularly difficult, in the view of the Advisory Board, for these agencies to devote sufficient time and attention to training staff and providing technical assistance to recipients of Federal funds to recognize and act to prevent discrimination. This is especially true for the increasingly subtle and complex forms of contemporary discrimination which have largely supplanted more blatant forms of discrimination typically found in earlier decades.

To Burkhardt for reply
after you have seen?
Yes ☒ No ☐

cc: Matthews Gene
Winston Frank Barnes
COS Chuck Runk

THE PRESIDENT HAS SEEN
THE WHITE HOUSE
WASHINGTON

12-9-97

December 9, 1997

✓
Mr. President:

Sylvia and Judy Winston wanted
you to see the attached letter.
We have sent copies to Erskine,
Gene, Frank Raines and Chuck Ruff.

Phil Caplan

Keep Reggy
still covered up w/ a
mask. Come for Reggy
then later -
BR

November 30, 1997

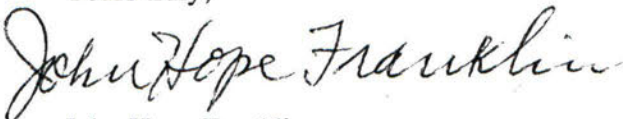
On behalf of the entire Board, I recommend the following actions to you for further attention:

- Strengthening civil rights enforcement throughout the United States: in the FY 1999 budgets, help create partnerships with States and localities that enforce comparable laws to those that operate at the Federal level, with the goal of strengthening all of the agencies' capacity to effectively enforce the civil rights laws they administer;
- Expanding and strengthening the Federal government's ability to collect, analyze, and disseminate reliable data on the nature and extent of discrimination based upon race and national origin, not of course to the exclusion of data collection on other protected classes. A well-designed and coordinated process of generating relevant indicators would then become part of an annual report covering such areas as education, health, employment, housing, and the administration of justice. Such a report would not only assist policy makers but help to increase cooperation among the various Federal agencies involved in civil rights enforcement and education. The information will also aid the public by identifying trends, and these reports and indicators can be replicated with data for local areas. Central to our concerns is the need to significantly improve the level of information about *all* minority groups.
- Implementing fully the series of bold new initiatives announced at the White House Hate Crimes Conference aimed at better data collection, enforcement, and prevention. Improved hate crimes prosecutions along with HUD's initiative to assist victims of hate crimes obtain money damages from their attackers are necessary complements to an improved capacity at the FBI to identify and track trends in hate violence.

I expect that the Board will address these issues again in subsequent meetings, and I look forward to reporting back to you on our findings and further recommendations. I would, of course, be pleased to discuss these recommendations with you.

My best wishes.

Yours truly,

A handwritten signature in cursive script that reads "John Hope Franklin". The signature is written in dark ink and is positioned above the printed name.

John Hope Franklin



ONE AMERICA IN THE 21ST CENTURY

The President's Initiative on Race

'97 DEC 8 PM3:5

The New Executive Office Building
Washington, DC 20503
202/395-1010

To: Sylvia Mathews
Deputy Chief of Staff

From: Judith A. Winston *JAW*
Executive Director

Subject: Dr. Franklin's Letter to the President

As you know, the Advisory Board discussed discrimination and civil rights enforcement issues during its November 19 meeting at the University of Maryland. Attached is a letter from Dr. John Hope Franklin to the President which follows up on that discussion and contains several recommendations from the Advisory Board members.

I hope that you can help forward this letter to the President as soon as possible for his consideration. Thank you.

Sylvia,

This letter merely memorializes the advice given to the President -- advice that he and we have already referred to in several meetings

JAW

- J/B

please copy for me.

cc: Bruce Reed and Chuck Rutt

FBI.

- Phil Caplan -

will you get the attached letter to the President

*TY
Smart*

'97 SEP 5 PM7:34

THE WHITE HOUSE
WASHINGTONTHE PRESIDENT HAS SEEN
12/10/97

September 5, 1997

COPIED
Reed ✓
COS ✓

MEMORANDUM FOR THE PRESIDENT

FROM: Bruce Reed

SUBJECT: Tobacco Update

When you return next week, Secretary Shalala and I will give you detailed recommendations on how to proceed on tobacco. We are scheduled to meet with you on Friday, and you are scheduled to announce your position on Tuesday the 16th. This memo is a brief summary of what we are likely to recommend and what strategic and policy decisions you will need to make.

I. Overview

Although the industry was hoping for quick passage, some Republican leaders in both houses said this week that the tobacco settlement was too complicated for Congress to enact before they adjourn in late October. Lott would still like to get it done this year, but with the legislation being referred to six committees in the Senate alone, we need to stake out positions that can hold up over time.

Over the past two months, we have held extensive discussions with the public health community, attorneys general, members of Congress, and farmers. The public health community will welcome our recommendations on most issues: guaranteeing full authority for FDA to regulate nicotine; imposing tougher penalties on the industry if it fails to reduce teen smoking; demanding an additional \$50 billion to offset the credit in the budget agreement; making it somewhat easier to disclose industry documents; looking out for tobacco farmers; and so on. The only concerns of tobacco opponents that we cannot easily meet are dramatically increasing the overall price tag (Kennedy would like to see it doubled, to \$700 billion) and demanding to see all the documents before capping liability (Leahy, Waxman, and Skip Humphrey are pushing for "no immunity without disclosure").

The central strategic question is how far we want to push the industry for additional concessions, at the risk of losing this opportunity altogether. Bruce Lindsey and I have

repeatedly pressed the industry on the most important issues -- FDA, penalties, and documents -- with only modest progress. We met with them again today, and will continue to press them next week, but penalties remain a serious stumbling block.

Bruce believes we should not go forward unless we have the industry on board, because without an agreement on everything the industry will be free to use its considerable influence in Congress to undermine provisions it doesn't like -- for example, gutting the FDA provisions if it wins in the 4th Circuit. Secretary Shalala and the Vice President strongly believe we should not reach agreement with the industry, because any deal with tobacco companies will be suspect, and won't have enough congressional buy-in to withstand 6-12 months of debate in Congress.

This debate may become moot, if we can't get the industry to come around by next week on our bottom-line issues. In that case, I believe we should be both tough and reasonable, by demanding more than the industry can stomach right now (on FDA and penalties), but not more than they can possibly swallow in the end. I share Bruce's concerns about the industry's clout and penchant for mischief, but a little tension between us and the industry might actually help us during a drawn-out congressional debate. If we make this a fight over tougher penalties to reduce teen smoking (rather than how much money we want in return for capping liability), I believe we can beat the industry on a few points, even in this Congress -- especially in an election year.

II. Major Recommendations

A. FDA Authority

The first priority of the Administration in considering any tobacco legislation should be to confirm and protect the jurisdiction of the FDA to regulate tobacco products. The FDA must be able to regulate tobacco products, including by ordering the reduction or elimination of nicotine or other constituents, through its normal procedures in the furtherance of public health interests -- without any special procedural rules or requirements. We should call on Congress to pass legislation specifically empowering the FDA to require the modification of tobacco products based on a finding that this change would reduce the risk of the product to the public and is technologically feasible.

The industry still wants to put one hurdle in front of FDA, by saying the FDA may not go forward if a party affirmatively demonstrates that the action would create a significant contraband market in tobacco products. But we believe the FDA should only have to consider contraband as one of many relevant factors, including the number of addicted tobacco users and the availability of alternative products. We would eliminate two other weaknesses in the settlement -- the 12-year waiting period before FDA could ban nicotine, and the special procedural hurdles such as formal rulemakings.

THE PRESIDENT HAS SEEN

12-10-97

B. Documents

For decades, the tobacco industry has failed to disclose essential facts in its possession about the dangers and addictiveness of tobacco products, and used attorney-client privilege to cloak scientific research and findings and possibly shield evidence of criminal or fraudulent behavior. It is therefore necessary to establish an effective and speedy mechanism to pierce fraudulent or otherwise improper claims of privilege and to force the disclosure of information that will advance public health interests. The documents issue has become a rallying cry for the most strident opponents of a settlement, led by Skip Humphrey.

The settlement calls for a national documents depository and a three-judge panel to provide expedited rulings on whether documents should remain privileged. We recommend strengthening the document provisions by 1) allowing litigants to challenge privilege claims in individual lawsuits, even if the three-judge panel had already ruled, and 2) providing the FDA with access to all health-related documents, notwithstanding any claims of privilege. That will enable the FDA to put the industry's considerable expertise on nicotine to good use.

Even these steps will not go far enough to please Leahy, Waxman, and Humphrey, who want to break the companies' attorney-client privilege and insist that the tobacco companies disclose all privileged documents before any consideration of a settlement. But the Justice Department has expressed serious concerns about any broad abrogation of the privilege, arguing that such an approach would undermine the privilege generally and might enable a tobacco company official charged with criminal conduct to assert a violation of his Sixth Amendment right to effective assistance of counsel.

C. Penalties

The settlement sets ambitious targets to reduce youth smoking by 30% in 5 years, 50% in 7 years, and 60% in 10 years, and would require companies to pay \$80 million for each percentage point they fall short. Public health groups have praised the idea of targets and penalties, but complain that the current scheme does not give companies sufficient incentive to stop hooking teenagers. Our main problems with the current penalties are that they are tax-deductible, abatable, capped at \$2 billion, and too small to serve as a deterrent.

