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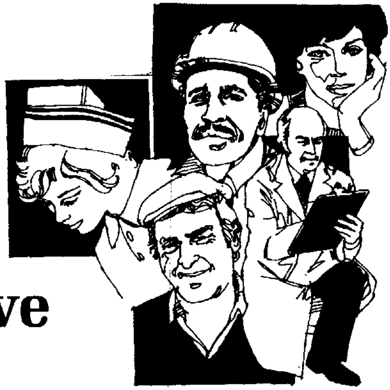
Clarence B. Carson

A Question of Being Productive



If we must have statistics (a doubtful proposition), and if there must be a Bureau of Labor Statistics to collect, collate, and expound them (equally doubtful), it strikes me that there are potential statistics of considerably greater economic import than those being bandied about by the Bureau. The best known of the Bureau's calculations, of course, are those dealing with unemployment. Although they are less likely to get much notice from the media, the Bureau also releases figures from time to time on the number of people who are employed. The Bureau must compile other interesting tidbits, otherwise it probably would not qualify for such exalted status among government undertakings, but those items rarely attract attention.

Although the best I can do amounts to no more than lukewarm support for any of them, this is not intended as an attack on statistics, *per se*. Still, it might be well to point out some of their shortcomings at the beginning. The most general objection to statistics is that they are reductionist in character. That is, statistics are compiled by lopping off all the individual ways in which things differ from one another to arrive at their common traits. What emerges is almost inevitably a lowest common denominator for all of them. All too often, too, the common feature is the least revealing and least important aspect of what is being categorized.

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Take the matter of statistics on unemployment. When they are reported in the media, they are made to sound as if they were absolute numbers. We may be told, for example, that during the past month there were 8,250,000 unemployed in the United States. The figures are further broken down into percentages for cities and regions. For example, the Bureau may announce that 12.7 per cent of the work force in an area was unemployed. That sounds precise, exact, certain, and beyond doubt. This apparent precision is achieved, however, by the extension of figures collected in surveys, by the acceptance of self-serving claims, and by the adoption of a convenient fiction.

Lumping into Groups

The convenient fiction concealed in unemployment statistics, let me hasten to explain, is that there is such a thing as a completely, or totally, unemployed person or that if there is, they are very numerous. It is conceivable, of course, that there are some persons who spend their waking hours seeking jobs: going over want ads, writing letters of application, making telephone calls, going to places of employment to get on their lists, and so on. It is even conceivable that some people might do this for as much as several weeks or even longer. But that such people exist by the millions in the United States is a fiction which is able to parade as fact only by lopping off large portions of reality.

Among those listed as unemployed are those for whom the status is essential for them to continue to draw unemployment compensation. Their claims to being unemployed are self-serving. That is, they expect to benefit from the acceptance of the claims. In fact, many of them are working, part time or full time, for themselves or someone else. The Internal Revenue Service has announced, even, that the number of those who are working at something, or something extra, and not reporting their incomes is legion, and that their earnings may amount to several hundred billions annually. Many of these are undoubtedly listed as unemployed.

It is not my point, however, that the category, unemployed, is meaningless. There are undoubtedly many people who do not have regular employment for which they receive a regular and predictable paycheck. There are those who have difficulty finding employment in their profession or trade. There are some who would consider themselves partially or temporarily employed, when employed at all. The figures of the Bureau of Labor Statistics may even reflect, roughly, the fluctuations in all of this. My point is that the reality is much less precise than the statistics suggest, or declare, and that the condition is rarely the one that is sentimentalized for the popular imagination.

But the labor statistics duality of employment-unemployment has at least two other major difficulties peculiar to it. One is that it leaves out of account a considerable portion of those with whom it might be expected to deal. It not only fails to account for the whole population, but also leaves out of account a portion of the potential work force, whatever that may be taken to mean. To put it more directly, the employment-unemployment figures do not balance with the population figures. Suppose, for example, that we are told in a report that there are 112½ million people employed and 8½ million unemployed. That adds up to 121 million. But if there are 230 million people, say, in the United States, 109 million of them are missing from the statistics. Undoubtedly, they can be placed in this or that or the other category, but they are still in an employment-unemployment limbo.

Misleading Categories

The other difficulty, too, tends to disqualify the dual employment-unemployment category. The trouble is that it is not a very apt economic category, if it is an economic category at all. It does not tell us anything much that is applicable to economics. Economics has to do with the effective use of scarce resources—i.e., land, labor, and capital—so as to provide those goods that are most wanted. Employment and unemployment figures may appear to get at that, but the appearance is deceiving. Whether those who are employed are aiding in the economic endeavor is not revealed. As to the unemployed, the statistics themselves are silent on the impact on the economy.

What is wanted, it seems to me, are some different categories, categories which embrace the whole population, which are economic in focus, and which are more nearly self-explanatory. (If the new categories present problems of quantification, they will not differ in that from the present ones. The distortions in statistics are inherent, hence, unavoidable.) Since the production and distribution of goods is the main concern of economics, it would be quite appropriate to have the categories concentrate on that rather than employment and unemployment.

Therefore, the following three categories are hereby nominated as replacements: (1) the Productive, (2) the Unproductive, and (3) the Counterproductive. Everyone falls in one or the other of these categories, or some variant of it. The categories are unquestionably economic in character. Classifying people according to them poses no greater difficulty than those in use. Above all, the third category, a highly important one, gets entirely ignored in the present classification.

