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THE WORLD BANK

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Interview/Photo OP: Mr. Jim McTague
Washington Editor, Barrons Magazine

Wednesday, May 6, 1998
11:00 - 12:00
JDW Office

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President Wolfensohn - Briefing Book for President's Meetings - Meeting Material
Interview and Photo Op - Jim McTague - Washington Editor - Barrons Magazine -

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Document Log

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A. CLASSIFICATION

- ☒ Meeting Material
- ☐ Trips
- ☐ Speeches

- ☐ Annual Meetings
- ☐ Corporate Management
- ☐ Communications with Staff

- ☐ Phone Logs
- ☐ Calendar
- ☐ Press Clippings/Photos

- ☐ JDW Transcripts
- ☐ Social Events
- ☐ Other

B. SUBJECT: INTERVIEW / PHOTO-OP: MR. JIM MCTAGUE, WASHINGTON EDITOR, BARRONS MAGAZINE (B) (N) // VENUE: MC-12-750 (OFFICE) FOR INTERVIEW // MC-12-755 (MTG. ROOM) FOR PHOTO-OP
AGENDA: WORLD BANK, JDW, EAST ASIA // PROGRAM:
11:00 TO 11:45 A.M. : INTERVIEW // 11:45 A.M. TO 12:00 P.M.: PHOTO-OP
CONTACT: KLAS @ 33798 // ALTERNATE CONTACT: MERRELL TUCK @ 39516 // WB ATTENDEES: JDW, MERRELL TUCK (FOR MMB), CAROLINE //
EXTERNAL ATTENDEES: MR. JIM MCTAGUE, WASHINGTON EDITOR
MR. MANUELO PAGANELLI, PHOTOGRAPHER // (B) EXTVP // DUE: FRIDAY, MAY 1 // EXC: CA // ALI (4/20)

DATE: 05/06/98

Brief includes:

- Note to JDW from M. Tuck, May 5
 - Bio; IDA Issues and Questions; WB Press Backgrounder: The Strategic Compact --- One-Year Progress Report, Apr. 1998; Excerpt from Barron's - Article by Jim McTague, Aug. 18
 - Card for JDW from Seido and Kanda River praising the Barrons Article about JDW, Jun. 25, 1998
- COPY OF NEWSPAPER ARTICLE (MAY 25) ADDED BY WENDY

C. VPU

Corporate

- ☐ CTR
- ☒ EXT
- ☐ LEG
- ☐ MPS
- ☐ OED
- ☐ SEC/Board
- ☐ TRE

Regional

- ☐ AFR
- ☐ EAP
- ☐ ECA
- ☐ LAC
- ☐ MNA
- ☐ SAS

Central

- ☐ CFS
- ☐ DEC
- ☐ ESD
- ☐ FPD
- ☐ FPR
- ☐ HRO

Affiliates

- ☐ GEF
- ☐ ICSID
- ☐ IFC
- ☐ Inspection Panel
- ☐ Kennedy Center
- ☐ MIGA

D. EXTERNAL PARTNER

- ☐ IMF
- ☐ UN
- ☐ MDB/Other IO
- ☐ NGO
- ☐ Private Sector

- ☐ Part I
- ☐ Part II
- ☐ Other

名所江元百景

昌平橋
聖堂
神田川

昌平橋



ACHIEVEMENTS, BUT FOR ALL THE OTHER THINGS YOU'VE DONE, AS WELL — CARNEGIE HALL, KENNEDY CENTER, IFMSS AND THE DISABILITY MOVEMENT, AND MORE.

THE WORLD BANK CERTAINLY SOUNDS LIKE A HUGE CHALLENGE AND IT MAY INDEED BE A CAPSTONE TO YOUR LONG CAREER OF PUBLIC SERVICE; THEN AGAIN IT MAY ONLY BE ANOTHER PRELUDE! WHO KNOWS THE FUTURE?

I'M SURE YOU GET MANY WORDS OF PRAISE, AND DESERVING AWARDS, TOO — FROM THE GIANTS OF INDUSTRY, THE LEADERS OF ACADEMIA AND THE MOGULS OF GOVERNMENT AND FINANCE. BUT SOMEHOW I HOPED YOU MIGHT ENJOY A WORD OF ADMIRATION AND, YES, GRATITUDE FROM SOMEONE "BELOW THE SALT," AS IT WERE — A ONE-TIME

SATURDAY, 20 JUNE 1998

DEAR Jim -

EACH TIME I DISCOVER ANOTHER GOOD ARTICLE ABOUT YOU, I LEARN SOMETHING NEW — AND PRAISEWORTHY! AND EACH TIME I SOLEMNLY PROMISE MYSELF THAT I WILL DROP YOU A NOTE. NOW, AFTER THAT RECENT FRONT PAGE PORTRAIT AND LENGTHY PROFILE IN THE 25 MAY ISSUE OF BARRONS, I REALLY HAD TO WRITE. I HOPE THAT THIS DOESN'T GET LOST IN A STACK OF CARDS AND LETTERS FROM COUNTLESS OTHERS. EVEN SO, I WANT TO ADD A FEW WORDS OF MY OWN.

CONGRATULATIONS, OF COURSE! BUT NOT ONLY CONGRATULATIONS, FOR IF I MAY, I ADD A WORD OF GRATITUDE! AND NOT ONLY FOR YOUR CURRENT

ASSOCIATE WITHOUT AN OXE TO
GRIND OR A FAVOR TO ASK OR
SEEK.

SO, HAIL TO A REAL PROGRESSIVE
AND AN UNASHAMED LIBERAL (HOW
GREAT!) — AND A TRUE MODERN
DAY HUMANITARIAN. TIME OUT
TO SAY "THANKS, JIM, FOR ALL
YOU DO!"

SINCERELY

John F. Kennedy

SEIDŌ AND KANDA RIVER
FROM SHŌHEI BRIDGE

Utagawa Hiroshige, Japanese, 1797-1858
Woodblock print in colors from the series
One Hundred Famous Views of Edo

THE METROPOLITAN MUSEUM OF ART

The Howard Mansfield Collection

Purchase, Rogers Fund, 1936 JP 2512

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Printed in the U.S.A.

*There
are
actions
Do we know
who sent this
to him when*

Andrew

It's a New World

An Aussie-born Wall Street veteran shakes up a big multinational lender

BY JIM McTAGUE

WHEN WORLD BANK President James Wolfensohn was still a young man, the brash Australian obtained a law degree from Sydney University, competed in the Olympics as a fencer and earned an MBA from Harvard before heading off to Europe, where he became one of the Continent's investment-banking standouts. Along the way, the son of working-class parents developed a fine eye for art and a sophisticated ear for music.

A forceful opening movement, indeed, and the second was equally impressive. Wolfensohn, an impeccably mannered man who sounds more like Professor Henry Higgins than Crocodile Dundee, wowed them on Wall Street as a member of the Salomon Brothers team that helped extricate a financially distressed Chrysler Corp. from the jaws of its creditors. He went on to become a naturalized U.S. citizen, start his own investment firm, amass a personal fortune exceeding \$100 million and, as a patron of the arts, straighten out the finances of both Carnegie Hall in New York and the Kennedy Center in Washington. His powerful friends and advisers include Washington lawyer Vernon Jordan, former central banker Paul Volcker, Federal Reserve Chairman Alan Greenspan, President Vartan Gregorian of the Carnegie Corp., Chairman Juergen Shrempp of Daimler-Benz and CEO Louis Gerstner of IBM. Queen Elizabeth II honored him with a knighthood in 1995.

Wolfensohn, 65, is now composing the final movement of his professional life's symphony. He's attempting to bring Wall Street creativity to the World Bank, which boasts \$162 billion in total assets (versus \$280.7 billion for Chase Manhattan, currently the largest U.S. bank). It is also the planet's largest and most august international development agency — and perhaps its most intractable bureaucracy. One of seven multilateral banks of which the U.S. is a member, the World Bank is charged with fighting poverty by helping to integrate developing countries into the global economy. The aim of the avowed liberal Wolfensohn is to transform what arguably is a largely ineffectual operation, with a record of policy failures that obscure its triumphs, into an effective organization that is at once efficient, environmentally friendly and gender-sen-



The World Bank's Wolfensohn

"Don't write off Asia because of problems in Indonesia."

sitive — while adjusting to a post-Cold War world of governments reluctant to pour taxpayer funds into global backwaters. In contrast to private-sector restructurings, Wolfensohn is constrained by politics to execute the bank's radical transformation with a minimum of bloodletting among its 10,000 employees (more than 5,000 of them at the bank's headquarters in Washington). This is no mean feat and involves changing a deeply ingrained culture dominated by desk-bound policy wonks.

When the ruffled financier arrived at the World Bank in 1995, he told one U.S. senator he believed he had about a

50-50 chance of succeeding. But these days, despite surveys that peg employee morale near rock bottom, he's considerably more optimistic. "If you come back in 18 months, I believe you will find the most exciting of the world's multinational institutions," he predicts. That target date roughly coincides with the official end of his first five-year term. Wolfensohn is willing to delay retirement to his Wyoming log cabin designed by Cesar Pelli and put in another five years to see that his reforms have an opportunity to work: "I'll have to see if they want to reappoint me for another five years and I'll look at

my health and see if I can carry on. My predisposition is to carry on."

At this point the affable Wolfensohn has no serious opposition. He's been scoring points with the bank's most vociferous critics, like environmentalists who had raged against its big dam and road projects; scientists in Costa Rica recently named a species of beetle after him, in honor of his efforts to preserve the country's biodiversity. (Critics say Wolfensohn has bought the silence of environmental groups with consulting contracts and projects like an \$80-\$150 million outlay in a partnership with the World Wildlife Fund to protect 62 million acres of Amazon jungle in Brazil.) Governments of some poorer countries in Africa are thrilled that he is forgiving their considerable debts — \$5.7 billion in seven countries so far, in a program that eventually could include 80 nations and as much as \$125 billion in IOUs. Political conservatives in the U.S., who believe the World Bank is irrelevant at best and, at worst, shores up bad economic systems, nonetheless have been leaving it largely alone, concentrating their fire instead on the International Monetary Fund, which is more heavily dependent on taxpayer dollars and plays a more visible role in economic crises like those in Asia (the IMF makes short-term loans to governments when they have balance-of-payment difficulties).

