America: from workshop to slot-machine of the world

by Richard Freeman

Most public schools in the United States are scheduled to open this week; but in South Dakota, they may not, or may open on a short schedule. In July, the South Dakota State Supreme Court outlawed video gambling. So perversely dependent is the state Treasury upon video gambling—at $65 million, the state's second largest revenue source—that Gov. Walter D. Miller now proposes massive cuts in state-directed and state-funded services to compensate for the lost revenue. One state senator has pointed out that the cost to the state in the increase in crime, and thus the need for police and other social services, outweighs the gambling revenues themselves. The state budget for social services in South Dakota has gone from $46.3 million in 1990 to $102.5 million today.

In Charles County, Maryland, a similar story on the possible postponement or curtailment of school operations is playing out, also due to gambling—but gambling run by Wall Street. There, the county treasurer was lured by nine major investment institutions to invest the county's *entire* portfolio of $27 million in various financial derivatives, about one-third of which are mortgage-backed securities, the market for which virtually disappeared during the first quarter (see *EIR,* Aug. 19, p. 4). Derivatives are highly leveraged, speculative instruments that loot the economy. County officials now report they have no money to pay bills for the next 45 days, and will delay payments to local agencies such as the school board and the sheriff's office.

Thus, the lawfully debilitating effects of gambling, in both its casino and financial markets form, threaten to close down essential services. Yet, in the 1980s, state and local governments turned to the "miracle powers" of gambling to save vital services. Since the 1960s, but especially during the last decade and a half, the U.S. physical economy has ratcheted downward in depression collapse. This has ravaged state and local government revenue bases. Rather than address the national depression, governments and businessmen sought out quick-buck expedients. America has descended into the stumble-bum category of depending on the throw of the dice, or its derivatives equivalent, for its financial survival. Once the workshop of the world, America has become now the slot-machine of the world. The degradation proceeds as Shakespeare's Hamlet described the behavior of his mother following her husband's death: falling as "from hyperion to a satyr."

Wall Street runs both ends of the operation. Seven large commercial banks and six investment banks control more than 90% of America's $18 trillion in derivatives holdings outstanding. These same institutions control the Taj Mahal Casino in Atlantic City (Donald Trump); Caesar's Palace (former Drexel confidant Steve Wynn); Bally's; Foxwoods; Circus Circus, and their offshoots and dummy front organizations which work the Indian reservations. It is both the derivatives gambling, and the casino and card-playing gambling, in close coordination, that are crushing what remains of the physical economy.

California as the paradigm

Consider the two-pronged nature of the attack in the case of California, America's largest state, with more than 30 million people, which, if it were a separate country, would rank as one of the world's 15 largest economies.

The national depression has hit California with a vengeance. This was supposed to be the first year of California's "recovery" after six years of decline. But that recovery never materialized.

The standard shock therapy of severe budget cutting has been applied in California, but to no avail. During the past three and a half years, Gov. Pete Wilson, part of George Bush's political machine, has cut the state budget by $7 billion. But predictably, the state has a new projected current budget deficit of $1 billion. As a result of the national depression, California lost 600,000 jobs over the last several years, 150,000 in the high-technology, well-paid aerospace and defense sector, where, since 1990, employment has fallen from 350,000 to 200,000. The University of California at Los Angeles Business Forecasting Project predicts that 30,000 more defense workers will be pink-slipped this year. In San Diego, General Dynamics Corp. is selling off a 242-acre industrial parcel, after closing its Convair fuselage division. Layoffs: 1,900. Not far away, Teledyne Inc.'s Ryan Aeronautical will shut down for two weeks, idling some 800 workers, in hopes of postponing permanent cuts. In July, Calfiornia's unemployment rate jumped by an astounding 0.7% in one month.

Forty-one percent of the state's counties have reduced library service, and in Humboldt, the city fathers are "repaving" a road using gravel, because they can't afford either asphalt or concrete.