The Productive

The Productive consist of those who produce the goods on which they live. They may produce the goods for themselves or for sale in the market, or, what is most common, some combination of these. No distinction need be made between goods and services, and the provision of a service is here considered as the production of a good. Thus, the housewife is as much the producer of a good when she prepares a meal or vacuums a room as when a factory worker contributes to the production of a widget. The crucial distinctions pertain to whether or not what is produced or provided is an economic good and whether or not what is produced constitutes what they live on. The productive, then, provide their own livelihood, either individually or as a family, and they do so with the goods they produce, whether they consume or sell what they make.

It might be well to emphasize, too, since such distinctions have sometimes been made, that those included in the productive category may do work that is predominantly physical or mental, may be employed by others or work for themselves, may work on assembly lines or be presidents of corporations, may be doctors, nurses, homemakers, farmers, miners, millers, butchers, bakers or candlestick makers. None of these distinctions matters in the determination of whether or not anyone is productive. Nor does it matter whether the productivity was in the past or is going on in the present. That is, those who are living off savings, a surplus from past productivity, have a residual claim to be classified as productive.

The Unproductive

The Unproductive consist of those who do not (or did not) produce the goods on which they live. This is a hodgepodge category. One of the categories had to be if everyone was to be fitted in somewhere. It includes the partially productive as well as those who produce nothing. It overlaps with the third category. That is, some people would fall in both categories logically, though since the counterproductive is the stronger category, those who fall there basically need not be listed among the unproductive.

Since the Unproductive category is so diverse in its makeup, those who fall into it should probably be divided into sub-classes. The partially productive might well be distinguished from the wholly nonproductive. This latter class would include infants and small children, students (not otherwise employed), the aged infirm, the temporarily unemployed, and so on. A more controversial sub-class would consist of those who are fully employed but economically unproductive. Among these could be listed such pursuits as those of the police, full time politicians, judges, soldiers, bureaucrats, and the like.

These categories are not devised to reflect on the importance of some occupations *vis á vis* others or for the purpose of making moral judgments. I take it that the police perform vital functions, even functions that make possible more effective economic activity. So it may be with soldiers, politicians, and some of the others. Students may be preparing themselves to be more effective at their work in the future. It is no reproach to infants that they are not economically productive. My intent here is to describe, not prescribe or proscribe. The point is that policemen, as policemen, students, as students, and so on, are not economically productive. Nor, though these categories do emphasize production, do I mean to suggest that production is the only or most important of human functions.

Shifting Categories

But place it where you will in your scheme of valuation, there can be no reasonable doubt that production is essential to our lives and well-being. Nor are there any plausible grounds for doubting that all who continue to live are dependent for their livelihood on what is produced. Moreover, they either produce it themselves or get it from that which is produced. More succinctly, the unproductive must be provided for from the labors of the productive, or, if you will, from the land, labor, and capital of the productive.

Thus, the changing proportions between the productive and the unproductive are of more than passing interest. Such evidence as we have indicates that the proportion of the unproductive to the productive has been increasing over the years. No statistics are available for this, but there are statistics and there is evidence which provide clues. Probably, at the time of the founding of the United States as much as 80 per cent of the population was productively employed much of the year. Most people lived on farms, and only infants, very small children and the bed-ridden were excused from work ordinarily. In towns and cities, too, the young usually went to work as soon as they were able to do much, and worked until they were no longer able. Most of this work, of course, was performed by families.

By contrast, the National Taxpayers Union said a while back that there are "only about 50 million real taxpayers left. The rest of our people are living off of recycled government money—federal payroll, pensions, grants, contracts, loans, subsidies, revenue sharing. . . ," and the like.

While that does not absolutely distinguish the productive from the unproductive, it gets close to it, and it may suggest that something less than one-fourth of the people do the bulk of the work. (The major distortion in these figures is that housewives do not pay taxes in connection with that endeavor but, in my view, are productive.)

The Counterproductive

Even so, the Counterproductive may be a much more important category in many respects than the unproductive. The counterproductive are those who place obstacles in the way of those who would be productive. Although it would be interesting to know the number of them and whether they are actually increasing in proportion to the population or decreasing, it must be admitted that their impact on society is much greater than their numbers. Indeed, many of those who would have to be classified as unproductive are in that category because of counterproductive forces. I say "forces," because the counterproductive are not just people, but people acting with force.

Who would be classified as counterproductive? Let me begin with two important sub-classes in the category. One is made up of those who criminally obstruct production and interfere with commerce. Among them are thieves, embezzlers, saboteurs, terrorists, extortionists, intimidators, and all who make freedom of movement and commercial activity difficult. Crime deters all peaceful undertakings, and crimes of violence have been on the upsurge generally for years now.

The second sub-class of the counterproductive is labor unions. The most dramatic activity of labor unions in obstructing production is the strike. Strikes often stop all production in a factory, sometimes an industry, and often interfere with (when they do not shut down) related businesses. Boycotts can have similar results. More broadly, though, virtually the whole power of unions derives from their ability to hamper production. They do this not only by strikes, boycotts, and violent activities but also by slowdowns, by work rules restricting production, by featherbedding, by specifying the limited types of work which may be assigned to a given job, by minimum wages, and by time-consuming meetings and negotiaton sessions.

But the greatest and most extensive obstacles to production in the United States today are placed there by governments. It has already been noted that most, if not all, government activity is unproductive. That is, the basic business of government is not the production and distribution of goods. Beyond that, though, much of government activity today is counterproductive. This has not always been the case. In 1840, say, very little of government activity was counterproductive. The United States government did levy a tariff on imports, and, though it was not high, it may have limited some kinds of commercial activities. Beyond that, state and local governments would have had some restrictions, but they were usually minor. In the twentieth century, however, there have been mounting regulations, restrictions, inhibitions, limitations, and prohibitions on productive activity by all levels of government.