The World Bank has flirted with political disaster. Some lower-level managers recently approved a loan package to India for a health system without advising Wolfensohn and top management that some of the money would be used to fund abortions in both the first and second trimesters. (Republicans in Congress are stalling IMF funding until there are reassurances that no U.S. tax dollars will pay for abortions; the World Bank, which Wolfensohn says has a policy precluding abortion funding, will approach Congress for funds next year.)

Wolfensohn's strategy calls for luring investor money to some of the world's most backward countries by providing guarantees against political risk, promoting joint ventures, and, most important, by getting his bureaucrats to put down their pencils once in a while and teach the locals how to build stable, sustainable civil and financial systems. Instead of lending money exclusively for big dams, superhighways and the other physical

trappings of industrialized nations, the World Bank will advise governments on the drafting of strong commercial and environmental laws, effective tax-collection systems, educational institutions and financial regulation that demands the kind of disclosure found in developed countries. A lot of the governments already have gotten religion, Wolfensohn says. He currently sees opportunity for private investors in both Asia and Africa, despite the political and economic problems on both continents.

"Don't write off Asia because of problems in Indonesia," Wolfensohn advises. He's impressed at the speed at which other troubled Asian economies are adopting market reforms – notably Korea and Thailand. "I think the Koreans and the Thais understand that there is a need for fundamental change," he says.

At Wolfensohn's urging, the World Bank became part of the bailout of Korea when a credit crunch crippled its balance-of-payments late last year. The bank provided long-term loans to help stave off the country's private-sector creditors.

That was apparently a one-shot deal. Though the U.S. supported the bank's role in that bailout, Treasury Secretary Robert Rubin, who is briefed regularly by Wolfensohn, doubts the bank will play a similar role in Indonesia. But he adds that the final decision is up to Wolfensohn and his bank's directors.

Wolfensohn is also "personally positive" on Africa, a region he frequently visits. "I think there's a new leadership and a new spirit in Africa," he declares. He notes that South Africa, the continent's economic keystone, could undergo some transitional problems when President Nelson Mandela steps down at the end of 1999. But Wolfensohn deems Mandela's successor, Deputy President Thabo Mbeki, an able executive.

The World Bank president is even upbeat – for the record, at least – about prospects for economic and social progress in Russia. In Moscow last week conferring with President Boris Yeltsin and other leaders, Wolfensohn urged the Russians to address social problems that contributed to recent battering of financial markets. But, he told legislators, "you are not Indonesia, thank God."

Indeed, with angry citizens looting and burning Indonesia (a client whose economy Wolfensohn and the bank prematurely praised less than a year ago), and with the new rulers of India, another big borrower, frightening the rest of world with nuclear testing, Wolfensohn might seem at best a cockeyed optimist.

But he does harbor some concerns. One is that the Japanese, who are doing some belt-tightening at home, might reduce or eliminate their contributions to the World Bank, despite assurances from Tokyo. When the U.S. Congress threatens to cancel funding for the IMF, it makes it harder for Japanese politicians, faced with budgetary constraints, to resist cutting funding to multilateral institutions.

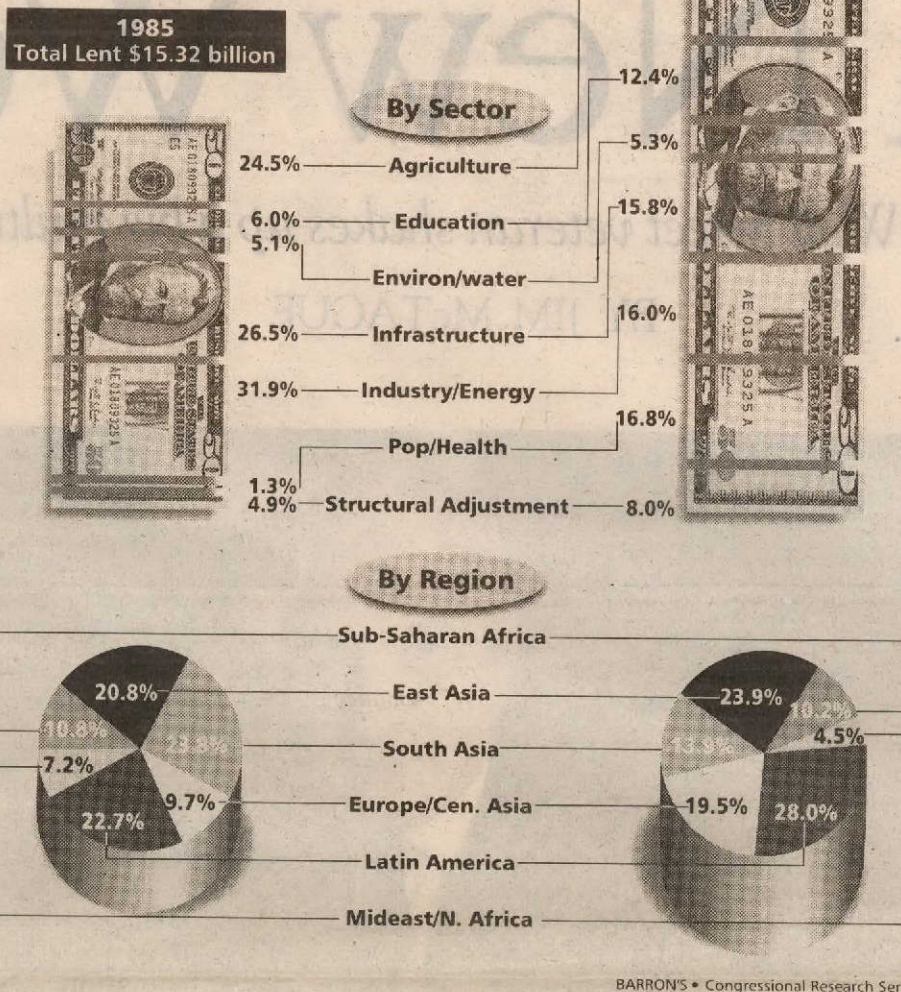
"I think the Congress is wrong on their positions about funding the IMF," Wolfensohn states. "But when it comes to social issues, which are the principal areas in which the bank is involved, issues of health, education, fighting AIDS, infrastructure, of putting projects together that can develop American exports, there's a stronger, more visible case we can make."

Wolfensohn sees U.S. corporations as

World Bank Lending: 1985 vs. 1995

(as a % of total lending; billions of U.S. dollars)

►The World Bank's lending under James Wolfensohn has been shifting from projects, like infrastructure and energy, that promote industrial development, to programs, like health and education, that foster social advancement.



big beneficiaries of World Bank missionary efforts. But he seems genuinely passionate about helping socio-economic underdogs. "Jim Wolfensohn is generous by nature," says Washington lawyer and Presidential pal Vernon Jordan.

Friends note that Wolfensohn and his wife, Elaine, feel an obligation to share their good fortune. Wolfensohn grew up under the tutelage of parents who, although poor, were active in helping Jewish refugees settle in Australia after World War II. "Jim has his own little foundation that he doesn't much talk about," says Jordan. "He supports promising artists and musicians. One year he brought three students over from Russia to teach them investment banking." Wolfensohn has put 20% of his salary (currently \$224,650, after taxes – he also nets \$111,410 in expenses) into the foundation for most of his working life.

Wolfensohn is highly competitive, says Jordan, who plays tennis and golf against the banker. Adds Lloyd Cutler, former White House counsel for President Clinton, "He doesn't suffer fools" – a useful trait for the leader of the World Bank at this juncture.

Over the past 10 years, private capital that has been pouring into many developing nations has dampened demand for credit from the World Bank. The share of total lending by the bank to its six most credit-worthy borrowers fell to 6% in the

fiscal years 1987-96 from 14% in fiscal '77-86. While the bank now faces growing demand for its services in Europe and central Asia (their share in total lending has grown to 11% in fiscal '87-96 from 2% in fiscal '77-86), many of these countries have the capacity to recover rapidly and may cease being eligible for World Bank loans within the next few years. As a result, strife-torn countries, and those where policy distortions are

proving difficult to rectify, might well account for most of the bank's clientele in the next century.

This is no news to Wolfensohn. "The environment in which we operate has vastly changed in the last 10 years," he observes.

"The reason you have to focus people on change – in the last 10 years, the role of the multilateral and overseas development assistance has been reduced from \$60 billion a year to roughly \$40 billion a year. During that same period of time, private-sector investing in the developing world has gone from \$30 billion to \$260 billion. What that says about this institution is that we better work more closely with the private sector. The private sector is now the financial, and in some sense is the technological, engine of growth in many countries. And what you need to do is tap into that entrepreneurial activity and reconceive our own development plan within the context of what we do in partnership with the private sector."

Wolfensohn is the ninth bank president

since the institution, along with the International Monetary Fund, was established in July 1944 at the United Nations Monetary and Financial Conference in Bretton Woods, New Hampshire. All the World Bank's presidents, by tradition, have been Americans, named by the bank's 24-member executive board of directors. The U.S. government actually conducts the search for candidates – Wolfensohn was on the short list in 1979, even though he was an Aussie citizen at the time. Each of the World Bank's five largest shareholder nations, including the U.S., appoints one executive director; the other directors are appointed by groups of countries.

The bank was established to make loans to countries rebuilding from the devastation of World War II. When Robert S. McNamara came on board as bank president in 1968, he felt the time had come to expand the institution's mission.

"I considered the bank a development organization as opposed to a commercial bank," says McNamara. "I focused on poverty reduction. It had been the belief that a rising tide lifts all boats; that if you raised a country's GDP, all levels of society would benefit. A related theory was that if you diverted resources to the poor, it would hurt the GDP. I didn't believe that. You could not help the poor with redistribution of wealth per se. The poor are poor because their productivity is low. So if you raise their productivity, you advance GDP growth of the rest of society. We proved that empirically."

