Boom, Bubble and Bust

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In a paper this past spring, Bill Sena, with his usual erudition and insight gave the Club a comprehensive and compelling analysis of the economic dynamics that led to the recent financial crisis. In this paper, I offer a smaller scale case study which may serve to amplify the role human nature plays in creating booms, bubbles and busts. I lived through one. Yes, I was at the very epicenter of the 1975-76 boom and bust in .... toilet paper. While not an existential threat to the economy, it was a source of irritation to every American.

At that time I managed P&G's production lines in Green Bay producing that iconic brand Charmin Bathroom Tissue. I witnessed first-hand human over zealousness in acquiring a valuable commodity, then taking its purchase beyond any reasonable projection of need. I saw an industry straining and grunting to keep up with demand, and watched as the final collapse of the bubble brought misery even to those not directly involved.

Green Bay sits at the north end of the Fox River Valley, a major paper-producing area. The mills along the Fox River generally serve the segment known as "sanitary tissue products," that is, paper towels, toilet tissue, napkins and so on. Many of these mills were old, economically marginal, and still family-controlled businesses. The big dogs were P&G's Charmin Paper and Kimberly Clark.

By the mid 1970's, the environmental legislation of the late 1960's was finally getting to the stage of published regulatory requirements. Complying with the regulations to clean up the air and water necessitated substantial capital investments. Capital was in short supply and interest rates were high. Thus the paper mills along the Fox River did what any economically marginal, capital starved, family owned business would do when faced with expensive regulations - they complained to their Congressman. The Congressman in this case was a recently elected Republican. He did what any newly elected Congressman would do when faced with a group of constituents complaining about regulatory overreach - he issued a press release. The media did what they do when presented with a Congressional press release - they completely ignored it.

Now so far, the entire system was working as it is supposed to. Unfortunately, one media outlet did not ignore it. The writing staff for Johnny Carson knew a gift when they saw it. The next week his monologue included Johnny's trademark deadpan lead-in announcing that "a Congressman from Wisconsin is now predicting the next big shortage will be toilet paper- that's right folks, toilet paper." This lead was followed by several further humorous swipes at the topic, predictable, in questionable taste, but serving to draw his viewers' attention to impending disaster.

This seed fell on very well-fertilized ground. Today, with high unemployment, rampant over-capacity and new patterns of international trade, most people would greet this news with a yawn and assume that China would simply add toilet tissue to its next shipment to Wal-Mart. But, just as Bill began his discussion with Nixon's imposition of wage and price controls, I will also begin there. When Nixon imposed wage and price controls in 1971, they did what every instance of wage and price controls has done throughout human history. Their only contribution was to introduce shortages and distortions into the economy. News reports had mentioned spot shortages of various commodities with regularity. We had likewise experienced shortages of some key construction and maintenance materials in the paper mill. Then came the big shock. The Arab Oil Embargo of 1973-74 led to a very sharp run-up in gas prices and shortages at the pump. I should point out here that the federal government's oil allocation program produced further distortions, but that is another whole paper. In any case, the American public was well primed to believe in a shortage of anything.

The US economy is resilient and American consumers are enterprising. Throughout the wage and price controls sharp-penciled accountants had developed justification for price increases, purchasing agents found new supplies, and harried expeditors somehow kept things moving. But this wasn't gasoline - this shortage would strike at the very seat of human existence. Advances in technology kept us from regressing to older, simpler solutions. The supply of corn cobs was very limited in most urban areas and Sears Roebuck catalogues were no longer a staple of the average home. Reminding people to use both sides might help with a shortage of printer paper, but does not provide a useful approach in the toilet tissue category. This left only one option - buy up as much toilet paper as possible before the hoarders got to it. And buy up they did.

Like all good Proctoids, we understood the quantitative details of our business. We knew to two decimal places what percent of consumers are "folders" versus "wadders." We knew how many more sheets per day a woman uses than a man. In the interests of retaining a measure of decorum in these august chambers, I will spare you the actual calculations we used to link human physiology and consumer bathroom habits to our sales volumes. Suffice it to say that even a cursory look at the human physiology will indicate that the ultimate final use of the product is remarkably steady. It is also not particularly sensitive to economics. Wage gains or financial windfalls are unlikely to make someone suddenly decide to increase their use of toilet paper as conspicuous consumption to impress neighbors. It has little seasonality - Wednesdays are remarkably like Saturdays in this category.

In the week following the memorable monologue, many shoppers decided to toss an extra four pack of TP into the grocery cart just in case. The more fearful or prudent tossed in two. The truly aggressive tossed in even more, confident that in any case the prices would be going up and they would save money on the increases by buying now. By the end of the week, the shelves sat gaping in their emptiness where the toilet paper used to sit.