Away from the Productive

In one way, at least, all government undertakings tend to be counterproductive. So far as they are supported by taxation, wealth is taken from its potentially productive use to an unproductive use. That is counterproductive. It follows, too, that all expansion of government activity tends to increase the unproductive sector at the expense of the productive. Thus, the growth of government tends to be counterproductive in its impact. This is not meant to suggest that there may not be legitimate reasons for an increase in the size of government. Rather, it is to point out that in respect to taxation, at least, the economic impact is away from the productive.

But much of government activity today is counterproductive, the financing of it aside. The most obvious of the counterproductive impact occurs when people are prohibited to be productive. The most striking example of this is child labor laws, which prohibit children from engaging in most productive efforts. Compulsory schooling, which is a counterpart to this, pushes children into the unproductive category, willy-nilly. Government encouragement of schooling, or retirement, and such like, is also counterproductive. It is also obviously counterproductive when government deliberately restricts production, as in crop restrictions, marketing quotas, or any other device for holding down production.

Minimum wage and maximum hour laws are also counterproductive. Minimum wage laws are counterproductive because they tend to price the unskilled, the partially disabled, and the less productive out of the labor market. Maximum hour laws are counterproductive in two ways. Where they actually reduce the number of hours that can be worked at a job, as for commercial pilots, flight attendants, truck drivers, and others, they may reduce production directly. In many instances, however, maximum hour laws are not absolutely prohibitive; they only require higher pay for hours above a certain maximum. This has a similar counterproductive impact to that of the minimum wage.

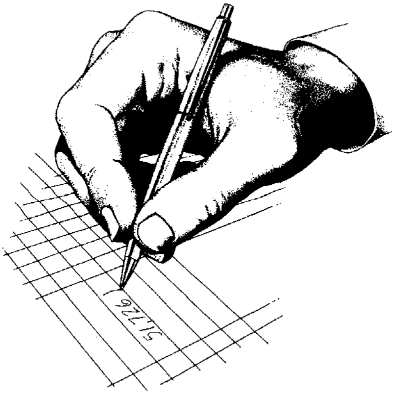
Anything that hampers or makes production more difficult is counterproductive. Licenses, franchises, schooling requirements for occupations, government granted monopolies, and restrictions on entering any field of endeavor are counterproductive. Government regulatory activities, such as are carried on by the Interstate Commerce Commission, Federal Trade Commission, Food and Drug Administration, Occupational Safety and Health Administration, Environmental Protection Agency, and many others, are counterproductive. All business and personal record keeping for government, such as employment records for the Equal Employment Opportunity Commission, are counterproductive. So, too, are all business tax collection for or payment to government, such as Social Security, unemployment compensation, sales taxes, withholding taxes, and so on. They require the use of time and energy for government, which is unproductive, rather than the use of them for production.

Among the sorts of people who would be counterproductive, either part or full time, would be inspectors, enforcement personnel, administrative law personnel, judges (while enforcing regulations of production), Justice Department officials, politicians and their aides (while considering and enacting such laws), and the numerous bureaucrats that have something to do with them in one way or another. Whether all business personnel directly involved with looking after the regulatory and other hampering activities should be classified as unproductive or counterproductive is an interesting question.

No effort has been made here to evaluate from every angle all government programs which hamper production. Whether this one or that one or the other might be justified on adequate grounds was not my concern. Rather, I proposed to look at the matter only from the perspective of the question of being productive. That does not mean, of course, that production is all that matters. In that regard, my point is that production matters, that it is important, that it should be taken into consideration.

Nor was it my purpose, ultimately, to spur the issuance of statistics on whether people are productive, unproductive, or counterproductive, though I think they would be interesting and revealing, if it could be done. Rather, by delineating the categories in some detail, it was my hope to focus attention on whether people are productive, unproductive, or counterproductive in their undertakings. Our livelihood and well-being depend upon the weight of the answers to this question.

Bill Anderson



DEFICITS ARE NOT THE ONLY PROBLEM

PITY the poor Federal deficit. What was once hailed as a western economic savior has been relegated to a public whipping boy. Politicians and liberal economic writers who a decade ago declared that deficits were "actually desirable because this meant the federal government was pouring funds into the economic stream" now declare with equal sincerity that these same fiscal shortfalls are a menace to economic growth.[1]

How, an astute observer of our political economy might ask, can the Federal deficit have fallen into such disrepute, especially among its onetime supporters? Did not Keynesian economists tell us in triumphant words that the so-called capitalist problems of boom and bust were to be solved by government fiscal policy of which the deficit was an integral part?[2]

Consider one economist's claim that the 1964 Federal deficit was a "desirable" element of the nation's economy.

> The basic explanation for our achievement (a prosperous economy), I think, is that, in 1964, our politicians finally "grew up" into mid-20th century fiscal policy thinking. As a result, there was nothing less than a revolution in economic thought at the highest policy-making levels of our government.
>
> In the past, our politicians have always considered it imperative to hail an annually balanced budget as economic purity, to condemn a budget deficit as fiscal sin, and to shrink from tax reduction in the face of budget deficits as unspeakably reckless. But in 1964, the federal budget deficit was accepted as actually

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desirable because this meant the federal government was pouring funds into the economic stream, and this money would help lift us to levels of full employment and full use of our great industrial capacity.[3]

One is hard pressed today to find a description of the present Federal deficit made in such hushed, reverent tones. But, then, the numbers have changed as well. In 1964, the Federal deficit to which Ms. Porter attributes such sterling results as "full employment" and "full use of our industrial capacity" was $5.9 billion, or roughly five per cent of the total budget.[4] The *proposed* Federal deficit for the coming year (and remember, proposals usually fall way short of real spending) is about *$100 billion,* nearly 15 per cent of the tentatively-approved U.S. Government budget. Even allowing for the galloping inflation since 1964, the present numbers are clearly out of hand. The "harmless" (or helpful, depending on one's point of view) deficits of two decades ago have grown into what seems to be an uncontrollable monster.