McNamara expanded the bank resources available to developing countries. And he dramatically increased the bank's presence in global capital markets, borrowing not only in dollars, but in marks and yen, as well.

The bank focused on funding big and complex projects, like huge hydroelectric dams. The projects never seemed to help jump start the local economies they were intended to help, largely because the underlying financial and political systems were corrupt.

The organization became as big and complex as its projects. Currently the World Bank Group – the formal name of the organization Wolfensohn heads – comprises five organizations and writes about \$20 billion each year in new loans. The bank makes most of its loans at market rates to middle-income countries through its International Bank for Reconstruction and Development, which has been self-funding since its founding and has \$107 billion in loans outstanding. Below-market loans to poorer countries funnel through the International Development Association, which alone among the five components depends on taxpayer funds from 11 donors, including the U.S., because its borrowers often are unable to repay. It's been replenished 11 times, including last year, when it received \$800 million from the U.S. alone (IDA may be back for more money next year). Financing for private firms comes from the group's International Finance Corp., a key factor in the World Bank's growing emphasis on private investment sources; and guarantees to insure private investment in developing countries are the purview of the Multilateral Investment Guarantee Agency. A fifth agency, added in 1995, is called the Consultative Group to Help the Poorest; it makes small loans to Third World entrepreneurs.

Before Wolfensohn's arrival, the bank



Wolfensohn Beetle

Costa Ricans named a species honoring the World Bank chief for his efforts on behalf of bio-diversity.

A picky analyst finds a bushel of growth stocks to like in the Midwest

Heartland Heroes

An Interview With Walter H. Morris • While mega-mergers and other flashy developments have been grabbing headlines on Wall Street lately, analyst Walter H. Morris has been doing what he's done for years: searching for prosaic-sounding stocks with market-beating performance. For nearly 25 years, Walter has been scouring the country, particularly the

Midwest, looking for small and mid-cap issues that meet his rigorous criteria for classification as attractive growth stocks.

Three years ago, he rejoined Robert W. Baird & Co., the Milwaukee-based investment banking and brokerage firm, after a 10-year detour at the nearby Strong group of mutual funds. His work in the Midwest uncovering stocks has helped expand the following of a number of them. *Barron's* interviewed him recently in Chicago, where he was participating in a growth-stock conference sponsored by Baird.

— Harlan S. Byrne

Barron's: Walter, tell us how you operate at Baird.

Morris: Well, during my entire career I've been a research analyst. My real joy is getting out in the field and visiting companies, turning over a lot of rocks here in the Midwest to find undiscovered value.

Q: Do you have help?

A: I head a team with three associates: David Manthey, Christopher Schweitzer and Michael Schneider. We cover 44 companies at the moment. We've got two major coverages. One is an industry coverage: pumps, valves and filtration equipment. Then we have a special situations list, without a specific industry focus, but primarily small to medium-size Midwestern companies that we think can make money for our clients. I've got a wide charter at Baird because of my experience with a lot of these companies.

Q: Could you tell us about something you oversee called Equity Twenty?

A: This is a research product originally developed by Crandall Hays, a former research director at Baird. The concept behind Equity Twenty is to focus on some of the most profitable companies in America. Our definition of profitability is a minimum 20% after-tax return on equity.

That's the one ironclad requirement that we have for inclusion on Equity Twenty.

In addition, we're looking for sustainable high return on equity. That is, we don't want just a cyclical company that surges to a 20% level, then falls back when the cycle turns down. We want companies with strong balance sheets, free positive cash flows. We want annual sales, preferably, of less than \$1 billion, and that's because we want companies that we believe are still relatively early in a rapid growth phase. I'm what is called a GARP — growth at a reasonable price — analyst. I'm especially looking for excellent managements. And I like businesses I can understand, Midwestern locations preferred. From a stock price standpoint, I like companies that trade at a sizable discount to the market multiple, which often means companies that are under-followed. In these situations, you should make money on the stocks with low levels of risk.

Q: In this pricey market, is it becoming more difficult to find these kind of companies?

A: Yes, it is, clearly. And I have to pinch myself every couple of weeks to remember that the market is up in a 21, 22, 23 price-to-earnings range. Being one of the handful of guys who survived the market decline of '74, when anything in double-digits was considered pricey, it takes a while to get used to these P/E levels.

Q: The 'Seventies are ancient history for some of today's investors. So what's been the record of Equity Twenty, in relation to other market measurements?

A: In the 19 years since it was first compiled, Equity Twenty has compounded at just under 17%, nicely above the broad market indexes. However, there is one other wrinkle that makes it even more attractive. We have roughly 35 stocks on our Equity Twenty

list, despite its name. Thus we draw on the entire Baird research coverage in selecting companies that meet the criteria, especially the minimum 20% return on equity.

The 35 companies still is a large group for our brokers to work on. So we rate each company on the list every month, using a point system from one to five, with one being the most attractive.

And these rankings are determined by a fairly sophisticated analysis of the relative valuation of one company to another. If you look at the performance history of the various ranking groups, the stocks that have done the best have done much better than the overall Equity Twenty, which you remember itself has outperformed the market. Over the past 19 years, stocks with our No. 1 rankings have compounded at a 35% annualized rate.

Q: What about risk?

A: We caution our brokers that these are smaller market-cap stocks, with less liquidity than the big Dow and S&P stocks. And they are only appropriate for investors with high risk tolerance. For that portion of an investor's portfolio that is aimed at taking higher risk, Equity Twenty has been a great product.

Q: What would prompt you to remove a stock from the list?

A: Above all, there's our rule that if a company's return on equity on a trailing 12-month basis falls short of 20%, its stock comes off the list. This is a strict sell discipline because, obviously, when a company's ROE falls below 20%, at the very least its earnings momentum has slowed. So it's a kind of ride-your-winners discipline. We start

with what we think is a high-quality, rapidly growing mix of companies, and we'll stick with them as long as they compound at a very high rate. But if they don't, they come off the list and theoretically are candidates for sale.

Q: Does a sharp rise in price lead you to remove a stock from the list?

A: No, not necessarily, as long as we still view the stock as providing superior returns.



tended to view the world from its comfortable headquarters in Washington. One former federal official familiar with the institution says it had evolved into a university faculty without any students. The work force was overly concerned about position and tenure.

This is exactly the kind of challenge that gets Wolfensohn excited. Says John McArthur, a lifelong friend and onetime Harvard Business School dean: "He's gotten into things up to his elbows throughout life. He's intellectually honest and courageous, and when he sees something he thinks is wrong he weighs in and tries to change it and, from his point of view, improve it." McArthur is now at the World Bank helping Wolfensohn with the reorganization.

"These guys always turn up and always tell me how to do the job better," says Wolfensohn. "And the great thing is that I've known them long enough, so they don't take any of my nonsense."

Wolfensohn also picks the brains of some of the world's leading corporate executives: "They come here and I sit with them; and I talk about the issues of change. And the issues of change we face here are the same issues of change faced by big industrial companies, but it's more complicated because we have a board composed of representatives of 180 governments; so it's not just a commercial board. Secondly, we have a development function which is different from a profit function. Thirdly, we have staff from 140 countries, and it's not easy to move around that staff or just fire people onto the global market because you have a responsibility to them. But what all these chief executives tell me is that you need to establish your message; and then you have to keep repeating it and repeating it and repeating it for three or four years."

He's currently running about 400 World Bank executives through a six-week management training course, including two weeks at Harvard, designed specifically for the bank. Others are being shipped from their offices in Washington to offices around the world, where they can see first-hand how bank-financed projects are faring. "I'm trying to encourage people to think beyond their past experience," says Wolfensohn.

In effect he is trying to turn members of his highly educated staff into something more akin to Indiana Jones, the cinematic Ph.D. who is a man of action, nimble of foot and mind. Wolfensohn wants his experts to be as comfortable in the field helping governments set up healthy financial systems as they are behind a desk typing out project reports and memos. He also wants them to develop the listening skills of crack Wall Street salesmen and listen to what loan clients are telling them, rather than ramming a program down their throats. Of course, all 10,000 can't don safari jackets and hit the jungle trail. So Wolfensohn is constructing a global communications network at the bank so that by the year 2000, politicians, businessmen and farmers in client countries can communicate with World Bank experts by Internet or interactive video. Wolfensohn says the bank has the talent in house to become the world's premier expert on development.

Wolfensohn is by no means dismissive of his highly educated work force. When we pointed out that employees were not

yet bouncing off the walls the way they do in the financial district, he jumped to their defense. "Well, they are not bouncing off the walls here but if you look at our computer access at midnight and 1 in the morning, the thing is flying with people working at home. The tradition of Wall Street, as you know, is that you have to be there and be seen at 1, 2 or 3 o'clock in the morning because of this crazy syndrome which occurred in my own firm and at Salomon Brothers and other places. I don't think that people here work any less hard. They work differently. But the thing which I am trying to bring from Wall Street is to get the people to feel a sense of accountability and a sense of client orientation."

WHAT DETERMINES a country's eligibility for the World Bank's cut-rate loans, though presumably it's per capita income, is largely subject to the prevailing international politics of the day. Currently China, with the world's fastest-growing economy, is the largest borrower, accounting for 12% of the bank's annual lending, or \$4.3 billion, according to the Congressional Research Service.

Almost every country is a member. The exceptions: Cuba, North Korea, Brunei, the Vatican, Taiwan and a few micro-states. So far the bank's full-time board of directors, which meets as often as twice a week, is standing four-square behind Wolfensohn. His ability to obtain the support of what in the past has been a fragmented body is testament to his diplomatic skills. Juan Cariaga, who represents Argentina, Bolivia, Chile, Paraguay, Peru and Uruguay on the board, says the World Bank has become more efficient at making loans since front-line services were decentralized, resulting in more employees out in the field, visiting with client countries. "It is a tremendous change — a cultural revolution," exclaims Cariaga. "We're getting rid of the arrogant culture that we had and replacing it with a more client-centered culture."

