

# The Political Forum

*A review of social and political trends and events  
impacting the world's financial markets*

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Friday, December 27, 2002

**A REPRINT FROM A PIECE PUBLISHED DECEMBER 18, 1996**

**BULLISH ON THE GOOD OLD U.S. OF A. -- WITH CAVEATS**

**Mark L. Melcher**

My past three annual forecast pieces have reflected almost unbridled optimism. Indeed, my December 8, 1993, forecast article (entitled, coincidentally, "Bullish On The Good Old U.S. Of A. -- With Caveats") opened this way:

By virtually any measure, the United States is better off today than it has ever been in its history. We are the most powerful nation in the world economically and militarily. Our culture, our economic system, many of our most cherished ideals, and even our language are spreading throughout the globe.

Our enemy has been defeated. No nation can threaten our existence. If we chose, we could accomplish that to which the likes of Alexander, Genghis Khan, Tamerlane, Hitler, and the Soviet Empire aspired, namely world domination,

Our industries are competitive everywhere. Our technology is unsurpassed. Inflation and interest rates are under control. Our standard of living is extraordinary. The poorest citizens of the United States eat better, are better clothed and better educated, have better housing, and have greater opportunities to improve their lot than the middle class in most countries.

We are making remarkable headway in cleaning up our lakes, rivers, ground water, and air. Growing markets in Latin America, the Pacific Basin, and Asia offer unlimited opportunities for the sale of U.S. goods and services, promising a continuation of American prosperity for decades to come.

In short, I am enormously bullish about the future of the United States. This is a truly great nation, and the end of the cold war has provided us with opportunities other generations of Americans could scarcely have imagined.

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Most of the caveats I expressed in that piece related to reservations I had about what Bill and Hillary, and the Democrats who then controlled Congress, had in mind for the nation. But I was generally upbeat even about this. In fact, I noted that "the fly in Clinton's ointment, as I see it, is that the public really doesn't want the stuff he and Congress are doing . . . Thus, I am very optimistic that the liberal Democratic juggernaut that has gripped Congress for so many decades will be relegated to the dustbin of history by a surprisingly strong Republican victory in both the House and the Senate" in the 1994 off-year elections.

Then I added the following comment: "I may be too optimistic about this, but I like to think that the burst of new spending programs and new taxes enacted this year and certain to be enacted next year in the face of clear and growing public distrust of and distaste for government, and even clearer evidence that the nation cannot afford such folly will mark the end of 1960s'-style liberalism in the United States,"

My prediction on this score turned out to be pretty good. In my subsequent forecast piece, published December 7, 1994, I introduced a theme that I have used periodically ever since, including last year's forecast, namely that "It Just Doesn't Get Any Better Than This."

This year, I am still optimistic, especially on fiscal and tax policy and other matters that are of immediate concern to the business community and the financial markets. In fact, [ I would say that from Wall Street's perspective, it still just doesn't get any better than it is today.

But this year, I would like to temper my optimism somewhat, as I did in 1993, I will discuss the nature of my concerns in the specific forecasts that follow. In the meantime, I should note that I am no longer much concerned, as I was three years ago, about the Clintons and the Democrats. They have consistently lost power during the past several years, both in Washington and in a majority of state capitols across the nation, and there is every reason to believe that this trend will continue, at least for a while. They have found, as I predicted, that their old brand of big-government liberalism no longer sells very well, and they have abandoned some of their most pernicious notions, becoming reluctant advocates of many of conservatism's favorite themes, such as balanced budgets, lower taxes, welfare reform, and more cops.

Some Democrats can even be heard today extolling the importance of traditional families. And, of symbolic importance if nothing else, Bill has even abandoned the idea of federally financed midnight basketball as a corrective for teenage crime in favor of, you guessed it, curfews and school uniforms. Finally, Hillary Rodham Clinton, who once frightened conservatives even more than her husband, has almost dropped from sight. Her national health insurance scheme is no longer mentioned, and when she recently stated that she planned to have a formal role in monitoring the progress of welfare reform, the White House quickly explained that she had been mistaken.

So, without further ado, here are my forecasts for 1997.

**Forecast #1: Budget Agreement Ahead.** I agree with my colleague Chuck Gabriel that the federal budget debate next year will not be pretty. In fact, I don't doubt that there will be days when the partisanship appears so intense that the bond market will begin to stew about a likely breakdown in the process.

But by year-end, I believe Congress will have arrived at a deal that will look very good to the financial markets. It may not cut spending as much as conservatives would like, and it may rely on more smoke and mirrors than Wall Street would like. But it will pay bipartisan homage to the idea that a balanced budget is both desirable and necessary, and that, in my opinion, is a very big deal, especially when viewed from the perspective of the past 15 years or so, when the deficit skyrocketed and even conservatives didn't complain much.

