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P. Dean Russell

JOBS— and How *Not* to Increase Them

WHEN jobs are plentiful, all other domestic problems of a nation can be solved. But when jobs are scarce, other problems automatically become worse—especially social problems.

The individual who cannot find a job will eventually become either hopeless or desperate. If hopeless, he degenerates into a permanent liability on society. If desperate, he is a likely prospect for revolution. These two possibilities are equally destructive of the person and his society. Thus, from every viewpoint—social, economic, moral, or whatever—it is vital that we understand what causes unemployment. For only then can we work effectively toward solving this most pressing of all social problems—jobs for all who want to work.

As normal human beings, naturally we are distressed by the suffering that comes to the families of persons without jobs. But fortunately for the unemployed, our interest in the matter goes beyond mere pity. There is a far more vital reason why we want everybody in the United States to have a job. It is a selfish reason that directly concerns our *own* families. It is this. When they have jobs they can buy more from us and our jobs are thereby made more secure and better paying. That's a powerful incentive and a primary reason why we should support any policy, and participate in any program, that will provide more permanent jobs at higher real wages.

When all is said and done, there is finally only one reason why any

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person in the United States who wants to work can't get a job: His potential employers believe that the cost of hiring him is more than the anticipated income from his production or service; for no one—neither you nor I nor any employer—will knowingly hire workers at a loss.

An obvious way to test the validity of that statement is to assume that it's false, and then to examine the consequences. So let us assume that there are unemployed persons who want to work, and that the product of their labor will sell for more than the cost of employing them, and that the potential employers know this, and that they just deliberately and knowingly refuse to add to their profits by hiring these men.

Such an assumption just doesn't make any sense; for no businessman really prefers lower profits to higher profits. Businessmen have been accused of many things, but never that! The reason we can know with certainty that no businessman acts this way is because you and I don't act this way. You and I would like to have more money for many reasons; the desire for a Caribbean cruise is included, as well as our wish to feed little children who are starving to death all around the world today. For in a "money economy" such as ours, the only thing that will keep them alive is *money*. That's why you and I will *always* choose more money over less money, if that is the only issue involved. And that's why businessmen will never choose smaller profits over larger profits in the long run. For businessmen are people too—as are stockholders and employees—and we all have a use for more money.

A Universal Principle

This universal principle of human motivation and action applies to everyone, regardless of the use to which the additional money may be put. Obviously, we never hire a person voluntarily if we believe that the cost of employing that person will exceed the income from that person's production or service. Stated positively, we will always hire a person when we believe that we can thereby increase profits.

When you get right down to it, this same universal motivation of self-interest is what causes the unemployed person to search for a job in the first place. He, too, has a long list of desires that require money for fulfillment; and the fact that food and housing and medicine come ahead of his desire to donate to charity does not in any way deny this universal principle of human action.

Now before we try to use this particular theory as an aid in solving the problem of unemployment, we first need to understand another (and closely related) principle that is also based on universal human action.

The textbooks in economics usually list it under the heading of "marginal analysis"—in its various forms of cost, price, production, and so on. The explanations in those textbooks, however, sometimes become unduly involved with "tables and charts," and the authors tend to forget that what we are talking about is not mathematics but human beings and why and how we exchange our goods and services.

All of us understand, of course, that no two persons are ever equal in all things, including their desires and abilities to work. We know in advance that when we measure the production of a group of persons, some will have produced more than others—unless, of course, it is forbidden by some law or regulation. Over a significant period of time, there is always one person who produces *less* than anyone else in the group; he is called the marginal producer or worker. That means simply that he's the one whose production results in the least profit. Presuming that he's paid the same hourly rate as his fellow-workers, the cost of hiring him will (under certain conditions) sometimes exceed the income from the sale of his product. Naturally this "marginal employee" is the one we let go first when someone has to be laid off. Obviously we don't lay off the best workers first, not if we have any real choice in the matter.

The Marginal Unit

While we observe and practice this procedure all the time, we often forget just why we act this way. It's because we prefer profits to losses, higher profits to lower profits, and higher wages and salaries to lower wages and salaries.

That's why no employee keeps his job if he continually produces less than he is paid—other things being equal, of course, and presuming that his pay-production ratio is the only issue involved. The jobs of these marginal workers are always in danger. Any increase in costs of employment (without an offsetting increase in production and income) will *always* cause a decrease in jobs in any situation where pay is based on production.

This cannot be otherwise; for since we human beings are not equal, there is always a worker "at the margin" where profit shades into loss. And even a minor increase in costs can push him across the line. And when he loses his job, there is always another "marginal worker" right behind him. For the purpose of illustrating how this works, assume that the "cost of employment" for a given worker is $4 per hour, and "sale of his hourly product" is $4.10. As long as this relationship continues to exist, that job is reasonably secure; for no company wants to decrease its income, not even by ten cents an hour.

Now increase payroll taxes—Social Security, for example—by four per cent, thus raising "cost of employment" above "income from sale of product." Presuming that production and sales remain the same—and presuming no increase in the price of the product—that man loses his job. This must automatically follow; for a company will soon go bankrupt if its policy is to hire men who cost more than they produce. Such a policy would accomplish nothing except to throw all of that company's employees into the ranks of the unemployed persons we wish to help. You might think that such a simple truism is understood by everyone; but as we shall soon see, it isn't.

There are a score and more other ways that this same loss of jobs can be achieved—wage increase with no increase in production, decreased production at the same wage, a decrease in price with no increase in sales, and so on. Always the marginal worker (including, of course, the marginal worker on the management level) loses his job when cost of employment increases relative to income from production. Nor does it make any difference whose fault it is—government, union, or management; the job still disappears. And, of course, there are "marginal departments" and "marginal companies" in exactly the same sense that there are marginal workers; the only difference is that *groups* of persons lose their jobs when costs of a department or company exceed income from the production of that department or company. That's what "red ink" means—cost has exceeded income; there are no profits, but only bankruptcies, loss of capital, and unemployment.

Creating More Jobs

With this background on how and why you and I act the way we do—and why managers of successful companies act exactly the same way—perhaps we are in a better position to study some of the measures now being proposed to increase jobs in industry. Among them are the shorter work week at the same (or more) pay, double time for overtime, increased minimum wages, longer paid vacations, earlier retirement with higher pensions, increased social security coverage, and a host of others. The argument in support of these measures is that they will force employers to hire additional men, or that the measures will increase incomes and spending and thus (indirectly) will increase jobs, or both of these hoped-for results at the same time.

Clearly, each of these proposals has an effect on costs of production. Thus, necessarily, each has an effect on jobs. Since the minimum wage is perhaps the most popular (and certainly the least understood) of these measures, let's here use it as representative of all of them. Just what is the relationship between jobs and minimum wages?

Apparently the advocates of minimum wage laws are unfamiliar with marginal analysis and the fact that every human being has a long list of unsatisfied wants. Even though the advocates of minimum wages will never knowingly spend two dollars to get back one dollar, they fail to understand that all businessmen are bound by this same principle of universal human action. For example, the overwhelming majority of the advocates of a minimum hourly wage of $3.35 for restaurant and laundry workers will *not* pay 30 per cent more than they now pay for a meal in a restaurant or for the work done by commercial laundries. Like you and me, they never spend their money for something they value *less* when they are free to spend it for what they value more. Thus because they need their money for more pressing desires (a new spring outfit, for example), they will eat at home and patronize the local laundromat—while continuing to advocate compulsory wage levels above those that have been determined by their own voluntary spending practices.

They don't understand that every businessman who lays off a worker because of an increase in costs is acting just as they do when they eat at home because restaurant meals have increased in price but not in quality or quantity. The principle is not merely related, it is identical. Any person who has ever refused to make a purchase "because it cost too much" was following this universal principle of human motivation and action.

Consumer Preferences

Sometimes the advocates of increased minimum wages argue that if *all* restaurants and laundries were compelled to pay the same wages, then no employee would lose his job. The reasoning here is that since costs would rise equally for all, no restaurant or laundry would be put at a competitive disadvantage. Since sales and income would remain about as before—with the weakest (or marginal) firm retaining its former relative position—there would be no reason for laying off any workers.

That argument only demonstrates again the absence of any understanding of how and why people (including themselves) act as they do when they exchange their goods and services. For when people are free to choose, *any* increase in costs—for *any* reason—will cause a decrease in sales and thus in jobs. The fact that costs and prices may have increased for everyone in the restaurant business is beside the point. You and I react to price increases by buying less or going without or using a substitute. Since at any given time, our incomes are allocated in a certain spending pattern, a hefty increase in laundry and restaurant prices will necessarily cause a re-allocation of our customary spending. This cannot be avoided. Since you and I value "music lessons for our children" more than we value that customary restaurant meal—and since we must now choose between them—we choose to eat out less often; and another restaurant worker "at the margin" thereby loses his job.

There is nothing that any government or law (or for that matter, union) can do to change how and why we human beings choose first to spend our money on what we value most. True enough, governments can (and often do) initiate measures that cause the appearance of more money in the economy than is called for by the annual increase in production of goods and services. This procedure tends to conceal or suppress for a while the customary marginal effects of increasing costs and prices; for a ten per cent increase in prices doesn't greatly affect your spending pattern if you get a ten per cent increase in income at the same time. But since this procedure is in no sense a solution, the problem itself continues to be with us. In due course, this process of increasing the money supply usually begins to operate on a sort of speeded-up "treadmill principle"; like Alice of "Looking Glass" fame, we must then begin to run twice as fast merely to stand still. If "more money" could really solve our problems, obviously our government would have solved them long ago. Let us remember that in spite of a steady increase in money over the past half century, large-scale unemployment has continued to be our most pressing social problem in peacetime.

Please the Customer

When all is said and done, there is only one way the unemployed person can get a lasting job in an economy where we consumers are free to buy or not to buy. Obviously, he must offer a product or service at a price that someone else is willing to pay. The "asking price" for a product must be in harmony with the "market price" if the product is to sell; just so must the unemployed person reduce the "asking price" for his labor to a point where the income from his production will exceed the cost of hiring him—if he wants to be hired. When that happens, every potential employer will be pleased indeed to bid for his services because the employer himself thereby expects to have more money to spend for the goods and services *he* wants to buy; a self-interest factor is added.

If the "market price" (that is, what you and I and others will voluntarily pay) for labor is below the minimum wage that is set by law, the unemployed worker necessarily remains unemployed. For neither you nor I nor any potential employer will knowingly hire him at a loss; no human being spends $3 to get back $2. An unknown number of workers without jobs today are unemployed because the minimum wage is above their productive capabilities as determined by the actions of consumers who are free to buy or not buy the product or service. That's too bad for the unemployed, but there is absolutely nothing that potential employers can do about it; clearly, the responsibility lies with Congress which made the law.

Now it is true that employees in high productivity companies don't need to worry about minimum wage laws directly. Every such employee is paid more than the current or proposed minimum; he's paid more because he produces more, and because the price that consumers are willing to pay for the product of his labor is more than the cost of his labor. That's why wages in such companies are so high. Thus an increase in minimum wages doesn't affect those employees directly.

An Indirect Effect

Indirectly, however, there is an effect—a most undesirable effect. When marginal workers in other industries lose their jobs because of uneconomic wage increases, they can no longer consume as much as before. And when sales of high productivity company products fall off, the marginal producers in those companies also lose their jobs—or take a substantial cut in pay. This *must* happen because the product of their labor no longer sells at the price or volume needed to cover the cost of hiring them. It is too often forgotten that there are marginal workers *at every level of pay*.

Thus it is that minimum wage laws always cause a reduction in jobs below what they would or could be if there were no such laws. Based on how and why you and I act, the result cannot be otherwise. For you and I (and others) simply will not pay the higher prices for certain products and services that have been caused by increases in minimum wages. We would rather spend our money for something else that we value more highly. Exhortations and wishful thinking won't make any difference. We won't—in fact, we *can't*—continue to buy the product; for the increased prices compel us to re-allocate the spending of our money, which has not been increased by the minimum wage laws. It so happens that those products at higher prices turn out to be the marginal products—the ones we give up first or decrease the use of.

Every employer acts exactly the same way you and I act, and for exactly the same reason. He won't continue to pay $3.35 for a product or service (wages for an hour) when he discovers that he can sell the product of the labor for only $3.00. He won't do it because his company would suffer decreased profits, and perhaps losses. That, in turn, would decrease his own earnings, perhaps drastically. Then he would have to give up some product or service that *he* wants—and that he values far more highly than he values hiring a worker at a loss! Thus the employer lays off the unfortunate marginal worker who has been "assisted" toward a higher level of living by law. There really isn't anything else he can do. And to call him nasty names is about as logical as cursing yourself because you refuse to buy a $15 item when you have only $10 to spend.

The Difference Between Coercive and Voluntary Measures

Legal measures to increase wages and jobs simply do not do so—not in the long run and when all the effects are understood. Such measures can't bring the desired results because they do nothing to increase productivity or sales or profits. In a society where people are free to spend their own earnings, there is only one possible way to increase wages and jobs permanently: Make it profitable for one person to hire another person. Then—and only then—will there be an increase in real and lasting jobs. We can be certain that the employers will then hire more workers because they can thereby earn more money to be used to buy the things they want, including better education for their children, donations to the Salvation Army, trips around the world, or whatever it is they value most. We cannot know what the employers will use the money for. We can know only that their motivation is identical to the motivation that causes you and me to act. When we refuse to buy the product they manufacture, they, in turn, *must* refuse to buy the products that go to make it up—including, for the most part, human labor. But when we buy their goods and services at a price that is profitable to them, they then automatically buy more of the "raw materials" that go to make up the product or service, including, for the most part, human labor. To understand how you act is to understand how the employer acts. The motivation is identical.

And all along the way, each employer acts exactly as you and I act when we decide to buy or not to buy a given product. If we are getting more than we are giving up for it (in our opinion), we will buy; otherwise we won't buy. Whether the product is labor or the result of labor has no bearing. Whether the purchaser is an employee, employer, or consumer makes no difference; basically we all act alike when we voluntarily exchange our goods and services. While our tastes and value scales differ radically, no person ever gives up something he values more for something he values less—not when *all* the factors are considered.