Wolfensohn also seems to have changed the image of the bank for the better. "The old image was that the bank was unconcerned with the environment and social issues," says Franco Passacantando, who represents Albania, Greece, Italy, Malta and Portugal. "It was accused of damaging developing countries, assisting corrupt governments. No one knew if funds would reach the intended beneficiaries or remain in the pocket of some intermediary. The bank is now active in education and health and assessing the social impact of development loans."

"We've had a lot of problems," says Wolfensohn. "We've made a lot of progress, I think we've got more to make." He started off the interview in what a pop psychologist would interpret as a defensive posture, arms and legs crossed tightly. Now he's loosening up, showing us around his office. "I think everyone should hope we make it. Because if we do, I think it will be the most effective development instrument that the world has ever seen. It will not be arrogant. It will not be haughty. It will not be defensive. It will be open. It will be ready to learn. And it will be at the disposal of clients." ■



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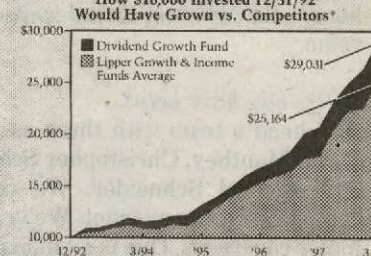
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*40.21%, 21.66%, and 22.51% are the fund's average annual total returns for the 1-year, 5-year, and since inception (12/30/92) periods ended 3/31/98, respectively. Figures include changes in principal value, reinvested dividends, and capital gain distributions. Investment return and principal value will vary, and shares may be worth more or less at redemption than at original purchase. (Source: Lipper Analytical Services, Inc.)

**Morningstar proprietary ratings reflect historical risk-adjusted performance as of 3/31/98. These ratings may change monthly and are calculated from the fund's 3- and 5-year average annual returns in excess of 90-day Treasury bill returns with appropriate fee adjustments and a risk factor that reflects fund performance below 90-day Treasury bill returns. The fund received 5 stars for the 3- and 5-year periods. The top 10% of the funds in an investment category receive 5 stars. Read the prospectus carefully before investing. T. Rowe Price Investment Services, Inc., Distributor.

DGF041764

OFFICE MEMORANDUM

DATE: May 5, 1998

TO: Mr. James D. Wolfensohn, EXC

FROM: Merrell Tuck, Acting Division Chief, EXTME



EXTENSION: 31956

SUBJECT: Interview with Mr. Jim McTague, **Barron's**, Wednesday, May 6, 11 -11:45 a.m.; followed by photo session, 11:45 a.m.- 12 noon

Jim McTague, Washington Editor of **Barron's**, the Dow Jones business and financial weekly, is planning a cover profile of you. Barron's readership consists of approximately 30,000 influential businessmen, bankers and wealthy investors. McTague has been a banking reporter since 1987. Before joining Barron's in 1994, he wrote for American Banker and USA Today. He also worked as a general assignment reporter for several local US papers and did a stint as a securities salesman for Merrill Lynch. His c.v. is attached.

Barron's has hired professional photographer Manuelyan Paganelli to take your picture. The photo session is scheduled immediately after the interview, from 11:45 a.m. to 12:00 pm in your meeting room (MC-12-700 or in the waiting room area of your executive offices).

To confirm, Mark Malloch Brown and I will accompany Mr. McTague to this interview.

McTague wants his profile of you to be different than those done previously by **Institutional Investor**, **Washington Post Magazine**, and the **New York Times**. Since McTague spends most of his time covering banking issues and politics on Capitol Hill, he will ask about your relationship with US Treasury and the office of the US executive director. Indeed, McTague interviewed Jan Piercy and has a request in to interview Treasury Secretary Rubin for this piece. He is also trying to reach several of your former Wall Street colleagues and other close business associates, including Mr. Volcker. McTague said he also plans to interview Jim Leach, Chairman of the House Banking Committee (R-Iowa), who is a neighbor of yours in Kalorama. He spoke today at length to John McArthur, which Mark arranged.

Also on the political front, McTague may ask about how confident you feel about IDA 12's passage on Capitol Hill next year (see IDA briefing note attached).

On the Bank's image, McTague would like to know if the Strategic Compact, and our new initiatives with outside partners have improved the Bank Group's reputation, particularly on Wall Street. According to McTague, several of the sources he has spoken to consider that, while laudable, the Bank is beginning to take on too many new initiatives.

On finance and our triple-AAA standing, McTague will ask about income dynamics and the East Asia crisis. Is the Strategic Compact still the right corporate strategy, post-Asia crisis? Was the Bank left flat-footed in the wake of the financial meltdown? Are staff unhappy about the

changes being made and are they up to the tasks ahead? (Briefing note on the Strategic Compact is attached).

On leadership style, McTague would like to know how difficult has it been for you to adjust to the Bank's large bureaucracy and he'd like to know what you think your goals might be for your second term as president.

McTague is also interested in your philanthropic interests outside the Bank, as well as how your business philosophy fits in with your humanitarian interests.

Enclosed is latest issue of Barron's, with Edgar Bronfman on the cover, as well as a recent cover story McTague did on New Democrats.

cc: L. Passamonti, A. Tstatsakis, J. Holden, L. Foong (EXC); M. Malloch Brown (EXTVP),
K. Bergman (EXTME)

Attachments

To Meryl Tuck, World Bank
From Jim McTague, BARRON'S

Meryl, here's the brief bio that you requested:

I've been covering the federal government for BARRON'S for the past four years. Prior to that--I've forgotten the exact dates--I was Washington bureau chief and a managing editor for AMERICAN BANKER newspaper; banking reporter for USA TODAY; banking reporter for AMERICAN BANKER (I believe that brings us back to 1987); banking reporter for the DALLAS TIMES HERALD in Dallas; a securities salesman for Merrill Lynch; state government correspondent for the PHILADELPHIA DAILY NEWS; and general assignment reporter for the ASBURY PARK PRESS; etc., etc., etc. Obviously I like changing jobs.

I'm reluctant to admit that in this undistinguished career I've never won any sort of a journalism award. Nor have I been able to interest a publisher--or an agent for that matter-- in my two novels. I was arrested once as a peeping Tom and an eaves-dropper in the course of my dogged pursuit of a corrupt government official; and happily acquitted of all charges.

I have an MA in English from the Pennsylvania State University, which I received in 1972; and a BS in English Literature and Philosophy from St. Joseph's University in Philadelphia, 1971.

I have four children. Deirdre is a classics major at the University of Chicago; Alexandra is studying biology and the piano at Cornell; Kevin is a high school sophomore; and Patrick is in the eighth grade.

IDA Issues and Questions

IDA 12

- The negotiations for IDA 12 are now underway and we expect them to be concluded by the end of the year.
- The donor countries and the Bank are in agreement that IDA lending allocations should be based on strong performance by recipient countries.
- The negotiations are taking place in the positive atmosphere which has been created by the United States having become fully current on its obligations to IDA.

As President Clinton highlighted on his recent visit to Africa, performance has improved in many countries in the region—as it has in other IDA countries—and so the prospects for effective use of IDA resources have never been brighter.

It is too early to say how large the replenishment will be. That is ultimately a decision for the donors. However, we have analyzed the country assistance strategies that have been prepared for the vast majority of IDA countries, and, based on very solid numbers from these and the possibility of several countries "re-activating" during IDA 12, the needs point towards a substantial replenishment.

Possible Questions

- You will almost certainly be asked *how much money we are looking for IDA 12*. It is **important to keep your answer general as indicated above, you should not be drawn into any speculation as to whether IDA 12 will be larger or smaller than IDA 11, which was \$22 billion, of which \$11 billion was new donor resources.**
- You may be asked about *potential reactivators*. You should say that it is too early to say, but **there is the possibility of several countries like DR Congo and Liberia.**
- You may be asked *if any East Asian countries are going to slip back into IDA eligibility, especially Indonesia*. The answer is that **for a variety of reasons we do not expect any of these countries would be eligible (or would wish to be) in the foreseeable future.**

NGO Activity

Oxfam International will be releasing a paper in Washington the week of the meetings, "IDA 12: A Chance to Deliver on World Bank Promises." Ask Mark if you haven't seen it. The paper, which is more aimed at the IDA deputies than the press, expresses strong support for a full IDA-12 replenishment, but hones in on three areas where the Bank needs to strengthen its work:

Social Sector Commitments -- The paper asserts that the Bank should honor its earlier commitment to spend \$5b annually on health, education, and other basic social services. If it can't make this commitment, it should not just argue that disbursements are rising and year to year fluctuations do not reflect general trends: it should also explore more and explain why commitments are declining. IDA borrowers should also promise to increase their support for investments in the social sector areas.

- **Bank's response:** We are committed and ready to provide whatever level of assistance our borrowers can absorb and utilize effectively for education, health, and other basic social services. And whether that amount is \$5 billion a year or less or even more than that, we are absolutely prepared to give as much support as our borrowers can handle.

The issue here is not any reluctance on the Bank's part. Rather, it is that our borrower countries can take on only so much at a time. Their capacity to implement new initiatives productively is not unlimited, and the amounts they want to borrow each year are not unlimited. We are pushing ourselves as hard as we can, and our borrowers are pushing themselves hard too, and that will continue.

Results in Education -- Focusing mainly on Africa, the paper claims that 130 million primary school aged children in IDA countries currently do not go to school, and by 2000, 56 million children in Africa will be out of school. Meanwhile, 1997 IDA lending fell to one-third of its 1996 level, and in Africa, total IDA education lending only amounted to \$100m in 1997. The Bank, donors, and borrowers should together develop action plans for borrowing countries that set out how they will achieve universal primary education by 2015 (the target date set by OECD/DAC). To achieve this goal, at least 10% of IDA resources must be devoted to primary education lending annually.

- **Bank's response:** We are totally committed to helping our borrower countries achieve major improvements in education -- including reaching universal primary education -- at the earliest date possible. What needs to be understood is that a lot depends on what each country is willing and able to do. The Bank can help -- and will, to its utmost ability. But in the end, everything depends on country commitment and follow-through.

