WHAT THE #@&% HAPPENED?

The current economic crisis has roots reaching back three decades—a series of wrong turns and missteps by our national leaders in both political parties. This group of three articles is intended to help NALC members understand the origins of the crisis and the opportunity it presents, its impact on the Postal Service, and how individual citizens contributed to the crisis, often with the encouragement of irresponsible financial institutions.

Understanding the Why is the Key to Building a New Shared Prosperity

I. The collapse of the Reagan Revolution

The economic recession pummeling the United States—and the rest of the world—began more than a year ago. Fourteen months on, the picture is bleak. More than 3.6 million Americans have lost their jobs. Auto sales and housing starts are the lowest in more than 50 years. The stock market and housing prices have fallen at a gut-wrenching rate and the nation's GDP fell at an annual rate of nearly 4 percent in the last quarter of 2008.

Why is this happening? The answer is not as obvious as it seems, and it is not just an academic issue, either. Knowing why we are in this mess is key to figuring out how to get out of it, and understanding where the nation took the wrong path is central to building a future in which workers benefit from economic growth and all Americans can enjoy a shared prosperity.

On the one hand, it now seems pretty clear what "caused" the economic meltdown—a housing bubble of historic proportions burst. Between 1990 and 2007, the mortgage debt of the American people soared from $2.5 trillion to $10.5 trillion as tens of millions of Americans used their homes as piggy banks to borrow and spend like there was no tomorrow *(see story on page 14)*. Home prices escalated year after year and Americans borrowed against their inflated home equity to finance a boom in consumer spending.

Not content to stop there, we all—or at least many of us—maxed out our credit cards to keep the boom going and U.S. savings rates dropped to near zero while our global trade deficit soared into the stratosphere. Of course, there were villains in the banking and financial services sector who aided and abetted us with new-fangled subprime and interest-only mortgages. And Wall Street corruption, greed and so-called "innovation" that generated the financial voodoo of credit default swaps and Alt-A subprime mortgage-backed securities surely contributed to the crack up that followed. But the basic cause of the crisis is understood: the collapse of an enormous housing bubble.

On the other hand, the story is really a lot more complicated than that. The housing bubble did not just materialize out of thin air. It was not a natural phenomenon like Hurricane Katrina or some "hundred year" flood. Rather, it was just the latest of a series of asset bubbles that have been created—and then burst—over the years. Remember the savings and loan crisis of the 1980s, which hinged on a commercial real estate boom? How about the Asian financial crisis of the 1990s, when the "five tigers" turned into cowering kittens? Or the dot-com bubble in the early years of this decade?

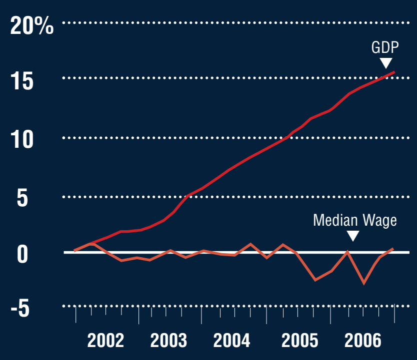
These repeated boom-and-bust cycles did not happen by accident. They are a direct result of deliberate policy choices by our government over the past three decades—choices to deregulate banking and finance, choices to promote "financial services" rather than manufacturing or other industries, choices to advance globalization and free trade, choices to favor trading and selling over producing in America.

II. The Democratic co-conspirators

Historians point out that the "Reagan Revolution"—when the politics of America shifted decisively to the right—actually began during the Democratic administration of Jimmy

Divergence

The median wage has lagged behind overall economic growth since the expansion began. Cumulative change:



Carter. In the face of double-digit inflation (a result of oil price shocks in 1973 and 1979), corporate America began to get the upper hand in American politics and economic policy-making.

Trucking and airlines were deregulated in the late 1970s and President Carter refused to support labor law reform in Congress even before Ronald Reagan was elected. But it was Reagan who openly pursued a virulently anti-union policy, first firing the striking PATCO air traffic controllers in 1981 and then packing the federal courts with right-wing judges who weakened the labor movement by making it legal for companies to "permanently replace" strikers and to shift union work to non-union subsidiaries. And it was Reagan who started the country down the path of financial chaos with the deregulation of the savings and loan industry in 1982.