Freedom to Choose

Always and everywhere this relationships exists. This is as true in Russia as it is in the United States. The Russians, too, are people—and thus they will not willingly and knowingly spend two rubles to get back one. To the greatest possible extent, they will always arrange it the other way around. True enough, the Russians have less freedom of choice than we have. But to the extent that each is free to choose, each will always do his buying and hiring on this principle of universal human action. This applies to the Communist manager of a cement factory (with his positive production quota and his potential bonus) as well as to the non-Communist peasant who uses his little "privately assigned" plot of ground to grow beets and cucumbers to sell to the highest bidder.

Again, all of us have a real and selfish reason for wanting everybody in the United States to have a job; our own jobs thereby tend to become more secure and better paying. That's why we are anxious to find and support those policies that will provide more permanent jobs at higher real wages. And that's why we must ask this question about any program or policy that promises more jobs or higher pay. Do these programs and policies increase costs without an identifiable increase in productivity and profits? If so, we know that jobs will be lost. We know this because no human being will spend his money for something he values *less* (continuing to pay a worker to produce at a loss, for example) when he is free to spend it for something he values more. Any law or policy that increases costs ahead of income cannot be of value in solving problems of unemployment.

John Stuart Mill

IDEAS ON LIBERTY

WHAT a country wants to make it richer is never consumption, but production. Where there is the latter, we may be sure that there is no want of the former. To produce, implies that the producer desires to consume; why else should he give himself useless labor? He may not wish to consume what he himself produces, but his motive for producing and selling is the desire to buy. Therefore, if the producers generally produce and sell more and more, they certainly also buy more and more.

Gary North

THE MORAL ISSUE OF "HONEST MONEY"

BECAUSE of the nature of the economics profession—"guild" might be a better word—it is necessary to put quotation marks around the words, "honest money." Economists will go to almost any lengths to avoid the use of moral terms when they discuss economic issues. This has been true since the seventeenth century, when early mercantilistic pamphlet writers tried to avoid religious controversy by creating the illusion of moral and religious neutrality in their writings. This, they falsely imagined, would produce universal agreement, or at least more readily debatable disagreements, since "scientific" arguments are open to rational investigation. The history of both modern science and modern economics since the seventeenth century has demonstrated how thoroughly unreconcilable the scientists are, morality or no morality.

Nevertheless, traditions die hard. Economists are not supposed to inject questions of morality into their analyses. Economics is still supposedly a "positive" science, one concerned strictly with questions of "if . . . then." *If* the government does A, *then* B is likely to result. *If* the government wants to achieve D, *then* it should adopt policy E. The economist is completely neutral, of course. He is just an observer who deals with means of achieving ends. The economist can therefore deal with "complete neutrality," with this sort of problem: "If the Nazis wish to exterminate 50,000 people, which are

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the most cost-effective means?" No morality, you understand, just simple economic analysis.

The problem with the theory of neutral economics is that people are not neutral, effects of government policies are not neutral, social systems are not neutral, legal systems are not neutral, and when pressed, even economists are not neutral. Because societies are not neutral, the costs of violating a society's first principles have to be taken into account. But no economist can do any more than guess about such costs. There is no known way to assess the true costs to society of having its political leaders defy fundamental moral principles and adopt any given policy. And if the economists guess wrong—not an unlikely prospect, given the hypothetical moral vacuum in which economists officially operate—then the whole society will pay. (This assumes, of course, that policy-makers listen to economists.)

The inability of economists to make accurate cost-benefit analyses of any and all policy matters is a kind of skeleton in the profession's closet. The problem was debated back in the late 1930s, and a few economists still admit that it is a real theoretical problem, but very few think about it. The fact of the matter is simple: *there is no measuring device for balancing total individual utility vs. total disutility for society as a whole.* You cannot, as a scientist, make interpersonal comparisons of subjective utility. The better economists know this, but they prefer not to think about it. They want to give advice, but as scientists they cannot say what policy is better for society as a whole.[1]

This is why politicians and policy-makers have to rely on *intuition,* just as the economists do. There is no scientific standard to tell them whether or not a particular policy should be imposed. Without a concept of morality—that some policy is morally superior to another—the economists' "if . . . then" game will not answer the questions that need to be answered. *Without moral guidelines, there is little hope of guessing correctly concerning the true costs and benefits to society as a whole of any policy.* The economist, as a scientist, is in no better position to make such estimations than anyone else. If anything, he is in a worse position, since his academic training has conditioned him to avoid mixing moral issues and economic analysis. He is not used to dealing with such questions.

What Is Honest Money?

Honest money is a social institution that arises from honest dealings among acting individuals. Money is probably best defined as *the most marketable commodity.* I accept a dollar in exchange for goods or services that I supply only because I have reason to suspect that someone else will do the same for me later on. If I begin to suspect that others will refuse to take my dollar in exchange for their goods and services in the future, I will be less willing to take that dollar today. I may ask the buyer to pay me a dollar and a quarter, just to compensate me for my risk in holding that dollar over time.

A currency unit functions as money—a medium of *voluntary* exchange—only because people expect it to do so in the *future*. One reason why they expect a particular currency unit to be acceptable in the future is that it has been acceptable in the past. A monetary unit has to have *historic* value in most instances, if it is to function as money. Occasionally, meaning very rarely, a government can impose a new currency unit on its citizens, and sometimes this works. One good example is the introduction of the new German mark in November of 1923, which was exchanged for the old mark at a trillion to one. But normally the costs are so high in having people rethink and relearn a new currency unit that governments avoid such an imposition.

Historic Stability

The question policy-makers must ask themselves is this: To avoid the necessity of imposing a totally new currency unit on a population, what can be done to convince people that the future usefulness of the currency in voluntary exchange will remain high? What can be done to improve the historic value of money in the future? In other words, when people in a year or a decade look back at the performance of their nation's currency unit, will they say to themselves: "This dollar that I'm holding today buys pretty much what it bought back then. I think it's safe for me to continue to accept dollars in exchange for my goods and services, since people trust its buying power. I have no reason to believe that its purchasing power will fall in the future, so I can take the risk of accepting payment in dollars today." If people do not say this to themselves, then the dollar's purchasing power is undermined. People will demand more dollars in payment, meaning prices will go up, if they *suspect* that prices will go up. This, in turn, convinces more people that the historic value of their money has been unreliable, which then leads to higher prices.

The economist will tell you that prices cannot continue to go up unless the government, working with the central bank, accommodates price inflation by expanding the currency base. The economist is correct in the long run, whatever the long run is these days, or will be in a few years. *But governments have a pernicious tendency to accommodate price in-*

flation. Dr. Arthur Burns was forthright about this back in 1976:

> These days the Federal Reserve is now and then described as pursuing a restrictive monetary policy. The Federal Reserve is described as being engaged in a struggle against inflation. The Federal Reserve is even charged with being more concerned about inflation than about unemployment, which is entirely false. It is by generating inflation, or permitting inflation, that we get unemployment on a massive scale eventually. But let us in the Federal Reserve ask this question: Are we accommodating inflation at the present time or not? The answer—the only honest, professional answer—is that, to a large degree, we are accommodating the inflation; in other words, are making it possible for inflation to continue.[2]

So we get a kind of self-fulfilling prophecy. The government expands the money supply in order to finance its deficits, or create a temporary economic boom, or whatever, and the prices for goods and services rise. Everyone in the "great American auction" has more dollars to use in the bidding process, so prices rise. Then the public gets suspicious about the future value of money, because they have seen the loss of purchasing power in the past. They demand higher prices. Then the Federal Reserve System is encouraged by politicians to accommodate the price inflation, in order to keep the boom going (to keep the "auction" lively). The dollar loses its *present* value, because it has lost its *historic* value, which encourages people to discount sharply its *future* value.

The secret of retaining the public's confidence in any currency unit is simple enough: *convince users of the money that the issuers are responsible, reliable, and trustworthy.* Government and its licensed agents have a monopoly of money creation. Private competitors are called counterfeiters. Sadly, in our day, it is very difficult to understand just what it is that counterfeiters do, economically speaking, that governments are not already doing. Fiat money is fiat money. (Perhaps the real legal issue ought to be the illegal use of the government's copyrighted material. *Copyright infringement* makes a much more logical case for Federal prosecution than counterfeiting.)

Who Guards the Guardians?

There is an ancient question that every society must answer: "Who guards the guardians?" Or in more contemporary usage, "Who referees the referees?" The public needs *an impersonal guardian* to restrain the actions of those who hold a legal monopoly of money creation: the government, the central bank, and the commercial banks. The public can guard the guardians if citizens have the right to go down to the local bank and receive payment in gold, silver, or some other money metal. The issuers of money need only stamp on the paper money (or check, or deposit book entry) that the holder of the currency unit has a legal right to redeem his *warehouse receipt* for a stated weight and fineness of a specific metal.[3] Whenever the issuing agencies begin to issue more receipts than they have reserves of metal, the public has the option of "calling the bluff" of the issuers, and demanding payment, as promised by law. It is this restraint—implicit economically, but explicit legally—which serves as the impersonal guardian of the public trust.

The government can always change the law. Governments do this all the time. Whenever there is a major war, for example, governments suspend specie payments. They also suspend civil liberties, and for the same reason: to increase the power of the state at the expense of the citizens. Governments in peacetime are frequently unwilling to reestablish pre-war taxes, pre-war civil liberties, and pre-war convertibility of currencies, long after the war is over. Civil libertarians have not generally understood *the case for a gold standard* as *a case for civil liberties,* despite the obvious historical correlation between wartime suspension of civil liberties and wartime suspension of specie payments.

When the authorities declare the convertibility of paper into specie metals "null and void," it sends the public a message. "Attention! This is your government speaking. We are no longer willing to subject ourselves to your continual interference in our governmental affairs. We no longer can tolerate illegitimate restrictions on our efforts to guard the public welfare, especially from the public. Therefore, we are suspending the following civil right: the public's legal right to call our bluff when we guarantee free convertibility of our currency. This should not be interpreted as an immoral act on the part of the government. Contracts are not moral issues. They are strictly pragmatic. However, we assure you, from the bottom of our collective heart, that we shall never expand the money supply, or allow the historic value of the currency to depreciate. It will be just as if we had a gold standard restraint on our printing presses. However, such restraints are unnecessary, and besides, they are altogether too restraining."

Redeemability Required

Critics of the gold standard tell us that the value of any currency is dependent on public confidence, not gold. But what the critics refuse to admit is that the existence of *the civil liberty of redeemable money* is an important psychological support of the public's confidence in money. Even when the public does not understand the gold standard's theoretical justification—an impersonal guard of the monopolistic guardians—citizens can exercise their judgment on a daily basis by either demanding payment in gold (or silver, or whatever) or not demanding payment. Like the free market itself, it works whether or not the bulk of the participants understand the theory. What they do understand is self-interest: if there is a profit to be made from buying gold at the official rate, and selling it into the free market (including foreign markets) at a higher price, then some people will enter the markets as middlemen, "buying low and selling high," until the government realizes that its bluff has been called, and it therefore is forced to reduce the expansion of the money supply.

What is the morality of a gold standard? Simple: it is *the morality of a legal contract.* A government's word is its bond. A government promises to restrain itself in the creation of money, in order to assure citizens that the monopoly of money-creation will not be abused by those holding the monopoly grant of power. The *gold standard* is very much like a *constitution:* an impersonal, reliable institution which has as its premier function the counterbalancing of potentially damaging monopolistic power.

"Flexible" Money

Flexible money is a euphemism for the government's ability to increase (but, historically speaking, rarely to decrease) the money supply. The degree of flexibility is determined by the political process, not by the direct response of those affected, namely, individual citizens who would otherwise have the right to demand payment in gold. Flexible money means monetary inflation. Very flexible money means a whole lot of monetary inflation. Monetary inflation means, within 24 months, price inflation.

Civil libertarians instantly recognize the danger of "flexible administrative law," or "flexible censorship," or "flexible enforcement of speed traps." Yet they have great difficulty in recognizing precisely the same kind of evil in "flexible monetary policy." The threat comes from the same institution, the civil government. It comes for the same reasons: the desire of the government to increase its arbitrary exercise of monopolistic power over the citizenry, and to limit public resistance.

The inflationary implications of "flexible monetary policy" can be seen in a revealing exchange between Arthur Burns and Henry Reuss:

DR. BURNS: Let me say this, if I may: the genius of monetary policy—its great virtue—is that it is flexible. With respect to the growth ranges that we project for the coming year, as I have tried to advise this committee from time to time—and as I keep reminding others, including members of my own Federal Reserve family—our goal at the Federal Reserve is not to make a particular projection come true; our goal is to adjust what we do with a view to achieving a good performance of the economy. If at some future time I should come to this committee and report a wide discrepancy between our projection and what actually happened in the sphere of money and credit, I would not be embarrassed in the slightest. On the contrary, I would feel that the Federal Reserve had done well and I would even anticipate a possible word of praise from this generous committee.

CHAIRMAN REUSS: You would get it, and the word of praise would be even louder and more deeply felt if you came up and said that due to the change in circumstances you were proving once again that you were not locked on automatic pilot and were willing to become more expansive if the circumstances warranted. Either way you would get praise beyond belief.[4]

Praise beyond belief! Who wants anything less? Just take the monetary system off "automatic pilot," and turn it over to those whose *short-run political goals* favor a return of the inflation-generated economic boom, once the boom has worn off because the printing presses are not *accelerating* the output of fiat money—fiat money being defined as former warehouse receipts for metal, in which even the pretense of a warehouse has been abandoned. *Gold is a tough-minded automatic pilot.*

Politically, there is a great deal of flexibility in monetary affairs. Few people even pretend to understand monetary affairs, and most of those who do really do not understand the logic of the gold standard. The logic is very simple, very clear, and universally despised: *It is cheaper to print money than it is to dig gold.*

Problems with Fiat Money

Fiat money is indeed more flexible than gold, especially in an upward direction. Fiat money allows the government to spend newly manufactured money into circulation. It allows those who gain early access to the newly created fiat money to go out and buy up scarce economic resources at *yesterday's prices*—prices based on supply and demand conditions that were being bid in terms of yesterday's money supply. But this leads to some important problems.

1. Yesterday's prices will climb upward to adjust for today's money supply.
2. People will begin to have doubts about the stability of tomorrow's prices.
3. Producers and sellers of resources may begin to discount the future purchasing power of today's dollar (that is, hike today's prices in anticipation).
4. The government or central bank will be severely tempted to "accommodate" rising prices by expanding the money supply.
5. And the beat goes on.