A lot of countries are in fact making better progress now. We currently expect our new lending for education to be up significantly this year compared to last.

Citizen Participation in Policy Dialogue -- Oxfam supports the Bank's recent efforts to open up policy discussions to civil society groups (e.g., SAPRI and the Inspection Panel). But they would like to see participation made deeper and broader, particularly regarding the CAS. They would like IDA Deputies to instigate clearer guidelines for participation in the CAS and a more systematic means of incorporating poverty, gender, social and environmental considerations. Their suggestions for making participation more effective include: (a) establishing clearer timeframes and greater transparency related to CAS consultations; (b) establishing clearer criteria for selecting and involving a wide range of credible civil society groups, especially those groups that would not normally be included in such discussions; (c) involving civil society groups in discussions around the IMF's PFP and in CG meetings; and (d) making the CAS available in draft and final versions (and in local languages) to those involved in consultations around it.

- **Bank's response:** We now, in the context of the recent Board Meeting on NGO relations, have discussed participation in Bank projects and policies. While we all desire openness and partnership in our operations, and would like the Country Assistance Strategies to more publicly vetted, this has to be balanced against the government's interest in confidentiality. The recent agreement on information disclosure policy on the SAPRI initiative is a good example of how we are trying to balance these competing priorities.

The World Bank



THE STRATEGIC COMPACT

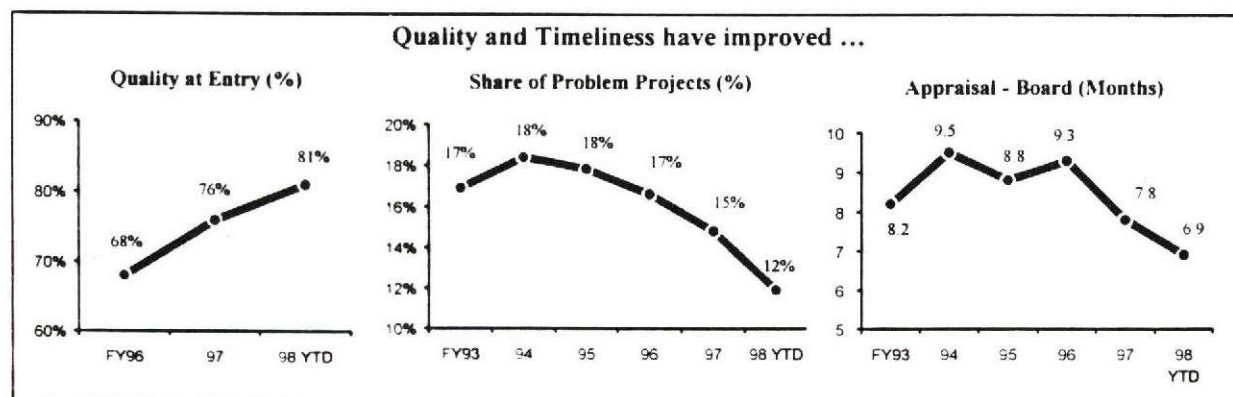
One-Year Progress Report

The Strategic Compact is an action plan to make the World Bank more effective in reducing poverty. It was proposed by World Bank President James D. Wolfensohn at the World Bank/IMF Annual Meetings in the fall of 1996 and unanimously approved by the World Bank's Board of Executive Directors in March 1997. Funding resources became available on July 1, 1997.

Through the Compact, the Bank's shareholders and management are investing in a series of changes to transform the way the institution does business: improving its products, speeding up its processes, lowering its costs, and increasing the impact of its work in developing countries. The Compact is also establishing clear performance criteria against which progress will be measured, and for which management will be held accountable.

Under the Compact, the Bank will become closer to clients, quicker, more responsive and flexible, more focused on results, technically excellent, more accessible and open to partnership, and more cost effective.

The Compact will achieve that by: (a) improving and retooling its current ways of doing business, and (b) taking new initiatives, and creating and offering new products and services to better meet its clients' needs.



Quality and Quantity of Lending is Up

One of the Strategic Compact's linchpins is to focus more on *results* – something that has paid off in the first half of the current fiscal year in both quality and quantity of lending.

The quality-at-entry of Bank operations has continued to climb, according to the Bank's Quality Assurance Group (QAG). The number of Bank projects found to have satisfactory or better quality at entry rose while the number of problem projects fell. Meanwhile, the Bank sped up the time between project appraisal and Board approval.

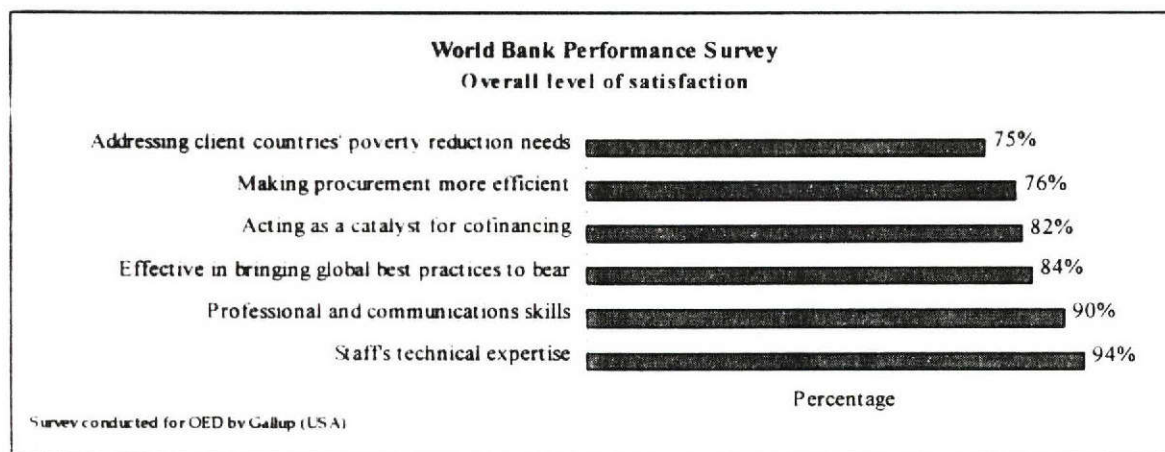
On the quantity side, both IBRD and IDA commitments and disbursements hit *all-time record highs* in the first six months of FY98. Excluding Korea, commitments reached \$8.8 billion by mid-FY98, up from \$7.4 billion in FY97; while disbursements rose to \$11.4 billion in the first part of FY98 from \$10.6 billion at mid-FY97. The increased lending is due to adjustment operations, mainly in Russia (SAL and Coal SECAL) and Thailand (Financial Restructuring Loan).

The overall increase in IBRD/IDA lending may also reflect the Bank's improved responsiveness to clients as well as client demand factors – both influenced by the work of staff and country directors, many of whom are now located in the field. On *decentralization*, the Bank is moving decisively, with 22 country directors having already moved from Washington to the field – compared to only three in June 1997.

While the Bank has been decentralizing to get closer to its clients, its staff at headquarters have been changing *the way they do business* to improve service to borrowers. Under the new system, country directors control their own budgets. Each is responsible for planning the Bank's country assistance strategy and then using their budgets to contract with the Bank's new *networks of expertise* to find the right staff with the appropriate skills to fulfill their country workplans.

Clients See Quality Improving

Borrowers have noted the improvement in the quality of Bank performance. A borrower survey conducted by Gallup (USA) for the independent Operations Evaluation Department (OED) in the fall of 1997 showed that borrowers' perceptions of the Bank are generally positive and improving.



The Gallup survey, which covered 281 people in 30 developing countries, showed that Bank performance in project preparation and appraisal is viewed as having improved during the past four years. 64 percent of respondents say performance has improved while only 10 percent say it has deteriorated.

Meanwhile, a *survey of 10 African countries* conducted by the Bank's Africa region between May 1997 and January 1998, also showed that the Bank's African clients had a generally positive view of the Bank's work. The African client surveys, however, also pointed to the need for continued progress in adapting global knowledge to the circumstances of particular countries, making Bank policies more flexible and understandable, and increasing the impact of the Bank's services on the poor. Similarly, while the Gallup survey gave cause for optimism, it also revealed areas where the World Bank can improve.

Technically Excellent, Cost-Effective

The Strategic Compact emphasized the need to improve the Bank's technical excellence. As part of this, the Bank's Board approved a sweeping reform of the institution's *human resources policies* on April 2. The reform tackles the areas of employment, compensation and benefits, recruitment and skills mix; but it also addresses the issues that support the development of staff which are key to the successful renewal of the institution - a commitment to greater diversity, an emphasis on learning, a focus on mentoring and leadership training, and effective performance management.

Another big part of the retooling of the Bank's human resources reform was the decision to improve *Bank management*. Last summer, 150 managers were chosen from the Bank's pool of managers for a limited number of managerial slots. Some 400 managers have also attended an executive development program. Meanwhile, the Bank's *cost-effectiveness* effort will lead to lower costs and higher productivity.

New Products for Borrowers

In the fall of 1997, the Bank's new products team rolled out the first two products created under the Strategic Compact to make loans more flexible and faster to approve and disburse; *Adaptable Lending Loans*, and *Learning and Innovation Loans*. Aside from these new products, the Bank made available *single currency loans* earlier in 1997. Also, the Bank is working on a pipeline of new ideas, including the launch of a prototype of the *Global Carbon Initiative*.

Responding to Change in Development Arena

While the Bank is steadily unveiling new products, it has also sped up its response to global economic changes and its borrowers' changing needs.

In response to the East Asian crisis, the Bank moved quickly to address the social and financial problems in the region. A special budget of up to \$25 million per annum -- initially for two years -- has been approved for this purpose.

Meanwhile, the Bank has also signaled its willingness to tackle new development issues such as *corruption* and *debt*. The Strategic Compact's focus on partnerships and responsiveness to client needs are both reflected in the *Highly Indebted Country (HIPC) Initiative*. On April 7, the Bank and IMF, along with other creditors, agreed to provide exceptional support under HIPC amounting to nearly \$3 billion in debt-service relief for Mozambique, making it the sixth country to benefit under HIPC.

