

SENATOR JOHN HEINZ -- REPUBLIC NATIONAL BANK OF NEW YORK
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It's a great pleasure to be here at the Republic National Bank of New York. I do want to say that I am honored by the invitation to be here because the speakers you have had here are really extraordinary and able people, and I'm quite flattered to be placed in their company.

The Senate's schedule this year, as you might have gathered, has been unusually hectic, and so one's not always sure one can work the time in.

I must say, however, that it's been delightful to have a chance to chat with some of the people at the table. I've discovered many things in common with Mr. Safra: he and I are both married to multi-lingual women, both having as their native tongue Portugese. We both look forward with some trepidation to the day in which they meet, because then we will both become superfluous in any language.

Let me say to you, Mr. Safra, as honorary Chairman of this honorable group, that the Republic National Bank has quite an extraordinary record. From your establishment sixteen years ago, you have grown with great rapidity, and in the process of growth you have not sacrificed what people in the financial institutions industry would call "paying attention to the fundamentals."

The past several years have been incredibly dynamic years for financial institutions. They have been not only dynamic, but they have managed to inflict a good deal of challenge and difficulty on many financial institutions. I found in your annual report that your bank

has just in the last year set another record for its deposits growth and for its earnings growth. At a time when other institutions are not nearly so fortunate, I think that's a very significant record, and it speaks extremely well for your philosophy of banking.

Today I was thinking of what I might most appropriately address, and there are three areas that I would like to cover as briefly as I can. I think the most important one is the overall economic situation: What we in the Congress -- in the new Republican Senate -- see as the options, and maybe where we're going to head.

Then, I'd like to progress to some of the particular challenges facing financial institutions. As you know, our Senate Banking Committee, chaired by Senator Garn, has been going through nearly a month of rather detailed hearings on the issue of financial institutions deregulation and of the level playing field and a variety of issues of that kind.

Finally, I would like to touch on an area which is of special interest and concern to me, and that is international trade patterns, what they signify to this country, and what they mean for us in a very practical sense.

I come to you as someone who is very deeply committed to the change, the new direction, that we have managed -- in fairly short order -- to begin to put in place in this country. I worked rather hard as Chairman of the Republican National Senatorial Committee to try to elect a Republican Senate. And nobody -- except perhaps Howard Baker, who became the Majority Leader -- was happier than I was after having spent two years beating the bushes on behalf of my now colleagues, to give us a fifty-three to forty-seven majority in the Senate.

My only regret is that a very dear friend of mine, Jack Javits, was not among those present to become a committee chairman. He would

have been -- with no disrespect at all to Chuck Percy, who could have been a chairman of another committee -- a great chairman of the Foreign Relations Committee . . . and we all dearly miss him, and what he would otherwise be contributing to us.

But that Republican majority, frankly, gave Ronald Reagan and us a chance to put into practice some fiscal responsibility, and an opportunity to provide incentives to the American enterprise system. And after twenty-five years of the opposite, it is my view that the shift in emphasis was long, long, long overdue.

You know as well as I do what the tax package is comprised of. I learned better than most what was in both because I'm a member of both the Finance Committee and the Banking Committee, and these two committees accounted for two thirds of all the spending cuts and one hundred percent, obviously, of all the tax cuts. So I come before you to confess that readily, and also to confess that it is a job that we have only started, but not yet completed.

I suppose the big question that everybody asks me is, "What happened between the time Congress adjourned for the August Recess and the time we got back into town after Labor Day?" At the beginning of August Recess I never saw a happier group of people: I don't mean just my Senate colleagues, I mean all the small business people I talked to. People generally thought what we had done was absolutely wonderful and I made the mistake, like my colleagues, of leaving town to spend some time in England and France with my family. When we got back, what we found was that there was no longer a bond market, short term interest rates were up around twenty-plus percent, the number of bankruptcies was soaring, and the number of people expected to go

bankrupt was even higher than that -- to the point that one of my constituents said, "Senator, if there is one good thing about this, it's no longer dishonorable to be bankrupt. Faint praise!