What are people in the state doing about this catastrophe? In 1993, the treasurer of Orange County, one of America's largest counties, placed a sizeable portion of the county's funds into derivatives contracts. One deal went bad, and the county lost $147 million. Various levels of government in California have several billion, perhaps tens of billions of dollars riding on derivatives contracts. At the same time, 265 California counties or districts have licensed video gaming—i.e., electronic card dealing. In the last few months, 40 more districts have applied for licenses, to get in on the "revenue gravy train." Scarcely anyone gives a thoughtto how to restore California's 600,000 lost jobs, and the lost physical output.

National gambling

The California model is being writ large upon the nation.

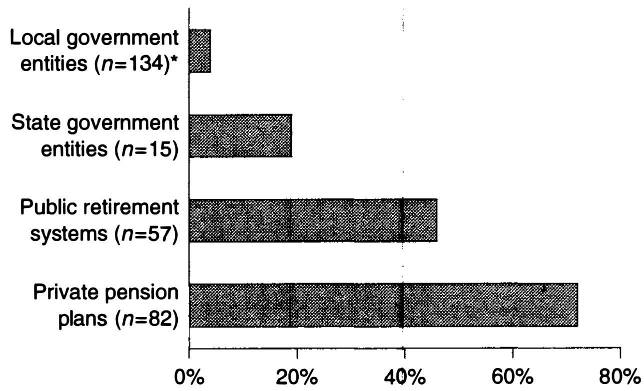
On May 18, the General Accounting Office of the U.S. Congress released a report, titled "Financial Derivatives: Actions Needed to Protect the Financial System." Several congressional offices had asked the GAO to compile a report on state and local government, as well as public and private pension plans' investment in derivatives. This analysis, titled "Derivatives Use by State and Local Governments and Private Pension Plans," was made Appendix 1 of the overall report.

Figure 1 displays the conclusions of that appendix. The results are for the year 1992, showing that of 3,276 local governments, 134, or 4%, have some of their money invested in derivatives. This is a small percentage, but it is growing; most of that investment occurred in 1992. The figures for 1993 would undoubtedly be higher, and 1994 higher still. The bar chart shows that, according to those who responded to the GAO survey, 19% of state governments, 45% of all public retirement funds (nearly half), and 72% of all private pension plans invested their clients' hard-earned money into highly

FIGURE 1

Extent of derivatives use by local and state governments and private pension funds

(percent of entities responding to poll)



* The letter "*n*" denotes the number of respondents using any derivative product.

Source: General Accounting Office.

leveraged derivatives. This is truly staggering. (Figure 1 shows, as a percent, the number of institutions, not the asset size, invested in derivative instruments.)

The GAO report's appendix also shows that among the respondents who replied that they do employ derivatives products, 48% of local governments that use derivatives are invested in interest-rate swaps, 31% of the state governments are invested in forwards, 70% of the public retirement funds are invested in foreign exchange, and 52% of all the private pension funds are invested in options. How safe is that money?

Meanwhile, in 1993, in America, there were 92 million visits to casinos. Casino gambling revenues reached $30 billion, which is more than the combined take for movies, books, recorded music, and park and arcade attractions. Thirty-seven states have lotteries; 23 have sanctioned casinos. More than 60 Indian tribes have gaming compacts with 19 states. The July 17 *New York Times* reported: "As the century turns, it's expected that virtually all Americans will live within a four-hour drive of a casino. . . . Never has government been such a devoted bookmaker, taking in $25 billion a year on lotteries. The amount Americans spent on all forms of legal wagering last year—$330 billion—has set an historical precedent of its own."

Atlantic City, New Jersey shows the future of locales that adopt gambling. After 10 years of gambling "prosperity," it still does not have a shopping center or a movie house. In that time, 100 of 250 local restaurants have closed, and retail store business has dropped by one-third.

This is how state and local governments are planning to stay alive; this is how public and private pension funds are investing people's money. This insanity represents America's decline.