Corruption has also taken center stage on the Bank's development agenda. In March 1998, the Bank issued new guidelines for Bank staff to help stem fraud in Bank-financed projects -- and in client countries more generally.

Expanding Partnerships, New Services

The Strategic Compact's emphasis on making the Bank more accessible and open to partnership has spurred on the Bank's efforts to reach out to new partners. Recent partnerships include an agreement in February 1998 with the World Conservation Union to create global standards on *dam building* and a

More Flexible Products

Adaptable Loans -- these support projects that are implemented in stages. The first loan in a given series will be reviewed and approved by the Bank's Board while Bank management is given the authority by the Board to approve following loans. Interest in the program is high. The first Adaptable Loan was approved in March 1998 -- \$60 million for India's power sector.

Learning and Innovation Loans -- these loans have a fixed ceiling of \$5 million and will be used to test new approaches and new sectors, often in start-up situations, and with new borrowers. They will be approved by management rather than the Bank's Board, (who nonetheless must be informed of the loans.) In December 1997, the Bank approved the first loan of this type, \$4.7 million for the judicial sector in Venezuela.

partnership struck in June 1997 with the World Wildlife Fund to help conserve the world's forests and promote their sustainable development.

The Bank is also working hard to expand its advisory role for its borrowers. A big part of this is creating the "Knowledge Bank" – which will help developing countries to draw on the Bank's vast pool of development expertise. At the same time, the Bank will reach out to its partners for the best knowledge they have to offer. The Bank recently allocated increased resources to facilitate rapid development of knowledge systems and the program is already being implemented in many areas of the Bank's work.

Costs

A high and rising share of the Compact's overall costs will be met through a stringent program of savings and redeployments. Net additional investment under the Compact—excluding the cost of staff separations—is \$250 million. This funding will be phased in to ensure that it is in line with the Bank's absorptive capacity: \$100 million annually in FY98 and FY99, and \$50 million in FY00. Approval of the Compact's funding will be contingent on the Board's annual review of the Bank's budget and work program.

By FY01, the administrative budget will return to its current level, subject to demand for the Bank's improved products and services. This goal will be met through significant increases in productivity as well as the program of savings and redeployment, aided by a comprehensive cost-effectiveness review.

The total cost of staff separations is projected at \$100-150 million over the Compact period, with a first installment of \$60 million approved in March 1997. Separation funds will not be used where retraining or reassignment is an option, nor to finance the release of poor performers. The Board will receive full reports on the implementation of the separation program every six months.

For more information on the World Bank's Strategic Compact, go to our website at WWW.WORLDBANK.ORG and search for "Strategic Compact".

Updated by External Affairs April 1998

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Blame it all
on the Internet

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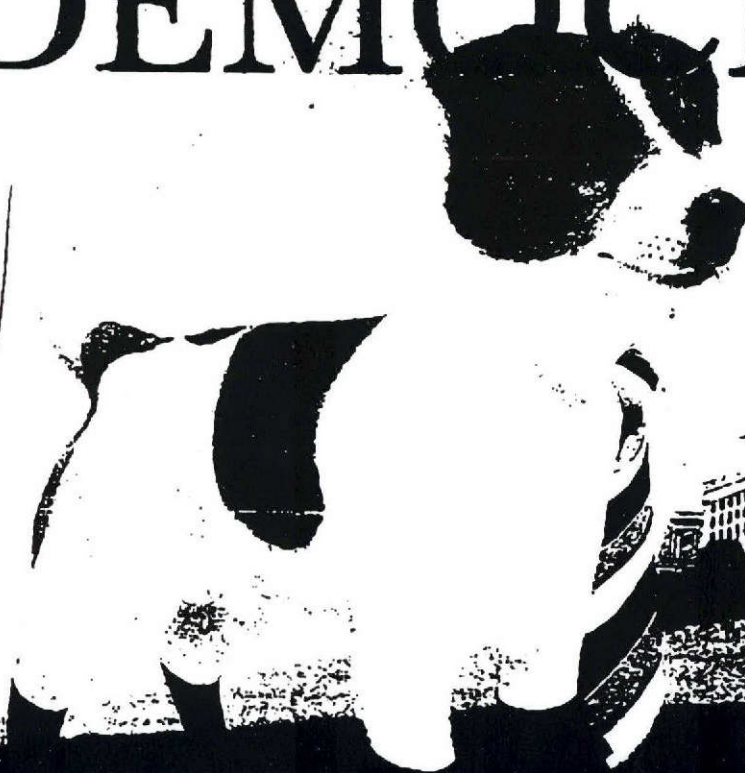
Why hotel stocks
still look good

BARRON'S

THE DOW JONES BUSINESS AND FINANCIAL WEEKLY

AUGUST 18, 1997 \$3.00

NEW DOG DEMOCRATS



*This new conservative breed
proved crucial in balancing
the federal budget.
How their ascendance
will help U.S. investors
for years to come.*

To Meryl Tuck from
5 pages
Fax 522-26

New Dogs

Moderate Democrats tug at the party's leash, help shape budget deal, threaten fight over trade

BY JIM MCTAGUE

THE REPUBLICANS AREN'T the only party living in a House divided. The Democrats in Congress are being tested by heated disputes over economic policies between the party's left and right. And, like Republican conservatives, Democratic liberals are scandalized by the moderate forces of their party. They watch in anger as "New Democrats" like President Bill Clinton and Vice President Al Gore attempt to pull the party of FDR and LBJ toward the philosophical center, where New Democrats believe most voters now reside. The balanced-budget and tax-cut legislation, derided by both the Republican right and the Democratic left, was a victory for the New Democrats — and especially for a breed of congressional New Democrats who style themselves "New Dogs."

Thus far the party has kept its differences from escalating into the kind of public blowups that have embarrassed Republicans. But keeping their tempers leashed will become increasingly difficult next month when the President asks for authority to expand the North American Free Trade Agreement, a New Democrat initiative that is vigorously opposed by labor, a powerful liberal ally. The fight promises to be more bitter than the original NAFTA brouhaha during Clinton's first term.

This struggle may be trouble for the party, but it bodes well for investors, at least as long as the New Democrats keep racking up victories. Their economic philosophy is near enough to the market-friendly GOP's to augur a significant reduction in political risk for investors in the years ahead.

If the party is to win future elections, New Democrats preach, it must remain pro-employee, yet cease being anti-business; and Democratic regimes no longer must view government as a means to overtax the wealthy to reward the indolent, but perceive it as an investor in

growth-spurring enterprises like education, infrastructure, and research and development.

Reed Hundt, the current chairman of the Federal Communications Commission and a close friend of Vice President Gore, says this isn't a left-to-right shift for the party, but an evolution. "The population is older, and hope-

more to the financial pages and away from Washington news. Private investment plans are where Baby Boomers look these days to build their retirement nest eggs; they've lost faith in the Social Security system. Republican pollster Bob Teater says his surveys for The Wall Street Journal/NBC News Poll indicate that 50% of all adults currently have more than \$5,000 each in mutual funds and stocks. "People who have a financial stake in the country are a little more careful

Reagan for the Presidency in 1984. Mondale ran as a typical tax-and-spend Democrat; he carried his home state and the District of Columbia. As a handful of Democrats read the results, the public was tired of rowing to Washington's drum beat. They created an unofficial party lifeboat called the Democratic Leadership Council and began preaching a right-of-center message that the majority of the Democratic congregation found repulsive.

The very first chairman of the organization was a young party Turk from Missouri named Dick Gephardt, who, as DLC historians sadly tell it, has since drifted leftward and is now classified a paleoliberal.

Clinton headed the DLC in 1990, and after his election as President in 1992, he was expected to reinvent the party so that it became conservative on fiscal policy and moderate to liberal on social issues. But Clinton was slow warming to the task. During his first two years in office he vacillated between old-fashioned liberalism — his

health-care proposal, gays in the military — and the New Democratic philosophy. In part, he had to govern to the left because Congress was dominated by passionate liberals of the Gephardt variety and the Republicans refused to work with the new President. Clinton's early style also reflected an internal White House debate between New Democrats and old believers.

"We were trying to spend money on research and education and at the same time be fiscally responsible," recalls Laura D'Andrea Tyson, a former Clinton economic adviser. "The deficit was seen



fully as we age," Hundt reflects. "We've learned, for instance, that markets generate wealth."

Liberals, especially those in the House of Representatives, counter passionately that the party has lost elections because it no longer runs vigorously enough to the left. Followers of both parties and election results, however, support the New Democrats' strategy. Voters' eyes are drawn ever

in the way they vote," observes former President Gerald Ford.

The Democratic divide is as deep as the one among Republicans in the House, where right-wing groups like the Conservative Action Team, or House CATs, tried to dethrone Speaker Newt Gingrich for steering down the middle of the road. That eruption made headlines.

New Democrats are the inadvertent spawn of Walter Mondale, the Minnesota liberal who jousting with Ronald

ILLUSTRATIONS: ROMAN GENN FOR BARRON'S

as a problem that had to be dealt with, which is a New Democrat position. But the older liberal philosophy was at work, too. They were adjusting the tax code to make it more progressive and raise taxes at the top, and expanding the earned-income tax credit at the bottom."