The problems resulting from the size of the Federal deficit are not in dispute. For example, in 1965, when President Lyndon Johnson greatly expanded domestic Federal spending, the U.S. Treasury took approximately 18 per cent of available funds from the nation's credit markets. Today that number stands at nearly 80 per cent. Funds for investment, our economy's seed corn, are being devoured at an alarming rate which can only spell out a real decrease in standards of living for most Americans. Rates of inflation, though recently somewhat diminished, have severely depreciated the dollar, caused malinvestment and brought about economic decline.

The Real Issue: Spending

But the real issue of the Federal budget is lost in a semantic word game which, at best, diverts people's thoughts from the main sickness—that being Federal spending—to deficits, which are only a symptom of the disease. This is not to say that budget shortfalls are not dangerous. They are. But when one simply concentrates on condemning the deficits while ignoring the dangers of government overspending, it is, to paraphrase the New Testament, straining at a gnat and swallowing a camel.

A recent editorial of a nearby major metropolitan newspaper demonstrates this kind of naivete. In the editorial, titled "Tax Hike or Recession," the writer accurately noted that the shortfalls would have to be covered either by creation of fiat money—and thereby inflation—or by Federal borrowing from hard pressed credit markets. Both "solutions," he pointed out, would effectively raise interest rates and limit capital expenditures.

His solution? Raise taxes, of course. Thus, he indicated, the deficit would be eliminated in this relatively painless manner, interest rates would fall and the economy would recover. The only barrier to prosperity, he reasoned, was the lack of courage by politicians to reverse the tax cuts they had given us last year.

This editorial writer has not been the only one to endorse tax increases as the way to solve the budget problems. Radio and television commentators, both liberal and conservative politicians, and economists who should know better have also jumped onto this short-sighted bandwagon declaring that tax increases are the only way to prosperity. But they ignore the fact that *deficits* are only a *symptom*. The *disease* is *too much spending*.

None of the Alternatives Is Acceptable

When the Federal budget is discussed on the news, the ultimate point of discussion is the proposed $100 billion deficit. Few commentators—and economists—ever discuss the gargantuan size of the Federal budget. This year Federal spending will most likely exceed *$800 billion.* The official Federal debt is more than *one trillion dollars.*[5]

But why, one might ask, is it not better to tax in order to curb deficits than to borrow or print money? After all, the perils of inflating are widely known even to the most economically illiterate persons, while excessive Federal borrowing not only "crowds out" capital but also diverts money from productive uses to nonproductive ones. The answer is that none of these "alternatives" is acceptable.

While past budget deficits were often run deliberately in order, as Ms. Porter writes, to pour "funds into the economic stream," there is plenty of historical evidence to show that governments inflate even when their budgets are officially balanced. During the 1920s, as Economist Murray Rothbard has noted, the U.S. Government raised the money supply by nearly 62 per cent in the face of balanced Federal budgets.[6] From 1977 to 1980, the nation of Colombia suffered an annual increase in inflation of more than 25 per cent, despite the fact that its tax revenues exceeded government expenditures.[7] The problem here is not deficit spending, but rather *government monopoly over the supply of money*. Governments may use deficits as an excuse to print money, but when government controls the "creation" of money, any reason will do.

Nor would increased taxation eliminate government borrowing, either at local or Federal levels. As long as governments continue to involve themselves in enterprises beyond protection of citizens' life and property, there will always be dams to build, school buildings to erect, canals to dig and individuals to support. Such multi-million (and billion) dollar ventures require vast sums of capital which can only be borrowed.[8] Thus, deficit or no deficit, governments will continue to suck capital from private markets in order to fund projects that could be handled more efficiently and with less expense by the private sector.

One is left, then, with the question of taxation. The issue is not, as many "born-again budget balancers" have declared, choosing "less-painful" taxation above borrowing or inflation. Increasing taxes to balance a budget is not a panacea for our economic ills, as many would tell us. Consider economist Alan Reynolds' warning.

> In the depths of the Great Depression, Wall Street and the financial editors agreed that restoration of confidence required a balanced budget. In 1932, the Hoover administration complied by signing the biggest percentage increase in tax rates in peacetime history. Needless to say, that did not strengthen the economy, calm financial markets or balance the budget.[9]

Unseen Consequences

People are often short-sighted on the evils of heavy taxation. They can *see* the credit markets being drained of capital by the government. They can *see* the leap in prices as inflation takes hold on the economy. But taxes go beyond their visual effects. One can see public treasuries fill up with tax revenues. What is *not seen,* however, is the *loss* of funds that might have gone into capital markets, the *loss* of potential investments, the real *loss* of income for individuals who pay huge portions of their earned income to government. Money that might have been invested in profitable, wealth-creating projects is used, instead, for government consumption. To increase the level of taxation would not enhance investment opportunities. Indeed, to confiscate revenue through taxation is no better than to devour it straight from the markets or to print it on the printing presses at the Bureau of Printing and Engraving. The damage done to the economy will not be lessened by choosing taxation over borrowing or printing.

Heavy taxation also encourages people to take their income from productive investments—which often fall in the reach of the Internal Revenue Service—and place them in less productive tax shelters. Again, this problem is an invisible one, since people cannot see the factory that was not built, the invention that was not marketed or the entrepreneur's dream that was unfulfilled.