We can strengthen the penalties in a variety of ways -- all of which the industry has so far resisted -- but our current preferred option is a two-tier system, with graduated penalties that get stiffer if the industry misses the targets by a substantial margin. The first tier of penalties would require companies to pay \$80 million per point if the industry missed the targets by less than 5 points in year 5, less than 10 points in year 7, and less than 15 points in year 10. This penalty would be non-deductible, could not be abated, and would reflect a company's share of the youth market. If the industry missed by a greater margin, companies would pay the full first-tier penalty, and their settlement payment would be increased by a penny a pack for each additional

Yes - I'm
Leahy, Waxman, and Humphrey
attorneys
privilege is worth
it's strong

percentage point by which they missed the target. This second-tier penalty would cost companies about \$240 million a point, and has the additional virtue of locking in a permanent price increase that will help further reduce smoking by youth (and adults). Under this approach, if youth smoking went down by 30% over 10 years, instead of 60%, the industry would pay \$1.2 billion in financial penalties and be forced to raise prices another 15 cents a pack on top of that.

D. Farmers

We have made clear that tobacco farmers should receive protection in any legislative settlement, and that the Administration will work closely with members of Congress from tobacco states to forge a consensus. Secretary Glickman has traveled to tobacco markets in Virginia and North Carolina to express this commitment directly to farmers.

Farmers are primarily interested in continuation of the governmental tobacco program, guaranteed purchase at set levels of tobacco crops by cigarette companies, and some provision for buy out and transition to other crops, on a voluntary basis. Because farm groups and tobacco state members have not yet coalesced around a consensus proposal, we don't need to commit to a specific plan yet. The most discussed proposal is one released this month by Senators Ford and McConnell that would require companies to buy a minimum amount of domestic tobacco over 25 years and would install penalties on companies that do not meet the stated goals for tobacco buying. The proposal would also create a "Tobacco Community Revitalization Fund" administered by USDA, but not subject to the appropriation process, which could spend up to \$1 billion a year for 25 years from the settlement fund and would cover costs related to the tobacco program such as administration and crop insurance, make supplemental payments of up to \$500 million to producers whose income from tobacco drops substantially below the 1996 level, pay up to \$100 million in benefits for displaced cigarette factory workers, and provide up to \$250 million a year for rural economic development grants.

E. Funding

Although the settlement is advertised at \$368.5 billion, a variety of factors conspire to leave us with considerably less than that to spend on any new initiatives. The \$368 billion is a 25-year number, and must be adjusted downward to reflect a projected drop in cigarette consumption of about 15%. For scoring purposes, OMB adjusts the amount down still further to reflect lost business tax revenue and lost federal excise tax revenue from decreased consumption. Most of the rest of the money in the settlement is already spoken for, to pay for civil suits, cessation programs, counteradvertising, and the states' Medicaid claims. The main decision you will need to make is how best to spend the \$25 billion research trust fund, which most of us believe should be a 21st Century Research Fund dedicated to cancer and other tobacco-related research.

Some in the Administration (primarily the Treasury Department) and in Congress (led by Kennedy) believe the industry should be soaked for \$600-700 billion. This is probably a dealbreaker for the industry, but it would free up additional funds for new initiatives.

F. Other Issues

We will need to propose improvements in other, less prominent areas, which we will detail for you next week. These include limiting the industry's antitrust exemption to prevent unnecessary collusion and removing a little-noticed cap on punitives for future misconduct.

We will give you a more detailed memo on all these recommendations next week, and bring you up to date on our discussions with the industry, the Hill, and the public health community.

Memorandum for the President

From: Sylvia Mathews

Subject: Note to Edley

THE PRESIDENT HAS SEEN

12-10-97

1 Lin Booy
a b c d e

Attached is some suggested language for a handwritten note to Chris, per our conversation this morning. (I have also attached the Edley and Loury pieces that appeared in the **Post** yesterday.)

Dear Chris,

Thanks for all your help on the Race Initiative. As I know you are fond of saying "this is harder than rocket science" and it is. I know that this issue means as much to you as it does to me and I appreciate your dedication to it and assistance to our efforts.

copied
cos
mathews

Professor Glenn C. Loury
Boston University
Director, Institute of Race and Social Division
704 Commonwealth Avenue
Boston, MA 02215

WASHINGTON

12/10/97

Dear Glenn,

I enjoyed reading and
appreciate your article in the Post
and agree with much of what you
said.

I look forward to seeing
you for further discussion:

On a recent meeting, I
sympathize with the backing you
have taken from other conservatives
when you have veered from the
party line. I have felt it in my
own doubts on my position on
budget, trade, crime, and welfare.
As a fellow apostate, you are the
company I'm very keen.

Sincerely,
Bill Clinton

To Glenn Loury

Professor Christopher Edley
Harvard University Law School
Griswold 405
Cambridge, MA 02138

Dear Chris -

Thanks for your fine article
in the Port. You have worked so
hard and thought so deeply on the
issue & sometimes feel you are
pulling out of my mind what I
ought to be able to get out myself.

Let's keep at it. We'll do
something profoundly important

Sincerely
Bill Clinton

To Chris Edley

Why Talk About Race?

President Clinton's first nationally televised town hall meeting on race left at least one question hanging in the air: Will all this talk lead to action? Outlook invited the president's adviser on racial matters and a noted commentator to debate where the initiative goes from here.

President Clinton's Initiative Is More Than a Gabfest

By Christopher Edley Jr.

Why should we have hope for the president's race initiative? Because without a national conversation on race—for which last week's meeting in Akron was meant to serve as a model—we can't build the bridges we need to connect people across our divisions of color and class. But if you think that's easy, then you haven't tried it—or you are a saint. We've failed at it since 150 years before the Declaration of Independence. And by my reckoning, we are failing still—in our personal lives, work relationships, communities and public debates. Let me give several examples.

Six years ago, when my son was in second grade in the Cambridge, Mass., public schools, he came home crying because, we soon discovered, he had been tracked into the lowest of three reading groups. We were shocked, given the warm, consistent praise from his teachers and principal for more than two years. And we were dismayed, fearing some learning disability. After we paid \$2,000 for testing by a child psychologist, we learned that he had no problem—far from it. We came to believe he was a victim of a kind of racial discrimination, expressed as low expectations; he had been tracked by color, not by ability. Regrettably, we sacrificed the public school's rich diversity and transferred him to a private school, and later to a suburban public school. Was this discrimination, or school failure?

Recently, a Latina law student asked me to supervise her independent research project. Already badly overextended, I had rejected similar requests from a few other students, all white. America's Race Problem came crashing down on my head: I wanted to make an exception for her for no reason other than my general supportiveness of minority students. Was I being fair, or racist?

Last year, an urban school superintendent spent two hours with me discussing his staggeringly complex agenda: endemic underachievement, frightful drop-out rates, unsympathetic legislators and state bureaucrats, the growing numbers and isolation of impoverished students, as well as a

See RACE, C4, Col. 1

RACE, From C1

local political class that was undistinguished by profiles in courage. His overarching challenge, however, isn't the difficulty of building an innovative curriculum: It's overcoming the racial divisions that for decades have prevented consensus on reforming his schools. So, is K-12 excellence a race problem, or not?

In a series of recent conferences at the Harvard Civil Rights Project (where I am co-director), leaders from higher education, the testing industry and civil rights organizations, along with researchers, have been unanimous in their dismay over widespread public misunderstanding about the use of standardized admissions tests for selective colleges. Yet critics of affirmative action often treat paper-and-pencil test scores as if they are complete and accurate measures of merit, and these critics speak of "preferences" with robotic regularity because polling shows that the public generally supports "affirmative action" while opposing preferences.

The Washington Post

SUNDAY, DECEMBER 7, 1997

Even the test makers agree that the SAT and other such tests—which are designed solely to predict first-year grades—are an incomplete and imperfect measure of "merit"; that sensible schools must look at a variety of factors about individual applicants, the mix of applicants and the mission of the institution; and that test results strongly reflect a student's educational and class advantages. The test mania and garbled public discourse are slowly closing doors only recently unlocked. So are we having an honest discussion about values and policy, or are we playing race-card games in which the winners get opportunity and the losers get left out?

The great national conversation on race isn't on track yet, despite a very good show in Akron. With hard, confusing issues like these, can Clinton's initiative possibly succeed? To answer that question, it may help to understand that this is not some raining program for a boomer president who, facing a long retirement, might prefer pinching for Oprah to being a spokesmodel for credit cards and golf balls. There is actually a theory at work.

The president speaks so often of "One America" (the name we have given to the race initiative) because he views dealing with difference as one of a handful of millennial challenges—problems we *must* face to be our best in the next century. One might also list the budget deficit, trade, a post-Soviet security regime, K-12 excellence and environmental security. In Clinton's One America vision, we don't just "tolerate" our differences, we "celebrate" them as a source of richness, strength and competitive advantage. He means, I think, national identity without homogeneity—yet one where our hyphens matter less than our shared values and mutual commitments.

To me, the best analogy is our rich religious diversity. We are fairly united as one of the most religious nations on earth, but we worship differently, celebrate that fact, and recognize that religious differences should play only a limited role in our social and economic lives. Perhaps a model along these lines is what is needed in race. If so, then the question is how to get there. One of the president's year-end goals is to provide such a plan.

Of course, this will be tough to pull off. To do it, Clinton's race initiative is pursuing two tracks. First, there must be policy development, because strategies that create opportunity are the best way to change the social and economic facts in people's lives. That is happening now, on a kind of month-by-month installment plan, rather than waiting until the end of the initiative. But incremental policy tinkering, reflecting the political and fiscal constraints, can only get us so far. So there is a second and ultimately more significant track: finding new, realistic models for talking about our differences.