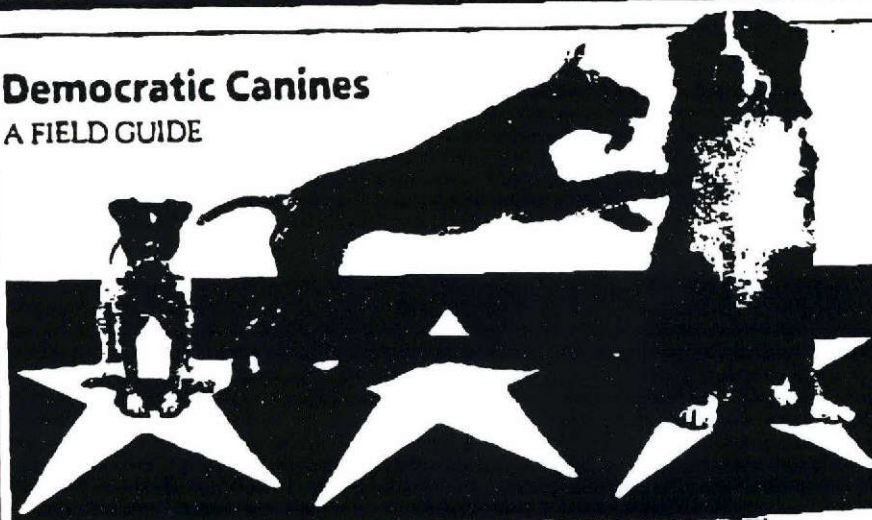
FOR CLINTON, THAT debate was settled decisively when the GOP trounced the Democrats in 1994's mid-term election and took control of both houses of Congress for the first time in 40 years, says Elaine Kamarck, who until a few weeks ago was Al Gore's senior policy adviser. (She's now at Harvard, where she will run a program for the John F. Kennedy School of Government, called "Visions of Governance for the 21st Century.") And yet about a mile away, a majority of the Democrats on Capitol Hill believed the party had lost that election because its message hadn't been liberal enough.

In the 1996 Presidential race, Clinton seemed to have proved the House members wrong. He ran as a New Democrat against Republican Bob Dole, sounding the balanced-budget and smaller-government themes. As always with the President, there was some backsliding, which angered his New Democrat brethren. For example, he vetoed legislation aimed at curbing class-action lawsuits by tort lawyers, big contributors to his Presidential campaign. Most of the lawsuits were leveled at Silicon Valley, home of the new industries the New Democrats claim they want to promote.

But Clinton won the election, and along with him a small but vocal bloc of House members who also had campaigned on New Democrat themes — like balancing the budget and using tax cuts to help the middle class. They were largely elected in suburban districts where voters lean right yet were turned off by the extreme rhetoric associated with Newt Gingrich and his CATs during the 1995 government shutdown.

Democratic Canines

A FIELD GUIDE



NEW DOGS

Habitat:

Predominantly found in suburbs, though some occasionally show up in more rural areas.

Identifying features:

- Right of center on fiscal and economic issues and just left of center on social issues.
- Primarily interested in three issues: the "new economy," education and trade.
- They preach fiscal responsibility, are business-friendly, favor free trade and envision a leaner, albeit not meaner, government.

Personality:

Frisky, energetic, loud bark, some bite. The 37 members of the New Democratic Coalition, dubbed the "New Dogs," want to pull the party away from the left and more toward the center of the philosophical spectrum.

Habitat:

Predominantly rural areas in the Deep South, though a few strays can be found in other climes.

Identifying features:

- The 24 members of the Blue Dog Coalition have been around since February 1995.
- They are "blue" because their moderate to conservative views were choked off by the liberal wing of the party.
- They have been most focused on balancing the budget. They are also conservative on social issues, more so than the New Dogs.

Personality:

Extremely independent. They will work with the GOP to obtain their goals. The GOP leadership often solicits the group's help to counter the House's liberal wing.

Habitat:

Primarily urban areas.

Identifying features:

- These old-style liberals still champion the social-welfare state and a tax system designed to redistribute the nation's wealth.
- They tend to be older than New Dogs and have much more seniority.

Personality:

Loud bark, not much bite. They have been known to turn on President Clinton when they think he is moving too far to the right on issues. But unlike the members of the conservative wing of the congressional GOP, they are less inclined to get into fights with other party animals.

done? They claim they are fundamentally different from Republicans: Their brand of conservatism, they say, is humane, while Republicans, they argue, have a sink-or-swim attitude toward the poor. Says Roemer, "We want smaller and smarter government — with a lot of heart."

Tom DeLay of Texas, the House Republican whip, contends the New Dogs merely are liberals trying to disguise their spots from the voters. Other Republicans concur, pointing out that New Democrat Clinton wouldn't approve a welfare-to-work bill until a business-unfriendly minimum-wage provision favored by liberal giants like Sen. Edward Kennedy of Massachusetts was thrown in.

NEW DOG MORAN doesn't talk like a liberal, but in the past he has voted with them 58% of the time on economic matters and close to 70% of the time on social issues, according to the Almanac of American Politics. Scolds the privately thoughtful but publicly pugnacious Moran: "The Democratic Party has tended to stand for redistribution of wealth, excusing criminal and abnormal behavior, and creating entitlements for people instead of opportunities. We're more reflective of the New Deal — enablement to give a helping hand to those when it's needed, but not to create long-term dependency."

With the economy humming and the stock markets exuberant, the President and his New Dog pack are convinced that his second term represents a once-in-a-lifetime opportunity to polish the party's image so that it will be identified with economic growth and opportunity, not the Great Society. This is why Clinton, with the assistance of New Dogs, car-jacked the GOP's balanced-budget and tax-cut vehicles in the face of opposition from influential party liberals like House minority leader Gephardt, who fret about deep cuts in programs benefiting their traditional

Known as New Dogs, to distinguish them from the more socially conservative Blue Dog Democrats, their New Democratic Coalition of 37 members has helped overcome liberal resistance and create momentum for the Clinton agenda in Congress, especially his balanced-budget plan.

"New Dogs are much more interested in what makes the economy tick than in social issues like abortion," says the chairman of the House Democratic Caucus, Vic Fazio of California, who runs with the new pack. Adds former Gore

aide Kamarck: "The old Democrats love jobs but hate the employers. The New Democrats want lots of jobs and good wages but understand that the private sector is where jobs are created. They practice fiscal prudence and wage no class warfare."

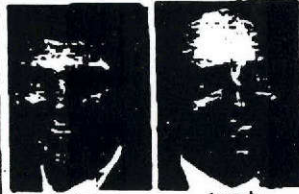
The New Dogs were collected into a caucus by three House members from suburban and rural districts: James Moran of Virginia, Calvin Dooley of California and Tim Roemer of Indiana. Why didn't they just convert to Republicanism, as some of their frustrated colleagues had

NEW DOGS



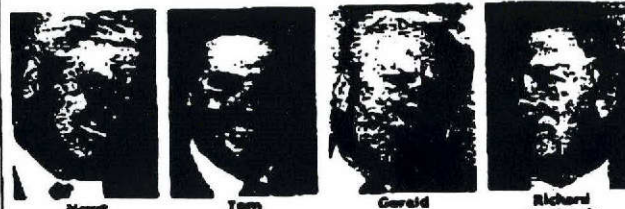
These three Democrats were concealing their plan to form the New Democratic Coalition early this year at about the time that most House Democrats were lining up to oppose balanced-budget and spending-cut legislation. Says Roemer, "We want smaller and smarter government — with lots of heart."

...THEIR FRIENDS...



Daschle, leader of Senate Democrats, isn't a formal member of the coalition, but he sympathizes. Colleague Lieberman hopes to coordinate New Dog efforts in the House with those of their friends in the Senate.

...AND NOW THEY'RE VIEWED BY OTHERS



He survived a coup attempted by radicals, allies but he and Clinton both won with New Dog help.

The Republican whip in the House dismisses the New Dogs as old-style liberals in disguise.

"People who have a financial stake in the country are a little more careful in the way they vote."

"We're all New Democrats," says the House minority leader, a rival of Gore in 2000.

constituents — labor, inner-city blacks and environmentalists.

Clinton also has loyal supporters in the Senate. Minority leader Tom Daschle, while not a card-carrying New Democrat, says: "I'm very sympathetic to the DLC agenda. They have a major contribution to make to the caucus and the party. I support most if not all of what the DLC has proposed." Sen. Joseph Lieberman of Connecticut, the current chairman of the Democratic Leadership Council, is attempting to coordinate efforts between New Dogs in the House and sympathizers in the Senate so that more of the agenda is enacted before the President's term is up in 2000.

"Voters ratified this way of thinking when they elected Ronald Reagan President in 1980," says Will Marshall, an economist at the Progressive Policy Institute, a Washington think tank that supplies intellectual fodder to New Democrats. But will "this way of thinking" continue to play well enough in the nation's growing suburbs, where lightly regulated high-tech marketplaces have produced the best jobs? Here reside the swing voters, who usually determine which party controls the White House and Congress. But though their instincts are right on, the New Democrats might well be underestimating the rightward drift of the voters, who, new polls show, are more concerned about ups and downs on the stock tables than the ins and outs of politics.

Bob Teeter, whose polling firm, Coldwater Corp., is based in Ann Arbor, Mich., asked people between July 28 and 28 if they had more than \$5,000 in stocks or mutual funds. Much to Teeter's surprise, 50% of all adults answered affirmatively. The number is astronomical because it cuts across all races, sexes and income levels: 53% of the affirmative respondents were white and 32% were black; 45% were women; 39% made between \$30,000 and \$50,000 a year and 15% earned under \$20,000. Mutual funds, which have conducted similar polls, are aware of the trend, but the political ramifications of the numbers have been overlooked by both parties.

"I don't know if many of my Democratic colleagues have made the connection yet," Sen. Lieberman told us the

"The likely consequence of the budget deal is a decade or more of Democrat Administrations...."

Gephardt is completely out of step with the times."

— Dick Morris

other day. "There's still a lot of wailing about capital-gains tax breaks benefiting the rich."

Clinton certainly has made the connection. The success of the economy is one reason the public has awarded the President a 61% approval rating despite Whitewater, Paula Jones, campaign-finance scandals and other negative publicity.

Class-warfare rhetoric about the balanced budget and tax cuts came predictably from the lips of Gephardt, who most Democrats believe will raise the liberal challenge to Gore for the party's nomination in 2000. Gephardt, while not making any predictions about his political future, told us he isn't an old-time liberal and disputes the DLC's account of his leftward drift. "We're all New Democrats," he says.

Gephardt claims he brings fresh solutions to old problems, which is part of the New Democrat mantra. He's not anti-free trade: "Everyone's for free trade. The question is, on what basis?" Gephardt says the debate is over whether provisions mandating human and labor rights and environmental safeguards should be part of any treaties. He believes they should.