Paying for the Guards

It is quite true, as Milton Friedman has stated so graphically, that the gold standard is expensive.[5] We dig gold out of the ground in one location, only to bury it in the ground in another location. We cannot do this for free. Wouldn't it be more efficient, meaning less wasteful of scarce economic resources, Dr. Friedman asks, just to forget about digging up gold? Why not keep the government or the central bank from expanding the money supply? Then the same ends could be accomplished so much less wastefully. Save resources: trust politicians.

This is a very strange argument, coming as it does from a man who understands the efficiency of market processes, as compared to political and bureaucratic processes. The gold standard is the way that individual citizens, acting to increase their own personal advantage, can profit from any monetary inflation on the part of the monetary authorities. They can "buy low and sell high" simply by exchanging paper money for gold at the undervalued, official exchange rate, and hoarding gold in expectation of a higher price, or selling it into the free market at a higher price. Why is the price higher? Because individuals expect the government to go back on its promise, raise the official price of gold (that is, devalue the currency unit), or close the gold window altogether. Citizens can become future-predicting, risk-bearing, uncertainty-bearing speculators in a very restricted market, namely, *the market for government promises*. It allows those who are skeptical about the trustworthiness of government promises to take a profit-seeking position in the market. It allows those who trust the government to deposit money at 6 per cent or 10 per cent or whatever. Each side can speculate concerning the trustworthiness of government promises concerning redeemability of the currency, or more to the point, government promises concerning the future stability of the currency unit's purchasing power.

Let the Market Function

Defenders of the commodity futures markets—and this includes Dr. Friedman—argue that the existence of a market for future delivery and future payment of commodities smooths out market prices, since it opens the market to those who are willing to bear the uncertainties of predicting the future. Those who are successful predictors increase their profits, and therefore increase their strength in establishing market prices according to the true future conditions of supply and demand. Those who are less successful soon are forced out of the futures markets, thereby passing along capital to those who are more successful predictors. The public is served well by such markets, for obvious reasons. Prices adjust to future consumer demand more rapidly, since accurate future-predictors are being rewarded in these markets.

Then why not a market for future government promises? Why not a market which can test the government's willingness to deliver a stated quantity and fineness of gold or silver (but preferably gold, given international exchange)? The monopolists who control the money supply then are faced with a market which offers rewards to those who are willing and able to "call the monopolists' bluff" and demand gold for the government's warehouse receipts.

Why not just rely on the standard commodity contracts for gold in the commodity futures markets? Won't skeptics be able to take their profits this way? Why bring in the "spurious" issue of a convertible currency? The answer is simple enough: once society has given a monopoly to the government to create money, then the full redeemability of the currency unit is a direct, immediately felt restriction on government power. Of course the free market in commodities allows speculators to take advantage of monetary inflation, if their timing is correct. But this does not mean that the public at large will exercise effective action to force a political change in present monetary policy. There is no immediate self-interest involved in expending resources in what could prove to be a fruitless, expensive campaign to stop the inflation.

Fixing the Responsibility

In the commodities market, one investor wins, and one investor loses (unless the price stays the same, in which case only the broker wins). By establishing the gold standard—full redeemability of gold on public demand—the government forces the Treasury to risk becoming an immediate, measurable loser. It forces the Treasury's officials to come back to the politicians and announce, "Folks, we have lost the bet. The public has called our bluff. They have drained us of our gold. We can't go on much longer. We have to stop the inflation. We have to convince the public to start trusting the currency, meaning that they should start trusting our competence in securing them a currency with a future. We have to balance the budget. Stop inflating!"

An open commodities market in gold is desirable, of course. But it is no substitute for a gold standard, if the state has a monopoly of money creation (along with its licensed subcontractors, the banks). Unless there is full redeemability, the Treasury is not forced by law to "go long" on its promises whenever anyone else wants to "go short."

Without full redeemability, the Treasury, meaning the government, can keep on shorting its own promises, despite the response of organized commodities markets, until an expensive and successful political campaign can be launched to stabilize the money supply. As free market analysis tells us, these campaigns are expensive to launch because of such factors as information costs, costs of organizing pressure groups, and the lack of an immediate, short-run pay-off to "investors" who contribute money to such a program. Full redeemability allows market forces to work. Self-interested forecasters can speculate in the government promises market. The public never has to be told to vote, or send letters of protest, or do anything. The self-interested speculators—a small but well-capitalized elite—will do the "policing" job for the citizens free of charge.[6] (Well, almost: there are transaction costs.)

So when we are told that it is inefficient to dig gold out of the ground, only to deposit it in a vault, we are not being told the whole story. By tying the currency unit to that gold—which is wonderfully expensive to mine, as any *monetary brake* should be and must be—the body politic enlists a cadre of professional, self-interested speculators to serve as an *unpaid police force*. This police force polices the trustworthiness of government monetary promises. The public can relax, knowing that a hard core of greedy capitalists is at work for the public interest, monitoring Federal budgets, Federal Reserve policies, and similarly arcane topics. By forcing the Treasury to "go long" in its own *promises market*, the guardians are guarded by the best guards of all: future-predicting, self-interested speculators whose job it is *to embarrass those who do not honor contracts*—monetary contracts.

Conclusions

I suppose I could invest more time in presenting graphs, or faking some impressive-looking equations, or citing innumerable forgotten defenders of the gold standard. But I think I have reached the point of diminishing returns. The logic of the gold standard is really fairly simple: *Treasury monopolists, like all other monopolists, cannot be trusted to honor their promises.* Better put, they cannot be trusted *at zero cost*. The gold standard is one relatively inexpensive way to impose high costs on government monetary officials who do not honor their implicit contracts with the body politic to monitor and deliver a reliable currency unit that will have future value—a trustworthy money system.

There are *moral* issues involved: honoring contracts, preserving social stability, providing a trustworthy government. There are *civil liberties* issues involved: protecting citizens from unwarranted taxation through monetary inflation, protecting citizens from arbitrary (read: "flexible") monetary policies, and restricting the expansion of government power. There are *economic* issues involved: designing an institutional mechanism that will bring self-interest to bear on political-economic policies, to stabilize purchasing power, to increase the spread of information in the community, and to increase the political risks for money monopolists. No doubt, I could go on, but these arguments seem sufficient.

The real question is more fundamental: Do we trust governments *or* the high costs of mining precious metals? William McChesney Martin, Dr. Burns' predecessor as Chairman of the Federal Reserve Board, gave us the options back in 1968, in the midst of an international monetary crisis: "It's governments that you have to rely on. Basically, you can't rely on a metal for solvency."[7]

Those of us who cannot bring ourselves to trust the government with any monopoly over the control of money prefer to trust a metal. It may not be the best thing to trust, but it is certainly more reliable than governments.

Keeping Government Honest

The case for a gold standard is the case against arbitrary civil government. While politicians may well resent "automatic pilots" in the sphere of monetary policy, if we had a more automatic pilot, we would have less intensive "boom-bust" cycles. When the "automatic pilot" is subject to tinkering by politicians or Federal Reserve officials, then it is not automatic any longer.

The appeal of specie metals is not the lure of magical talismans, as some critics of gold seem to imply. Gold is not a barbarous relic. Gold is a metal which, over millennia, has become acceptable as a means of payment in a highly complex institutional arrangement: the monetary system. Gold is part of civilization's most important economic institution, the division - of - labor - based monetary system. Without this division of labor, which monetary calculation has made possible, most of the world's population would be dead within a year, and probably within a few weeks. The alternative to the free market social order is government tyranny, some military-based centralized allocation system. Any attempt by the state to alter men's voluntary decisions in the area of exchange, including their choice of exchange units, represents the true relic of barbarism, namely, the use of force to determine the outcome of men's decisions.

The gold standard offers men an alternative to the fiat money systems that have transferred massive monopolistic power to the civil government. The gold standard is not to be understood as a restraint on men's freedom, but just the opposite: a means of restraining that great enemy of freedom, the arbitrary state. A gold standard restores an element of *impersonal predictability* to voluntary exchange—impersonal in the limited sense of not being subject to the whims of any individual or group. This predictability helps to reduce the uncertainties of life, and therefore helps to reduce the costs of human action. It is not a zero-cost institution, but it has proven itself as an important means of reducing arbitrary government. It is an "automatic pilot" which the high-flying, loud-crashing political daredevils resent. That, it seems to me, is a vote in its favor.

—FOOTNOTES—

[1]For those who are curious about this great debate over the impossibility of making interpersonal comparisons of subjective utility, see the exchange that took place between Sir Roy Harrod and Lionel Robbins: Roy F. Harrod, "Scope and Methods of Economics," *The Economic Journal* (Sept., 1938) and Lionel Robbins, "Interpersonal Comparisons of Utility: A Comment," *The Economic Journal* (Dec., 1938). For some "new left" conclusions concerning the results of this debate, see Mark A. Lutz and Kenneth Lux, *The Challenge of Humanistic Economics* (Menlo Park, Calif.: Benjamin/Cummings, 1979), pp. 83–89. For my own observations on its implications, see Gary North, *The Dominion Covenant: Genesis* (Tyler, Texas: Institute for Christian Economics, 1982), ch. 4.

[2]*Federal Reserve Consultations on the Conduct of Monetary Policy,* Hearings Before the Committee on Banking, Currency and Housing, House of Representatives, 94th Congress, 2nd Session (July 27 and 28, 1976), pp. 26–27. Printed by the U.S. Government Printing Office, Washington, D.C.

[3]On money as a warehouse receipt, see Murray N. Rothbard, *Man, Economy and State* (New York: New York University Press, [1962] 1975), pp. 700–3.

[4]*Federal Reserve Consultations,* p. 13.

[5]Writes Prof. Friedman: "My conclusion is that an automatic commodity standard is neither a feasible nor a desirable solution to the problem of establishing monetary arrangements for a free society. It is not desirable because it would involve a large cost in the form of resources used to produce the monetary commodity." *Capitalism and Freedom* (Chicago: University of Chicago Press, 1962), p. 42.

[6]"By creating monitors with a vested interest in the maximization of a given set of values, property rights reduce the social cost of monitoring efficiency." Thomas Sowell, *Knowledge and Decisions* (New York: Basic Books, 1980), p. 125.

[7]William McChesney Martin, quoted in the *Los Angeles Times* (March 19, 1968), Pt. I, p. 12.

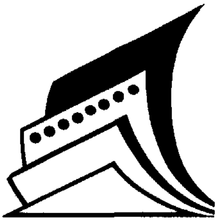
A Glut of Money

IDEAS ON LIBERTY

It can, I think, be laid down as a universal rule that all inflation is caused by the acts or politics of government, among which is any large increase in the debts of the central government. A large increase in government debt by borrowing at the banks creates a glut of money, which causes money to lose value.

SAMUEL B. PETTENGILL, "Inflation Is a Burglar"

Mark D. Isaacs



BUREAUCRACY, PRODUCTIVITY, AND INFLATION

WHAT IS WRONG with this country? American-made products, once the world standard for superior workmanship and quality, are now regarded as "cheap and inferior." Many American workers are grumbling and demanding more benefits, longer coffee breaks, and a voice in company affairs. Managers on the other hand often complain that today's workers are less competent, dependable, and motivated than 10 or 20 years ago. Poor job performance, chronic absenteeism and theft of company equipment plague many domestic firms. Workers are now paid more than ever before (the average wage for a nonagricultural industrial worker during October 1981 was a record $258.55 a week) and yet, American workers are still unhappy. Money no longer seems to motivate, and traditional managerial methods no longer seem to be effective. It seems, from the perspective of the business world, that things are really falling apart. On the surface it appears the Protestant work ethic, with its traditional virtues of hard work and thrift, does not apply to the "complex modern world."

In the past few years, an increasing amount of media attention has been focused on this latest domestic problem. Management experts, politicians, and other "opinion leaders" who professionally ponder and write about these momentous issues, have officially dubbed this the great "productivity crisis." One common characteristic of the "crisis" literature produced by these authors is that it usually manages to trace the source of the problem to some anti-social group or some strange mass metaphysical affliction. When they are not blaming society as a whole these thinkers often blame inferior private sector management. Some claim it is the fault of greedy labor unions, others say it is the "new values" of the baby-boom generation, and a few attribute the problem to a lack of knowledge of Japanese management techniques. The solution, say

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these writers, must be found; it is an issue of "national pride," and a problem that only a bigger federal government can solve.

Two Types of Management

This productivity problem that has recently received such wide media attention is not due to society, inferior private sector management, unions, "baby-boom" generation value shifts, or ignorance of Japanese culture. As interesting as these theories are, perhaps in their efforts to assign blame, these "crisis" experts have missed the main problem: the insurmountable problem of trying to manage, produce, and market goods in an economic environment polluted by the government's depreciating fiat currency. To understand the ramifications of this, and its link to the "productivity problem," we must examine two basic terms employed by Ludwig von Mises in his 1944 book, *Bureaucracy*. These terms are: profit management and bureaucratic management.

Ludwig von Mises described profit management as that form of management directed by the profit motive and measured by economic calculation. Economic calculation via the double-entry bookkeeping system is the device profit managers use to allocate scarce resources and to make rational business decisions. In an unhampered market economy, the objective of every manager is to direct production to achieve a profit and avoid a loss. Entrepreneurs hire managers (a specialized form of labor) for this expressed purpose. Economic calculation, measured in terms of money (the common medium of exchange) provides a standard unity of objective for the endless variety of private-sector firms found in a free economy. Employees of business ventures are clearly aware of this basically simple objective, i.e., "to make money." Accounting records are kept in these standard units of exchange. These records provide profit managers with detailed information as to which area, or departments of the firm are in need of labor or capital reallocation. In this way, errors, which will occur in any human system, will be corrected early in the production process and inefficiency is thereby minimized.

Furthermore, because economic calculation is so precise, outstanding managers, employees, and departments can be directly and individually rewarded for their superior performance and hard work. Economic calculation also enables managers to identify individuals that are not performing up to expectations. Once identified, these individuals can be specially motivated, replaced, or transferred, depending on managerial discretion. This emphasis on direct reward for individual performance is the special and unique attribute of the profit management system. Therefore, because merit alone is the measure of each individual, and because labor is a scarce resource, sexism, discrimination, nepotism, and other employment evils commonly found in economic systems where profit management is suppressed, become a costly luxury few firms could afford.