**Forecast #2: Tax Relief Soon.** I believe that Congress will make excellent headway next year toward enacting some sort of tax cut that includes a capital-gains reduction. I'm reluctant to predict that a tax bill will actually be passed by year-end, since favorable tax legislation is usually enacted in election years. But I think it will become clear that taxes are headed downward and that savings incentives, including a capital-gains tax reduction, are inevitable.

I don't think this will happen because Congress and the White House suddenly decide that tax cuts are good economic policy. I think it will happen because Congress and the White House will decide that tax cuts are good political policy.

It is no secret that the nation's baby boomers are awakening to the fact that, unless they markedly improve their savings rate, their prospects for a happy and prosperous retirement are dim. As I've been saying for a couple of years now, the political side to this observation is, in my opinion, that the boomers are about to demand in unison that Washington help them address the mess they are in by lowering their tax burden, by giving them a tax break for educating their kids, by strengthening tax incentives to save, and eventually, I believe, by lowering the estate tax, so they will receive more when their parents die.

Congress won't give the boomers everything they want right away, of course. But the process of responding to their needs will, I believe, begin in earnest next year, and continue for the next ten years or so. And, as the old 7-Eleven radio ad for a 79-cent hot dog and a Coke used to say, "That's a pretty good deal!"

**Forecast #3: Social Security Reform Will Be The Talk Of The Town.** I think Congress will take the opening steps next year in the process of privatizing a large share of Social Security. This process could take four or five years at least, and Congress will do nothing next year but talk about it. But the talk will be serious, and skeptics will, I believe, be surprised at the large amount of support the idea has, even among Democrats.

Every legislator on Capitol Hill knows that eventually something must be done to "fix" Social Security, and not one of them is excited about the prospect of raising payroll taxes or cutting benefits. As a result, the idea of restoring a degree of fiscal stability to the program by the relatively simply method of investing some of the funds in the private sector has growing bipartisan appeal.

Social Security privatization is, I believe, destined to become one of the biggest, possibly the biggest, Washington issue on Wall Street because it has the potential to add \$100 billion per year of money to the equity market. Serious congressional consideration of the idea will, I believe, begin next year.

**Forecast #4: Whitewater Woes Will Accumulate In 1997.** I think the Clinton "Whitewater" scandals will finally come to a head next year, and that the accompanying firestorm will rock the White House and the nation. Special Prosecutor Kenneth Starr's two grand juries have been meeting for a very long time now, and it seems almost certain that some new indictments will be forthcoming before summer. It is possible, of course, that these will all be against minor players, and that the resultant dust-up will be short and of little consequence. But somehow, I doubt it. There's just too much smoke around the White House for there to be no fire.

It is with some trepidation that I make this prediction, since my track record on Whitewater has been mixed. On the plus side, I was very early in recognizing that the Clintons had serious ethical and legal problems that would plague them throughout Bill's presidency. I began saying this in the fall of 1993, at a time when virtually the entire mainstream media believed Bill when he said that his would be the most ethical administration in the nation's history.

On the negative side, I have consistently overestimated the speed with which the story would develop. The mainstream press has given Clinton more slack, Clinton's fellow Democrats have been more supportive of him, the public has shown itself to be more tolerant of ethical and legal missteps, and the Republicans have been less aggressive and less astute in their handling of the affair than I had expected.

Probably more important, however, is the fact that I underestimated Bill's remarkable political skills. In marshaling forces against his Whitewater foes, from New York Senator Alfonse D'Amato (R.) to Ken Starr, Bill has demonstrated a will of Schopenhauerian proportions; the political chutzpah of Huey Long; the stoicism in the face of battlefield casualties of General George Patton; and the tactical skills of Chief Joseph. I simply didn't think he had it in him. In retrospect, I now think that in my 34 years in Washington I have never seen a politician more adept and better adapted to political street fighting.

I continue to believe, however, that Clinton is fighting against overwhelming odds, and that he will eventually be forced to announce, as Chief Joseph did, that he too will "fight no more forever." In modern-day parlance, this may involve nothing more than admitting, in what columnist William Safire would call the "past exonerative tense," that "mistakes were made" and throwing a few more "friends" to the wolves. My guess is that it will be a little tougher on him and Mrs. Clinton than that. In any case, I think 1997 will be the decisive Whitewater year

**Forecast #5: Lippogate Will Hurt, Not Kill.** I think that Lippogate will develop into a big enough scandal in 1997 to keep both the White House and Capitol Hill Democrats off balance all year and, more importantly, to cripple the Democratic party's fund-raising efforts for years to come.