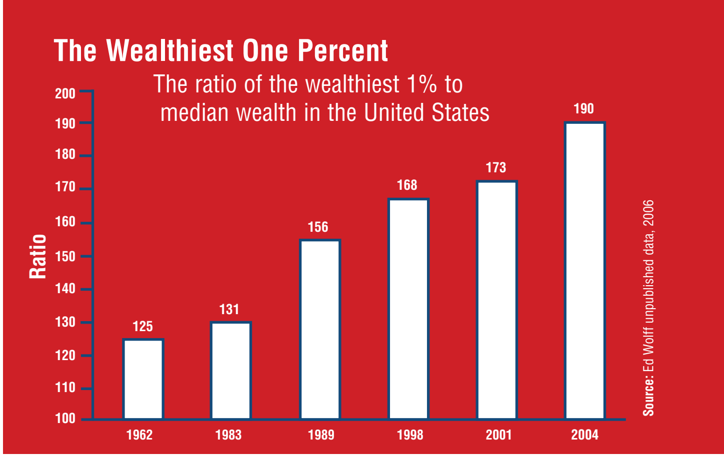
Add in Reagan's policies favoring free trade and privatization of government services and you see the beginnings of the economic model that has dominated our country for nearly three decades—through administrations both Republican and Democratic. Wages began to stagnate even though productivity continued to slowly rise *(see the chart at left)* and union density—the share of workers who belong to unions—began to fall, from 23 percent in 1981 to 12 percent today. Manufacturing began to go overseas and our trade deficits began to soar, reaching more than $900 billion in 2007. And, of course, consumer and mortgage debt began to take off. A low-wage, debt-based economy that placed banks and financial services at the center of the economic universe took hold.

All through the 1980s, the Federal Reserve punched holes in the architecture of the financial regulation set up during Franklin Roosevelt's New Deal. Banks were allowed to cross state lines and exceptions were made to the 1930s-era Glass-Steagall Act, which prohibited commercial banks from engaging in investment banking activities, like merger finance and stock trading. Even as President George H.W. Bush set up the Resolution Trust Corporation to bail out the collapsing S&L industry, corporate lobbyists pressed for more deregulation and more free trade. They did not succeed until President Clinton reached the White House. Clinton signed the Gramm-Leach Act, which effectively repealed Glass-Steagall and opened the way for mergers of banks, stockbrokers and insurance companies. Clinton also joined forces with the Republicans to win approval for the North American Free Trade Agreement over the objections of most of his party. Even the Asian financial crisis of the late 1990s and the near bankruptcy of Mexico in 2000—which damaged the American economy indirectly—did not disrupt the disastrous policy trend.

With the election of George W. Bush, the Reagan revolution was complete—despite the bursting of yet another bubble at the beginning of his term, this time involving wildly inflated dot-com stocks.

A frontal assault on the labor movement was resumed, the minimum wage was frozen, Labor Department regulations on overtime pay were weakened and wages again began to fall, reversing a brief upward trend seen in the second half of the 1990s. Labor's share of national income hit an all-time low in 2005 and income inequality rose to levels not seen since the pre-Depression 1920s—the top 1 percent of Americans raked in 21.2 percent of national income while the bottom 50 percent of families got less than 13 percent. The economy grew only because consumers continued to sink deeper into debt, wooed by the easy credit made available by the Federal Reserve and the home equity bubble it facilitated.

If that were not bad enough, regulators in the Bush administration were simply asleep at the switch. Fed Chairman Alan Greenspan denied there was a housing



In 1962, the wealthiest one percent of Americans held 125 times the wealth of median income workers. The disparity has grown steadily ever since.

bubble and refused to step in to stop the spread of subprime mortgages. The Securities and Exchange Commission called on investment banks to engage in "self-regulation," even after it authorized a tripling of the debt they could take on. And nobody was paying attention to the proliferation of "derivatives" like credit default swaps—"financial weapons of mass destruction," in the memorable phrase of investment wizard Warren Buffet. That brings us to where we stand today—facing a total mess, to put it politely.

III. The Reagan Revolution is Dead —Long Live 'Shared Prosperity'

With the election of Barack Obama, the Age of Reagan appears at last to be over. During the campaign and in the first weeks of his presidency, Obama made it clear that America must change course dramatically. The economic policies of the past 30 years have been thoroughly discredited. Of course, the Obama administration cannot recreate the New Deal or even the world pre-1980—too much has changed since then. But it must lay the foundation for an economy that makes it possible for workers to enjoy what progressive economists call "shared prosperity." That will depend on four pillars of economic policy: a strong labor movement, sound regulation of the global financial system, massive public investment, and a new social contract that ensures health care and secure pensions for all. These are the key changes that must come:

➡ **EMPLOYEE FREE CHOICE ACT:** Congress must make it easier for workers to organize and bargain for better pay and benefits. As it was between World War II and the late 1970s, economic growth should be based on consumption and savings derived from decent wages that rise with productivity. Without a stronger labor movement, workers cannot win a fair share of the nation's economic pie.