Indeed, the problem is, I think, plain to all of us. I agree with the conventional analysis. The conventional analysis is that short-term rates are so high because investors have been burned so many times, they are not interested in the bond market. Nobody can sell their long term issues, as you have gathered this week. And as a result, there's a lot of crowding in short-term issues and short-term interest rates, which show the effects of demand relative to supply. And the recession that we are now experiencing is a result of high interest rates being very, very successful in choking down both some parts of the economy and some parts of the country, much more successfully than some other parts.

Some small businesses, for example, simply do not have the options in the financial market that larger businesses do.

Someone who comes from a highly industrialized northern state might get particularly concerned about the high interest rates because when states like Pennsylvania, New York, Illinois, or any of our northern or eastern states lose jobs through the crunch of high interest rates, we are least likely to be able to recover from the standpoint of our economic base. More new businesses are formed, but they tend to be formed in other parts of the country -- in the Southwest.

It is my view that, strangely enough, the President who put forward a plan to try and bring his budget goals more into line with what was needed, has been in fact too modest and too shy in what he has asked of the Congress. It's probably pretty well known by now

that even if we enacted exactly the budget reductions the President proposed to us a few weeks ago, we would still come up short in 1984.

I was reliably informed that the President had gotten a somewhat similar assessment the week before. That's good news and bad news. It's good news to know that the President had gotten the news before Jimmy Jones, Chairman of the House Budget Committee, made it public. The bad news was that he hadn't gotten it from us in the Senate. Because for months people in the White House, I think, have been trying to tell the President that everything really is all right with his economic program. That's not to be critical of the program, it's to be critical frankly of people who end up protecting other people's egos and maybe other people's reputations, rather than dealing with the problems.

I think that we are going to have to do a good deal more in the way of budget cutting, and we are going to have to do a lot more on the revenue side. We have that wonderful word "revenue enhancement." The goal that we should set for ourselves is to close the aggregate deficit gap over the next three years by a total of about a hundred and fifty billion dollars. That's ambitious, I think. If we did it, however -- if we sat down and really put the pieces of that puzzle together -- it would have a very significant effect on the long term bond market and on the financial health of the country.

I do not believe that supply-side economics, in which we have now a very substantial investment, will work at eighteen and twenty percent interest rates. I believe it will work quite well because of the kind of incentives we have put in. And we can have a fiscal climate that allows interest rates to go significantly lower. I'd be very happy to see interest rates down about five points and stay there.

And I think that would be higher than anybody ever wants, but it would be quite satisfactory from the standpoint of achieving economic performance.

The one hundred and fifty billion dollars deficit reduction target could be met, I think, by taking about thirty billion dollars out of spending programs over three years. I think that we have to tackle the entitlement programs, otherwise we lose credibility . . . The credibility at issue being whether or not Congress is willing seriously to attack the growth of federal spending.

We didn't do badly the first time around. We made budget cuts in entitlement programs totalling some one hundred and thirty-five billion dollars over three years. That's never been done before. We should have at least, if not a sense of some euphoria, a sense of some satisfaction.

But we shouldn't stop at that given the fact that so many programs still remain indexed to the increase in the cost of living. The fact that our basic ability to pay our way is indexed either, depending on your point of view, to real growth, or, if you will, to growth in wages, which for the last five years have grown more slowly than prices, is legitimate cause for concern in this country.

I think we could do a lot better, frankly, on the defense budget than the President is willing to do. I could support up to a thirty billion dollar cut in the defense budget over the next three years. We couldn't get a third of it this year, but we could get five or six or

seven of it this year depending on what decisions we made. And the remainder I think can come from other appropriated programs. That's not too much to ask.

It is too much to ask a second twelve percent across the board cut -- in my judgment and in the judgment of most of my colleagues -- of a program we've just finished cutting. That can't and won't apply.

And then, I think we could get the other seventy-five million dollars in revenue enhancement. Whether you are talking fifty or a hundred it's still a tough choice. Now my own personal preference at this point is that it should be a mixture of some excise taxes and some stretch out of the individual '83 and '84 tax cuts, and that we should give up the so-called indexing provision which I think was pretty silly to commit to three or four years before we had to.