No doubt, as Reynolds writes, the Federal budget, all $800 billion of it, could be balanced as "a matter of sheer bookkeeping."[10] He points out:

> . . . we could probably balance the U.S. budget by disarming, or by doubling the

corporate tax, or by confiscating all income above $50,000 a year. In practice, any of these options would probably destroy the country.[11]

Intervention Brings Stagnation

Economic stagnation is not the price of "curing deficits." Rather, it is the price the people of a nation must pay when its federal government spends far more than its citizens can afford, taking from Peter to give to both Paul and Peter—minus a hefty commission.

This is not to say that budget deficits are not a problem. They are. But the issue at hand in discussing deficits is not just bookkeeping, but also ignorance and arrogance. Since the 1930s economists have promised that budget deficits will permit politicians to circulate new money into the economy, thereby "spreading the wealth," and politicians have eagerly obeyed. But, as a decade of runaway inflation has demonstrated beyond a doubt, dumping fiat money into an economy creates only the illusion of wealth, not wealth itself.

Since deficits became a staple of government fiscal policy, people have deceived themselves into believing that increased prosperity, the rise in real income, and a rising standard of living were due to their politicians' spending more than was taken in taxes.

But as deficits have widened and seemingly run out of control, it has been equally deceptive for people to believe that prosperity will return as soon as the books are balanced. Prosperity will return only when citizens stop demanding their governments give them a standard of living that they cannot themselves produce, as individuals acting within the free market.

—FOOTNOTES—

[1]Sylvia Porter, "Focus on the Economy," *The World Book Year Book*, 1965, p. 27.

[2]Austrian economists, particularly von Mises and Rothbard, have conclusively demonstrated that government monetary policy is usually the *cause* of boom and bust cycles. It can hardly be expected, then, that erratic fiscal policies can somehow solve the very problems they create.

[3]Porter, p. 27.

[4]Source: *Statistical Abstract of the United States, 1980*. The federal budget in 1964 was approximately $118 billion.

[5]Economic writers such as Irwin Schiff and others have estimated that the liabilities of the Federal government are up to 10 times greater than the officially-admitted debt.

[6]Murray Rothbard, *America's Great Depression* (Kansas City, 1963), p. 86.

[7]Alan Reynolds, "That Budget Deficit Is Not the Problem," *Wall Street Journal*, October 5, 1981, p. 28.

[8]Contrary to what some may believe, governments usually pay for public projects with borrowed money. The payments are paid back with tax revenues (except in the case of New York City in 1975, which paid back borrowed funds with more borrowed funds).

[9]Reynolds, p. 28.

[10]*Ibid.*

[11]*Ibid.*

Dennis Bechara

The Development of Puerto Rico

THE DEVELOPMENT of the Puerto Rican economy sheds light on the true causes of economic growth. The history of the island's development is peculiar to it, but the policies implemented in Puerto Rico to achieve progress hold universal appeal. A review of the economic situation since the turn of the century may help us grasp the lessons of the Puerto Rican experience.

Historical Background

As a result of the Spanish-American War, the United States assumed jurisdiction over Cuba, Puerto Rico and the Philippines. Subsequent events led to the political independence of Cuba and the Philippines, but the relationship between Puerto Rico and the United States continues.

Economic conditions were dismal in Puerto Rico at the turn of the century. Life expectancy in 1900 was 32 years. The literacy rate at the time was only 15 per cent. The island's economy consisted of subsistence agricultural efforts. The production of coffee, once one of the island's most successful crops, began to languish when access to the Spanish market was lost.

The nature of the political relationship between Puerto Rico and the United States began to change as Congress gradually granted more autonomy to the island. In 1917 American citizenship was granted to Puerto Ricans and certain measures of self-government were enacted. The President, however, continued to appoint the governor and it was not until 1948 that the people were allowed to elect one.

In 1952, Congress approved a Puerto Rican-drafted constitution, and the island became known as the Commonwealth of Puerto Rico.

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Puerto Ricans are allowed to elect a non-voting member of Congress. Though they are citizens, they are not allowed to participate in Presidential elections.

The Sugar Economy

One of the immediate effects of the Spanish-American War was to place Puerto Rico within the U.S. tariff wall. In 1870, Congress had enacted a tariff to protect domestic producers of beet sugar, and this had the effect of driving many of the island's sugar producers into bankruptcy. Once the United States acquired jurisdiction over Puerto Rico, however, there was free trade between the two. Capital flowed into Puerto Rico with the effect of modernizing its sugar processing mills. A glance at the production figures illustrates the magnitude of sugar in the Puerto Rican economy. In 1899, approximately 40,000 tons of sugar were produced, whereas in 1934, Puerto Rico produced approximately one million tons. By 1940, the sugar industry employed one-fourth of the labor force. "Sugar . . . paid the major part of the insular taxes, employed the major part of its workers, created the major part of its business, supported seventeen of Puerto Rico's twenty seaports in the sense that those seventeen handled sugar exclusively and had no warehouses or other facilities for anything else."[1]

In spite of its importance in the island's economy, sugar became the subject of many attacks. Puerto Rico was not immune to the ravages of the Great Depression. The island, which was poor to begin with, had made some progress but it was nevertheless insufficient to drastically change matters. The rise of the sugar industry, however, provided the scapegoat upon which to blame the poor conditions of the island.

There is no doubt that Puerto Rico, during this time, was impoverished. Theodore Roosevelt, Jr., who in 1929 was governor of the island, wrote the following in *The New York Herald Tribune:* "We were and are a prey to diseases of many kinds. In the fiscal year ending June 30, 1929, 4,442 of our people died from tuberculosis. Our death rate from this disease was 4½ times the death rate in the continental United States. Our death rate from malaria was 2½ times the rate in the continental United States. Some 35,000 people in our island are now suffering from tuberculosis, some 20,000 from malaria, and some 60,000 from hookworm."