Unchecked Bureaucratic Management

Ludwig von Mises described bureaucratic management as that form of management that cannot be measured and checked by economic calculation. In the private sector, profit managers must generate all revenues in voluntary transactions with free-willed consumers. Management decisions are directly linked to profit and loss figures. A bad management decision will be reflected as a decline in revenues. This direct relationship between satisfying consumer needs and the generation of revenues keeps profit managers "in tune" with their customers.

In the public sector, however, this direct relationship between serving consumer needs and sources of revenue does not exist. Governments are political organizations of coercion. When governments need money, they do not offer goods and services to the public in return for voluntary contributions. Governments generate revenues by levying taxes on the private-productive sector. In other words, public-sector revenues are derived by involuntary means, and are not linked in any way to positive performance or servicing consumer needs. As a result, the achievements and blunders of bureaucratic management are independent of monetary incentive and disincentive. Bureaucratic management decisions are therefore not restricted by "petty" consumer demands. In the public sector, the whims of political action displace economic calculation.

Since bureaucratic managers do not have the benefit of economic calculation as do their fellow private sector managers, public administration can never hope to be as efficient as the private sector management. In fact, it is hopeless to expect the public sector to even approach private sector efficiency levels. To manage at all, public administrators are forced to employ inferior nonmonetary managerial methods. These methods are inferior for many reasons, but the most glaring is that the direct link between performance and revenue sources has been severed.

Performance of public employees can not be measured in precise monetary terms, so subjective yardsticks like peer review or political judgment must be used instead. These methods are inferior because subjective standards of measurement vary from manager to manager and from bureau to bureau. It is not surprising then to see how at times these non-monetary "standards" can clash and cause conflicts between various bureaus or departments.

In the public sector, because the concrete measuring mechanism of economic calculation is missing, inefficiency becomes chronic, and limited resources are wasted keeping tabs on various non-monetary standards. Red tape chokes the system, and corruption becomes rampant. Administrative costs grow unchecked, and errors go undetected and are compounded.

The Anarchy of Central Planning

Despite reams of historical evidence documenting the total impossibility of a successful non-monetary management method, the quest for the "ideal" non-monetary method continues unabated. Socialist and interventionist academics are experts at producing elaborate non-monetary schemes that attempt to manage and allocate resources. During the past 150 years, socialists of all parties have produced literally hundreds of various schemes that exclude economic calculation and replace it with a variety of more "humane" methods such as central planning by elite bureaucrats working in the "public interest." Indeed, this is the very cornerstone of socialist theory, to rid the world of despised money and the social evils it allegedly causes. The problem is, once money has been destroyed, nothing remains but the anarchy of central planning to fill the void.

So what does bureaucratic management, and profit management, have to do with the so-called productivity problem in America today? Everything! Consider this. In 1944 Ludwig von Mises wrote "Bureaucratic management is the only alternative available where there is no profit and loss management." The problem with productivity in America today is that the private sector has become bureaucratic. The private sector has become bureaucratic not because of some natural tendency of capitalism to form giant inefficient monopolies (as some interventionists have charged). Rather, the private sector has become bureaucratic in reaction to years of systematic governmental intervention. Government intervention of course takes many forms, but the form we are concerned with here is inflationism.

Profit management presupposes sound money. Sound money is the yardstick profit managers use to perform their economic calculations. Inflation (an increase in the quantity of money) alters this yardstick. Money no longer is a standard unit of value, but instead a flexible unit; controlled by political forces, it can rapidly depreciate over short periods of time.

Inflation alters the real profits and losses of a firm. Profits are overstated, which attracts greater amounts of capital, which is then malinvested by misinformed managers. Depreciation figures tend to be understated, and capital accumulation is retarded or eroded. The private sector's double-entry bookkeeping system is basically crippled. Accounting data become so blurred that rational economic calculation becomes merely a business school theory. Inflation then is more than just an attack on sound money, it is an attack on profit management itself. For without economic calculation, profit managers are no better off than their hapless public sector counterparts who are forced to blindly manage and measure the bureaucracy by non-monetary methods.

Real Earnings Decline

Let's restate the basic problem once again: (1) workers are unhappy, (2) money no longer seems to motivate, (3) job performance is poor, (4) absenteeism is chronic, and (5) younger employees seem to have abandoned traditional values. As we stated above, workers are paid more now than ever before. On the surface, it would appear that today's workers have adopted new values and goals. This record wage figure however, is in current or nominal dollar units. When inflation is factored out, and average wages are measured in constant or real dollar terms (in this case 1967 dollars), a very different picture emerges.

The Department of Labor, Bureau of Labor Statistics, reported that during November 1972, the real weekly earnings of an average private nonagricultural worker was $110.22. This figure reported for November 1972 is significant because this was and still is the record for this series. Since November 1972, the average nonagricultural worker has taken a cut in real wages virtually every month. By October 1981, the average nonagricultural worker in real dollars earned only $92.41 a week. Today's average worker then, earns $17.81 less in real dollars per week than he did during November 1972 for doing basically the same job!

This category is perhaps too general, because, of course, not every worker or employee fits into the "average." But, during this period, almost every profession or job class has been affected by similar cuts in real wage rates. *U.S. News and World Report* recently cited several specific occupations whose real wages have been cut by inflation. *U.S. News* reported the average salaried lawyer suffered a 4.4 per cent loss in earnings between 1971 and 1981, the average journeyman engineer earned 7.5 per cent less between 1971 and 1981 and a mid-level accountant lost 5.2 per cent in real earning power during the same period. The point here is that average real American wages in the private sector are less than they were ten years ago. This means most people in most occupations are worse off financially than in 1972.

How Workers Respond

Individual workers react in different ways to these cuts in real incomes. Some complain, or some stay home more; they figure "What's the sense in working when my money is worth less anyway." Some workers no longer care, so they do sloppy work on the job. When inflation destroys their real incomes, employees adjust to new compensation conditions over time. "Minimum work for minimum pay" replaces honest work for honest pay. Money no longer seems to motivate because many employees have realized they are no longer paid in real money.

When real wages decline, underpaid workers feel stuck, exploited and used by their employers. (This is beneficial to union organizers.) Morale suffers, and worker discontent further disrupts production. Values have not shifted, as some writers suggest; today's workers are rationally reacting to new market conditions just as their forefathers would have done. As in the past, today's workers are merely substituting a more satisfactory state of affairs (leisure) for a less satisfactory one (declining wages). This is basically the productivity problem from the labor point of view.

In an inflationary business environment, behavior of profit managers also changes. Because of the destruction of economic calculation by the government's inflationist policies the private sector is forced to employ non-monetary management methods in an effort to keep the wheels of production rolling. This is why Japanese management (Theory Z), management by objective, worker self-management, and other such non-monetary schemes are so popular in the private sector today. These methods are popular not because they are superior or more efficient, but because they are the *only* alternatives. When sound money has been destroyed, profit management and efficiency are destroyed along with it.

In closing, we should recall the words of Ludwig von Mises. In *Human Action* Mises wrote, "For more than a hundred years the substitution of socialist planning for private enterprise has been the main political issue." The issue here is not "productivity," but a continuation of this "planning" assault on the private sector, via depreciation of currency. Unless sound money and economic calculation are restored, "America's great productivity problem" can only further deteriorate. ⊕

Clarence B. Carson

Reasoning on the Nature of Things

SEVERAL YEARS AGO, a friend of mine suggested that there needed to be a renewed interest and emphasis on rights in the discourse on economic matters. It was all well and good, he said, to be told that it was not expedient to regulate this or that or the other, that confiscatory taxation produced undesirable social consequences, that redistribution of the wealth reduced incentives to work, that increasing the money supply resulted in the declining value of the money, and that government intervention in the economy produced assorted social ills. He did not question that such assessments were correct. But it was equally or more important, he thought, to get back to the basic concept of rights.

My friend was aware, of course, that there was hardly a shortage of talk about rights. Just about every sort of thing imaginable was, and is, being asserted and claimed as a right, ranging from the alleged right of women to abort unwanted pregnancies to the right of prisoners to a precise number of cubic feet of space. Every session of the Supreme Court seems to bring forth a new crop of rights, if in no other way than by its refusal to entertain appeals from decisions of lower courts which have elaborated some new set of rights. Even acts of Congress sometimes contain provisions which take on the color of rights.

He was not speaking of this new crop of rights, however, for he understood, I think, that however august the bodies which proclaim them they are but assertions of the will and power of men. These alleged rights have no more substantial backing in right than do Federal Reserve notes now have in silver and gold. They are fiat rights much

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in the same fashion as our money is fiat money.

Natural Rights

The rights my friend had in mind were of much more ancient vintage and claimed something much more substantial for their authority. They were rights said to subsist in the nature of things and to antedate governments, courts, and constitutions even. The economic rights he had in mind consist of such things as the right of man to the fruits of his labor, to exchange his goods freely with other owners, to have, to hold, and to dispose of his property, and to be secure in his possessions without arbitrary interference from any person or governmental authority.

The importance of his point has become much clearer to me in recent months. The election of Reagan to the presidency, the gaining of a Republican majority in the Senate, and the increase of conservatives in the House, have been interpreted as a major change in the thrust of government. Also, Reagan has been most vigorous in promoting his economic program during the first six months or so in his term of office. There has been considerable talk of economic freedom, of freeing enterprise, of removing government controls, and the like. But the justifications of these, so far as I am aware, have been made almost solely in utilitarian and pragmatic terms.

The justification for lowering taxes was not that people have a right to the fruits of their labors but that it could result in more saving, capital formation, more jobs, and increased production. In short, the emphasis is wholly on the social benefits to be obtained, not the vindication of the rights of individuals. Some of the weaknesses of this approach are already becoming apparent. It hinges everything on good economic results, which may or may not be forthcoming shortly. Moreover, it is readily interpreted in the framework of economic planning, though different from some that has preceded it. It makes it appear, too, that government is responsible for making the economy perform well, a conception that underlay the increasing government intervention over the years.

It is not my purpose, however, to make a critique of the Reagan programs. Rather, I call attention to them only to make clear that there is something missing from the justifications being offered. Nor is it merely something incidental to them; it is critical, even essential to their justification and direction. The gap in the thinking of the Reagan people, the omitted justification on the basis of rights, is not something peculiar to them, however. It is characteristic of our times. There is a gaping hole in modern thought.

Thinking in terms of the nature of

things, which is essential to the discovery and ascertainment of rights, while it occurs, is not in keeping with generally approved modes of thought. It is no less valid today than it ever was, but for many years now it has not been in keeping with intellectual fashion. It will be helpful, then, to examine how that came about and what was involved before giving some examples of how it works.

The Natural Law Philosophy

Reasoning on the nature of things was part and parcel of a complex of ideas which are sometimes referred to as the natural law philosophy. It needs, then, to be examined within that context.

The natural law philosophy was largely abandoned in the course of the nineteenth century. Its abandonment signified a major shift in thought. Natural law doctrines had been a staple of Western thought since the time of the Roman Stoics, and its antecedents go back even further than that. Interest in it was not constant, of course; it waxed and waned over the centuries. But every revival of learning and renaissance (harking back to and rediscovering aspects of Ancient thought) brought renewed interest in natural law, up to and including the classical revival of the seventeenth and eighteenth centuries. Indeed, Otto Gierke declared that "The development of natural-law ideas . . . attained its culmination at the end of the eighteenth century. After that time," he continued, "we can begin to trace a process of collapse and disintegration in the natural-law system of thought."[1]

I referred to it as a philosophy above, yet it was never quite that in an all-embracing sense. It did attain to the rank of a philosophy of law in ancient Rome, was revived as part of a more comprehensive scheme of law by Thomas Aquinas, and undergirded the development of modern law from the Renaissance down through the eighteenth century. Overall, though, it was more of a way of perceiving reality than a consciously elaborated philosophy. As such, it was an offshoot of metaphysics, from which it entered decisively into the development of science in the seventeenth century. Those who view it simply as a legal theory, or even more broadly, as a theory of society and the state, understate its claims and impact. In its varied applications it suffused thought in the eighteenth century, ranging from music and poetry to politics and science.

The impact of the natural law idea is suggested in this summary by a contemporary scholar: "It was a theory which culminated in the American Declaration of Independence in 1776 and the French Revolution in 1789. It was a theory adorned by many illustrious names—Hooker and Suarez; Althusius, Grotius and Pufendorf; Milton and Sidney; Hobbes, Locke and Rousseau; Spinoza and Leibnitz; Thomasius and Wolff . . . Vico and Beccaria; Fichte and Kant."[2] But if we examine the extended impact of the concept, many more famous names should be included in the roll: Newton, Galileo, and Franklin; Haydn, Mozart, and Vivaldi; Jefferson, Adams, and Paine; Blackstone; Hume, Smith, Turgot, and Ricardo; Pope, Addison and Steele.

Perhaps, the natural law theory can be best understood in terms of certain doctrines developed out of it. Underlying these doctrines was the belief that this is an orderly universe, that there is an underlying natural order that makes it so, that there is a law for man and a law for things, that everything has its own nature imbedded in it, that these things account for perceived regularities, and that there is a remarkable harmony pervading all of Creation. The following are some of the natural law doctrines: state of nature, the laws of nations, social contract, and natural rights.

Natural Law Doctrines

The key to the natural law doctrines is that they come into view when we focus our attention on the enduring features of reality. They are discovered by an act of the mind in stripping away all that changes, that is ephemeral, that is cultural, that is a result of history, that is peculiar to each individual thing. It is in this fashion that we discover the nature of things, the laws that govern or pertain to them, the way they are and can be. For example, if we would know the nature of man, we must remove everything that is accidental to any particular man (or woman) in any particular time or age: dress, language, size, girth, how hairy he is, color, and what have you. Then, we ask what the distinctive features of his kind are. What are the potentialities of his being? By such methods and with such questions we may come to a grasp of the nature of man.

Much was lost, as I say, by the abandonment of the natural law concept by so many thinkers in the nineteenth century. I do not mean to suggest, of course, that it has been entirely abandoned or that relics from it are not still around. The natural law theories have been kept alive by some Catholic scholars, particularly Thomists. Such thinkers as Joseph Wood Krutch, Leo Strauss, and Eric Voegelin have kept some of the basic concepts alive in our time. And, so long as the United States Constitution or classical economics, to take two examples, remain, something of the natural law-natural rights doctrines will remain.