The goal is not to close the chat gap, but to find the mutual understanding that can somehow lead to a stronger sense of community. The premise is that you care more about neighbors you understand than about strangers who are different. I do not know how to create these connections. But surely that is researchable and teachable. For my money, perhaps the greatest contribution Clinton and Co. can make is to find those promising practices around the country that may be instructive to the school superintendent, the union local official, the rabbi and the state legislator who want to build bridges but are not sure how. That is one key task the president has given to his advisory board, and the preliminary results are posted on the White House Web page.

Successful dialogue means including ideologically different voices. But the people who come to the table must be responsible, honest and willing to search for the kernel of truth in what the other side is saying. No points for latitudes, and no points for polemics, either.

My hypothesis is that the most fruitful dialogue will be the kind that is quickly connected to some sort of action, where people work with each other to accomplish something. Whether that might be a coalition to improve schools, clean up a toxic-waste site or support community policing, the search must be for the conversations and experiences that will change the sense of who is us and who is them.

There is also the challenge of struggling with vexing policy questions, getting beyond platitudes and recognizing where our differing positions may reflect our race-related differences in experiences. Hours after the Akron meeting, I was having Chinese food with a group of largely Latino scholars, assembled in Los Angeles for a summit on the Latino civil-rights crisis. I questioned them about the value of bilingual education, grilling them about the research evidence, the politics within the Hispanic community and the political assault that is building steam in California and elsewhere.

The discussion reflected varying degrees of support for the policy and was fabulous, but discouraging as well. We shared a deep pessimism that public debate on the issue will really reflect the social science research, rather than people's prejudices. And sadder still, we recognized the pall of color: How many of the strident critics of bilingual education are motivated primarily by concern that those children receive less than a full measure of opportunity, and how many are primarily concerned that America is becoming less white, less Anglo?

Racial paranoia, you may say. No, just evidence of our divisions. Of course there are limits to the significance of race, but where do we draw the lines? You may say that Mark Fuhrman's bigotry was unusual for the L.A. Police Department; that employment and housing discrimination are of vanishingly small social and economic significance; that the excellence of a constitutional law class or a newsroom has nothing to do with the mix of experiences and perspectives assembled—or at least has so little to do with it that no affirmative efforts are justified to create that mix. And you may think that slavery, conquest and Jim Crow are such distant memories that the only really important problems now are class and, say, family structure.

To others, however, the persistent legacy of color-coded disadvantage is so obvious that they can't understand how anyone could ignore it or tolerate it. They attribute this blindness to some sort of racial animus.

Too often, our perceptions and priorities divide along color lines (imperfectly, of course). That reflects the distance between our communities, which fuels at least some of our disagreements about everything from criminal justice to affirmative action, from school reform to welfare reform. Many voices—and not only conservative ones—are declaring that race is declining in significance. But to others of us, the truth of that proposition is blown out of proportion and is being used to justify abandoning the unfinished business of justice.

My son's experience with being unfair tracking brought back my own almost identical experience in seventh grade, and I still feel some anger about both his and my experiences. More to the point, I'm looking for advice—not just how to discuss such conflicts constructively, but how to make connections that will change values and perceptions. Leaving race out of the analysis won't work.

In the end, I chose to help my Latina law student, but I know I would be furious if a white male colleague made a special effort to help white male students for whom he felt some special affinity. While I may not be persuasive, I can explain my choice easily enough: Symmetry and color blindness have a superficial appeal, but the law school realities of white and minority students are vastly different. Will ignoring that difference help it go away? I doubt it.

More generally, "de-racializing" issues, as some term it, is almost as crippling as turning everything into a question of color. My friend the school superintendent knows that he needs a strategy for racial reconciliation if he is going to have a shot at bringing about school reform. But, as in my personal examples, saying the right words may be only a small step in creating understanding, much less consensus. The president's initiative, if successful, will provide lessons in how to wrestle with the tough issues.

The post-Martin Luther King Jr. generation has seemed lost on the race issue. For some, the answer was to define "reverse discrimination" as the nation's greatest civil-rights problem. For others, well, I think we came of age watching the successes of the 1950s and '60s, and mistakenly concluded that progress was inevitable. Apart from a few warriors, we've been coasting, neither teaching nor agitating. Clinton has seized the problem, defining it in terms of One America. He will fail, unless we share the burden.

Christopher Edley, a Harvard Law School professor, is an adviser to the White House on racial matters and author of "Not All Black and White: Affirmative Action, Race and American Values" (Hill & Wang).

The Washington Post

SUNDAY, DECEMBER 7, 1997

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Welfare and Crime Demand More Than Feel-Good Chat

By Glenn C. Loury

Last June, when President Bill Clinton announced that he would lead the country in a "national conversation on race," the initiative was greeted with skepticism and questions. Who would be included in such a conversation? What would be discussed? Ultimately, what could be accomplished? Now, even after Clinton's artfully conducted town hall meeting last week in Akron, Ohio, the answers remain elusive.

The seven-member commission impaneled to advise him on this matter, chaired by historian John Hope Franklin, has only added to the sense that the initiative is sputtering. Last month, as the commission planned to conduct hearings on racial diversity in higher education, Franklin left observers befuddled by declaring that opponents of affirmative action would not be permitted to testify. Just what kind of "conversation" did he intend to facilitate, critics asked, if such an important point of view were to be excluded?

Of course, racial conflict in America is a matter of the utmost seriousness and one deserving of presidential attention. As Clinton stressed more than once during his remarks in Akron, other countries around the world have suffered terribly when conflicts between ethnic, religious, or racial groups have been permitted to spin out of control. It would be extremely imprudent to assume that we Americans are somehow immune to this disease. Unless the focus

of Clinton's initiative can be sharpened and its goals clarified, there is the distinct possibility that little will come of this noble effort.

A therapeutic model of group dynamics seems to underlie the president's initiative. We are supposed to be getting our long-hid-

den fears, resentments and frustrations out in the open. "Be blunt," Clinton instructed his Akron audience. Yet, absent a relationship of trust having been established among the parties to the conversation and without the privacy that

See TALK, C4, Col. 4

TALK, From C1

ensures one's unguarded comments will not be taken out of context, this is a vain aspiration. A nation cannot talk like a family, no matter how earnest and articulate its political leaders might be.

This is not to deny the existence of prejudices and misconceptions that divide us and that might yet be clarified by the educational effects of public discussion. Certainly, stereotypes or suspicions harbored by one group of Americans toward another might, with sufficient effort, be dispelled in this way. But such an educational mission can hardly be the best use of a president's scarce time and awesome, if fleeting, command over public attention.

How can Clinton's initiative be restructured to increase its prospects of success?

An important first step would be to move the discussion beyond the familiar categories of partisan conflict on racial issues. Rather than seeking common ground between the extant camps of racial liberals and conservatives, the national conversation should instead aim at redefining the debate so as to develop ideas that can appeal to people in both camps and thus foster a new sense of common purpose.

We are at a historic moment of social and political transformation on racial matters. One indication is that irrevocable and deep improvement in the status of black Americans has taken place over the past half-century. While the trend has been apparent for decades, a powerful case for this view has been made by the president's antagonist in Akron, Abigail Thernstrom, along with her husband Stephan Thernstrom, in their new book, "America in Black and White: One Nation, Indivisible."

True enough, blacks continue to bear a burden of racial stigma—reflected in, among other things, widespread police (and civilian) suspicions that young black men are likely law breakers. And, of course, there remains the deeply entrenched problem of the black underclass, whose condition has grown more desperate even as most blacks have been making good progress. But these considerations to the contrary notwithstanding, truly remarkable change has occurred.

As a result, the 1960s-style civil-rights approach to race relations—in which blacks petition the courts and the federal government for relief against the discriminatory treatment of private or local state actors—is now insufficient. Petitions of this sort should continue to be brought, but the predisposition to view black-white relations through the civil-rights lens is no longer a constructive one.

The profound demographic transformation ongoing in American society over the past three decades is also rendering the old black-white framework obsolete. Twenty million immigrants, most from non-European points of origin, have arrived on our shores since 1965. Blacks will soon be overtaken by Hispanics as the largest minority group in the country. This is not to deny that blacks occupy a unique position in any discussion of race in America; only that a dialogue focusing solely on the old tension between blacks and whites will miss something of fundamental importance.

A final change, which after the past two elections hardly needs elaboration, is the rightward shift in the ideological landscape that has occurred over the past generation. As Clinton famously put it, "The era of big government is over." In changing times, the most familiar issues of racial contention—welfare, affirmative action and criminal justice policy—do not fit neatly into the old boxes.

Perhaps the president's initiative can best achieve a long-term impact on the nation's public life by recasting the ongoing policy dialogue in these areas:

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■ **Welfare:** Race and welfare policy are intimately tied together because poor minorities, especially blacks, are significantly over-represented (by percentage) on the welfare rolls. Revolutionary changes in the federal-state welfare policy framework were enacted into law in 1996. Much of the old debate—over the propriety of forcing recipients to work, for example—was ended by Clinton's passage of welfare reform.

Nevertheless, the impact of the new law on minority communities appears to be profound. There is good reason to worry, for example, that these policy changes could adversely affect the physical and mental development of many tens of thousands of young children living in inner-city ghettos.

Important welfare policy decisions remain to be made, about the provisions of child care to poor working mothers and about the degree to which the most disadvantaged cases will be exempted from eligibility cut-offs. It is wholly legitimate to focus public attention on how these changes will affect the well-being of the roughly one-third of African American children who depend for their subsistence on the cash grants, food stamps and medical assistance provided by government.

The president's dialogue could promote a healthy consideration of the racial dimension of this issue, while at the same time reinforcing the broadly held public judgment that the terms of the social contract between indigent families and the rest of the society have been permanently changed.

