



The Education of an American Dreamer

Peter G. Peterson

Introduction by Peter Nicholas

The 1948th Stated Meeting, held at the House of the Academy on November 11, 2009



Peter Nicholas

Peter Nicholas, a member of the Academy Trust, is Co-Founder and Chairman of the Board of Boston Scientific Corporation. He has been a Fellow of the American Academy of Arts and Sciences since 1999.

Introduction

Pete Peterson's story, which resonates in many ways with my own family's experience, is a classic rags-to-riches saga. He has fully lived the American dream, a fact he acknowledges in the title of his wonderful new memoir, *The Education of an American Dreamer*.

The subtitle of Pete's book, *How a Son of Greek Immigrants Learned His Way from a Nebraska Diner to Washington, Wall Street, and Beyond*, hints at the path he's taken in realizing that dream. Pete's father arrived penniless in America at age seventeen and somehow ended up in Kearney, Nebraska, in the central part of a state that's in the center of this great country. After changing his name from Georgios Petropoulos to George Peterson, Pete's dad opened and ran a diner for twenty-five years. The diner was open twenty-four hours a day, or 24/7 as they say these days. Young Pete was pretty

good at math and was allowed and encouraged to man the cash register from a young age.

After graduating from Northwestern University, Pete began a career that led from market research to advertising to business. He joined the Bell and Howell Corporation in 1958 and became Chairman and CEO of that company at the young age of thirty-six. In 1971 two fellow Academy members, Douglas Dillon and George Shultz, recruited Pete to Washington to serve in the Nixon White House, first as Special Advisor for International Economic Policy and later as the nation's twentieth Secretary of Commerce. *Time* magazine referred to Pete as the most powerful Secretary of Commerce since Herbert Hoover. Pete then moved to Wall Street, where he served as Chairman and CEO of Lehman Brothers

from 1973 to 1977 and of Lehman Brothers, Kuhn, Loeb from 1977 to 1984. He left to co-found the Blackstone Group, a private equity and investment management firm in New York City. In 2008 he retired from Blackstone after twenty-three years with the company.

Pete is a tireless multitasker who has contributed his wisdom and leadership skills to numerous other careers outside the business world. He is Chairman Emeritus of the Council on Foreign Relations and the Founding Chair of the Peterson Institute for International Economics in Washington, D.C., renamed in his honor in 2006. He was Chairman of the Federal Reserve Bank of New York, the Founding President of the Concord Coalition, a member of President Clinton's Bipartisan Commission on Entitlement and Tax Reform, and Cochair of the Conference Board Commission on Public Trust and Private Enterprise.

His new memoir is the latest of several books he has authored over the years that talk about how to fix what he sees as fundamental problems in this country. They include *Running On Empty: How the Democratic and Republican Parties Are Bankrupting Our Future and What Americans Can Do About It* (2004), *Gray Dawn: How the Coming Age Wave Will Transform America – and the World* (1999), *Will America Grow Up Before It Grows Old?: How the Coming Social Security Crisis Threatens You, Your Family, and Your Country* (1996), and *Facing Up: How to Rescue the Economy from Crushing Debt and Restore the American Dream* (1993). Pete's most recent project is the Peter G. Peterson Foundation, which he launched last year and endowed with a personal commitment of \$1 billion of his own funds, which represents a substantial portion of Pete's net worth. The Foundation focuses on what Pete has called "the undeniable, unsustainable, politically untouchable threats to this nation's future."

The Academy was proud to elect Pete as a Fellow in 2006.



Peter G. Peterson

Peter G. Peterson is Co-Founder and Chairman Emeritus of The Blackstone Group and Founder and Chairman of the Peter G. Peterson Foundation. He was elected to the American Academy of Arts and Sciences in 2006.