The prevailing conditions during this period of time, however, were not unusual given the historical background of Puerto Rico. To put the blame on the sugar industry for conditions which existed before sugar became the most prominent industry is glaringly unfair. The island, moreover, did make strides in many areas during this time which benefited the entire population. As an example of this, life expectancy had risen to 42 years in 1930 and 46 years in 1940; economic conditions had improved concurrently with these developments.

Stumbling Blocks Erected

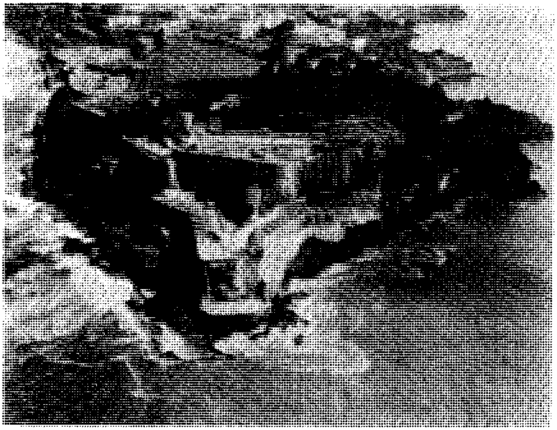
The sugar industry confronted its first obstacle when in 1934 Congress enacted the Costigan-Jones Act. This statute empowered the U.S. Secretary of Agriculture to administratively determine the sugar consumption requirements of the country and to set production quotas from the different areas that supplied sugar to the U.S. market. A consequence of this statute was to freeze the growth of Puerto Rico's sugar industry. This, coupled with future land reform, served to cripple the industry permanently.

During the later part of the 1930s, public discussion revolved around the low wages paid by the sugar industry as well as by the industry's large landholdings. In 1937, for example, the average hourly wage rate of agricultural employees in the sugar industry was 12 cents. This was thought to be convincing enough evidence to condemn the industry, and served as a justification for the government's continued intervention. Yet, the Bureau of Agricultural Economics reported the average hourly wage rate for agricultural employees for that year in Puerto Rico to be higher than prevailing farm wage rates in fourteen states.

Another of the perceived evils of the sugar industry was its alleged displacement of thousands of farmers who became unable to support themselves after losing control of their land. The statistics concerning land ownership, which are mentioned below, are sufficient to refute this. However, it should be pointed out that as a result of the implementation of modern sanitation and health practices, the island's population nearly doubled by 1930. Even had the sugar industry not flourished, it is doubtful that the island would have been able to be agriculturally self-sufficient. In fact, now that land has been redistributed in order to curb these alleged injustices of the sugar industry, the island is still not agriculturally self-sufficient.

Land Reform

As a result of the desire to uproot the perceived evils of the sugar industry, a land redistribution program was enacted in 1941. During a frenzied period of time, the Land Authority, the administrative agency empowered to take over all corporate lands that exceeded an arbitrary 500 acre limit, acquired thousands of acres and either administered the land on its own or subdivided it into smaller plots and transferred them to those deemed



The old Spanish fort "El Morro" in San Juan's outer harbor. Begun in 1539 and completed over a period of two and a half centuries, the fort was one of the principal bastions of the Spanish Empire in the New World.

deserving. By 1950, the Land Authority had "acquired nearly half the corporate holdings in excess of 500 acres and was operating 48 proportional-profits farms, as well as two sugar mills."[2]

Why corporate holdings in excess of 500 acres were repugnant may be traced to a Congressional Resolution pertaining to the Foraker Act of 1900, which established Puerto Rico's position with regard to the federal government. Under this federal statute, Congressmen expressed a fear that Puerto Rico's inclusion within the U.S. tariff system would encourage corporate holdings by the sugar and tobacco "trusts" that would dwarf the local population. Consequently, Congressional Resolution No. 23 of May 1, 1900 was enacted whereby Congress expressed its displeasure about the matter. Years later, an energetic politician, Luis Muñoz Marín, who was later to become Puerto Rico's first popularly elected governor, campaigned on a platform of enforcing this Congressional Resolution.

True, in order for the sugar industry to efficiently compete and produce, it was altogether necessary for modern sugar processing equipment to utilize large holdings of land in order to lower the unit costs of raising sugar cane. As a result of this, the average yield per acre increased from a half a ton of sugar per acre in 1899 to 3.3 tons of sugar in 1937.

According to the U.S. Soil Conservation Service, Puerto Rico has a total of 2,103,000 acres, of which, 1,222,284 are tillable. The four largest sugar corporations controlled, before 1941, an estimated 166,000 acres, which represented less than 20% of all tillable land. If one investigates the available data more deeply, one can discover the astonishing fact that in 1899 there were 39,021 farms in Puerto Rico whereas in 1935 the number increased to 52,790. In 1910 there were 539 farms which exceeded 500 acres, whereas in 1938 the number had decreased to 335. On the other hand, farmland with an area of no more than twenty acres had increased during this same period of time from 38,274 to 42,004, which represented over three quarters of all tillable land.[3]

However convincing these statistics may be, when confronted with an emotional "share-the-wealth" argument, the downfall of sugar became inevitable. No sugar mill was able to compete efficiently with a 500 acre limitation. Interestingly, in recognition of this, the government's position after acquiring all of those landholdings was to drastically reduce the scale of any further significant land expropriations. But by then the damage was done. Sugar never recovered from these setbacks. One by one all of the sugar mills in Puerto Rico either closed or declared bankruptcy. Naturally, in the 1970s the government, recognizing sugar's importance to the economy, stepped in and created a government agency called the Sugar Corporation which leased some of the mills and proceeded to run them on a profit and loss basis. Predictably, the Sugar Corporation has succeeded in amassing substantial losses, at the present totalling more than $600 million dollars.