■ **Affirmative action.** The consensus that once supported color-conscious racial policies is collapsing, though it remains unclear what will eventually take its place. A dramatic moment in the Akron town meeting occurred when President Clinton sharply engaged Thernstrom over the issue. The audience there seemed to support "affirmative action," but the president had to concede that similar support for "racial preferences" could not be assumed. Thernstrom, for her part, avoided answering directly when the president pressed her on whether she would abolish the U.S. Army's affirmative action efforts. She conceded that the Army does a fine job at raising the skill levels of its black personnel.

In my view, neither the rear guard preservationists (whose "mend it, don't end it" slogan was coined by the president himself), nor the colorblind absolutists (who prevailed at the ballot box in passing California's Proposition 209 in 1996) can, or should, prevail. While racially discriminatory means are increasingly unacceptable to the American public, the goal of narrowing racial disparities is still widely endorsed as a legitimate end of public policy.

In Texas, the state legislature responded to a court ruling that forbade the practice of affirmative action in college admissions by passing a novel law. The state now guarantees any high school student finishing in the top 10 percent of his or her class admission to any public university in the state. The law is intended to benefit students with low SAT scores but good grades at less-than-competitive high schools. Those students helped by a colorblind policy will be disproportionately black and Hispanic.

■ **Criminal justice:** As the president reminded his Akron audience, crime rates are down. He made no mention, however, of the fact that the imprisonment rate of young black males, already extraordinarily high, continues to rise. Scholars attribute this development over the past decade to mandatory minimum sentences given to low-level drug offenders, who are disproportionately black. These sentencing practices, strictly construed, are not racially discriminatory. But they may nevertheless be morally and practically questionable because of their disparate racial effects.

With something approaching one out of every 10 black males under lock and key on any given day, the limits of the punitive response to inner-city law breaking should be apparent, even to the most die-hard drug warriors. The issue is not simply whether those (of whatever race) who "do the crime" should "do the time"—they should. The larger issue is whether we want to reap the whirlwind of dysfunctional behavior now being sown in those institutions of higher criminal education that we call prisons. Most Americans, I believe, want to get beyond the tired thinking that assumes maintaining public order must be somehow incompatible with narrowing racial disparities.

In Akron, the president complimented a white young man who admitted that he is sometimes afraid of a poorly dressed black male who is walking toward him on a city street. Such candor is admirable, but the success of the national conversation of race depends far less on the courage of individual speakers in a town meeting than on the courage of national leaders who, having gained the nation's attention, must now begin to channel it in new and useful directions.

Glenn Loury is professor of economics and director of the Institute of Race and Social Division at Boston University.

The Washington Post

SUNDAY, DECEMBER 7, 1997

THE WHITE HOUSE

THE PRESIDENT HAS SEEN
12-10-97

~~POTUS~~ -

Little by little, our effort to
get landmine message across is
producing results.

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Who's blocking progress on land mines?

Stephen Chapman

In the melodrama over the international treaty banning the production and use of anti-personnel land mines, the United States and President Clinton have been cast as the villains. Upon winning the Nobel Peace Prize for her work as head of the International Committee to Ban Landmines, Jody Williams excoriated Clinton as a "weenie" who hears "only the voices of the generals and not the voices of the poorest of the poor."

After the accord was signed by some 120 nations at

a meeting in Ottawa last week, protesters piled old shoes outside the White House to represent all the limbs lost to these weapons every year. One speaker at the demonstration accused the U.S. of being "part of the global land-mine problem."

Washington is part of the land-mine problem like South Dakota is part of Australia. The only American sin is declining to sign a treaty that would needlessly hinder the U.S. in carrying out its perpetual responsibility for keeping people elsewhere from slaughtering each other. In fact, none of the

countries in Ottawa has done as much as the U.S. to eliminate the evils of anti-personnel mines.

Supporters of the treaty habitually invoke the image of Third World children being maimed and killed by the 100 million mines scattered across countless former war zones. What the advocates neglect to mention is that this agreement does virtually nothing about those mines: It focuses on the future production and use of these weapons. But the mines of the future are not the ones killing people today.

To reduce the toll means doing something about the anti-personnel weapons that are already out there. But the Ottawa treaty slights this critical task: Signatories don't commit themselves to spending any particular sum of money to clean up old mine fields, and they have up to 20 years (and in some cases longer) to complete the task—by which time hundreds of thousands of additional victims may pile up.

A single country has taken the lead in de-mining the planet: the United States. Even such Clinton critics as Physicians for Human Rights and the Vietnam Veterans of America acknowledge as much. While other world leaders have been content to make high-flown speeches about ridding the Earth of this plague, the U.S. has chosen to actually do something.

In the last four years, we have spent \$153 million on de-mining efforts in 15 different countries—more, according to State Department figures, than the rest of the world combined. This year, we've allocated another \$80 million for the job. So far, we have destroyed 1.5 million mines, and the plan is to destroy another 1.5 million by the middle of 1999.

Lately, the administration has tried in vain to draw attention to this unglamorous side of the issue. On Oct. 31, Secretary of State Madeleine Albright announced a campaign to increase worldwide spending on de-mining efforts fivefold, to \$1 billion a year. Unlike the Ottawa treaty—which is largely unenforceable and doesn't bind such non-signatories

as Russia, China, India, Pakistan, Libya, North Korea, Iran, Iraq and Vietnam—this effort would actually prevent countless casualties. Albright's thanks from Jody Williams was a demand that "the United States should put up the entire billion dollars."

Why should we? It's not as though Americans bear special guilt for the carnage of these weapons. The damage is done by "dumb" mines sown carelessly in places where they can claim civilian casualties long after the war is over. The U.S., however, no longer deploys these devices—except in Korea's De-Militarized Zone, where they pose a danger only to invading North Korean soldiers.

Instead, the American military relies on "smart" anti-personnel mines that self-destruct in hours or days—making them harmless after the fighting is finished. But it has gotten no credit for developing weapons expressly designed—at considerable extra expense—to spare innocent lives.

It is not the Clinton administration that is being unreasonable. The U.S. has already outlawed the export of even smart mines. And the president agreed to a global ban on them.

The only ones he wants to keep are those used to prevent enemy soldiers from clearing anti-tank mines during those battles that Americans are often called on to fight in someone else's corner of the world. Our European allies use similar explosive devices attached to anti-tank mines for the same reason—but they got an exemption for their weapons in the Ottawa accord.

The U.S. has nothing to apologize for. In recent years, it has been a model of responsible behavior in the use of land mines, and it has led the way in getting rid of millions of mines that are no threat to its own citizens. Its reward is to be portrayed around the world as the chief obstacle to progress against this cruel scourge. Who says actions speak louder than words?



9 December 1997

President Bill Clinton
The White House
West Wing
Washington, D.C. 20500-2000

Dear Mr. President,

There's a situation that you should know about because it is one that could be twisted to make you look bad.

The city council of San Francisco has voted to negate all contracts with agencies that do not give medical benefits to domestic partners ~ including those who refuse to grant them to partners of gays and lesbians. I can certainly see the reason for such a decision, considering all the gay and lesbian taxpayers in that city. However, this will especially hit the Salvation Army, which receives several million dollars from the city for services rendered.

Is there some way that exemptions can be granted for religious organizations? Can the federal government have any impact on decisions made at the local level?

If nothing is done, then the Salvation Army will end its contractual relationships with the city by mid-January. What I fear is that the likes of Jim Dobson and Jerry Falwell will seize this issue and make it a rallying point against you, and against the gay and lesbian community. The cry will be that this is the beginning of a national trend and that soon all religious organizations will be forced to make such concessions to the gay and lesbian community.

I thought that you should know about this.

Yours sincerely,

Tony Campolo

cc: Maureen Shea

TC:am

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12-10-97
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12-9-97

THE WHITE HOUSE
WASHINGTON

December 9, 1997

MEMORANDUM TO THE PRESIDENT

FROM: STEPHANIE STREETT 
SUBJECT: SCHEDULING DECISIONS
CC: JOHN PODESTA & SYLVIA MATHEWS

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ACCEPT:

Date of Event:

Description of Event:

12/12/97

Interview with *People Magazine*
Staff Contact: Mike McCurry

This interview will be included in the annual *People Magazine* year-end issue.

12/15/97

Press Conference
Staff Contact: Mike McCurry

The recommendation from the Senior Staff was to postpone the Jim Lehrer interview until January, and for you to participate in a press conference on Monday, December 15.

12/17/97

Presentation of 1997 HMX-1 (Marine One) Christmas Card
Staff Contact: Virginia Apuzzo, Alan Sullivan

12/17/97

Presentation of the Congressional Space Medal of Honor, Posthumously, to the Families of Astronauts Edward White and Roger Chaffee, Who Died in the 1967 Fire on Apollo 1
Staff Contact: John Gibbons

12/17/97

Meeting with Family Farmers
Staff Contact: Maria Echaveste, John Hilley

12/19/97 Meeting with Conservatives on the Race Initiative
Staff Contact: Sylvia Mathews, Maria Echaveste

1/6/98 Participate in One-Hour Discussion Concerning Work and Families
Staff Contact: Ann Lewis, Rahm Emanuel

1/20/98 Presentation of the Medal of Honor to Major General James L. Day, USMC, (Ret)
Staff Contact: Virginia Apuzzo, Alan Sullivan

1/29/98 Meeting with Secretary Cohen and Senior Military Commanders
Staff Contact: Samuel Berger

1/29/98 White House Reception and Dinner for Service Chiefs, Military Commanders-in-Chief and Spouses
Staff Contact: Samuel Berger

2/5/98 46th Annual National Prayer Breakfast
Staff Contact: Maria Echaveste, John Hilley

Please note we are shortening the participation by you and the First Lady at this breakfast due to the Blair Official Visit Arrival Ceremony.