There was a time when a scandal such as Lippogate could have threatened the presidency. But I doubt that that will happen today. As I said above, Bill and his fellow Democrats are highly skilled and very aggressive in handling such things; the Republicans are blockheads; the mainstream press has little interest in pursuing Democratic scandals; and the public doesn't much care about such things anymore. In addition, no special prosecutor is involved in Lippogate, at

least so far, and it is highly unlikely that Janet Reno's Justice Department and Louis Freeh's FBI are going to find wrongdoing by anyone very high up in the administration food chain.

Nevertheless, numerous Republican committees plan to have public hearings on Lippogate, and some Democrats are likely to be tarred badly, including some of the party's leading fund raisers and biggest contributors. Political fund-raising is a highly prized skill and those who are good at it are as important to a political party as any quarterback in the NFL is to his team. Big contributors are also rare and precious. At a minimum, I think that Lippogate will put a host of big-shot Democratic fund raisers and contributors out of the ball game for a while, which will make it difficult for the party to field a winning team in 1998 and could hurt their chances of retaining the White House in 2000.

The *Washington Post* recently quoted an unnamed "prospective candidate" for the chairmanship of the Democratic National Committee (DNC) as saying that morale at the DNC "is at an all-time low. It's horrible. The donors have got to be scared to death. It's a big, big problem." The problem is aggravated by the fact that when the DNC closes its books on the 1996 election cycle it will be well over \$4 million in debt. In addition, the party's principal large organizational donors, such as the AFL-CIO, the National Education Association, the National Teachers Association, and the Trial Lawyers Association, are pretty well spent out, having thrown every penny they had, and some they didn't have, on the 1996 election in hopes of regaining Democratic control of the House, which of course didn't happen.

Democrats will try desperately to force the GOP to agree to limits on campaign spending in future years, as a way of mitigating their newly acquired disadvantage. But it won't work, The Republicans are dumb, but they aren't that dumb.

All of this is, I think, very good news for the GOP, for the financial markets, and for the nation as a whole. In fact, I have believed for quite some time now that the period between the end of the cold war and the end of the 20th century will be recorded as a high point in American history, as well as in the history of democratic capitalism. If not culturally, at least economically and militarily, the United States is truly in a golden age, just as surely as Athens was in the days of Pericles. But just as in those days, there are troubling signs on the horizon. I won't go into these in any depth in this piece. But briefly stated, I am concerned about the following developments.

**Forecast #6: Mideast Peace Unlikely.** I think the situation in the Middle East is likely to get extremely dangerous next year. I am not predicting war, but I do think things could get nasty enough over there to cause some nervousness in the markets.

As Bob Dole not so gently pointed out during the recent campaign, Iraq's President Saddam Hussein is much better off today than he was four years ago. Iran, America's other major self-avowed enemy in the region, is unquestionably stronger also. Indeed, it appears now that Iran felt comfortable enough last year about the weakness of the Clinton administration that it helped launch a murderous terrorist attack on U.S. troops in Saudi Arabia. Many experts feel that another big one is likely sometime after mid-February, when the Moslem holy month of Ramadan ends,

Unfortunately, our friends in the region, including Saudi Arabia and Israel, haven't fared so well during the Clinton presidency. By all accounts, the Saudi royal family is increasingly nervous about its future; and rightly so, in my opinion, given that the United States has all but admitted that American troops stationed there, ostensibly to protect the Saudis, can only protect themselves if they hide out in a well-fortified desert compound.

As for Israel, it is, in my opinion, not one step closer to the will-o'-the-wisp "peace" accord that every U.S. president since Jimmy Carter has coveted as a quick ticket to a Nobel Peace Prize. This despite making constant concessions to the Palestinians in response to assurances from the Clinton administration that Yasir Arafat is really a terrific guy, and despite Secretary of State Warren Christopher's ridiculously numerous, quixotic, hat-in-hand trips to Syria's President Hafez al-Assad to plead for a kind gesture toward Israel.

The result is that the Middle East becomes more explosive every day, as the Saudi position and the Israeli position weaken in concert. In an article in the December issue of *Commentary* entitled "The Tragic Predicament of Benjamin Netanyahu," Norman Podhoretz puts Israel's situation this way:

[R]esisting a full withdrawal from the West Bank to the pre-'67 borders—even apart from Jerusalem—will be more difficult and more dangerous [than holding on to the Golan, which Podhoretz thinks can be done without "looking like the 'bad guy' in American eyes"]. It could easily trigger mini-wars like the one that erupted over the tunnel, and one of these might then escalate, bringing the big war envisaged by the "strategy of stages" ahead of schedule and even before the actual establishment of the Palestinian state. But early or late, *that big war will come* [emphasis added]. And everyone will say that it was caused not by the premature hopes of Rabin and Peres, or by the evil dreams of the Arab world, but by the policies of Benjamin Netanyahu, which will have been based on a sober expectation of the jihad ahead and will have been designed to avert an Israeli defeat.