But there are other schools of thought. Everybody is casting around for a better solution, and I myself am not enthusiastic about the prospect of having to redo if not undo something that we just did. And the President's people are rather reluctant to go along with any proposal that would have the effect of undoing the tax cuts, that **now** after the expenditure of a great deal of political capital are not marked into place. Yet I tend to believe that it is only if we give up some of that tax cut that we will be able to get the political support in the House of Representatives that we must have in order to cut the entitlement programs.

Now I wouldn't favor running out and reducing the tax cut, as I described, without tying it very, very securely and certainly to the spending cuts that I mentioned a moment ago. Particularly on the social and entitlement side. And if we can't do it that way, then the next

best solution is some kind of more expensive excise tax alternative. There are many of them -- not just liquor, cigarettes, gasoline and chewing tobacco -- but there are slightly more sophisticated excise taxes. Coming from a gas consumer state I am not at all in love with instantly deregulating all natural gas and putting a windfall profits tax on it because that has some inflationary consequences to my constituents. It also, however, does result in a significant amount of revenue. It is in part another excise tax, because the consumer obviously pays. I think in the next week we will be coming quite forcefully to grips with this issue.

I can tell you that a majority of the Republicans in the Senate are urging what I will call a bolder course of action than that course of action originally advocated by the President. I think the White House is beginning to understand that we just have to have a more substantial mid-course correction than originally thought, if supply side economics is going to work . . . and we all want it to.

I said to you that I would touch on financial institutions and also on questions of international trade. The principal response to the problems of the thrifts has been an omnibus banking bill introduced by Senator Garn a few weeks ago, which should really carry forward a number of additional deregulatory steps, and moves toward breaking down still further the differences between the variety of institutions we have in this country -- including a number of ones that affect commercial banks.

A number of significant changes in regulation are proposed. We would have the opportunity to do much more in terms of commercial banking. Banks would be allowed to have their own money market funds, and included in that package, by the way, is a bill of mine, bankers' acceptances,

to significantly increase the amount from the current ratio of one hundred percent of capital to two hundred percent of capital, three hundred if approved by the Fed. This would allow banks to issue substantially more acceptances, which are often the least costly way of financing exports.

It is really unclear to me whether Jake Garn's bill, as it is introduced, is going any place. On the one hand, the reason for having an omnibus banking bill is to have something in it for everybody, and he does. Also, by having something in it for everybody he has something in it that everybody is against. And the one clear thing that developed in our hearing was that people would come forward, and all they would testify to is what was wrong with the bill. A few people said that they liked the things in the bill. The ABA said they liked the things in the bill, but they also said that they didn't like the new powers the bill gave the thrifts. I've got to tell you that it is not exactly clear to me that things are going to go ahead.

It is clear to me that most members of the committee, including Senator Garn and myself, feel that the Depository Institutions and Deregulation Committee is making everybody's life much more difficult, and is going to come in for much more criticism. Not that we mind the concept of deregulation . . . if it hadn't been for the Senate Committee bill last year there wouldn't be any deregulation. Congressman Fernand St. Germain did not exactly push that one hard. That is something that we quite proudly can claim major credit for. But while the DIDC is clearly taking steps toward deregulation, in fact they have given thrifts, which we are worried about, very little more in the way of competitive power. Instead, they cost the thrifts a good deal of money, of which

they are in rather short supply.

I suspect that if there is going to be legislation this year it will be a much more modest version of Senator Garn's bill. But I also think that Senator Garn will press ahead -- I think appropriately-- with his basic contention that we should not approach banking problems on a piecemeal basis as I think we can be criticized for doing before, but in a more comprehensive and significant way.

Let me turn, for the last few minutes, to my concern about some international economic affairs. Recently, I was privileged to address the National Foreign Trade Council, which was meeting in Washington, D. C. I expressed to them my concern that there is a problem with protectionism, and the news media says Congress is in a protectionist mood. They forget that the Canadians, the French, the Swiss, the Austrians, and the Japanese apparently don't know the meaning of that word or are unwilling to pronounce it in spite of their actions to the contrary.