Collectivist Influences

The long term effects of the Great Depression are still being felt in Puerto Rico. As a result of the New Deal's welfare-oriented policies, the Puerto Rican economy became the object of governmental intervention with land reform as only one of its consequences.

In 1933 the Federal government created the Puerto Rico Emergency Relief Administration, which by 1935 became the Puerto Rico Reconstruction Administration. This agency was endowed with an operating yearly budget of $40 million with which it began social experimentation.

One of the PRRA's first activities was to purchase a sugar mill owned by a French corporation, called the Lafayette *Central* and proceeded to operate it as a model plant. As is usually the case whenever government operates a business, this did not prove to be profitable. Subsequently, the agency proceeded to subdivide the 10,000 acres it had purchased and to let the farmers who acquired these lots run the mill as a cooperative. Once again, the experiment proved to be a failure and the mill ceased to operate.

But the efforts of the PRRA went beyond operating a cooperative farm. The agency commenced building subsidized housing and built a cement manufacturing enterprise and a hydroelectric system. The agency became defunct by 1939 and most of its projects floundered. However, it set a pattern future island governments would follow.

Fair Labor Standards Act

In 1938, Congress extended the Fair Labor Standards Act to Puerto Rico. The immediate effect of this law was devastating. The U.S. Commerce Department, certainly no enemy of the minimum wage law, admits this in its 1979 *Economic Study of Puerto Rico:* "Significant job losses followed the introduction of Federally mandated minimum wages on the island, the most serious being a drop in home needlework exports from $20 million in 1937, to $5 million in 1940."[4]

As a result of the devastating effects of the minimum wage law in Puerto Rico, Congress approved an amendment, in 1940, whereby industries operating in Puerto Rico were allowed to pay wages below the federally mandated minimum, and tripartite committees, which represented industries, unions and the government, were set up to periodically upwardly revise the mandated minimum wages.

Parallel with this development, the island's government proceeded to enact provisions for mandatory paid vacations, sick leave and other conditions of employment to be applicable on an industry-by-industry level. The justification for this was that since the federal minimum wage was not completely applicable to Puerto Rico, local legislation was needed to supplement this measure.

Subsequent amendments to the Fair Labor Standards Act, however, have eliminated the exemption granted to Puerto Rico. As of now a substantial amount of industry which affects interstate commerce in Puerto Rico must comply with the provisions of the Fair Labor Standards Act. The mandatory decrees instituted by the Puerto Rican government to grant vacations, sick leave, and other conditions of employment, however, have not been abolished. Instead they continue to be amended in order to raise the benefits conferred therein. In addition to this, the Puerto Rican government has subsequently enacted provisions requiring employers to pay maternity pay, dismissal pay, nonoccupational disability coverage as well as a mandatory Christmas bonus.

The economic consequence of this so-called social legislation has been to raise the cost of hiring employees with an inevitable high unemployment rate. Unemployment has consistently been in the 10 to 12 per cent range during the past forty years. Presently, the unemployment rate exceeds 20% while the rate for those in the 14–24 age group is nearly double that figure.

Rexford G. Tugwell

In 1941, President Roosevelt appointed Rexford G. Tugwell governor of Puerto Rico, and with this appointment the welfare-oriented policies initiated by the Roosevelt administration took hold in Puerto Rico at a dizzying speed.

Tugwell's administration truly revolutionized the island, as he took an active part in the drafting of interventionist policies which have held Puerto Rico captive to this day. Under his leadership, countless statutes were enacted which followed and even exceeded in their zealousness the tenets of the New Deal.

Tugwell's administration was influenced in part by World War II, which had a substantial economic impact on the island. This was so because as the production of whiskey was curtailed in the continental United States by the federal government, the sales of Puerto Rican rum in the mainland soared. As part of the Organic Act that governed Puerto Rico's relationship with the United States, it was specified that all excise taxes collected in the mainland from any products originating from Puerto Rico would be returned to the Puerto Rican treasury. This meant that during the course of World War II the Puerto Rican treasury received a bonanza in excess of $160 million. As Henry Wells, author of *The Modernization of Puerto Rico,* put it:

> During 1940–41 the Puerto Rican government received only $4.5 million from federal internal-revenue payments, but a year later it got $13.9 million. Enemy interference with shipping in the Caribbean during 1942–43 held the federal payments to $13.6 million, but with the resumption of more normal trade in 1943–44 the amount turned over to the insular treasury came to a phenomenal $65.9 million. After that peak year the mainland thirst for Puerto Rican rum slackened and federal excise-tax yields declined accordingly, but in 1944–45 the insular government still received $38.6 million, and $35.3 million the following year.

The funds available from the rum excise tax served to finance many projects which were commenced after the War ended. According to Earl Hanson:

> Puerto Rico's budget, which before 1940 had been around $22,000,000, shot up to as high as $150,000,000; with such funds the government could build factories, purchase lands held in excess of five hundred acres by the sugar corporations, provide machinery for the working and distribution of those lands, stimulate its public-health service, implement its new social legislation, foster co-operatives, and engage in all the multiple activities of a stricken society reshaping itself . . .