➡ **GLOBAL FINANCIAL REGULATION:** The era of casino capitalism must come to an end. Financial institutions cannot be allowed to take dangerous risks with investors' money. Greater transparency is needed and rules must be set at the international level to ensure that financial crises do not race around the world overnight. Repeated asset bubbles have exposed deregulation as a failure—sound regulation is needed now more than ever.

➡ **PUBLIC INVESTMENT:** Our transportation, education and energy infrastructure has suffered through decades of neglect. Building a 21st century infrastructure for a modern economy is crucial to future growth. The economic stimulus legislation enacted in February is a start, but more must be done.

➡ **A 21ST CENTURY SOCIAL CONTRACT:** Creating an economy that works for everyone—not just the corporate elite and the mandarins on Wall Street—requires a new social contract. Universal health care and safe pensions are the keys to such a contract. Whether it chooses public systems or private-public approaches to these issues, Congress must enact comprehensive reforms to ensure health and retirement security for all Americans—and do so soon.

Rahm Emanuel, President Obama's chief of staff, joked after the election that "a crisis is a terrible thing to waste." He was on to something. The crisis we face poses some very serious challenges, but it also offers a major opportunity to repair the damage of the Reagan Revolution and to put us on the firm path to an economy based on shared prosperity. There is no better time to start than right now. ✉

ECONOMIC STORM BUFFETS U.S. POSTAL SERVICE

HOLDING ON UNTIL RECOVERY BEGINS

Scores of failed banks. Thousands of businesses ruined. Millions of homes foreclosed and millions of jobs lost. Trillions of dollars of wealth vanished. The country's best and brightest economists and investors didn't see the financial calamity coming. But letter carriers were among the first to sense the danger as the volume of mail on the loading docks at delivery units across the country started to shrink more than two years ago.

Postal economists have long known that mail volume is a leading economic indicator. Indeed, as the rest of the country was just beginning to feel the effects of the recession, the U.S. Postal Service was already facing rapidly dropping mail volumes and billions of dollars in losses. When several major financial institutions collapsed in September 2008, setting off alarms, the Postal Service had already recorded seven consecutive quarters of decline in mail volume. At the end of the 2008 fiscal year, the Postal Service announced it had delivered a whopping 9.5 billion fewer pieces of mail than a year before while posting an annual deficit of $2.8 billion. It turns out that our satchels were significantly lighter on both Wall Street and Main Street as the economy nosedived.

While the Postal Service has battled the electronic diversion of mail for years, the rapid downturn in the financial sector in 2008 was profoundly bad news—a deep, cyclical decline in volume was layered on a gradual structural decline. And the particulars of this recession to date are especially bad for the Postal Service because the real estate, housing, banking and insurance sectors are among the most mail-intensive industries in the country. In fact, revenue rich mail from these industries accounts for 10 to 20 percent of the mail we deliver. In 2008, credit card mail plunged 24 percent. Mortgage-related volume fell even more—an eye-popping 37 percent.

The link is undeniable: The volume of mail has plummeted because Americans are building and buying fewer homes and the credit markets have seized up, unable to get running again in the current atmosphere of financial fear and mistrust. The bleak landscape facing these industries has created a nearly unprecedented crisis for the

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Postal Service. In the first quarter of the new fiscal year, mail volume is down by another 9.3 percent—the largest quarterly decline since the Great Depression of the 1930s.

With the economy sinking into a deep recession, postal management responded with a rigorous campaign to cut costs. In FY 2008, it slashed more than 57 million work hours across all crafts, a 4 percent decline from a year earlier. While the USPS has not resorted to layoffs, nearly 30,000 career jobs were eliminated in 2008 through early-outs and attrition coupled with hiring freezes. And, in cooperation with the NALC, the Postal Service has embarked on an innovative interim route adjustment program that will expedite operational savings in the delivery function.

Looking for a lifeline

Despite these measures to weather the economic storm, the Postal Service still faces a severe financial crisis as we move deeper into the new fiscal year. With a significant economic recovery unlikely before 2010, USPS is projecting volume losses in the range of 12 to15 billion pieces for FY 2009. Volume loss on that scale would smash past last year's numbers straight into the basement and lead to a huge deficit. Postmaster General Jack Potter recently estimated the loss would amount to "$6 billion or more."

The key to avoiding a huge deficit is winning legislative relief for the Postal Service. Congress must reduce the financial burden of pre-funding future retiree health benefits on a schedule that seemed tolerable three years ago, but which is totally unaffordable in the face of this recession.

In 2006, the postal reform law required USPS to pre-fund 80 percent of projected retiree health obligations in just 10 years—a mandate never before imposed on any federal agency or private enterprise. Unless it is changed, the requirement will cost the Postal Service more than $5.5 billion per year through 2016. This 10-year amortization schedule would be difficult to meet in a good economy, but it is impractical in today's circumstances.