But from the early nineteenth century onward there was a decided shift away from the mode of thinking that nurtured the natural law concepts. Romantics continued to admire nature, indeed, many of them venerated it, but they concentrated on nature in the concrete rather than the abstract. They emphasized the particular and the unique rather than the general, the abstract, and the universal. One of the offshoots of romanticism was historicism, a movement to locate reality within the uniqueness of particular historical events. G. W. F. Hegel provided the philosophical ballast for locating reality within historical development. The evolutionary theories of the nineteenth century had residues of natural law, but they were changed into laws of historical development, and natural law became driving force rather than underlying order. The outlook had shifted from a focus on the enduring to the placing of the whole attention on the changing. History had largely replaced philosophy.

The Utilitarians

The abandonment of the natural law doctrines was not simply a matter of a shift in outlook. Some thinkers repudiated, denounced, and denigrated the very idea of natural laws. The utilitarians were among the more outspoken of these. Jeremy Bentham said of those who believed in natural law that they "take for their subject the pretended *law of nature;* an obscure phantom, which in the imaginations of those who go in chase of it, points sometimes to *manners,* sometimes to laws; sometimes to what law *is,* and sometimes to what it ought to be."[3]

John Stuart Mill attacked the very notion of a benevolent and orderly nature (attacking nature and charging it with cruelties much in the manner that some attack or question God). He said, "Nature impales men, breaks them as if on the wheel, casts them to be devoured by wild beasts, burns them to death, crushes them with stones . . ., starves them with hunger, freezes them with cold, poisons them . . ., and has hundreds of other hideous deaths in reserve. . . ." Moreover, "Even the love of 'order' which is thought to be a following of the ways of Nature, is in fact a contradiction of them. All which people are accustomed to deprecate as 'disorder' and its consequences, is precisely a counterpart of Nature's ways. Anarchy and the Reign of Terror are overmatched in injustice, ruin, and death, by a hurricane and a pestilence. . . ."[4]

Mill was, of course, dealing with nature in the concrete, as many romantics did, but without their admiration of it. Bentham, too, was misconstruing the natural law theory, to some extent anyway. All this is the more strange because none were more devoted to the principles of economics than were the utilitarians, and they surely did not believe that these were of man's devising. My suspicion is that they both misconstrued natural law and found it a nuisance in some of their endeavors. In his efforts at legal reforms, Bentham encountered natural law exponents as an obstacle and simply repudiated the theory. Mill became a socialist, at the last, which was a logical culmination of his utilitarian premises unrestrained by a countervailing belief in a natural order which made socialism impossible.

This brings us to the crux of the matter. For socialism even to have a chance at being intellectually respectable, it was necessary for the belief in a natural order (and a revealed Divine order), in a metaphysical realm in which it subsists, and in natural law, to lose its sway. There must be a belief that men can devise a system unhindered by any underlying order. That is not to say that those who do not believe in natural law inevitably become socialists. It is rather to suggest that socialism arose in the wake of the decline in the belief in a natural order (of which natural laws were believed to be the most precise evidence) and that the removal of this formidable obstacle prepared the way for it.

The economic rights to which my friend referred were natural rights in origin. The concept of natural rights was one of the natural law doctrines, and with the fall of natural law went natural rights as well. Men continued to speak of rights, of course, but such support as they had now was only in positive law. That meant that they could be extended or withdrawn at the will of the rulers, and only expedient arguments could be raised for or against them. But before looking further at natural rights there is a related point that needs to be made.

Classical Economics

Classical economics was born out of the belief in an ordered universe and the prevailing natural law doctrines. That is another way of saying that the idea of economic freedom was first given theoretical formulation out of this complex of ideas. Adam Smith's *Wealth of Nations*, published in 1776, was the landmark publication for the development of classical economics. Smith maintained that the industrious individual in the pursuit of his own interest contributes to the well-being of others when he buys and sells goods in the market. He is bent to the pursuit of his own interest by nature, and his condition in this world is such that if he pursues it in a productive way he must contribute to the general stock of goods. In doing this, "he intends only his own gain, and he is in this, as in many other cases," Smith said, "led by an invisible hand to promote an end which was not part of his intention."[5] There is a natural order of things, so to speak, which makes it so.

It is not necessary for government to intervene to bring about these conditions of economy, and it would be presumptive and disruptive, Smith held, for it to do so. Instead, "All systems either of preference or of restraint, therefore, being thus completely taken away, the obvious and simple system of natural liberty establishes itself of its own accord. Every man, as long as he does not violate the laws of justice, is left perfectly free to pursue his own interest his own way, and to bring forth both his industry and capital into competition with those of any other man, or order of men."[6]

Smith arrived at these conclusions by keeping his attention focused on the nature of things: the self-interested nature of man, the nature of production, the nature of society, and the nature of the market. It is easy to be misled, however, by his statement that a "simple system of natural liberty establishes itself of its own accord." This assumes a government which is attending to its proper business, that the "law of justice" prevails, and that individuals and voluntary groups are protected in the enjoyment of their rights. In short, it assumes that individuals have rights, and, given the intellectual outlook of the time, they were understood as natural rights.

The problem can be stated in this way: Given the existence of government with its monopoly of the use of force, what is to keep it from interfering in the economic undertakings of individuals? And, in any case, what is the boundary between the business of government and the business of individuals and voluntary groups? That is where rights come in.

Like an Auto Without Brakes

Government unrestrained by the rights of people under its jurisdiction is like an automobile without brakes. It would be possible, of course, to build such an automobile, or even to remove the brakes from those already built. Such automobiles would work very well, too, in most respects. They would run as well as those with brakes, accelerate, go up hills, and they might even get lucky passengers to their destinations. But I would not want to bet on the safety of the passengers or of anyone else in their vicinity. Automobiles without brakes would be a constant threat to the lives and property of all who used them or those around whom they were being used. Pedestrians would be run down at crossings; horrible crashes at intersections would be the norm; and even houses and buildings would be in perpetual danger.

Governments without brakes supplied by the rights of their citizens are equally, or even more, dangerous. Property is at peril when government is unrestrained; trade is precarious; all sorts of interventions may hamper the production and distribution of goods. In a broader sense, the lives and liberties of all are in perpetual danger. That such behavior by government would not be in the best interest of the people may indeed be a valid argument, but those with power in their hands are not likely to want for long justifications of every sort of depredation. Minus individual rights and the conception of a natural order, the arguments of Smith and the classical economists can be stood on their head.

It is not necessary to imagine this reversal, of course; it has actually taken place. Adam Smith stressed the social benefits to be derived from economy. The title itself, *The Wealth of Nations,* suggests that this is the end of economy, though that was hardly the point of the work. Nonetheless, this notion of the purpose of economy was planted, indeed, had already been planted by the mercantilists, whom Smith devoted his major effort to refuting. Nineteenth century utilitarians added the concept of "the greatest good for the greatest number" as the touchstone for the justification of an economy. They repudiated natural law and with it all but remnants of a conception of a natural order.

Enter, the Historicists

The stage was set for the historicists who would conceive of any economy as simply a result of historical development. The idea of public benefit as the goal of economic activity remained, but with only particulars to guide it, it was easy enough to show that many people were not apparently benefiting much from a given economic system. Hence, the justification for government intervention, or even revolution. The social benefits are to be achieved, in this scheme, at whatever intrusion upon the rights of individuals may be necessary to achieve them.

Now, let us set Adam Smith upright once again. He did not say that the goal of social benefit was the cause of the wealth of peoples and of nations. On the contrary, he declared that he had "never known much good done by those who affected to trade for the public good."[7] Nor, I should add, are economic principles the cause of the wealth of peoples and of nations. If they were, governments might conceivably apply them so as to achieve these ends. The cause of the wealth of nations, Smith said, is the application of their industry and capital by individuals and groups to enrich themselves. The optimum conditions for these endeavors are firmly established individual rights. The natural rights doctrine provided a foundation for such establishment.

Natural rights are discovered, as I said, by focusing the attention on the nature of things. The traditional formulation of the position, at least that of the seventeenth and eighteenth centuries, was that man has a right to life, liberty, and property. We can arrive at the justification of the right to life in this way. Who but a man has the right to his own life? In the very nature of things how could there be a prior claim upon it? In short, a man's own claim upon his life is primary. It is his by right. If it be forfeit, it must be by his own willing act.

The Right to Use One's Faculties as One Wills for His Own Ends

The right to liberty is most directly the right not to be restrained or imprisoned. To put it affirmatively, it is the right to go and come at will, without let or hindrance. In practice, it means the right to do this unless he must be restrained for some good reason, duly attested and proved. In its extended sense, the right to liberty is the right to use one's own faculties as one wills for his own ends. This, too, is founded in the nature of things. Only the individual is situated so as to use his faculties for constructive purposes. He must command their use by his own mind and issue the signals through his own nervous system. Only he can direct his faculties to their highest and best use. The right to the use of one's faculties is an adjunct to the right to life, too, for it is by the employment of them to constructive purposes that life can be maintained.

The natural right to property arises in this way. That which a person has conceived in his own mind, made with his own hands, utilizing his own tools, from his materials, is his by right. It is his right, then, to keep it or dispose of it at will: to save, to sell, or to bequeath to whom he will. The right to private property in land is a corollary to the natural right to property. The right to improvements on the land belong naturally to him who made them (unless he was otherwise compensated) but the right can only be secured by property in the land itself. To put it another way, he who owns the land owns the improvements on it as well. If he does not own the land, he does not own the improvements. That is in the nature of things.

There are many other things which can be learned by reasoning on the nature of things. Indeed, it is doubtful if reason itself could long survive the abandonment of thinking in terms of the nature of things. Moreover, men have never stopped thinking in terms of the nature of things, though they have not done so nearly so fruitfully for many years because they have not generally openly avowed and accepted the full range of the premise of an enduring order which is necessary to its validation. But there is only one other use that I would make of this mode of reasoning here. The use is to refer to the social contract, another of the natural law doctrines.

I mention the social contract because it is necessary to point out that natural rights are *not* absolute; they are limited. The rights to life, liberty, and property are limited by the equal rights of others to theirs. When the rights of others are violated, the violator may suffer restrictions upon or loss of his rights. It goes further than that, however, as we can see by reference to the social contract.

The Social Contract

The social contract is not a written agreement, nor do we willingly and consciously enter into it. Rather, it is that agreement which is necessary, in the nature of things, to the existence of society. It is everyman's tacit agreement not to use violence to get his way, to leave others to the enjoyment of the fruits of their labor, not to trespass upon the property of others, to fulfill the terms of his individually entered into agreements, to honor his parents, to succor his children, to keep his word, to meet his obligations. The social contract embraces, too, the obligation of the citizen to support the government—with a portion of his means and, if need be, even his life—which protects him and his in the enjoyment of their rights. If these are limits on individual rights, they contain also implicit limits upon government.

In conclusion, then, I agree with the friend who suggested that there needs to be a greater emphasis upon rights rather than upon economic expediency, social benefits, and practical measures by government. The fount of prosperity, if Adam Smith was right, is in the individual and voluntary employment of industry and capital. The ground of that is in individual rights. The rights of which I speak are not bestowed upon us by government. Rather, they are secured by restraining government. They are, as Jefferson put it, a gift of "Nature and Nature's God," and cannot be violated with impunity.

—FOOTNOTES—

[1]Otto Gierke, *Natural Law and the Theory of Society,* Ernest Barker, trans. (Boston: Beacon Press, 1957), p. 223.

[2]Ernest Barker, "Translator's Introduction" in *ibid.*, p. xi.

[3]Quoted in John Bowle, *Politics and Opinion in the Nineteenth Century* (New York: Oxford University Press, A Galaxy Book, 1964), p. 66.

[4]Quoted in Henry Hazlitt, *The Foundations of Morality* (Los Angeles: Nash Publishing, 1972), pp. 204–05.

[5]Adam Smith, *The Wealth of Nations* Edwin Cannan, ed. (New Rochelle, N.Y.: Arlington House, n. d.), pp. 29–30.

[6]*Ibid.*, p. 290.

[7]*Ibid.*, p. 30.

Dennis Bechara

Freedom for Less Developed Countries

THE PLIGHT of the less developed countries has become one of the most hotly debated issues in international affairs. World-wide organizations have been established with the common purpose of uniting the less developed countries to obtain resources from the developed countries. Opinion leaders are almost unanimous in their belief that the developed countries have a duty to aid the poor countries. The debate, in fact, is not whether this aid is legitimate, but what ought to be the extent of it. Conventional wisdom holds that the situation in the less developed countries is attributable to the industrialized countries. Is this assessment correct?

Many reasons have been advanced to explain the poverty of the underdeveloped countries, and conversely to interpret the cause of the wealth of the industrialized nations. A popular notion is that the rich nations owe their wealth to their exploitation of the poor countries. The argument is really an extension of the fallacy that in every transaction there is a winner and loser. The ideology that has been erected to explain the alleged causes of poverty in the underdeveloped world holds that the most direct cause of exploitation is colonialism. Therefore, the argument goes, the colonial powers owe their life-blood to the colonies.

There is no correlation, however, between a country's standard of living and its history of colonial power. Some of the countries in the world that presently enjoy a relatively high standard of living either never possessed colonies or, if they did, the

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history of their colonialism is inconsequential. Switzerland, Denmark, Sweden, Norway and the United States are examples of this. Some of the great colonial powers, on the other hand, are presently facing economic difficulties. Portugal, for example, possessed colonies which encompassed a territorial area larger than itself. Yet, Portugal's economic position does not substantiate the charge that colonialism has enriched the colonial powers.

The Myth of Colonial Exploitation

The historical evidence is simply nonexistent to demonstrate that the poor countries subsidized the developed countries' wealth. The argument, however, continues to flourish, with a new twist. It is asserted that the old colonial powers, although having granted political independence to their former colonies, continue to exert an invidious control over the economies of the underdeveloped countries. The relative prosperity of the old colonial powers is therefore attributed to the exercise of this degree of power, which has been termed "neo-colonialism."

According to this line of thinking, the industrialized countries have reached their present position of opulence as a consequence of their investments in the less developed nations. The belief is harbored that since developed countries have invested tremendous amounts of money in the underdeveloped countries, the resources withdrawn from the latter have therefore yielded the investors fabulous profits. This argument is popular because it nourishes envy. It is easier to blame foreigners for a country's misfortune than to recognize that the country's governmental policies contributed to the situation.

However, when the available evidence is analyzed, it becomes clear that the developed countries do not owe their prosperity to their trade relationship with the less developed countries. There is no correlation between a nation's present economic standing and its holding colonies in the past.