2/5/98 - 2/6/98 Blair Official Visit
Staff Contact: Samuel Berger

You will participate in an official arrival ceremony, official meetings, and the dinner on Thursday, February 5. The press conference will be held on Friday, February 6 at the State Department. We are currently exploring options for an event for you and PM Blair to participate in on February 6. We are also exploring the possibility of you and the First Lady going to Camp David with PM and Mrs. Blair to overnight on February 6.

PENDING:

Date of Event:

December TBD

Description of Event:

Photo for the American Film Institute's (AFI) Upcoming Celebration of the 100th Anniversary of American Movies
Staff Contact: Ann Lewis

Social Invitations:

12/13/97

Terry and Dorothy McAuliffe Holiday Party
McLean, VA
7:30PM

You are currently scheduled to attend the Arkansas DNC Dinner in Washington, D.C. from approximately 8:00- 10:00pm. *Would you like us to adjust your time at the Arkansas Dinner to allow you the option of dropping-by the McAuliffe party in McLean, VA before or after the Arkansas dinner?*

Yes _____ No _____ Discuss _____

12/14/97

Bob and Ellen Bennett Holiday Open House
Washington, D.C.
5:00 - 8:00PM

You are currently scheduled to attend Christmas in Washington in Washington, D.C. from approximately 5:00-7:00pm. You are also scheduled to take the Holiday Photo with the Social Aides after the Christmas in Washington event. *Would you like to have the option to drop-by this party after you attend the Christmas in Washington event, and before the Social Aide photo?*

Yes _____ No _____ Discuss _____

12/16/97

Council on Foreign Relations Holiday Reception
Washington, D.C.
6:00-8:00PM

You currently have the evening off on this day. *Would you like to have the option to drop-by this reception?*

Yes _____ No _____ Discuss _____

12/21/97

Drop-by Prince Bandar's 25th Wedding Anniversary
Dinner
McLean, VA
Cocktails: 7:30-8:10PM
Dinner: 8:15 - ???PM
Staff Contact: Mack McLarty

Prince Bandar has invited you to a dinner in McLean, VA to celebrate his 25th wedding anniversary. You are scheduled to participate in holiday receptions with family and friends that evening at the White House from approximately 4:30-8:30pm. With a 30-minute drive time to McLean, VA, you would be able to arrive at the dinner between 9:00 - 9:30PM. Sandy Berger also suggested that you could call into the dinner if you were unable to attend. *Would you like to drop-by the dessert portion of this dinner or phone in sometime during the dinner?*

*Will be there
I should be there*

Drop-by Dinner _____ Phone Call ☒
Discuss ☒

Spring TBD

University of Arkansas Investiture
Fayetteville, AR

Chancellor John White has invited you and the First Lady to participate in the University of Arkansas Investiture in the Spring. We have asked the chancellor's office to proceed with setting a date for the event. *Is this something you would like to consider attending once they set the date?*

Yes ☒ No _____ Discuss _____

REGRET:

Date of Event:

Description of Event:

12/11/97

Attorney General's Annual Holiday Reception
Department of Justice

You are scheduled to be traveling in Miami, FL on this day.

12-9-97

8242

THE WHITE HOUSE
WASHINGTON

'97 DEC 8 PM 6:45

December 8, 1997

INFORMATION

MEMORANDUM FOR THE PRESIDENT

FROM: SAMUEL BERGER (K) For

SUBJECT: Report of the National Defense Panel

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Berger
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COS

This memorandum addresses your question on how you should respond to the Report of the National Defense Panel (NDP). The NDP report is more innovative and forward looking than was the Quadrennial Defense Review report. Although some will probably portray the NDP's call for a transformation strategy as criticism of Administration defense policy, the report actually supports many of your policies and provides an important endorsement of Bill Cohen's efforts to reduce Defense infrastructure and reform Defense business practices. The report also calls for continued U.S. engagement in the world to ensure regional stability and endorses the report of the President's Commission on Critical Infrastructure Protection. A more detailed overview of the report is provided at Tab A.

As you know, the NDP report was submitted to Bill Cohen on December 1. Bill has until December 15 to forward the report with his comments to Congress -- he will provide you a copy of his comments before they go to the Hill and will probably ask for your support for actions he would like to take that are endorsed by the Report, such as requesting BRAC authorization from the Congress.

In light of the above sequence of events, you should wait until receiving Bill's views before responding to the NDP report.

Attachments

Tab A Overview of the NDP Report
Tab B NDP Membership

COZ

cc: Vice President
Chief of Staff

December 5, 1997

Overview of the Report of the National Defense Panel

The NDP Report acknowledges that the United States cannot ignore the near-term threats posed by Iran and Iraq in the Persian Gulf and by North Korea in Northeast Asia, concluding that, "to some degree," the two nearly simultaneous major theater wars criterion remains useful for force planning today. However, the NDP rejects two nearly simultaneous major theater wars as a basis for planning future U.S. forces because it will inhibit the transformation needed for the national security challenges of 2020. Instead, the report recommends that national security planning focus on six core functions: homeland defense, ensuring regional stability, projecting military power, space operations, information superiority and countering weapons of mass destruction.

The NDP briefly discusses future force capabilities but does not propose a specific alternate force structure. The report's discussion of strategic nuclear forces endorses every Administration initiative in this area, from START III to the stockpile stewardship program. The Report recommends against immediate NMD deployment, but supports a "hedging strategy" that permits rapid deployment if a threat should develop. The NDP recommends several major changes to the Army National Guard, including shifting some Guard combat forces to the Active component, placing Guard enhanced readiness brigades under the command of Active units, giving the Guard a central role in homeland defense (WMD, counter-terrorism and NMD), and reducing the Guard's role as a strategic reserve.

The NDP concludes that the wide range of future national security challenges demands that the United States transform not just the military, but the entire national security establishment. To accomplish that transformation, the report recommends a broad strategy with five major elements:

- The national security establishment would be transformed by institutionalizing a broad approach to national security, including interagency training and career paths analogous to the "jointness" requirements in the military, making the Treasury Secretary and Attorney General statutory NSC members, improving State-Defense regional coordination and establishing an interagency national crisis center.

- Innovation, experimentation and change would be institutionalized in the military by establishing joint organizations--battle lab, national training center, urban warfare center and concept development center--to integrate Service efforts in these areas.
- The Unified Command Plan would be transformed by creating a Joint Forces Command to perform the joint training function now performed by USACOM and an Americas Command that would take over the regional responsibilities of USACOM and Southern Command (both disestablished).
- The industrial base would be transformed by emphasizing commercial-off-the-shelf and dual-use technology, revamping the acquisition process to promote innovation and de-emphasize long production runs, identifying military-unique industrial technologies that must be preserved, and keeping industrial mobilization policies current with technological advances.
- Infrastructure would be transformed by two more BRAC rounds, supporting Secretary Cohen's Defense Reform Initiative, reforming the planning, programming and budget process to promote innovation and change, and reducing constraints on DoD financial management.

The NDP estimates that \$5-10 billion would be required annually to fund this transformation, which would come from the many of same sources identified in the QDR report (reducing infrastructure, acquisition reform, canceling some procurement, and reducing force structure and end strength). Almost all of these "bill payer" recommendations would require Congress to support initiatives more extensive than those in the QDR report, which it refused to support. Some of the NDP proposals would require Congress to partially sacrifice its control over the details of defense spending, which it has been reluctant to do in the past.

The NDP report will be criticized for not making specific alternative force structure recommendations, for not identifying "legacy" systems that should be retired and for not nominating procurement programs to be canceled. National missile defense (NMD) advocates will criticize the report for not calling for immediate NMD deployment and the Army National Guard and its supporters may criticize its recommendations for restructuring the Guard as an attempt to justify significantly downsizing the Guard.

National Defense Panel

Mr. Philip Odeen, Chairman

Mr. Richard Armitage

Gen. Richard Hearn

Adm. David Jeremiah

Hon. Robert Kimmitt

Dr. Andrew Krepinevich

Gen. James McCarthy

Dr. Janne Nolan

Gen. Robert Riscassi

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Jam today, road pricing tomorrow

FEW affairs have been more passionate in the 20th century than that between man and his motor car. The car has allowed millions to travel where they will, in comfort and security, at a time of their own choosing—truly, it has revolutionised people's lives. The car is not just an aspect of modernity, it is a precondition for it. Owning a car remains a goal for millions of poor people in every part of the world—and therefore, ideally, the affair should have continued for decades undisturbed. Unfortunately, it is not to be.

For years people have understood that the car was a cherished but dangerous thing. As one British inquiry put it in the 1960s, "We are nourishing at immense cost a monster of great potential destructiveness." The truth of that warning is all too apparent in the horribly polluted and congested streets of European, American and Asian cities.

Road transport accounts for about a quarter of the man-made gases that may be contributing to global warming, about which hands are being wrung in Kyoto this week. Actually, the role cars play in global warming is not the pressing question. More important, and more certain, is the enormous local damage (in terms of pollution, noise, ugliness and wasted time) caused by traffic congestion—and the great cost of the orthodox solution to that problem, which has been to keep on building roads.

Queue or pay

Cars in America may be 90% cleaner than they were a generation ago, but this improvement has been largely wiped out by growth. More and more rural areas are being buried under concrete in a vain attempt to tackle congestion on motorways and other major routes. Matters will deteriorate because the demand for travel is nowhere near to being sated. As economies grow, so does traffic. Governments understand this, and know that building roads is unpopular and offers no solution in congested areas. What then are they to do?