Opening Remarks

If you are presumptuous enough to write a book as a businessman, you have to be prepared to get roasted, and my favorite roaster is Ted Sorensen, President Kennedy's assistant. Of one of my earlier books he said, "This is a book that once you put it down you will not be able to pick it up." Of my last book he said, "We're here to anoint Peterson into literary sainthood. When I think of him, I think of Saint Paul, the duldest town in America." He renamed my *Gray Dawn* "Gray Yawn." So beware if you are a businessperson writing books.

I am an American dreamer. Because I am an American dreamer, I am concerned that the American dream may not be there for the generation of my five kids and nine grandchildren. This is the first time in history that a majority of Americans do not believe their children will do better than they did. If they are correct, it will change this country at its core.

This is not going to be an inspirational, charismatic speech, and for two reasons. First, I have negative charisma. Second, I am a great believer in the concept that an informed democracy is the best democracy. But Americans have been misinformed by politicians who believe that the American people cannot take the plain, hard truth. Our politicians

also believe that asking us to make sacrifices is not only politically incorrect but politically terminal to their careers. I do not accept these basic notions.

When I set up the Peter G. Peterson Foundation, many of my friends asked, "What makes you think you can make a difference?"

I don't *know* if we can make a difference. No doubt many will say I'm presumptuous to assume that we can effectively tackle some of the basic challenges facing this country, but I *believe* we can make a difference.

I was presumably educated at the University of Chicago, where a great Nobel Prize winner once said something that has stuck with me. He said, "If you have no alternative, you have no problem." Thinking about that and about how I would feel on my deathbed if I had not tried to do anything, despite feeling deeply that this country was challenged at its very core, I concluded that that was no alternative at all.

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Something else played a role in my billion-dollar decision. The billion dollars came about from a very surprising windfall when the firm I co-founded went public. The story goes that Kurt Vonnegut and Joseph Heller were at a palatial mansion of a hedge fund operator in the Hamptons when Vonnegut looks at Heller and says, "Joe, doesn't it bother you that this guy makes more money in a day than you made selling *Catch-22* all over the world?" Heller replies, "No, because I've got something this guy doesn't have." Vonnegut looks at him and says, "Joe, what could you possibly have that this guy doesn't have?" Heller answers, "I know the

meaning of enough.” I thought about that, knowing I had more than enough, and the decision to start the foundation wasn’t really a very difficult decision.

When I was in the Nixon White House, we had a Nixon humorist there. To Democrats the idea of a Nixon humorist might seem like an oxymoron, but Herb Stein really was a funny man. One day he said, “If something cannot go on forever, it will stop.” Then he said, “If you don’t like that one, there’s always the old saying, ‘If your horse dies, we suggest you dismount.’” Well, we’re behaving as though we can ride this horse we’re on indefinitely.

The Peterson Foundation has picked three challenges that are currently unsustainable in my opinion: entitlements (Social Security and Medicare); current account balance of payments and savings deficits, and the foreign borrowing that sustains us; and health-care costs, about which much is being said and little is being done.

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On entitlements, you hear a lot about the \$11 trillion public debt. What you do not hear about are the *unfunded* promises and liabilities that are much larger. Social Security’s liability is \$7 trillion. Medicare’s is \$34 trillion. Our total liabilities are \$56 trillion in today’s dollars. That’s a mind-boggling number: \$485,000 of hidden debt per American household; four times the size of the U.S. economy; more than the net worth of all households in America. In other words, we owe more money than we own. To meet these obligations with taxes, payroll taxes would have to double. I would call that gross taxation without representation. Many

people say, let’s just get rid of those damn Bush tax cuts; that will take care of the entitlement problems. Well, the Bush tax cuts amount to 1 percent of the gross domestic product of this country. Entitlement spending increases are 9 percent, or nine times more than the entire Bush tax cut package.

Now, some who believe in the supply side say we can grow out of these obligations, so relax and enjoy. I asked some experts to compute how fast we would have to grow in real terms in order to meet these obligations through growth alone. Turns out, we would have to grow in double digits, or four to six times as fast as we have ever grown in history.