The solutions espoused for the improvement of the underdeveloped countries' conditions reflect the redistributionist mentality on an international scale. It is politically fashionable to combat poverty with the compulsory transfer of income from the taxpayers to those deemed needy. Similarly, on an international scale, the predominant ideology is the same: to have the rich countries subsidize the poor countries. Therefore, the concept of redistribution of income is essentially the intellectual underpinning for foreign aid. In light of this, one must question whether or not massive income redistribution is the solution to the problem.

Aside from the libertarian position that it is immoral to force people to support others, the ideology of redistribution cannot be defended on grounds that it achieves what it sets out to do. Rather, the opposite is the case.

Foreign Aid Often Fails to Reach Needy Individuals

When a country receives foreign aid, it is a fallacy to presume that its citizens are necessarily any better off. This is so because the aid is received and handled by the host country's government, to use for its politically predetermined goals. For example, a country may wish to build an industry which is not economically feasible, but which grants prestige in the international community—such as an automobile industry or a steel mill.

Foreign aid makes it easier for the governments of the less developed countries to embark upon these projects, since part of the funds utilized to finance them have come from abroad. Therefore, the local taxpayer's opposition, which could otherwise have materialized, is lessened. In addition, foreign aid aggrandizes the power of the less developed countries' governments. The state becomes the beneficiary of this process because it has the power to apportion jobs and subsidies to its political favorites. Foreign aid, therefore, becomes an unwitting instrument of intervention in the internal political affairs of the host country.

Foreign aid is usually justified precisely on grounds that the recipient countries will ultimately become loyal to the country providing it; it is often proclaimed as an antidote to Communism. However, historical evidence fails to establish this. There is no causal connection between a nation's economic well-being and its vulnerability to fall under a Communist dictatorship. How various countries have fallen under Communist domination involves many historical explanations. Surely it cannot be argued that poverty automatically instills a pro-Communist attitude on the part of the population. If this were the case, most of the poor countries would have become Communist.

The idea that one country can purchase the allegiance of another through foreign aid is pernicious. In fact, it is commonplace to see the recipient countries become hostile to the donor countries. Foreign aid is viewed by the nationals of the recipient countries as a more subtle version of colonialism. Other factors, such as nationalism and cultural differences, account for a country's governmental attitude. It is, therefore, truly simplistic to assume that foreign aid can buy allegiance. Yet, those people who claim that one of the virtues of foreign aid is that it politically influences the recipient country are really conceding the fact that aid is not granted to improve the economic conditions of the recipient countries. Rather, the aid given is designed to obtain foreign policy goals, and consequently, no economic considerations are necessarily relevant in its granting.

The Need for Savings

A country, and for that matter, any individual, may increase its wealth in the long run only if part of its consumption is deferred for a later time. In other words, it is essential to save in order to increase one's wealth. Why is this the case? Because savings finance projects which, if economically necessary, increase productivity. For example, let us say that a railroad connecting farmlands to a market needs to be built. The railroad will increase the marketability of agricultural goods, and therefore the costs to consumers will be lowered as a result of this more efficient mode of transportation. However, savings are needed in order to finance the project.

The individuals who construct the railroad need funds to defray the costs of the project. Clearly, the money utilized by them constitutes their abstention from consuming those funds. The investors have placed their savings in the form of a railroad. If the investors do not have the funds to carry on their project, they may entice others to lend such funds. Whether the funds originate domestically or from foreign sources, these funds represent savings. A common way to finance many projects, however, contains the element of governmental coercion, or what is commonly called forced savings. This is the method of simply levying taxes or issuing paper currency to finance the projects. In either case, the citizens are forced to consume less of their income, because the taxes imposed reduce their disposable income, or the price increases which result from the increase in the money supply reduce their purchasing power.

The issue that is crucial to a nation's development, therefore, is where the savings should originate. Foreign aid is another form of compulsory saving—by reducing the consumption of the donor country's taxpayers. But as we have seen, foreign aid is not economically motivated when it becomes intergovernmental aid. Foreign investment, on the other hand, does utilize sound business justifications for its use. Foreign investors seek to place their capital in the most profitable lines of business. This benefits the recipient countries because jobs are created, and the marginal productivity of labor is increased. This tends to raise wages in the recipient country. The guidepost of profits, in addition, insures that scarce resources are not misallocated. When an activity is profitable, it means that consumers view its rendition in a positive manner. The high profits attract more investors, and this in turn serves to lower the prices charged to consumers. Foreign investment speeds up this process.

Increasing the amount of foreign investment available does benefit the recipient country, but is is not the only available solution to relieve the underdeveloped countries' position. For these countries to truly improve their condition, it is necessary for them to establish an institutional framework which will attract not only foreign investment, but encourage domestic savings and investment as well. The people best suited to know local conditions and local investment opportunities are the residents of these countries themselves. If the underdeveloped countries attempt to encourage savings and institutionalize the essential preconditions of a free market economy, there will be a sounder basis for growth. However, when one examines their record, the policies which have been followed are precisely contrary to the attainment of these goals.

The Protection of Property

Governments are instituted to safeguard pre-existing rights possessed by individuals. Among these rights is the right to own and possess property. This is essential because if a person is not entitled to his property, his right to survive is endangered. Since a person has the right to life, it follows that a person needs to keep the fruits of his labor in order to survive. Therefore, governments must respect property rights. What is the record of the underdeveloped countries concerning this?

The history of the less developed countries is scattered with instances of wide-scale nationalization of foreign-owned business enterprises. At the turn of the century, for example, Mexico nationalized its fledgling oil industry, which was prospering at the time precisely because the government had allowed private investors to place their capital there. India, after obtaining its independence from England, proceeded to establish onerous controls over foreign investments. Virtually every country in the "Third World" has experimented with some form of state ownership of enterprises. Brazil, which many point out as a beacon of hope in South America, has a large segment of its economy under the direct control of the government. With these facts merely as an illustration of the state of affairs of these countries, it becomes easy to understand why foreign investment represents such a small percentage of the United States economy.

The less developed countries have also pursued a very dangerous policy which has, in effect, discouraged savings and eliminated the long term capital markets. The policy is universally known as inflation. This policy of increasing the money supply with its consequence of a rise in prices, helped diminish the role of savings in those countries. Constant increases in the money supply, coupled with periodic devaluations of the national currencies and foreign exchange controls served to stultify growth.

Other Interventions

Aside from failure to protect private property and aside from inflating the money supply, many of the less developed countries adopted other policies detrimental to a free market. The newly independent nations created massive licensing requirements, implemented regulations and enforced policies that discouraged competition.

One of the most notable of the policies that were adopted by these countries was the progressive income tax. This rather recent development, however, is due to the influence the industrialized countries exert on the less developed countries. Under the aegis of the prevailing academic wisdom, it was the policy of the United States government to advise these countries of their duty to eliminate the broad inequalities of income in existence and to adopt a progressive income tax. The effect of these taxes, of course, has been to discourage capital formation. It is not uncommon to discover many foreigners holding substantial wealth outside the borders of their own countries because they are in search of a place which offers security and stability. Politically, many of these countries have experienced revolutions, sudden changes in governmental policy, and this instability has added an element of risk, making it less attractive for anyone to accumulate savings.

Another common feature in the less developed countries has been the prohibition of free foreign trade. This has occurred because it is feared that free entry of foreign goods could destroy local industries and therefore produce unemployment. The fallacy here, however, rests in not recognizing that if foreign countries do make better and cheaper goods, this benefits the country importing those goods. This is so because the citizens of the importing country will have resources left over as a result of their acquisition of the goods that cost less, while other goods may be acquired as well.

The principle of comparative advantage is applicable to trade. This means that a country has, if permitted to trade in a free environment, the incentive to specialize in the production of goods for which it is better suited. More wine is produced in France than in England, for example, because of this principle. If England, however, were to enact a law prohibiting the importation of foreign wines, in order to encourage its domestic wine production, its consequent inefficient production cannot be said to improve England's economic posture. The less developed countries, unfortunately, as a result of misdirected policies, have become quite protectionist.

In conclusion, it must be said that, outside of the ravages of natural disasters, or those brought about as a result of war, a substantial portion of the cause of the poverty of the less developed countries is directly attributable to their own governmental policies. This is not to argue that voluntary aid to the needy in the less developed countries should not be granted. Rather, the discussion here has centered around what policy the governments of the less developed countries should adopt. In light of this, the best advice the developed countries may grant to the less developed ones is to encourage capital formation. This can best be accomplished by trying freedom.

Hope for the Oppressed

IDEAS ON LIBERTY

ONLY when the state is restricted to the administration of justice, and economic creativity thus freed from arbitrary restraints, will conditions exist for making possible a lasting improvement in the welfare of the more miserable peoples of the world. It is often this very lack of justice in the poorer countries that keeps the people in their low economic state. An English economic advisor to an African state was shocked at the prevalent low wages and succeeded in securing a minimum wage law for the land. The result was that the thousands of workers who had earned forty to fifty cents a day were put out of work. Only the more efficient and essential workers remained and the whole economy suffered. It had been interventions in the market by the government, a lack of justice, that had kept the wages down in the first place by preventing capital accumulation and investment. Further intervention, in the form of the minimum wage law, only aggravated the situation, removing the one chance many had for some economic improvement. Were justice present in these lands, there would be no shortage of investment capital, for there would then be no fear of unjust confiscation or nationalization. Justice is the one condition that will lead to economic improvement.

FRANCIS E. MAHAFFY, "Social Justice"

John K. Williams

INTELLECTUALS, MORALISTS, AND THE FREE MARKET

"Capitalism stands its trial before judges who have the sentence of death in their pockets. They are going to pass it, whatever the defense they may hear; the only success victorious defense can possibly produce is a change in the indictment."

So wrote the noted economist and social scientist Joseph Schumpeter in 1942. The situation he depicts is worthy of Lewis Carroll; indeed, the bizarre principle of "justice" advocated by his "hanging judges"—"Verdict and sentence first; indictment afterwards"—is remarkably reminiscent of the slogan championed by Carroll's Queen of Hearts at the trial of the tart-stealing Knave of Hearts: "Sentence first; verdict afterwards."

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The irrationality of the situation described by Schumpeter is not confined to a verdict and sentence desperately seeking for an indictment. In the work from which the above quotation is taken he argues that the chances of a free market economy surviving are remote: "Can capitalism survive? No, I do not think it can." At the same time, however, he proffers a compelling case for holding that capitalism is a uniquely beneficent economic system enjoying an unsurpassed, and arguably unsurpassable, record for raising the standard of living of an entire community and thereby dramatically alleviating the penury and want of the worst-off. "The capitalistic process," he asserts, "not by coincidence but by virtue of its mechanism, progressively raises the standards of life of the masses." He wryly observes that "Queen Elizabeth (the

First) owned silk stockings. The capitalist achievement does not typically consist in providing more silk stockings for queens, but in bringing them within the reach of factory girls in return for steadily decreasing amounts of effort."

Schumpeter Confirmed

An examination of the diverse and mutually contradictory charges levelled against the free market confirms Schumpeter's judgment as to the desperation marking the critics' search for a plausible indictment. In Schumpeter's day the standard charge was that a free market economy had produced the Great Depression, creating economic stagnation and permanent mass unemployment. The data later presented by such scholars as Milton Friedman and Murray Rothbard documenting that the Great Depression was the creation of decades of governmental interference with the market, had been conveniently ignored (just as, in contemporary versions of a similar criticism, a plethora of studies documenting the consequences of minimum wage laws for those whose labor is of marginal value are ignored).

With the publication of John Kenneth Galbraith's *The Affluent Society,* however, a stunning change in anti-capitalist criticism made its debut: the free market was *too* productive, tempting men and women to sell their souls for an obscene affluence measured in terms of burgeoning super-markets and automobile tail fins. Today's fashionable charge is *either* that such institutions as private property, the free market, and material incentives to production, which once constituted a remarkably successful means for dealing with the problem of scarcity, are no longer necessary because we are living in a "post-scarcity" age, *or* that rapacious capitalism has greedily depleted the earth's material resources and, by ushering in a new era of world-wide scarcity, has brought about its own demise. Quaintly, some critics parrot both charges, happily indifferent to their mutually exclusive nature.

Schumpeter's case for the uniquely beneficent nature of the free market also stands scrutiny after four decades; indeed, his rebuttal of the boringly familiar claim that the productive success of capitalism, and hence its unintended lifting of the standard of living of the poorest, was the result of a chance combination of fortuitous circumstances and wise governmental constraints, has yet to be answered.

Further, those four decades have witnessed the demonstrable failure of a wide-ranging diversity of socialist experiments. Documenting the by now commonplace is tedious; suffice to suggest that the comparative beneficence of an economic system which, in the Soviet Union, results in the one-third of its working populace employed in agriculture being unable to produce the food required by a population of 265 million, and of an economic system which, in the United States of America, witnesses the four per cent of its working populace employed in agriculture vastly exceeding the food requirements of its 220 million people, is not hard to determine.

A Puzzling Attitude

Indeed it is simultaneously ironic and tragic that many Third World countries, in bold but fashionable defiance of observable empirical reality, should have opted for collectivist "agrarian reforms" and thereby have reduced nations once enjoying thriving agricultural bases to the unhappy situation of being obliged to import basic foodstuffs.

In passing, it is worth noting the moral astigmatism of such reports as the Brandt Commission's *North-South: A Program for Survival* and numerous similar publications of the World Council of Churches: one might have thought that the infliction of chronic food shortages upon an entire population by ideologues might be perceived as a betrayal of "human rights" or as incompatible with "social justice"—or even, perhaps, as a new and particularly vicious form of "exploitation." That such is *not* the case—indeed, that policies seemingly designed to produce equal destitution for all should be warmly commended—is a sad commentary upon the ideological captivity of many Western intellectuals.

It is that "ideological captivity" highlighted by Schumpeter's grotesque but perceptive image of capitalism's critics as "hanging judges" blindly determined to sentence capitalism to death, that merits careful thought and discussion. Why do so many intellectuals and moralists attack so readily and so unremittingly an economic system the worst about which even the most dogmatic of socialists can say is that it is the best yet, save for the particular untried version of socialism the socialist in question advocates?