The underlying problem is clear enough: cheap car-travel has been based on an illusion. Only by making drivers pay for the costs they impose on society can the demand for motoring be brought into line with restricted supply. The choice for drivers is simple: queue or pay.

If roads continue to be operated as one of the last relics of a Soviet-style command economy, then the consequence will be worsening traffic jams and eventual Bangkok-style gridlock. If, on the other hand, roads were priced like any other scarce commodity, better use would be made of existing space and the revenues raised could be used to improve public transport. The mere fact of making motorists pay their way would free capacity to such an extent that bus travel would



become easier and faster, and subsidies could be reduced.

Politicians have long shied away from this approach because it is difficult to persuade voters to pay for something that has long been free. But some governments are starting to accept that there may be no alternative. Charging for ownership rather than use, as most tax systems do, makes little sense. Heavy fixed costs, including vehicle duties, insurance and depreciation, merely encourage drivers to use their cars more because the perceived marginal costs of motoring are so small. The way forward must be to make cars more expensive to use.

Higher fuel duties are often suggested as a way of doing this. But increasing the price of petrol and diesel for all motorists is very crude. It makes no sense to penalise a rural motorist driving along empty country roads when the problem lies in cities and on congested motorways. Road pricing, adjusted for place and time, can, by contrast, be fixed precisely to reduce congestion. Motorists driving through city rush-hour traffic would see on their in-car meters that they were being charged peak rates. The same journey made during the early hours of the morning in uncongested streets would attract a much smaller charge or perhaps no charge at all.

Improving public transport is another frequently proposed alternative to road pricing. If only the buses, underground systems and railways worked cheaply and efficiently, then motorists would leave their cars at home. All the evidence, sadly, suggests otherwise. One European study found that halving bus fares would reduce car use by less than 1%. Drivers are so wedded to their cars that they will be deterred only by higher motoring costs or regulation.

Critics claim that road pricing would merely displace traffic on to side roads, and that it would infringe privacy (because drivers' movements are recorded). New forms of charging provide answers. Technology makes it possible to track vehicles via satellite to make sure that rat-runners do not escape charges. Even without that innovation, if charges merely diffused congestion by spreading traffic-peaks through time, the resulting "displacement" would be a good thing. Minor roads can meanwhile be protected by regulation. As for privacy, only charge-evaders need have a picture of their licence plate taken as they pass by.

Politics, not technology, remains the real barrier to the widespread introduction of charging. Some countries have made a start (see pages 21-23). In others, politicians are still terrified that their car-owning voters will savage any government that tries to introduce direct measures of restraint. But where pricing has been introduced, as in Scandinavia, it has proved effective and popular. Those who argue that road pricing

LEADERS

ing is unfair because it discriminates against the poor ignore the fact that people too poor to own a vehicle, together with the young and the very old, suffer the ill-effects of congestion without the benefits of personal mobility. Moreover, if the revenues were used to improve public transport, the poor would benefit disproportionately.

If road pricing is to be made politically acceptable, both the methods of charging and the use of the revenues must be

easily understood and made totally transparent. Borrowing against future streams of charging revenues will allow much-needed improvements in public transport to be brought forward. So long as road pricing is introduced as part of a package of other measures, then it should be possible to persuade drivers that paying is better than being stuck in ever-worsening jams. All that is needed is a commodity that often seems as scarce as space on the roads—political leadership.

Divide and quit?

No. This is not the time to abandon the Bosnian peace agreement signed at Dayton, Ohio, two years ago

AFTER four years of brutal warfare, Bosnia has, thanks to the presence of some 30,000 NATO-led troops, enjoyed two years of peace. Yet the Dayton agreement's plan for rebuilding a single Bosnian state, involving autonomy for both a Muslim-Croat federation and a Serb republic, has come to little. Bosnia's Muslims and Croats each run their own affairs, while the Serb republic has split between hardline nationalists based in Pale and more moderate nationalists centred on Banja Luka. Siren voices say it is time to accept reality, forget Dayton and leave the parties to go their separate ways.

These voices are especially loud in America. One line of argument there asserts that never in history have antagonistic ethnic groups successfully shared power in a democracy after a big civil war; when the fighting stops, the choices are outright conquest or physical separation. Applied to Bosnia, the logic of this argument points to a redrawing of the boundaries of the Serb republic to make it easier to defend, and then to letting it join Serbia; the Croat lands would be allowed to join Croatia, and the Muslims would get the rest. It is a prospect that has its attractions on Capitol Hill, where many senators and congressmen, keen to bring home American troops, fear that struggling on with a peace agreement they regard as unrealistic will require an indefinite NATO presence. For them, partition offers an exit strategy.

One day, it may come to that, but even if it does partition will not be easy: it would almost certainly provoke mass migration and further bloodshed. Though some Bosnian leaders have, in the past two years, privately discussed redrawing the map, they have never been able to agree upon who should give up what. In particular, the Muslims—who made up more than 40% of the population before the war—would never accept a deal that did not give them much more than the quarter of the country they now control. Moreover, any agreement on land swaps would prompt minorities caught on the wrong side of the new boundaries to flee. Fans of partition tend to ignore the situation in central Bosnia, where many Croats live in enclaves surrounded by Muslims. Knowing they would be left in a Muslim-dominated state, most of these Croats dread partition.

Tough, it may be said, but they can move, and moving would be better than fighting. Yet fighting might well ensue, certainly if NATO had departed, even if an agreement had been reached among politicians. And the fighting might not be confined to Bosnia. The spectacle of a partitioned Bosnia would hearten every separatist in the Balkans. In areas of eth-

nic instability like Macedonia and Kosovo, who would listen to the West as it urged the merits of sinking differences and living together in harmony?

For all these reasons, it seems wiser to press on with Dayton. After all, it was never realistic to suppose that, in such a war-ravaged country, a complex new constitution would be running smoothly within a couple of years. And not all the signs are discouraging (see page 52). Provisional returns from the recent elections in the Serb Republic suggest that the hardliners in Pale have lost their grip over its western half. Franjo Tudjman, Croatia's president, has handed over a clutch of Bosnian Croats indicted for war crimes to the tribunal in The Hague. The West's representative in Bosnia, Carlos Westendorp, has managed to link the various telephone systems and reopen some airports. The economy is picking up.

Stick it out

Such modest progress as there has been, however, depends on the presence of NATO peacekeepers, who are due to depart in June. Europe's governments, and, more hesitantly, the Clinton administration too, understand that the West will have to remain militarily engaged for several years to come. But there is a strong view in America's Congress that, if troops must stay in Bosnia, the United States should not provide any. After all, the argument goes, Bosnia is essentially a European problem, and the Europeans have never contributed enough to their own security. The Europeans retort that they now have twice as many troops in Bosnia as the Americans. And they are adamant that, if America were to withdraw its men, they would pull theirs out too.

Unfortunately, the American troops are still needed. Militarily, the NATO-led force is more credible if Americans are involved. Politically, the Dayton accords stand a better chance of being implemented if America is, through the presence of its troops, demonstrably committed to them. There is also the health of the Atlantic alliance to be considered; it would surely suffer if America shied away from such a crucial military task as the restoration of peace in Bosnia. If Congress really were to bring its boys home, the Europeans would probably—despite current protestations—choose to stay on, rather than watch Bosnia sink into bloodshed once more. But a continued American presence would be much better for Bosnia, and for the alliance—and indeed for the United States, if it aspires to lead NATO. It is too soon to give up.



LIVING WITH THE CAR



No room, no room

There is no space, no money and no appetite for endless road-building. That is why road pricing is coming

SINGAPORE invented it. Norway copied it. Stockholm spent 20 years and \$1 billion before thinking again. Hong Kong retreated at the last moment in the face of a popular revolt. Politicians are terrified of road pricing. How can you get people to pay for something that has always been free? Yet governments all around the world, faced by worsening traffic congestion and pollution, are steeling their nerves and forcing motorists to pay for road space. Tolling technology is advancing so fast that \$3 billion-worth of electronic charging systems have already been installed worldwide. From Bergen and Bilbao to Paris and New York, motorists are learning that road space does not come free.

The motives for charging vary. Many countries, notably Spain, France, Italy and Japan, and several American states have long collected tolls as a way of financing the building of new motorways. In New Zealand, road users pay directly for roads through vehicle-licence fees, a levy on gasoline and weight-distance charges for heavy goods vehicles. The latest automated tolling equipment, which deducts charges from electronically tagged vehicles (travelling at speeds of up to 100mph) is being installed in more than 20 countries around the world. The tags are linked to in-car meters which can be loaded either with a pre-set credit or used to log travel for billing later. Charging, aimed at deterring excess

traffic from entering cities, is more controversial but is gaining acceptance.

It is no surprise that Singapore, with its own peculiar brand of democracy (selling bubble-gum is illegal), has been the first to attempt to use road pricing to limit the growth of urban traffic. After 22 years' experience (see box on next page), its planners are convinced that road pricing is the key to solving the city's traffic problems. New technology to be introduced next year will enable its current relatively crude system of area-access charges, based on paper licences, to be replaced by electronic tolls that vary according to time of day.

In Europe, road-pricing schemes have been successfully operated for more than five years in Trondheim, Bergen and Oslo. Trondheim, Norway's third-largest city, desperately needed a ring-road to stop huge flows of traffic coming through the centre of town. After much debate, the local council hit upon the idea of charging for access to the city centre, by putting up a ring of 12 toll stations, and using the revenues to pay for the construction of the new road. A high tariff applies from 6am till 10am, a lower one from then till 5pm. After that, travel is free until next morning. There is also a discount for cars with an electronic tag which allows them to go through tolls without stopping, thereby reducing the congestion caused by toll queues.