Some politicians ask, what are you concerned about? The Social Security trust fund will remain solvent for another forty to fifty years, so relax and enjoy it. I have been collecting oxymorons ever since *Time* magazine referred to me as the most powerful Secretary of Commerce since Herbert Hoover. There has never been a powerful Secretary of Commerce. And the Social Security trust fund, I’m sorry to say, is an oxymoron: it should not be trusted, and it’s not funded. The fund contains nothing but liabilities and promises that we can’t afford.

Even if we got rid of the Bush tax cuts, got rid of earmarks, and ended the wars in Iraq and Afghanistan, we would be able to take care of only 15 percent of the fund’s obligations.

The second great unsustainable challenge the Peterson Foundation is focusing on is our current account balance of payment and savings deficits. Because we consume far more than we produce in America *and* because we save so little, we are in the position of having to borrow money from foreign sources. I asked the Peterson Institute for International Economics if they would create a series of scenarios for what our foreign debt will look like if we persist on our current path. If I wanted to give you a serious systemic digestive problem, I would share the Institute’s numbers. Instead I’ll quote one sentence from their report: “The projected path is so unsustainable and dangerous that a crisis would virtually be certain to occur long before the U.S. reached such a painful point of reckoning.”

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One of the great challenges we face is the quantity of the financing that will be required by the debts and deficits we are building and where we would get that money. The *National Journal* recently indicated that most experts’ estimates are, if anything, underestimates: “Even alarmists may be underestimating the size of the debt problem and how quickly it will become unbearable.” Paul Volcker, former Chairman of the Federal Reserve, believes the odds are 75 percent that we will see a dollar crisis within five years if we don’t change our ways. He describes such a crisis as a hard landing: the dollar falls suddenly and sharply, and interest rates rise steeply, producing both high inflation and low growth. If we had more savings both at the national and personal level, our country would not be as exposed to these major risks. We used to be one of the biggest savers in the world, but in recent years our personal savings rate has plummeted. If we are going to rescue our economic future, we simply must save more.

Finally, no serious discussion of unsustainable challenges can omit consideration of health-care costs. Much is being said about health care these days, including that the reforms working their way through Congress will be deficit neutral. Even if the new programs are deficit neutral, they will do nothing about the underlying longer-term problem of Medicare’s \$38 trillion in unfunded promises and liabilities. We spend twice as much per capita on health care as the rest of the developed world, and by many criteria our health outcomes are not as good. We are racing toward a day relatively soon when health care will consume 20 percent of the GDP, threatening the very

competitiveness of our economy. In the current debate on health-care reform, lowering health-care costs has been cited as a prime objective, but as I analyze the proposed legislation, I see little that does anything about the major causes of America's health-care cost crisis.

In a recent column that I wrote for the *Financial Times*, I pointed out ten health-care cost drivers that are being ignored. One is the utterly perverse payment system in Medicare called "Fee for Service." We pay for the procedures, we pay for the visits, we pay for the tests, and we pay for the surgery. Consumers have no stake at all – as far as they are concerned, it is free. The effect is what you might expect. If the providers have an incentive to do more and the consumer does not care about the costs, the result is a huge increase in the number of procedures. As a result, on a per capita basis we perform five times the number of CT scans as Germany. We perform five times as many coronary bypasses as France. Until we reform fee for service, we won't be attacking one of the great cost drivers in health care.

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Another major cost driver is the great variation in levels of treatment and costs from one geographic area to another. For example, in some states or regions in America six times more back operations and six times more prostate removals are performed than in other areas. I know we have "red" states and "blue" states, but am I to believe we have "bad prostate" states and "bad back" states? It's ridiculous. And yet we tolerate these enormous differences in costs.