There is nothing irrational about judging an economic system, as many moralists do, on the basis of how it serves the worst-off; what *is* irrational is that those committed to this criterion of judgment should display an almost instinctive abhorrence of a system which, at least to date, has demonstrably done best what they value most. It is this puzzlingly irrational abhorrence of the free market—an abhorrence not explicable in terms of some simple, factual disagreement as to the productive capacity or social consequences of an economic system—that the defender of the free market must seek to understand and to address.

Who Are the "Intellectuals"?

Attempts to define the notoriously vague term "intellectual" are legion, and none of them is entirely satisfactory. Perhaps the best that can be said was said some years ago by Friedrich A. Hayek in his justly famous paper, "The Intellectuals and Socialism." The intellectual trades in *ideas:* "What qualifies him for his job is the wide range of subjects on which he can readily talk and write, and a position or habits through which he becomes acquainted with new ideas sooner than those to whom he addresses himself."

Hayek goes on to note the truly astonishing number of contemporary professions and activities which belong to this class: "The class does not consist only of journalists, teachers, ministers, lecturers, publicists, radio commentators, writers of fiction, cartoonists, and artists—all of whom may be masters of the technique of conveying ideas but are usually amateurs so far as the substance of what they convey is concerned. The class also includes many professional men and technicians . . . who through their habitual intercourse with the printed word become carriers of new ideas outside their own fields and who, because of their expert knowledge on their own subjects, are listened to with respect by most others."

This description of the "intellectual" is substantially the same as the description usually provided of what such economists and social scientists as Fritz Machlup, Peter Drucker, Daniel Bell, Peter Berger, and Irving Kristol have called the "New Class." Irving Kristol has argued persuasively that, since the early 1970s, the most significant "class struggle" in Western nations is the struggle between the old "business class" and the "New Class," the ascendant elite based on the knowledge industry. Peter Berger, commenting on the power of this new elite, notes its "capacity to influence public opinion through the communications media and through the educational system." "This influence," he continues, ". . . even extends into the old business class itself: Corporation executives go to churches where they are preached at by New Class clergy, their wives read magazines written by New Class authors and editors, and their children go to colleges staffed by New Class professors."

Reasons for Irrationality

Perhaps the first feature to note about the "intellectual" is his essentially prescriptive stance. The journalist, the teacher, the minister, and the writer are more concerned to prescribe what "ought to be" rather than to describe "what is." To the extent that "what is" is described, it is described in terms of its departure from some norm defining what "ought to be." Put more simply, the intellectual is committed to the espousal and advocacy of values.

Ayn Rand to the contrary, the free market is supremely indifferent as to values. It prescribes no overall vision of moral or aesthetic or intellectual excellence; it aims toward no all-embracing end or purpose. It simply coordinates the activities and skills of diverse individuals seeking radically different goals and espousing widely varying values.

It does, however, *reveal* popular tastes and preferences. Commodities valued by the masses can, for the most part, be mass produced and sold cheaply; commodities valued by a few can, of course, still be produced but only if the few are prepared to foot the bill. And the tastes of the masses are deplorable. They prefer Agatha Christie to Dostoevsky; they rank the performances of "Abba" ahead of those of Pablo Casals; they value the compositions of Johann Sebastian Here-today-and-gone-tomorrow more than they value those of Bach.

That the intellectual finds such a state of affairs profoundly disturbing is not surprising. It *is* disturbing. And it is quite proper for the intellectual and the moralist to denounce vulgarity of taste and to attempt to transform the masses' tastes. To blame the free market for what it reveals is, however, supremely irrational—as irrational as indicting wet roads for rainy weather or thermometer readings for fevered temperatures.

Blaming the System

Yet the temptation to such irrationality is irresistible. To attribute deficiencies of tastes to the masses is to invite the charge of elitism, and that is a charge intellectuals will go to any lengths to escape. It is much easier, and much safer, to blame the "system," and the irrationality of the exercise can be disguised by extraordinary arguments to the effect that advertising skillfully depraves the admirable tastes and noble desires of ordinary people. The self-evident fact that advertising must, if it is to succeed, address itself to existing tastes, and the *prima facie* implausibility of any advertisement, however skillful, being able to sell and continue to sell food that is inedible, clothes that are unwearable, and gadgets that are unworkable, can conveniently be ignored—as can a multiplicity of studies documenting the conspicuous failure of advertising to sell goods not satisfying the fickle tastes of consumers. For such a strategy enables the intellectual to hold to values which in truth *are* elitist, yet simultaneously to sustain the false belief that "really" his values are those of the "ordinary people."

In the second place the intellectual and the moralist are attracted to systems which are the conscious creation of trained intellects and work to the advantage of those deemed "morally worthy." The free market is neither. To be sure the free market is characterized by order—it efficiently coordinates countless diverse skills, it automatically draws upon a totality of information embodied in innumerable individuals who for the most part never meet, it accurately indicates the tastes and desires of consumers and the most economic way of satisfying those tastes and desires, and it unfailingly indicates when random patterns of behavior "chance" upon new ways of more efficiently satisfying human needs—but this order is a spontaneous order, not a consciously contrived order. Its subtle rationality is akin to the subtle rationality of language: a subtle rationality which no person or group of persons deliberately and consciously designed and which trained linguists still strive to comprehend. Indeed, the market coordinates skills no intellectuals could list and draws upon an ever-changing totality of information no intellectuals could synthesize.

That the random and uncoerced activities of the many could give rise to a system defying conscious imitation by the gifted few is intrinsically threatening to the intellectual. And when that system "rewards" neither the best nor the brightest but those who actually satisfy the tastes and preferences of the masses—however depraved or unenlightened or tawdry those tastes and preferences might be—the threatening becomes abhorrent.

Conditions Change

Connected to this almost unconscious dislike of spontaneous as against contrived order, is the intellectual's preference for the abstract as against the concrete. This is, perhaps, nowhere more pronounced than in the enthusiasm of many economists for the abstract concept of "equilibrium."

Such a concept presupposes a static world devoid of ordinary human fallibilities, where neither past nor future human expectations matter. The concrete reality of purposive individuals seeking to improve their situation in a world characterized by imperfect knowledge and a consequent lack of coordination, but a world in which learning is possible, new opportunities for improvement can be perceived, and increasing coordination can be realized, is effectively ignored. Rather, the real world of purposive behavior in an environment of flux and change is supplanted by an eerie world of aggregates the adjustment of which to their controlled and perfectly known environment is the entire story.

That any theory couched in terms of "equilibrium" cannot be tested by measurements taken in a world of continuous *disequilibrium,* a world of changing tastes, changing expectations, changing technologies, changing information, changing opportunities, and changing material resources, was the great insight of such free market economists as Ludwig von Mises and Friedrich A. Hayek. Yet an enthusiasm for the abstract (and an addiction to what the philosopher A. N. Whitehead once called the "fallacy of misplaced concreteness") has led to a widespread disregard—albeit no rebuttal—of the arguments leading to this conclusion.

Galbraith's Outlook

The predilection of the intellectual for the abstract finds a less technical expression in a recent, and quite charming, volume from the prolific pen of the much lauded opponent of the free market, John Kenneth Galbraith. In *Annals of an Abiding Liberal* Galbraith writes patronizingly of those who, as an alternative to the system of wage and price controls advocated by himself, argue for a return to a self-regulating market economy. "Conservative economists," he notes, "if sufficiently archaic, have some justification for this theology; the full employment equilibrium is basic to the conservative creed, and inaction is the way to realize that equilibrium. Liberal economists must believe that they are of the chosen—that, as I've said often, God is a Keynesian Democrat."

Now it would be churlish to disallow Galbraith his much tried and frequently tested rhetorical device of describing views he dislikes in religious terms. Yet when such rhetorical flak is dropped his utterance reduces to the fascinating proposition that a fully employed economy would be marked by "inaction." What has happened is clear: in boldly heretical defiance of *The Shorter Oxford English Dictionary* Professor Galbraith has redefined the verb "to act" and the nouns "action" and "activity."

The words no longer refer to such concrete, flesh-and-blood realities as the labors of the carpenter, the toils of the garbage collector, or the exertions of the transport driver. They refer rather to the abstract ruminations of those who determine what people "ought" to value, decree what men and women "deserve" to earn, and decide how much money "should" be extracted from football fans and movie buffs to subsidize the extravagant tastes of ballet and opera enthusiasts.

A Vested Interest

The "most active" people of all are, of course, members of the veritable army of Keynesian economists who, perceiving the economy as a potentially workable, but always troublesome and recalcitrant patient, with a continual tendency to hive off into greater inflation or unemployment, function as Court Physicians, ever watchful of and ever tinkering with the economic patient. (That the disease from which the patient is alleged to suffer is iatrogenic—that is, caused by the procedures purportedly fighting the disease—is the thesis of so-called "Austrian" economists; not surprisingly, perhaps, such economists tend to be ignored in Court Economic circles.)

That the tidy mathematical abstractions so amenable to intellectual manipulation give rise to conclusions serving their creators' class interests is, perhaps, the decisive cause for intellectuals' dislike of the market. The majority of intellectuals derive their livelihood from public-sector employment; they *ipso facto* have a singularly tangible interest in expanding such employment.

The enthusiasm of the New Class for such fashionable contemporary causes as consumer protection, the environment, and—of course—the "war on poverty" makes perfect sense when related to the intellectuals' class interests. If business interests are served by the proposition that open access of producers to the market and ordinary laws prohibiting fraud are sufficient to protect the interests of consumers, those employed by State-funded consumer protection agencies are no less served by a denial of that proposition. If industry and consumers have an interest in holding back environmental protection measures that increase costs, the New Class has an equal interest in creating environmental protection agencies that provide its members with jobs and political power. If the participator in private enterprise has a vested interest in asserting that increased productivity proffers the only meaningful, long-term solution to the problem of poverty, those administering complex welfare systems have every reason to claim that such proffers no solution.

Part of the Problem

Interestingly enough, some of the most vocal critics of the "New Class" are to be found among those concerned to improve the economic lot of the poorest and most vulnerable of the community. Such black, ghetto-born U.S. economists as Professor Thomas Sowell and Professor Walter Williams have argued, and argued convincingly, that it is much more difficult for a disadvantaged minority in a "transfer society" to gain the political "clout" necessary to wrest substantial wealth from politically sensitive redistributors than it is for such a minority to gain economic power in a free market economy. Sowell has, in fact, gone much further, brutally stating that "The poor are a gold-mine. By the time they are studied, advised, experimented with, and administered, the poor have helped many a middle-class liberal to achieve affluence with government money." To suggest that the interests of the New Class, professional "poverty fighter" might not parallel those of his unhappy clients may be unkind; it is not, unfortunately, self-evidently untrue.

Enforced Equality: Reform the Tastes of the Masses

Anti-capitalist clergy constitute merely a special sub-set of "intellectuals"; the values they seek coercively to impose upon a society are, perhaps, more explicit than those of their fellow opponents of the free market, but no substantial difference obtains. They too are anxious coercively to reform the tawdry tastes of the masses; they too find the notion of "spontaneous" as against "consciously directed" order threatening; they too prefer the static abstractions of an idealized world to the dynamic change of the real world; they too have a vested interest in a society proffering positions of power to moralists decreeing who "deserves" to earn and own what.

They are, however, subject to two particular temptations. Firstly, the doctrine that all people are valued equally by God can easily lead to the notion that an economic system producing some "equality of distribution" is preferable to a system producing substantial inequities. Apart from obvious difficulties attending the very notion of "equality," the enthusiast for "equal distribution" simply cannot admit any liberty to dispose of initially equally distributed goods in his utopia.

Consider, for example, a society of one thousand persons, each of whom possesses exactly one thousand dollars. One member of this society happens to be Joan Sutherland. Suppose Joan Sutherland were to state that she was going to stage a concert and that any person wishing to forgo fifty dollars and hence other goods for which that fifty dollars could be exchanged might attend that concert. Suppose further that all the remaining members of the society prefer to forgo that sum of money (and alternative goods) and hear Joan Sutherland sing than to retain that money or procure such goods and not hear her sing. The exchange, in other words, is purely voluntary: each person surrenders what he values less for what he values more. At the conclusion of the concert massive inequity obtains: Joan Sutherland possesses $50,950 whereas each other member of the society possesses only $950. Yet if the initial state of affairs is deemed "just," and if the voluntary exchange of goods is also deemed proper (and if people are not at liberty to exchange what they value less for what they value more, the point of owning anything is obscure), it would seem to follow that the final distribution must be "just." As noted, however, "equality of distribution" is no more.

The Good Samaritan

In the second place it is extremely easy for clergy to glide from the claim that the carrying out of some action is "good" to the quite distinct claim that coercing others to carry out that action is good. It is instructive, however, to observe what such a glide does to a story familiar to all clergy. The wicked priest and Levite (interestingly a clergyman and an intellectual!) pass by a beaten victim of society, leaving him for dead. A Samaritan traveller (again, interestingly, a businessman prudent enough to have accumulated some capital) assists the stranger and funds his care and accommodation at an inn. The welfarist clergyman would, however, have to posit a "Better Samaritan." On espying the beaten stranger this Samaritan would rapidly return to Jerusalem, call out the Roman armies, coercively extract money from other wealthy businessmen, and establish an aid-to-wounded-travellers' benefit. The moral excellence of this strategy is, surely, obscure; so, for that matter, is the coerced "charity" of those whose money is forcibly redirected.

Can the Accused Get a Hearing?

Schumpeter was right to observe that capitalism is standing its trial, and standing it before judges with the "sentence of death in their pockets." He said, however, nothing about a jury; yet there is a jury. It is true that that jury is more familiar with the caricature of capitalism created by its accusers than the actual defendant, but while not warmly disposed towards that caricature the jury is not unambiguously enthusiastic about "intellectuals" either.

The jury, in other words, may well be ready to listen to a case for capitalism—especially if that case can stress that they, the ordinary consumers, are the ultimate beneficiaries and controllers of the free market. There is good evidence that ordinary men and women are becoming impatient with the only alternative to "profit management" in a free market: bureaucratic management. There is good evidence that the level of taxation demanded in a "transfer society" has led to the rediscovery of the core free-market principle of mutually benefiting voluntary exchange—whether that involves barter or undisclosed cash payments. There is good evidence that the almost inevitable consequence of a currency unrelated to the reality of the market and at the mercy of a State enjoying unrestricted, monopolistic control of the money supply is inflation—and inflation is not popular with the masses.