NALC is supporting bipartisan legislation, H.R. 22, to allow the USPS to pay its current retiree health obligations out of the existing $32 billion retiree health fund, and to reduce the level of pre-funding by an average of $3.5 billion per year. The legislation would save the Postal Service billions by evening out its payments over time without affecting the health benefits of future retirees *(see story on page 6)*.

The next year will be a critical period for the Postal Service, just as it will be for the economy as a whole. While waiting for the Obama stimulus package to take effect, the postal community—mailers, management and labor—is working together to ride out the storm. And when economic recovery is finally on the way, letter carriers will be among the first to know. Remember, mail volume is a leading economic indicator. ✉

SPEND, SPEND, SPEND

Destructive credit spree underlies economic crisis

Bad credit? No credit? No problem!

Buy a house with no money down and a mortgage with a ridiculously low interest rate. Or better yet, all you have to do is pay the interest on the loan. And how about a credit card with an introductory rate of zero percent?

Early in George W. Bush's first term, the high-tech bubble burst and the economy started sliding toward recession. Desperate to turn things around quickly, the president worked with a Republican-majority Congress to craft a stimulus package. The finished product lumped together attractive $300-per-taxpayer rebate checks with deep tax cuts for businesses and the wealthiest Americans. The message to consumers: Here's "your money," now spend, spend, spend—it's your patriotic duty to help kick-start the economy.

Meanwhile, the Federal Reserve, under the leadership of Chairman Alan Greenspan, cut key lending interest rates to the bone, a strategy cooked up to spur borrowing, which would put more spending money in Americans' hands. The message: Borrow now! Spend now! (Worry later about paying it back.)

But those lower interest rates meant slim profits for lenders, so banks and other financial companies began looking for creative ways to beef up their bottom lines. Housing values had continued to rise despite the downturn, so financiers rolled out new "products," including exotic adjustable rate mortgages, balloon-payment mortgages, and interest-only mortgages. And to make these appealing to as many potential home-buyers as possible, lenders often lowered their standards, opening the door to borrowers with soiled credit, spotty job histories and suspect financial records—"subprime" borrowers, as they came to be known.

All of this happened with the blessing of the White House and Federal Reserve,

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which were just as determined to avoid adding to the regulatory "burden" on the growing financial services industry as they were to revive the economy.

And it wasn't just home loans. Credit card companies rolled out offers for plastic with absurdly low introductory rates. It wasn't that long ago that a carrier's satchel was filled with credit solicitations, offering any number of incentives to sign up for one more card. The lure of "rewards" like frequent flyer miles or pennies back, just for buying on credit instead of cash, was financial catnip for millions of Americans.

Financial managers knew they were taking on additional risk by extending credit to just about anyone who could fill out a form, so they concocted ways to insulate themselves from potential losses. One technique was "bundling" mortgages together, mixing the bad in with the good, then selling bits of the bundle to eager investors, who saw nothing but dollar signs in the expanding housing bubble. When the bubble burst and mortgages started going into default, investors learned there was no way to untangle the bundles and the value of the whole package collapsed.

A house of cards

Unfortunately—although some would say, predictably—our credit-based culture began to fall apart. By 2007, borrowers who were struggling to make ends meet because of stagnant wages, health care costs, resurgent inflation and skyrocketing gas prices, too often were choosing to let their mortgage payments slide for a month or two, or three. Soon, defaults and foreclosures grew into the thousands, then tens of thousands, and investors and financial institutions found themselves saddled with what are now labeled "toxic" assets.

The Bush solution? Bail out the very financiers who had gotten themselves—and us, to large extent—into this fix in the first place. Last fall, in a stampede of action rarely seen in Washington, Congress approved and President Bush signed the Troubled Assets Relief Program, or TARP, which literally throws money over the problem. It authorizes the federal government to spread around $700 billion in future taxpayers' money to wipe bad debt off balance sheets and grease the wheels of the credit market.

While the TARP's merits and application are still being debated, there's little doubt the government will somehow rescue the "bad" banks and financial services giants. But what about the good and not-so-good individual borrowers?

As this issue of *The Postal Record* headed to press, President Obama presented a plan to help endangered homeowners avoid foreclosure and the Treasury Department was working with the Federal Reserve to get credit flowing again. With education and some luck, consumers will learn to restrain themselves and live within their means.

"The lesson here is that we need a culture that values honest work and an economy built around real wage growth," NALC President William H. Young observed. "When working families are paid the wages they deserve, they have more actual cash in hand and can maintain a comfortable lifestyle without relying on imaginary plastic money." ✉