In Oslo, motorists pay a toll of about

\$1.70 every time they enter the cordon ring. The pricing scheme has proved so successful in financing much-needed transport developments that the city authority is now considering whether it should be extended.

The Netherlands has a more ambitious plan to introduce road pricing, covering the densely populated Randstad area of the four main towns—Amsterdam, Rotterdam, Utrecht and the Hague. It is due to come into effect in 2001.

Cars will have to carry a smart card containing cash credits that can be used for other transactions. The charge for driving into each of the four cities will be set high, at about 15 ecus (\$17), between 6am and 10am, but the price will fall to 3 ecus at other times. Non-payers will be caught on video cameras and sent a bill by the tax office, using the registration details culled from the number plate. Toll plazas are being placed to prevent drivers diverting on to lesser roads; it will be impossible to enter the centre without passing a toll point. There is still some debate about whether the proceeds should be returned to the public in lower taxes or whether they should all be spent on public transport.

Even in France, where a former president, Georges Pompidou, once justified the construction of a disfiguring urban motorway along the banks of the Seine with the quip that "*les Français aiment leurs bagnoles*" (the French love their cars), there is now a change of heart. Last August the environment minister was scorched by the press when pollution in cities such as Paris, Lyons and Strasbourg rose to the so-called third level, at which it is generally considered dangerous to many frail people and damaging to the lungs of the population at large. By September, when fine weather produced more smog, the government banned cars from entering Paris on alternate days, according to whether they had odd-or

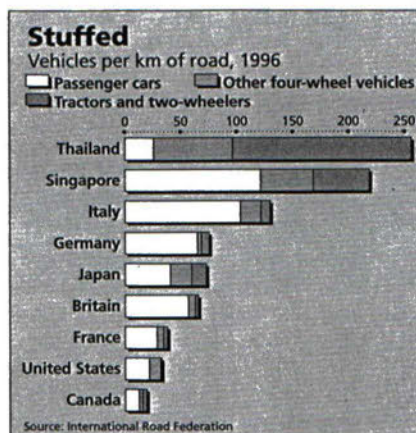
LIVING WITH THE CAR

even-numbered licence plates, and made public transport free.

It has the powers for such draconian action under a clean-air law passed 18 months ago by the previous administration. One French motorway company, which runs the A1 north of Paris towards Lille, introduced variable pricing, putting up the rate by 25% on Sunday afternoons to reduce the jam of weekenders returning to Paris. The result was a reduction of 15% in traffic with a consequential speeding up of journeys and reduction of jams. Motorway users either changed the time of their travel or changed their route or just travelled less.

Britain and Germany are much less advanced, but both have conducted trials of urban and motorway road pricing. Field trials in Leicester and Stuttgart have sought to establish how high charges must be before motorists are persuaded to leave their car behind and switch to other forms of transport. The Stuttgart trial, involving 400 drivers, yielded promising results, contradicting the view that car travel is relatively immune to price. If that were the case, very high charges would be needed to deter traffic, but the evidence from the preliminary trials is that a charge of DM15 (\$8) would be sufficient to deter significant numbers of drivers from entering inner cities.

Motorway tolling using automated collection techniques has proved easier to sell to voters than urban congestion pricing. By 2000 at least half the users of Portugal's na-



tional toll-motorway network are expected to be using a tag-based, non-stop electronic tolling system.

In America, an element of pricing is being introduced to lanes reserved for commuters who share cars. The federal government is spending \$14m to encourage such experiments. In California, a private company has built two express lanes in the central reservation strip along Route 91 near San Diego. Drivers pay to use this, at a cost of 50 cents off-peak, rising to \$2.75 in the rush-hour. Cars carrying more than three people pay nothing. Cars are identified by electronic tags passing roadside transponders. Rule-breakers receive an automatic \$15 fine. Users enjoy a saving of 40 minutes compared with driving in the normal lanes

along this ten-mile stretch of busy highway. Opinion polls before and after the introduction of the scheme showed public acceptance rising from only 40% beforehand to 70% after variable congestion pricing was introduced.

It is no surprise that much of the pressure for urban road pricing has come in crowded city states in Asia. Europe, with a population density four times that of the United States, is also a prime candidate. In one-third of all European cities, the average speed at peak times is 15 kilometres an hour or less. Over 60m Europeans suffer from traffic noise above the level where speech is intelligible and where stress is created by the persistent background roar. In most European cities, the air quality is very poor for at least 20 days a year. Cars stuck in traffic pollute three times as much as those purring along motorways, negating the effect of ever-cleaner exhaust emissions brought about by better catalytic converters and cleaner-burning engines.

Estimates of the costs of increasing congestion must be treated with caution. The European Commission, however, has calculated that the external costs of road transport in terms of accidents, infrastructure, environmental pollution and congestion, are 250 billion ecus (\$308 billion) a year, which is equivalent to 4% of the EU's GDP. By external costs, it means the costs not directly borne by those incurring them. Half of this 250 billion ecus, says the commis-

Singapore's plan

WITH incomes per head of \$23,000, a population of 3m, and an area of just 650 square kilometres, Singapore is a very rich, very small country. People want to cruise around in style. Their 370,000 cars (plus 310,000 buses, lorries, vans and motorbikes) translate into 220 vehicles per road-kilometre, one of the highest densities in the world. If nothing were done, the result would be endless jams.

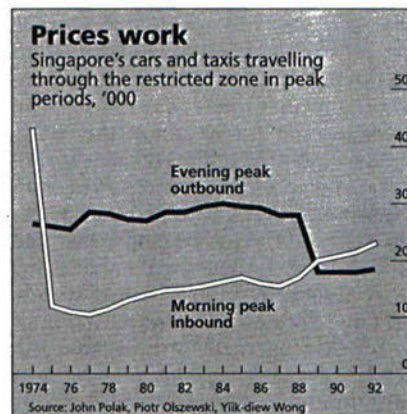
To curb growth in car ownership, Singapore has for many years slapped high customs duties on imported cars and set stiff registration fees and road tax. In addition, anybody buying a new car must get a permit; 40,000 new permits are issued each year. At today's rates they cost between \$27,000 and \$49,000.

As well as discouraging car ownership, the authorities have also restricted car use. For the past 20 years, to enter the central restricted zone, covering about 7 square kilometres, drivers have had to display a licence; a similar licence must be shown on the windscreen on the island's three expressways. In each case the tariff is now \$2 in the morning peak hour,

falling to \$1.30 at off-peak times. In 1989 the peak surcharge was extended to the evening rush-hour. That reduced afternoon traffic sharply (see chart) and raised average speeds inside the restricted zone by a fifth. Some drivers have switched to off-peak travel or now take buses or trains; through-traffic has declined.

From March next year the licence system will be automated with stored-value smart cards. With a built-in microprocessor chip, these can be preloaded to carry credit of up to \$150, and can be used for transactions other than traffic tolls. Unlike at traditional pay-as-you-go toll plazas, the charging will be done automatically by means of microwave communication between an electronic device in the car (where the smart card is inserted) and an overhead gantry, while traffic moves at speed.

Apart from that advantage, the main difference is that motorists will be charged more precisely for their actual contribution to traffic congestion. To avoid congestion surges at the end of expensive peak hours, the authorities may



introduce a so-called shoulder pricing system, with a tariff of \$2 at 6pm, \$1.50 at 7pm and \$1 at 8pm. Those who pass a gantry without a valid charge card will have their number plates snapped by video cameras and be fined.

Will this be the complete answer to Singapore's traffic problems? The planners think not. They once considered a plan to build a network of roads underground, but in the end it was the plan that was buried. Now they have shifted their attention to building a world-class public-transport system.

sion, can be blamed on congested roads.

Congestion and its associated problems are going to get much worse unless something changes. Over the next 13 years, the commission thinks road-freight traffic will grow by 37%, passenger cars by 58%. Most of Europe's people live and work in a densely populated area roughly bounded by London, Paris, Frankfurt and Amsterdam. This is where traffic problems are at their worst.

In the United States, where half the traffic on freeways crawls twice a day during rush-hour, the Transportation Research Board and the Federal Highways Administration estimate that, by 2010, traffic congestion on freeways will have quadrupled, making the peaks longer and longer. The time spent in jams will increase by 5.6 billion hours and the cost of delay will increase by \$41 billion. One example of the looming chaos: if present trends continued, a one-way 30-minute early-morning commute along Route 1 from New Brunswick, New Jersey, to Trenton, might turn into a five-hour crawl. Long before this, of course, many drivers would turn in despair to alternative forms of transport or simply avoid this journey.

Down with roads

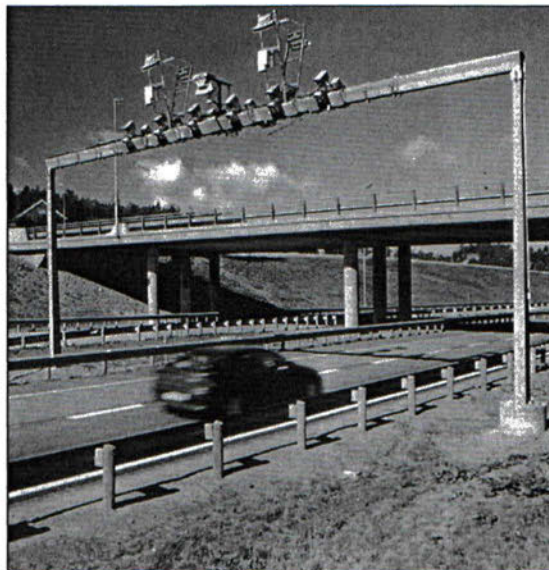
Until the beginning of the 1990s, the solution to rising congestion was seen as simple: predict the growth in traffic and provide extra roads to carry it. Several things have undermined that approach.