We are the only developed country in the world that has an open-ended cost-plus budget. Most of us have learned to live with

budgets. They force us to make choices. But because the federal government has no priorities for its budget, entitlements such as Medicare costs have exploded in recent years. This impacts our ability to fund core research, to make the necessary investments in our future. Forty to fifty years ago the government routinely spent 5 percent of its budget on research and development. Out of that research came the Internet, to take just one example. Today we spend less than 2 percent of the budget.

Roughly 30 percent of Medicare costs are associated with the last year of life. This is obviously a highly complex issue, but we have to face the fact that we spend significantly more than the rest of the world on heroic intervention in the last months of life. We must begin to confront the profound, difficult questions attached to this issue. Is the government obliged to prolong life indefinitely, or is its obligation only to prolong life as long as a reasonable quality of life can be maintained? Should the government be responsible for costly heroic interventions, or should these be the responsibility of the individual taxpayer? These issues are difficult, but if we start thinking about them we can perhaps realize outcomes similar to La Crosse, Wisconsin, where 96 percent of residents have signed an advance directive for end-of-life care. As a result, their end-of-life medical costs are 20 percent below the national average.

So much for the three challenges the Peterson Foundation is focusing on. What do we do about them? First, each of the challenges has many dimensions. We can't run away from the fact that all of the choices will be difficult and will often require us to make some shared sacrifice. The good news is that many sensible and workable proposals will also protect the truly needy. So the difficulty isn't so much with the proposals as with the lack of political will to do something. The good news here is that the public today is far more aware of and concerned about our fiscal future than at any time I can recall in the last twenty-five years.

Several ingredients will be required if we are going to come up with an answer. Presidential leadership is essential. So is bipartisanship. I was brought up in Nebraska, and

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we used to hunt for pheasants and turkeys, which leads me to talk about the "turkey shoot phenomenon." The poor turkey that lifts its head gets it shot off. Likewise for the politician who mentions reform and does so alone, whether of Social Security, Medicare, or most anything else. For reform to be successful, it must be bipartisan.

The Peterson Foundation is working to educate, motivate, and activate the American people to do something about these problems. Blaming the politicians is easy, but everyday citizens share a measure of the blame, too. The Founders expected that members of Congress would not have to give up their careers because they would go to Washington only for brief periods during the year and they would be there only for a limited number of years until they had achieved some particular objectives. Today most of our elected representatives view being an elected representative as their career, so their focus is not on the next generation but on the next election. Ultimately, we the people have to make it safer for politicians to do the right things. If you look at the political landscape, you see that the future in general and the youth in particular are not represented. We need a new special interest group in Washington, one that represents the future, the interest of our kids and our grandkids.

America in times past has been remarkably resilient. After World War II, our public debt stood at 110 percent of GDP – much higher than it is now. But in a period of about thirty to forty years, the Greatest Generation paid down that debt to about 30 percent of the GDP while also paying for the GI Bill, the largest infrastructure program in American history, and the Mar-

shall Plan. So we have done it before, and there's no reason we can't do it again.

The question before us is, will it take a crisis to get us to act? If we do require a crisis, its costs will be immense and could easily arise in the foreign exchange markets as foreigners lose confidence in our ability to manage our fiscal affairs and refuse to lend us money except at very high interest rates. Avoiding a crisis is one of the main focuses of the Peterson Foundation.

An important part of our effort will be directed at young people. You might remember the old philosophy class joke where the professor says to the kids, "Which is worse, ignorance or apathy?" And some sleepy kid from the back of the class says, "I don't know, and I don't care." Well, we have to make today's young people care and make them aware. To do so, the Peterson Foundation is going to mount a major digital media effort. We are already on MTV in a major way, and we are developing video games and other digital initiatives.

We used to be one of the biggest savers in the world, but in recent years our personal savings rate has plummeted. If we are going to rescue our economic future, we simply must save more.