I hope that I (and Norm Podhoretz) am wrong about this. But the fact is that jackals such as Hafez ai-Assad, Saddam Hussein, and Iran's Rafsanjani can smell, and will attack, weakness -- and the Clinton administration's Middle East policies over the past four years reek of it.

**Forecast #7: Increased Terrorism More Likely.** I am also very worried about the possibility of increased terrorist activities against U.S. interests at home and around the world. I wrote several articles on this subject this year, including one entitled "Apocalypse Soon?" published last January 10, so I won't dwell on it this week, except to say that every expert in the field with whom I have spoken recently is convinced that the worst is yet to come and that it won't be long in coming.

One of these experts is Peter Probst, who works in the Office of the Secretary of Defense as a senior adviser on issues relating to international terrorism, political violence, and infrastructure vulnerability. Probst points out that while politically motivated terrorism is declining, religious and ethnically inspired terrorism is increasing at an alarming rate. The prime thing to remember about such terrorism, he says, "is its relatively unconstrained nature." He says the world's new terrorists have a "thirst for carnage"

I am aware that a forecast such as this has no immediate value from an investment standpoint. But if Probst and others are correct, terrorism is likely to have a profound effect on American society in the 21st century, particularly on the always delicate balance between freedom and order. This in turn will eventually have a profound effect on our financial markets and on commerce in general. So, I believe, the topic is well worth contemplating as we move into a new year. More specifically, from the very narrow perspective of Wall Street, it is, I believe, important to point out that Probst is highly concerned that the American financial markets are a major target for infrastructural terrorism aimed at computer networks, electrical grids, and physical facilities.

**Forecast #8': International Crime Is The Issue Flickering On The Radar Screen.** Finally, as I have also said many times in recent articles, I am deeply concerned about the phenomenal growth in the size and economic power of international crime syndicates, and the fact that the Clinton administration is so poorly positioned to resist the spread of their influence here.

As with terrorism, large global crime networks threaten the core of the American political and economic system. Unlike terrorism, this threat is insidious; it enters the system silently, like a virus, and can remain undetected for years, sapping the vitality and life expectancy of its host. I am not predicting that the United States will become a banana republic next year. But I do think that more troubling signs will appear that confirm that the infection is growing strong enough here to begin to affect commerce in some key areas, and to influence government decision-making, particularly in the foreign-policy arena.

I have written quite a bit about this subject during the past year. Articles include one last April entitled "Honesty Matters, Now More Than Ever" and one last month entitled "If Lippogate Isn't Innocent, It Signals Big Problems." So I won't dwell on the issue this week, except to repeat a couple of lines from the Lippogate piece mentioned above.

The only defense against this pestilence is unimpeachable integrity at the highest levels of the government. Without this, I think it is safe to say that the forces of corruption around the globe are so powerful today that they will eventually overwhelm America's free and open society as they are doing in one nation after another around the world, including but not limited to Colombia, Russia, China, and Mexico.

I don't like to end on such a gloomy note, but I believe that just as it was inevitable that the end of the cold war would lead to a period in the United States of great prosperity, relative tranquility, and unrivaled economic and military strength, it was also inevitable that new threats would eventually arise to challenge American society and its position of leadership in the world.

As Peter Probst points out, fantastic strides in technology have given small groups of fanatics the kind of destructive power that only governments had in the very near past. It is, he says, certain that some of these will use this power against the United States, which they despise. As the relatively new quarterly journal *Trends in Organized Crime*, published out of Rutgers University, points out regularly, the rise of global cities and modern telecommunications has allowed giant international crime syndicates to develop and to operate freely across borders, forming and dissolving alliances of convenience with other criminal gangs and also with political and pseudo-

religious terrorist organizations. It is also certain, of course, that these organizations will find a home in the United States, the freest, most open society in the world.

As I said at the opening of this piece, I remain optimistic about both the short- and long-term future of America and the financial markets. The United States is a great and powerful nation that will, I think, not only deal effectively with the problems and threats that lie ahead, but will prosper and grow while doing so.

Nevertheless, it is apparent, I believe, that the post-cold-war honeymoon is over. It was a great decade, but it couldn't last forever. The world is now well into the process of reordering itself, and it looks as though the new order will, as each of old orders did, provide many challenges to all nations and peoples that strive to be free.

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