Whatever Gephardt ends up calling himself, he is clearly locked in a classic alpha-beta struggle for control of the Democratic pack. But he's been careful thus far not to tear any flesh and make the party look as ludicrous as the feuding Republicans. Though he has voted against Clinton's legislative initiatives and boycotted White House ceremonies celebrating bipartisan agreements, the protests largely have been symbolic. He hasn't actively tried to thwart the President by threatening New Democrats in Congress who have joined with moderate Republicans to pass budget, tax and trade legislation.

Fazio says that Gephardt always advises, "Vote your district. It's your first responsibility." Fazio, the No. 3 Democrat in the House, calls that "the kind of leadership you appreciate."

"Nobody ever grabs you and pressures you," says

ciaco's suburbs. "The leadership will try to sell you, but not bite you."

Tauscher and her New Democrat colleagues had better get a tetanus booster. Liberal flags already are bared in anticipation of the President's request that Congress revive his "fast track" authority to negotiate trade deals, under which lawmakers can't amend a trade pact but must vote it up or down by a statutory deadline. Every President since 1974 has had the power; Clinton's expired in 1994.

The President needs the authority to open the Nafta agreement to Chile and other South American countries. But in opposing fast-track, labor unions are arguing that Nafta has cost 420,000 American jobs. Gephardt is siding with the unions, which are doing all the leg-breaking for him. The AFL-CIO is warning Democrats who oppose labor on fast-track

ter Deutsch, a fiery young New Dog from Florida. Deutsch says there's a 50-50 division in the Democrat caucus between old-line liberals and the centrists. If that's true, the fast-track debate could leave the party divided as it moves into the 1998 congressional election season.

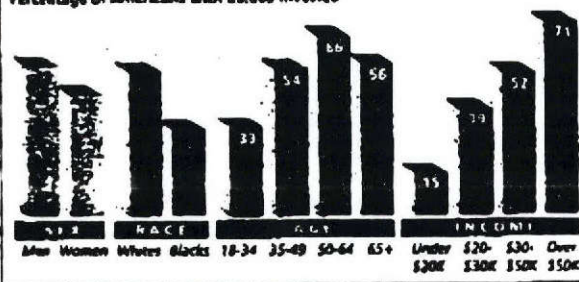
Some political analysts would argue that Clinton already has succeeded in transforming the party and that liberal House Democrats just don't get it. Says Kamarck, the former Gore adviser: "The Clinton Democratic Party in 1997 is in favor of a balanced budget, free trade, the end of welfare as we know it and a smaller federal government. These are four dramatic and significant changes in the image of the Democrats since 1991." She predicts New Democrat Gore will run on Clinton's legacy and promise to advance it with some New Democrat ideas of his own.

Dick Morris, the former White House political consultant, asserts that Clinton, by engineering balanced-budget and tax agreements, already has sold the public on the New Democrat agenda. "The likely consequence of the budget deal is a decade or more of Democratic Administrations," he says. However, he adds, because Clinton has been less successful in moving the party's congressional wing to the center, the result will be continuing control of the Congress by the GOP. For one thing, Morris asserts, "The American people prefer a divided government." More important: "Gephardt is completely out of step with the times." For this reason he predicts Gore will beat Gephardt decisively for the nomination in 2000.

They're All Capitalists

According to a survey by pollster Bob Teeter for The Wall Street Journal/NBC News Poll, the percentage of adult Americans across boundaries of sex, age, race and income—owning at least \$5,000 in stocks and mutual funds is supremely high. Politicians are taking note.

Percentage of Americans with \$5,000 invested



that the federation will openly fight them with millions of dollars in television ads in the 1998 election. Disobedient New Dogs will be a particular target. Says AFL-CIO lobbyist Peggy Taylor: "They are elitist. They are disparaging of some aspects of trade unionism."

The labor federation has been calling on freshman New Dogs to reconsider their affiliation. "We didn't ask the members to leave the group," Taylor reports. "We just pointed out that they are joining a group with a particular ideology: 'Is this really where you want to be?'"

The pressure appears to be working. For instance, New Dog Debbie Stabenow of Michigan, who sounded New Democrat themes when she defeated incumbent Republican Dick Chrysler in 1996 but ran on union money, appears to be wavering. Though she voted in favor of most-favored-nation trade status for China, a Clinton initiative, she's likely to oppose fast-track: "I don't intend to vote for it unless strong provisions on worker standards and environmental issues are incorporated."

New Dog Californian Robert Matsui, whose expertise on trade matters is respected by both parties, says the coalition will splinter on fast-track, but most of its members will side with the President. New Dog co-founders Moran and Dwoley, a Californian, will lead the charge. Matsui predicts, along with New Dog Jim Davis of Florida. Caucus members don't have to vote as a bloc to maintain membership.

"This is a battle for the heart and the soul of the Democratic Party," says

THIS DIVIDED GOVERNMENT is a continuation of the outcome of the 1996 election. Says Republican elder statesman Gerakl Ford: "The American people are philosophically more moderate than they are extreme. Take the 1996 election. The American people voted for Clinton because he appeared to be a moderate Democrat and they voted against Dole because he appeared to be too far to the right. On the other hand, they turned down the congressional Democrats because they are still hanging on to the old liberal Democrat philosophy and also because they wanted a check on Clinton."

Alvin From, the president and one of the founders of the DLC, recently released polling results showing that 58% of Democrats believe the government's role is to create opportunity, not redistribute wealth. Rank-and-file Democrats support the President's New Democratic agenda, he said, and 57% support giving Clinton fast-track trade authority.

Ford doesn't believe the Democratic Party has changed its philosophy dramatically. Neither do committed liberals



August 18, 1997

BARRON'S

like Rep. Barney Frank of Massachusetts. It is far too early, Frank believes, to tell if the New Democrats have triumphed. And he is reluctant to acknowledge that even Clinton and Gore, despite their numerous avowals, are true believers of the New Democratic creed. Clinton has simply been accommodating the GOP reality, Frank says, and the actual thrust of the Democratic Party is in a direction opposite the New Democrats'.

But if Frank is wrong and Morris and From are correct and the balanced-budget agreement has changed the Democrat Party, Clinton received help from an unexpected quarter - House Republicans.

Hard-line stands by the party's far right, which adds up to about 70 votes (the exact roster of the CATs is secret) tended to mold moderates in both parties into a cohesive and decisive force in the budget and tax debates.

Though the GOP controls the House, it does so by a margin of only 19 votes. The chamber has 435 members - 228 Republicans, 207 Democrats and Vermont's Socialist Bernard Sanders. (Sanders views Clinton's domestic policy as being "to the right of Richard Nixon" and laments, "We're seeing the merger of the two parties into one large, corporate party.")

The narrow advantage the GOP has in the House, coupled with a Senate majority that lacks the 60 votes needed to override Presidential vetoes, meant that the revolutionaries would have to be satisfied with incremental changes. Michael Castle of Delaware, who heads a group of 30-50 Republican moderates in the House, says ideological bickering on the fringes of both parties has given moderates of all stripes more influence in the Congress than they've had in many years - a plus for Clinton and a moderate agenda.

Early in the year Democrats in the House were lining up behind Gephardt to oppose the balanced-budget plan and its anticipated cuts. Had he succeeded, it would have reproduced the same gridlock voters opposed to revolt against in the 1996 election.

At about the same time, Moran, Roemer and Dooley conceived of the New Democratic Coalition. Declares Fazio: "The point of view they are trying to articulate always existed, but previously they had no way to be heard, except individually. The left of the party was better organized."

A speech by Tauscher to the caucus back in May is credited with sending a wake-up call to her colleagues.

Tauscher says that, having grown up in an Irish Catholic family in New Jersey, she is genetically a Democrat. She's also a former Wall Street trader and investment banker, and founded ChildCare Registry, which sells background information on child-care providers. Her narrow victory in California was personally expensive. She spent \$1.73 million of her own and her husband's money (William Tauscher, a Republican, is CEO of Big Board-listed Vanstar, a computer retailer).

Tauscher feared the caucus would turn its back on the balanced-budget proposal. "So I stood up and said, 'I've been here for five months, I really like it, I know the people from my 10th Con-



gressional District are going to send me back. But frankly, they could kiss me goodbye if we can't deliver a balanced-budget bill.' I told them the growth of opportunity for Democrats around the country is in districts like mine. Members like me must have this balance of fiscal responsibility and social moderation. We have to be for more of the things the American people want, but we also have to protect their pocketbooks. I had never stood up in the caucus before. I had never felt compelled before, plus I was the new kid and I didn't think they cared what I thought. But I was really concerned we could lose the opportunity of dispelling the label 'tax-and-spend liberal,' which does not apply to the vast majority of Democrats."

THE GROUP CAME TO THE attention of Clinton. He met with members at the White House. Gore visited them several times on the Hill; and the White House chief of staff, Erskine Bowles, and Clinton's legislative-affairs director, John Hilley, began attending the group's weekly meetings, using their input to draft a balanced-budget proposal to counter one offered by Republicans. Gore's chief of staff, Ron Klain, says Clinton and Gore latched on to the group because of that support and because of the view that they will become a pivotal group in the House.

Even some Republicans acknowledge the New Democrats' ascendancy. Observes the top aide of one conservative congressman: "The New Dogs have been Clinton's muscle versus Gephardt and have thus disarmed him in many battles with the President, which has been a surprise. The budget battle and the China MFN vote are two prime examples."

Democrats in swing districts will determine who controls Congress, and that gives the New Democrats moral authority," says Ed Kilgore, political director of the Democratic National Committee.

But what if the group splinters on fast-track, the first really tough test of the New Democratic agenda? New Dog Jim Turner of Texas, who is also a Blue Dog, seems optimistic the group will weather this first big political test: "The people involved understand how critically important this effort is to the future of the Democratic Party. There may be difficulty on select issues. But there will be many others where we will take a stand and try to provide leadership."

E. COMMENTS:

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