I have a dream that we will be able to create an organization to represent the interests of the young in the way that the AARP represents the interests of the elderly. We might call it the AAYP, the American Association of Young People. The AARP is thirty-nine million members strong, and its members vote a lot, lobby a lot, call their congresspeople a lot, and generally use every legitimate weapon available to promote their interests. What they are interested in can usually be described in three words, "I want more." We need a movement in this country of people who understand that we are going to have to get by with less in the public arena. Perhaps some day we'll see one

hundred thousand young people march on Washington, chanting in the spirit of *Network's* Howard Beale, "I'm as mad as hell, and I'm not going to take this any more."

The German theologian Dietrich Bonhoeffer once said the ultimate test of a moral society is the kind of world it leaves to its children. I say to all of us that we have to get off of our butts and make it safer for politicians to make the tough choices, to do the right thing, and less safe for them to continue to do nothing but slip the bills to our kids. Do we have any alternative but to try?

Reflecting on Prospects for America: A Conversation between Peter Nicholas and Peter Peterson

Nicholas: One of the most compelling aspects of your recent memoir is the remarkable journey you have been on and where it all started and how it came about. What were the particular ingredients of your success?

Peterson: I could ask you the same thing! Well, to start, I chose very good parents. And in my father I had a role model who made two great impressions on me. One was to develop a work ethic, a lesson that at times in my life I have carried too far. The other was to invest in the future. My father used to save large amounts of whatever he made, and he would send it back to the old country to help build roads and other things in the communities of his parents and grandparents. I have learned the ethic of saving, of thinking about and investing in the future. My father also taught me hard lessons. He kept a car longer than anybody I have ever known in my life, maybe fifteen, twenty years. So, if I needed a new bicycle, he would say the one you already have will do for another two years. In that way he taught me thrift, which was just as important as the work ethic and investing in the future.

Nicholas: Your books often talk about threats from within. Today you focused on the enormous consequences of America's unfunded debt and deficit spending and the reckless behavior and inability of politicians to do the right thing. But you have long been involved with the international

community around a whole range of issues, including arms control, Russia, and international economics. What are your thoughts on the threats that come from outside the country?

We spend twice as much per capita on health care as the rest of the developed world, and by many criteria our health outcomes are not as good.

Peterson: When I'm concerned about foreign debt, I'm not only concerned about the impact on our economy. But our debt has major geopolitical implications as well. In the 1950s the British made a big move on the Suez Canal and sent some troops there. This was very much against U.S. policy. At the time, we owned a large portion of British securities. President Eisenhower told his colleagues, "Get a hold of our British friends and just tell them 'our enthusiasm for what you're doing is very restrained, and if you don't get your troops out of there right away, we'll have no alternative but to dump your British pound securities.'" The Brits left in ten days. There's no reason that the Chinese, who are now the biggest foreign owner of the U.S. Treasury, can't decide for political reasons, and perhaps to some extent for economic reasons, to cut back their lending to us.

I was privileged to be in charge of the economic negotiations with the Soviet Union in 1972. At the time, everybody was telling me what a superpower they were, but I decided to do my own analysis of the situation. I had the CIA put together a large number of statistics, and a fascinating pattern emerged. Although at the time we called the Soviet Union an economic superpower, out of thirty-four categories of products we examined, in only one could they export to anybody other than their buddies in Eastern Europe. They were totally uncompetitive.

During one of my trips to the Soviet Union I was in the southern part of the country to see Leonid Brezhnev. One of the first things he wanted to do was to show me his Olym-

pic-size indoor-outdoor swimming pool. The pool was an extravagant structure with automatic glass doors that opened and closed so that Brezhnev could use the pool whenever he wished. Having heard much talk from the Communists about how their people were all equal, I was tempted to ask whether Olympic-size indoor-outdoor swimming pools were a standard piece of merchandise that everyone in Russia owned.

In reality, their economy was decrepit, a fact that was evident everywhere. I visited a photo shop that was selling cameras that had been dropped from American stores four years earlier. And as I was being driven to Brezhnev's villa, I noticed a lot of farm equipment standing idle. Before embarking on this trip I had been impressed with the fact that although the Soviets were spending more on farm equipment than we were, their productivity was only 9 percent of ours.