First, road construction has become increasingly unpopular with voters, particularly those who live near the path of planned new routes. In Britain, spectacular protests against by-pass highways, led by green activists but supported by tweedy, conservative country-dwellers, forced the government to scrap a huge road-building programme. In Japan, Tokyo residents succeeded in blocking a noisy new by-pass several years ago, and they won the right for noise pollution to be considered when building new roads—for instance, in Kobe, to replace the multi-level structures wrecked in the earthquake two years ago.

Second, economic growth in the 1980s and in the past few years has meant that new roads only briefly relieve congestion. Such is the level of suppressed demand that new roads attract even more traffic. It is now widely accepted that pouring concrete over large areas of the countryside in densely populated countries such as Britain and the Netherlands makes little sense. Professor Phil Goodwin, a transport economist at University College, London, and an adviser to the British government, recently pointed out that lack of space (rather than air pollution, greenhouse gases or the cost

of road accidents) means that traffic will have to be limited.

True, other measures short of road pricing could limit traffic after a fashion. Regulation has been used widely. Many European cities ban cars from their central areas, turning them over to pedestrians. Others such as Berlin and Bremen promote car-pooling clubs, so that people have access to cars when they really need them but otherwise tend to use public transport. Some 200,000 Germans now belong to such clubs in over 20 cities. Edinburgh city council is trying to import this idea into Britain, and it is also planning a car-free suburb, where residents can move in only if



Driving takes its toll

they agree not to have their own car.

Finally there is the burgeoning industry of transport "telematics"—beloved of the car industry because it puts fancy gadgets in cars. The ultimate in road telematics is the automated highway that was demonstrated near San Diego in California this summer. Platoons of cars are linked electronically; transponders in the vehicles talk to beacons by the road which keep them all in lane and properly spaced, allowing the driver to read a book or watch the scenery. A more modest version is being tried out in Europe by Mercedes-Benz. This links several lorries together with an electronic tow-bar so that they can travel closer together at higher speeds, using less road—all under the control of the front lorry's driver.

Until such science-fiction stuff becomes a reality, the real benefit of telematics is that its technologies offer a way to implement differential road pricing. At most, the future use of telematics could increase road capacity by little more than 10%, and even then the costs involved for highway authorities and for individuals may not be worth it. In the end telematics may prove better suited to reducing accidents than to

squeezing more traffic on to the roads.

All other forms of traffic demand-management amount to variations on command-and-control policies. Raising fuel duties is a blunt weapon which unfairly discriminates against rural motorists. Road pricing is the only method that can replace rationing-by-queueing with precisely directed charges. Even the most modest form of road pricing, tolls used for financing the construction of roads, can help provide extra road space. Once the infrastructure of toll stations is in place, raising charges at peak periods, as the French have done on the A1, could be done more widely.

Now sell it

Persuading motorists that road pricing is good for them is a task that politicians around the world are only just beginning to take up. The use to which revenues are put is crucial in convincing voters that road pricing makes sense. Borrowing against future revenues allows spending on better public transport to be brought forward so as to coincide with the introduction of road pricing. The success of Norway's city charging schemes shows that it is possible to persuade voters of the merits if they approve of the way the revenues are spent.

Most of the other obstacles to road pricing have been solved by technology, or soon will be. Privacy, the issue which forced the cancellation of Hong Kong's road-pricing scheme, is not a problem if drivers use pre-paid smart cards to pay tolls.

Such cards are already in use in 15 countries around the world, including Austria, France and Spain. The latest tolling equipment can charge vehicles on multi-lane motorways, even if they switch lanes at high speed. Recording of licence plates on camera is required only for vehicles which fail to carry a valid card. Vehicles diverting away from tolled routes on to minor roads are a more difficult problem. But the use of global positioning satellites, combined with in-car receivers and digital maps, allows vehicles to be charged wherever they are at rates varying according to the time of day and degree of congestion.

From now on politics, not technology, will dictate the pace of change. Governments around the world are still nervous about the impact of road pricing. But as more and more charging schemes are implemented and the benefits of less congested, unpolluted roads are felt, attitudes will change. In 20 years' time, when paying for road space will be regarded as the norm, people will look back and wonder why they were ever prepared to put up with the pollution, noise and paralysis of today's cities.

THE PRESIDENT HAS SEEN
12-9-97

THE WHITE HOUSE
WASHINGTON

'97 DEC 8 PM3

December 8, 1997

MEMORANDUM TO THE PRESIDENT

FROM: ANN LEWIS *ALW*
SUBJECT: ABIGAIL THERNSTROM

I have spoken with Abigail Thernstrom several times since the Akron Town Hall. She wanted to be sure you knew that she appreciated the opportunity to be part of the discussion; does not feel that she was "picked on"; and has told the press that she thinks what you are doing - encouraging discussion about race - is very important. When the Boston Globe misquoted her in a way that was negative to you, she called the editor and insisted on a correction.

She very much agrees with the emphasis on education and with the kind of school reforms underway in Chicago. (Abigail is a member of the K-12 Education Board in Massachusetts.) She and Stephen are looking forward to the conservatives meeting.

I thought you would be interested in her column this week in Newsweek which makes many of these points.

Thernstrom's column this week in Newsweek

*copied
Lewis
COS*

Going Toe to Toe With Bill

The conservative who sparred with Clinton over race on what she didn't get a chance to say about affirmative action. BY ABIGAIL THERNSTROM

IT WAS NOT A ROUTINE DAY FOR ME. I AM A SCHOLAR AND A writer; I spend most of my time working at my desk. But last Wednesday I found myself going head to head with the president of the United States. I was on a stage in Akron, Ohio, discussing race in America at a televised "town meeting" moderated by Bill Clinton. (I had been invited because I am the coauthor of a new book, *"America in Black and White,"* which chronicles black progress over the last half century and argues against the use of racial preferences.) As part of a yearlong initiative, the president has asked for open talk on race—and last week he got it. At the end of the two-hour meeting, Clinton turned to the audience in a University of Akron auditorium and asked, "How many of you believe in continuing affirmative action in higher education?"

With perhaps too much chutzpah, I shouted, "The issue, Mr. President, is not affirmative action but *racial preferences*." I didn't have the microphone in my hand at the moment, but the president heard me and wheeled around. "Abigail," he asked, "do you favor the United States Army abolishing the affirmative-action program that produced Colin Powell? Yes or no?"

This is not a question that can be answered with a yes or a no, and the discussion of race requires thoughtfulness, not theater. Most Americans believe in affirmative action as it was originally conceived: as outreach—a nondiscriminatory search for the best possible person regardless of race. But the overwhelming majority of Americans are opposed to racial preferences—numerical quotas, goals or timetables that lead to double standards. They do not think America has solved its racial problems. Few are so naive as to believe that the country has miraculously become colorblind. But most do not like policies that view people first and foremost as members of racial groups. They also know that in a society already too conscious of race, double standards in contracting, employment and admissions (that is, when less is expected of blacks and Hispanics than of whites and Asians) widen the racial divide, heightening rather than reducing race consciousness and racial tension.

The Colin Powell example is instructive. When the president turned to me, I told him that I do not think racial preferences made Powell. And I went on to note that the army does something very right: it prepares recruits to compete on a level playing field. But our short exchange ended there.

Preferences ignore and disguise the real problem: a racial gap in cognitive skills, a crisis the military understands and addresses.

The armed forces are an equal-opportunity program—or at least as close to one as we can get in an imperfect world. Minorities do well in the services because they are, by and large, treated equally, and rise or fall according to their merits, not their race. And most of the time, the best go far.

At one point in his career, Powell did benefit from the proper kind of affirmative action—not a quota but a widening of the net. The question was promotion to brigadier general. A list of candidates had been

sent to the secretary of the army, Clifford Alexander, and it included no blacks. Alexander sent it back saying, in effect, look again. Powell, who, among other accomplishments, had graduated second in his class from Command and General Staff School, was added. The rest, as they say, was history.

That approach to affirmative action—in the military, in universities, in the corporate world—is right; racial preferences are wrong. The debate often centers on higher education, and I believe that admissions should be colorblind. When, for example, the University of California, Berkeley, admitted black and Hispanic students with SAT scores 300 points on average below those of whites and Asians (and with similarly lower grade-point averages), that is a preference. In the short run, abolishing racial factors in admissions will mean fewer non-Asian minorities in top colleges, and that is painful.

But in the long run, there is only one genuine solution to the nation's continuing inequality: close the appalling, unacceptable racial gap in educational performance in the K-12 years. Today, on average, a black 12th grader reads almost four years behind the average white student. And there are similar disparities in other subjects. Shame on us that we set any of our kids up for

failure in a world in which only the highly skilled do well. We can do better—and we were doing better just a decade ago, when the gap between whites and blacks in educational performance was closing.

Thankfully, there is emerging agreement on this crucial point. "The era of dual standards is over," Hugh Price, president of the National Urban League, said recently. "We have got to get our kids clearly and unquestionably qualified." Precisely. Real equality of opportunity is the key to minority advancement, not double standards. Let's abandon the latter, and get to work on creating the former. That would be real progress.

TERNSTROM is the author, with Stephan Thernstrom, of *"America in Black and White: One Nation, Indivisible."*



RUTH FREEMAN—AP

Pointed exchange: Clinton with Thernstrom (far left)