I really believe there is just a rampage of world protectionism out there which we don't see. But the American public and the American news media seem to be hopelessly blind to some of the really obvious things that happen to tangible products. When Nippon Telephone and Telegraph says to Motorola, "We really do like your pageboy electronic paging system; we're going to buy one hundred of them, in spite of the fact that we have two hundred fifty thousand employees who might be able to use them." people think "Well isn't that nice." And of course, what they're really doing, is taking them apart and sending them over to Sony to copy them exactly, maybe making a few marketing improvements, and by the time Motorolas get into the market, there won't be one anymore.

But in the services industry, which is the one that all of you are in, the trends are no less dangerous, they are no less debilitating,

and they are no less omnipresent. I think that most of you are aware that Canada will allow you to engage in banking in Canada, but if you're going to do anything there, it has to be something rather significant, quid pro quo, such as you have to have your computer located there if you want to do anything to process it.

Even that bastion of free enterprise, the Federal Republic of Germany has said, "Yes, you can transmit data across our boundaries, but you have to process a majority of it in the Federal Republic of Germany." And this directly strikes your Republic National Bank, or Citibank, or American Express or Western Union.

Our Government's trade negotiators are not standing up for something that is in the best interest of everybody -- a much more free and open trading system, one where we insist on reciprocity, and one where we are willing to get rough to enforce that reciprocity in the interest of achieving a more open trading system.

Sometimes in my home state I get the reputation of being a great protector, and therefore, by implication, a protectionist of the steel industry which competed year in year out with subsidized competitors from the U.K., France, other countries. Those people fail to realize that anytime there is an introduction of government subsidies, it is just as pernicious as somebody who puts up a huge barrier. Both pervert the allocation of resources, both in effect make the world ultimately poorer, and neither are in our interest.

What are we doing about that? A number of things. The first thing we're trying to do -- and this really gets right down to my Subcommittee on International Finance -- is to stop shooting ourselves in the foot, as Adlai Stevenson used to say when he was on that committee.

And indeed we have been shooting ourselves in the foot for a number of years, by making it very difficult for Americans working for American domicile companies to work abroad. Section 911 913 of the Tax Act made it very unprofitable to be an American citizen. We have changed that in the 1981 Tax Act.

We have reported from my committee in one case an amendment to the Foreign Corrupt Practices Act, which heretofore made some people rather nervous to buy a foreign agent a cup of coffee. That legislation will move through the Senate -- it is moving more slowly in Congressman Wirth's subcommittee in the House, but I think he intends to move the bill. What kind of a bill we end up will remains to be seen.

We have passed by a vote of ninety-three to nothing, the Export Trading Companies legislation that would allow banks, among other things, to participate as owners in Trading Companies -- therefore, we assume giving banks a greater interest in being more aggressive financiers of exports.

Finally, we will be holding a set of hearings in the very near future to try and put the spotlight on some of these protectionist activities of other countries. We're going to focus on services very strongly. We'll focus on performance requirements and a variety of activities that our so-called trading partners undertake. I don't think American firms should be afraid of competition. What we should want, and what our government should demand, is for our firms to compete as free and equal and reciprocal firms.

I don't know what there is about people who move into that lofty address at 1600 Pennsylvania Avenue. Every single President and his

staff will start out with wonderful ideas. Ronald Reagan started with a lot of very tough talk about how he is going to stick up for and defend American interests . . . and, incidentally, he did a rather good job of it at Cancun, Mexico, and I think we gained a lot of respect from the developing world as a result. But when it comes to trade matters, for reasons best known only to mind-readers, Presidents and their staffs just seem to wipe their mental slate clean. They suffer from some kind of dangerous amnesia. And in that area to date, this Administration is unfortunately not doing much better than those that have gone before. We hope through these hearings to substantially increase the Administration's awareness, as well as public awareness of the kinds of problems that I've discussed. If we do it, it will be possible for us to make a good deal more progress, not only in the trade area, but if we can make progress on the budgetary and economic matters I discussed at the outset, we can really deliver to the American people on the promise of renewed economic growth, the promise of a healthier and more productive economy that has somehow managed to elude us for the last ten or fifteen years. That would be welcome news to us all, I'm sure.