So, during dinner, I asked the minister next to whom I was sitting to explain why so much of the farming equipment sits idle. He replied, "I've been to Iowa, and your situation is very different than ours. In Iowa the farmers own the land and the equipment, so it is their property and their business. Here the farmers own nothing. There, if the farmers sell their goods at a good price, they keep the revenues. Here, they keep nothing."

Wherever I looked in the Soviet Union, I saw an obsolete central planning system that couldn't possibly compete in the modern world economy. And sure enough, twenty years later that had become very evident.

Nicholas: Although Russia may not have had much to sell then, some people argue that today they are getting their arms around 70-plus percent of the world's oil and gas supply by virtue of hegemony in their part of the world. This, people say, is one of the reasons the Russians don't support our interests in Iran. At the same time, we Americans don't seem to be able to develop and articulate an energy policy. How is the public to think about this? And what needs to happen to resolve this issue before the fears of many people are in fact realized?

Peterson: We have created a political system that's all about "I want it now, and I don't want to pay for it," where shared sacrifice is

considered politically terminal. Our energy consumption per capita is much higher than in the rest of the world. One of the obvious changes that should be considered is a gasoline tax that would be refunded against other taxes. In Europe the average gasoline tax is now close to \$4 per gallon. The average in the United States is 47 cents. Somehow people have to be persuaded that reducing consumption is a must. The beauty of attacking the consumption problem is that it can be attacked much sooner and at lower cost than developing wind farms, solar systems, and so forth. However, the effort to reduce consumption ultimately must be combined with a major effort on alternative energy sources.

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Nicholas: Many people look to Wall Street as being responsible for much of our recent financial crisis. Do you think our recent experience has been a sufficient wake-up call to produce the kind of changes, regulatory and otherwise, that might prevent such crises from happening again? And, perhaps more important, how can business become a part of the solution, not the problem?

Peterson: Not long ago, Tom Friedman, writing in *The New York Times*, argued that today's business leaders are MIA, missing in action. This reminded me of the fact that in the immediate post-World War II period, a band of six senior corporate officers from major U.S. companies got together and decided that the long-term interests of our country would best be served if we poured massive amounts of aid into helping Europe and Japan reconstruct from the devastation of the war. They reasoned that if Europe and Japan – Europe, in particular – were leveled to the ground, U.S. businesses wouldn't have markets. Their idea led to the Marshall Plan, which the Ameri-

can people originally wanted nothing to do with. They wanted to come home. They were tired of costly foreign adventures. And so, at first, only 14 percent of Americans approved of the Marshall Plan. A huge movement was mounted to make the American people aware of why it was in their interest to have a Europe that was economically sound.

I'm not aware of any important, sustained effort by today's business community to talk and do something about the unsustainable problems facing this country, and yet the business community's health is closely related to our long-term economic health. So I recently wrote a piece about this for *Business Week* that won't endear me to most business executives, because I think Friedman is correct. We are missing in action.

On the need for regulation: I haven't seen details but the proposed financial reform legislation sounds like a comprehensive program of regulation. We seem to have learned our lesson on that score. Even Alan Greenspan has acknowledged that people don't always act in their enlightened self-interest. In some cases they don't know what their enlightened interest is.

The compensation system on Wall Street, and to some extent in corporate life in general, violated certain principles, one of which was not identifying closely enough with the stockholder. To address this, I would heavily base compensation on long-term performance and pay top executives more in stock. I would insist that this stock be held a substantial period of time. Prior to the financial crisis traders were trading trillions of dollars of derivatives and credit default swaps, marketing them at unrealistic values (because no one knew how to value them), and then taking huge bonuses, tens of millions of dollars, only to discover three years later that what they had been trading was far from being profitable. That's why we have to move to compensating for long-term performance and in stock. ■

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