The time is ripe—indeed is overdue—for the practitioners of the free market to enter the world of ideas and to promote the free market. Corporations simply must start supporting thinkers who challenge the dogmas of Statists. And such thinkers are not unknown. The collapse of the socialist ideal is a reality. The "new philosophers" of France (in particular Jean-François Revel and Bernard-Henri Lévy) have mounted a devastating critique of Marxian thought. Faculties of economics, torn by disputes between Keynesians, neo-Keynesians, "neo-Classical Keynesian synthesists," Monetarists, and Marxists are more prepared than was, until recently, the case to give some voice to pro-market economists. Dissenting intellectuals, such as George Gilder (author of the widely discussed volume *Wealth and Poverty*), are making out new and interesting cases for a free market economy.

That such materials are "translated" into terms accessible to ordinary men and women is vital. That corporations should, both individually and collectively, aid the dissemination of such translations is imperative. Michael Novak has put it well: "[The free market] is now engaged in a war of ideas. The methods and means for conducting such a war successfully can be clearly discerned—they are well known, even if seldom set forth in systematic form—and the resources for employing them wisely . . . and in an atmosphere of freedom and diversity are plainly available. The next step is to make them operational."

The time for that "next step" is now, while democratic institutions still exist. "Hanging judges" tend to dislike such institutions, particularly juries, for ordinary men and women are, so it is claimed, the unhappy victims of a "false consciousness" which prevents their seeing the free market for what it is. Only the enlightened few, the fortunate possessors of an "authentic consciousness," are able to see the truth. It is not sufficient that such "true believers" simply be judges. They wish also to be jurors. And executioners.

IDEAS ON LIBERTY

John Milton

FOR who knows not that Truth is strong next to the Almighty; she needs no policies, nor stratagems, nor licencings to make her victorious, those are the shifts and the defences that error uses against her power.

Instead of Regulation

FOR all its good work in pushing tax cuts and putting a hold on some forms of public spending, the Reagan Administration may be missing a bet in failing to give deregulation a high priority on its list of "musts." The costs of regulation are so far-reaching that they must challenge the over-issue of money as a cause of stagflation. If they could be done away with, the drain on the federal budget would be considerably lightened, and David Stockman, Reagan's budget director, might find his labors considerably more rewarding.

Fortunately, the way to a widespread dismantling of our regulation agencies has been charted in a collection of eleven searching essays by experts assembled by Robert W. Poole, Jr. of the Reason Foundation of Santa Barbara, California. The book, *Instead of Regulation: Alternatives to Federal Regulatory Agencies* (Lexington Books, D. C. Heath and Co., 125 Spring St., Lexington, Mass. 02173, 404 pp., $25.95), could, if its recommendations were to be acted upon, make eleven regulatory bureaucracies superfluous.

Lest his readers might feel that he is dealing with political impossibilities, Poole makes Stephen Breyer's and Leonard Stein's account of an already partially accomplished airline deregulation the lead-off piece in his collection. A phase-out of the powers of the Civil Aeronautics Board has already begun, with the Board itself ticketed for burial in 1985. Despite many anguished predictions that small cities would lose their access to air transport, the airline deregulation has been followed by an explosive growth of local-service and intrastate airlines. Former local-service carriers such as U.S. Air (once called Allegheny), Hughes Airwest, Texas International, Piedmont, Frontier, Ozark and Republic flew 32 per cent more revenue-passenger miles in 1979 than they did in 1978.

Deregulation Under Way

The airline success is not the only evidence that deregulation acts as an energizing prod. We are still paying for an expensive Department of Energy, but the lifting of controls on oil prices has already had its effect on well-drilling in the U.S. "lower 48" states. And trucking deregulation has already been authorized, with some semblance of compliance in the matter of accepting new entries in a field dominated by the Teamsters Union.

The successes enumerated by Mr. Poole's contributors, however, are only a bare beginning. In spite of the start on truck deregulation, George Hilton, in his essay on "Ending the Ground-Transportation Cartel," laments that the Interstate Commerce Commission—the daddy of all our regulatory agencies—still prevents a real revolution in surface transportation. Containerization, which gets rid of stevedoring costs, has brought new vitality to ocean shipping, but it has yet to hit the railroad freight business. If there were no ICC to prevent it, Mr. Hilton thinks there might be a proliferation of "true intermodel shipping companies." These would lease track rights from railroads, and freight would move to the ultimate consignee in containers that could be off-loaded between train and trucks with a minimum of strain.

In the Energy Field

The new oil wells that are being drilled as a result of the lifting of price controls give pleasure to Alan Reynolds, but his essay on "A Free Market in Energy" reminds us that we are still a long way from an uncontrolled energy market. Natural gas has not yet been deregulated. And there are continuing threats of investment controls. If Senator Teddy Kennedy could have his way, horizontal divestiture would be forced on oil companies to prohibit their entry into coal, uranium, oil shale, solar and geothermal competition. Divestiture, says Mr. Reynolds, would be "an attempt to hold capital hostage—a form of political allocation of capital."

When it comes to communications, we are technologically ready to end the current monopoly of the airwaves that is perpetuated by the Federal Communications Commission. The FCC has discriminated against pay-as-you-see TV for years, but the claims of cable-TV could not be denied forever. The use of satellites in broadcasting means that programs can be "bounced" into backyards anywhere. Property rights in wave lengths could be established without fear that a few companies would gain eternal monopoly positions. Ida Walters, in her essay on "Freedom for Communications," makes a most persuasive case for freedom in TV and radio broadcasting. Her efforts to tell us how monopolies in local telephone service can be ended are labored, and it is not entirely clear to this reader how established phone facilities could be shared between competing companies without some degree of regulation.

Airline Safety

Mr. Poole's essay on airline safety suggests that if air traffic control were to be turned over to private companies, such as Radio Schweiz in Switzerland, we might get better service with the taxpayer relieved of the cost. And the inspection of aircraft might be more trustworthy if private insurance companies were to do the job.

There is even a case for competition in pollution control and for establishing liability laws combined with free market insurance methods of bringing safety to drug manufacture. It will take time for Mr. Poole's contributors to be heard in appropriate Congressional committee hearings. But Mr. Poole's book makes a glorious beginning. It will have its impact in saving us a big part of the $100 billion per year which Council of Economic Advisors Chairman Murray Weidenbaum says we now spend on maintaining 136 federal regulatory agencies employing 141,000 people who might be more productively employed in private industry.

SEEDS OF THE HOLOCAUST: THE GERMAN ECONOMY, 1916–23

by Stanton Brody. Edited by Don Venes.
(Published privately, 1979. Glencoe, Illinois. Copies available from The Foundation for Economic Education, Inc., Irvington-on-Hudson, N.Y. 10533)
42 pages ■ $3.50

Reviewed by Bettina Bien Greaves

THE GERMAN INFLATION of 1923 is the classic illustration of what to expect when a government pursues a policy of inflation to the bitter end. It evokes vivid pictures of panicky buying, wheelbarrows overflowing with the paper money needed to buy a day's food, workers' wives taking their husbands' pay each morning and rushing out immediately to buy something, anything, before prices rose still more. By the end of 1923, prices of many everyday items were reckoned in the billions and trillions of Marks. Fantastic! Incredible! But true! Yet these descriptions reveal little or nothing of the effects the inflation had on the people themselves—on their mental, psychological and moral attitudes.

By the end of World War I, the defeated Germans were war-weary, exhausted and famished. Millions had been killed, maimed or were missing in battle. The Allied blockade had reduced their diet to "ersatz" foods, horse and dog meat. Many had not had a decent meal since 1916.

The Kaiser was ousted. The new government was weak and insecure. Yet it did what it thought best to help the people recover from the effects of four long years of fighting and deprivation. It tried to increase food supplies by imposing land reforms, subsidizing cereal imports and buying produce from farmers to sell cheap to the poor. But these programs cost money. And the government was as destitute as the people. Tax collections fell far short of what it spent. To finance its domestic expenditures, therefore, it continued the practice of printing paper money. By 1921, the German Mark—worth about 24¢ in U. S. money before the war—had fallen in value to about 1/15th of the U. S. dollar (6.6¢). A year later it had dropped to 1/450th of the dollar.

When England and the United States brought their wartime inflations to an end, both experienced economic depressions. Many were out of work while business enterprises were readjusting in 1921–1922. As a result, German officials concluded that inflation was the way to insure "full employment" and to expand exports—as indeed it was in the very short run. So the German government continued inflating.

By this time, every German was speculating on still more inflation and still higher prices for all goods and services. No one was saving any more. The demands of the Allies for reparations was an added blow to a people already beaten, impoverished and nervously exhausted by having to cope daily with the problems of inflation. They grew bitter at the heavy penalties exacted by the Allies. To pay the reparations, real goods—gold, minerals, factory products, investment securities—not paper money, had to be delivered to former enemies. The government had to impose heavy taxes for this purpose. Yet little or nothing remained for domestic expenditures. So the government continued inflating.

Discontent and political turmoil, already rife throughout the land, mounted. Restless agitators of every ideological hue—right, left, communist, fascist—attempted periodically to overthrow national and regional governments. Political murders or assassinations were commonplace—about 300 in four years.

No one was able to escape the catastrophic effects of the inflation and political unrest. The farmers, perhaps in the best position to weather the storm, had their savings wiped out and they themselves were worn down by government regulations. Laborers and salaried employees became destitute, for no wage or salary could keep pace with the spiralling cost of living. Landlords and tenants suffered as the quality of housing declined, because the government imposed ceilings on rents while all other prices were rising through the roof. University professors and students had to dig ditches, work in mines and factories or on farms in the summer to survive, and the quality of their library and research materials suffered. Because of the volatility of prices, businessmen found it impossible to calculate or plan. As they used up their investments, enterprises that had been profitable suffered losses. Even German bureaucrats who had always enjoyed prestige and high salaries were destitute. Less food was brought to the stores to be sold and the available consumer goods were of poorer quality. Standards of nutrition declined. Susceptibility to disease and infection increased. Children, always hungry, grew up undernourished and physically debilitated. Only those few Germans with investments abroad were able to avoid complete impoverishment.

By October 1923, the Mark was worth less than one four-billionth of its pre-war value. Inflation had utterly destroyed the German people financially, economically and morally. A people long known for their energy, industry, education and culture were destitute and degraded. Traditional methods of providing for themselves and their families—hard work and saving—proved useless. The people were emotionally, mentally and morally prepared to welcome a charismatic leader who offered hope. They were ready to believe Hitler's lies and promises of economic rescue and pride in the "Thousand Year Reich." By choosing Hitler over the economic disaster they knew, they accepted in time the consequences of that choice—controls, censorship, war and even the "holocaust."

Stanton Brody, the author of this booklet, was an established businessman in his mid-40s when he returned to college to study history. He became fascinated with this period in German history. In his desire to bring readers the important message—that inflation must be stopped lest we lay the groundwork for another world war and holocaust—he wrote this account and published it privately. Mr. Brody's booklet is well worth reading.

PRINCIPLES OF ECONOMICS

by Carl Menger
(Reprinted by The Institute for Humane Studies and New York University Press; distributed by Columbia University Press, 136 South Broadway, Irvington, New York 10533), 1981
328 pages ■ $20.00 cloth; $7.00 paper

Reviewed by Roger R. Ream

THE PUBLICATION of Adam Smith's *The Wealth of Nations* in 1776 is considered the starting point of the science of economics. However, it was Menger's *Grundsätze* (1871), along with the works of Léon Walras and William Stanley Jevons, that began the modern period of economic thought. Significantly, Menger's ideas provided the foundation for what is today classified as the Austrian School of economics. This important book of Menger's, not translated into English until almost eighty years after it was written, has now been reprinted by The Institute for Humane Studies and the New York University Press.

Menger is perhaps best known for his development of marginal utility theory, discovered almost simultaneously by Jevons and Walras. However, to comprehend fully the importance of Menger's achievement one must understand the context into which it fits. It was Menger who elaborated the logical foundations of marginal utility theory and it was his *Principles* specifically that served as the basic textbook for the Austrian economists (Böhm-Bawerk, Mises, and Hayek in particular) who followed him.

Menger began his formulations with a stress on methodology. He treated economics as a science: "The phenomena of economic life, like those of nature, are ordered strictly in accordance with definite laws." The purpose of the study of economics is to understand "the *conditions* under which men engage in provident activity directed to the satisfaction of their needs." Due to the scarcity of available means, especially time, but also labor and resource goods, individuals must choose which ends to attempt to satisfy. Menger calls this choosing "economizing" and focuses his study on the economizing individual.

Value theory is central to economics: What gives a thing value? Is value intrinsic to an object, as early economists surmised? No, replies Menger, because "goods of the same kind and in the same place lose their economic character with changing circumstances." Is the value of a good related to the amount of labor required to produce it, as Ricardo thought? No again, says Menger, for "experience tells us that many goods on which no labor was expended display economic character whenever they are available in quantities that do not meet our requirements."

Menger concludes that the value of goods "is entirely *subjective* in nature." He continues: "Value is thus nothing inherent in goods, no property of them, nor an independent thing existing by itself. It is a judgment economizing men make about the importance of the goods at their disposal for the maintenance of their lives and well-being. Hence, value does not exist outside the consciousness of men."

Contained in the previous passage is what Israel Kirzner calls Menger's Law. It is an important aspect of Austrian economics. The value a person attaches to a good at his disposal is based upon the value he places on the end it will enable him to satisfy. If certain goods cannot in any way satisfy a person's ends, he will not attach value to those goods. If, however, someone lacks only one good that is necessary to satisfy a specific end which presently is valued more than any other end, and if no substitutes to that good are available, the value he attaches to the good (the means to his end) will be considerable.

From Menger's Law it follows that resource goods and producer goods are valued according to the value of the ends they serve. Furthermore, the ends they will ultimately serve are determined by the consumer. Therefore, the consumer is the source of value and the guiding force in a market economy. Austrian economic thought places consumer demand in the role of guiding the production in an unhampered economic system.

Although Menger is acclaimed primarily for his role in developing what is now known as "marginal utility" theory, his writings on methodological individualism, subjective value, and the economic character of goods (Menger's Law) deserve more attention. His *Principles* is so lucid and understandable that it can serve as an introduction to economics for the intelligent laymen with no background in the subject. This new edition, with an introduction by F. A. Hayek, should guarantee that the work that has served as the basic text of successive generations of Austrian students and scholars will continue to improve economic understanding for years to come.