Store managers reacted by putting in urgent orders to the grocer's warehouse. Their order covered the usual week's supply, the extra cases needed to restock their now empty shelves, and some more for good measure. After all, they had an interest in making sure the shortage of toilet paper did not drive consumers down the street to a competitor that still had some available. They were concerned that their toilet paper consumers would soon be chaffing at the inconvenience of it all.

Few warehouses had an inventory adequate to cover this doubling or tripling of normal orders by all the stores they served. Thus, they shipped the stores only what they could. Once the order hit the stores, the packages of toilet paper immediately went home with consumers. The next round of urgent store orders to warehouses went largely unfilled. Diligent store managers posted signs on the toilet paper shelves apologizing to consumers for their inconvenience and helpfully pointing out that they were unable to get adequate supplies. Johnnie Carson was right - a major toilet paper shortage was already upon us!

Back at the paper mill where we actually made the stuff, orders arrived in a deluge. The grocery buyers not only had to restock their inventory, they wanted to make sure they got theirs by adding some extra to the order in case the manufacturers cut the order. These urgent shipments soon depleted our warehouse. We had orders in hand but our inventory was wiped out. Sure enough, in order to be fair to all customers our sales force put customers on allocation, cutting their orders proportionately to ensure all customers at least got some.

Meanwhile, we went to overtime trying to produce enough. Since we were already a three shift operation, all we could do was to make everyone work extra shifts on Saturday. Thus we took production up twenty percent despite our utter certainty that final consumption had not gone up in the slightest. We couldn't take the chance that our competitors would have more available and grab our hard won market share. The bubble had inflated.

This crisis now extended to national security. P&G has long had a thriving business in military sales. These sales were sent to commissaries and post exchanges, where national brands were sold to military families. Military families wanted the same choice of products as consumers everywhere. For those troops living in the barracks, a poor industrial grade of toilet paper sufficed. Now, we got an urgent call from the Pentagon seeking to buy Charmin for the barracks.

The veterans among us can attest that the barracks TP and old newsprint are roughly equivalent in softness, with a accent on the rough, but even the industrial grade tissue was unavailable. We agreed to ship forty or fifty railcars of Charmin. We were dealing with the federal government, so insanity soon ensued. The Pentagon reminded us that we had to use Military Specs to ensure we were shipping a quality product. This meant we were to load and seal the boxcars and park them on a rail siding. Then, using government tables, we would randomly select railcars from among those parked, randomly select a case in each, then open and unload the car to find the specified case, take it back into the plant and check for "quality." This demand beggared belief. We pointed out that Charmin was the number one brand as chosen by consumers, that there was really no comparison between Charmin and what passed for tissue in the barracks, and that in any case we were short of product, not orders. The Army surrendered and agreed to accept Charmin as we made it. We did our patriotic duty and shipped the fifty boxcars of Charmin to our desperate troops. When Napoleon said an army travels on its stomach he only understood half the equation!

Let's remember, however, what was happening in the average American home. Rolls of toilet paper had already overflowed their customary storage below the sink. Hall closets were bulging with rolls.

Basements and garages contained the strategic reserves. At some point buying slowed down. Inventories in the supply chain gradually rebuilt. Consumers saw store shelves once again held this scarce and vital commodity. The bubble had burst.

What happened next was entirely predictable. Consumers just stopped buying. They owned months and months of supply in their own homes. The stores, finding minimal sales, slammed the brakes on orders to their warehouses. The warehouses started cancelling orders to the manufacturers. The bust had arrived in toilet tissue.

Not only did we no longer run production on Saturdays, we went from three shifts to two shifts of Charmin production. The warehouse needed fewer people to load the non-existent orders. We soon reached the limit of our ability to carry the extra workers until things returned to normal. Over one hundred employees were laid off. Under the union contract the most junior employees were first out the door, even though the specific jobs they held had nothing to do with making toilet paper. The pain of the burst bubble set in.

My small homely example pales when compared to the world's recent financial boom, bubble and bust in the scale of the effects and of the subsequent economic suffering and dislocation. But aren't the dynamics precisely the same, whether it is toilet paper or Florida condos or collateralized debt obligations? Wasn't this a case of "irrational exuberance" to borrow a phrase from Alan Greenspan? Didn't consumers reassure themselves with the logic that the world will always need toilet paper, just as we heard the mantra that the world will always need housing? The CEO of P&G never said "as long as the music is playing, we have to keep dancing," as the CEO of Citibank said in 2008, but he could have.

Geoffrey Vickers, the former chairman of Rolls Royce Engines once observed, "to describe a trap is to describe the nature of the trapped." The trap that is booms, bubbles, and busts does describe the nature of the trapped - and it is our human nature.

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