Government Agencies Assume Role in Economy

During Tugwell's tenure, numerous government agencies were created which in turn assumed an active role in the economy. Among these were the Development Company and the Development Bank. Under their leadership, the government acquired the cement company which had been founded by the PRRA, as well as a pulp board factory, a paper company, a glass factory, a clay products company and a shoe company.

The experience of government handling and management of all of these enterprises, however, was very disappointing to the planners; eventually, by 1951, all were sold to private enterprise. This decision was motivated by the fact that those enterprises were inefficient, incurred losses and created only approximately 2,000 jobs, when the unemployment level stood at 200,000.

The local politicians reluctantly came to the conclusion that government investment was not the panacea it was thought to be. A change in policy was formulated, which could not be implemented because Tugwell opposed it. According to David F. Ross: "Governor Tugwell was firmly and emphatically opposed to the kind of development program which relied primarily on the offering of inducements to private capital and enterprise."[5]

Governor Tugwell, however, resigned on June 29, 1946, and this paved the way for the enactment of the Industrial Incentives Act of 1947, which granted tax exemption status to any company that settled in Puerto Rico to produce or manufacture designated articles.

Operation Bootstrap

The enactment of the Industrial Incentives Act of 1947 marked a new episode in the development of the Puerto Rican economy. The law took advantage of the fact that Puerto Rico is exempt from federal income taxes, and consequently, plants operating on the island would be free from this expense. The provisions of the Internal Revenue Code applicable both then and now permit United States companies to transfer the profits generated by their subsidiaries in Puerto Rico to the mainland tax free. There is presently a controversy between the IRS and some of these companies over the matter of intra-company pricing and its effect on profits. However, its resolution is not expected to adversely affect the tax exemption program.

The effects of Operation Bootstrap, as the incentive system is called, have been outstanding. Over 2,000 manufacturing entities have established plants in Puerto Rico as a result of the tax advantages, with more than 100,000 jobs created. This has been considered the economic miracle of the century, comparable to Germany's recovery after the war. The GNP figures for the applicable years are similarly impressive. In 1940 the GNP was $287 million, by 1952 it had risen to $963 million, in 1964 it was $4,531 million, and in 1981 it had reached $11,780 million.

However prosperous or fortunate the policy of granting tax exemption was, it was nevertheless insufficient to overcome the tremendous unemployment problem which has chronically affected Puerto Rico. As the 1979 U.S. Commerce Department study put it: "In the fifties, as the economy was engaged in the first phase of the transition from a monocrop agricultural system to an industrialized system, total employment contracted. The absorption of labor into the newly developed manufacturing sector fell behind the rate at which agricultural workers were being laid off. It was only after 1963 that a persistent employment expansion was underway. Under the momentum, spurred mainly by capital investment induced to enter the economy under the revisions in the Industrial Incentives Act, employment improved for a decade. Between 1963 and 1973 it increased on the average nearly 3 per cent a year. In that span of years, the average rate of unemployment dropped to just over 12.5 per cent as an average—still highly unsatisfactory, however."

Petrochemical Developments in the 1960s and 1970s

In light of the fact that unemployment was still at politically unacceptable levels, the Puerto Rican government redefined its industrial promotion in the 1960s and proceeded to attract oil-related industries. This approach was encouraged by the complex federal legislation which, in pre-OPEC days, placed a tariff on foreign oil but permitted the introduction into the country of cheap foreign oil, once it was processed and refined in Puerto Rico. During the early 1970s oil was imported to Puerto Rico at $2.00 a barrel, and this led to the massive construction of petrochemical complexes in the island. As a result of OPEC's policies, however, imported oil is no longer cheap, and Puerto Rico's distance from the mainland market has made most of those industries nonviable. Over 155 oil related plants alone closed operations in the years 1973 to 1975, and many of the remaining petrochemical complexes have filed for bankruptcy.

Migration has relieved the unemployment problem in Puerto Rico. Since American citizenship was granted in 1917, there are no barriers to migration to the United States and nearly one million Puerto Ricans now reside in the United States. During the 1950s, the average yearly migration was approximately 50,000 persons. The Planning Board, an agency of the Puerto Rican government, in commenting on the effects of migration on the unemployment statistics during the 1940s said the following: "Without emigration during the decade ... unemployment would have mounted to 201,000 as compared to the actual unemployment figure of 101,000 in June, 1950."

Yet, in spite of the government's concerted effort in attracting foreign capital to Puerto Rico and the effects of migration on unemployment, the economy has reached a standstill since 1973. Fewer industries have settled in the island and many of those that were already operating have closed their operations.

Institutional Obstacles

Reasons for a stagnant Puerto Rican economy can be traced to institutional factors. The laws of Puerto Rico, coupled with federal regulations, are very burdensome on business. Labor legislation is indeed one of the causes of unemployment in the island. But beyond that, the massive amounts of federal aid have served to create malinvestments of the greatest magnitude. The Puerto Rican government presently receives over $200 million a year in excise taxes from the U.S. Treasury. This sector provides about 9% of the Commonwealth's budget. During the 1970–77 period alone, over $1,000 million was thus received. This has been sufficient to perpetuate the government's power and to expand its role, while minimizing the taxpayer's cost of the government.

As a result of Federal aid, which represents approximately 30% of the island's GNP, the local government has been able to engage in many functions beyond the scope of the traditional role of government. The Federal government is currently providing Puerto Rico with such generous benefits that a majority of the island's families receive food stamps. The U.S. Commerce Department has acknowledged the role of federal aid when it stated that "Federal funds directly and indirectly supply such a large share of total Puerto Rican income that personal income exceeds the value of all goods and final services produced and remaining in the Commonwealth."

Puerto Rico offers certain statistics that confound anyone knowledgeable in economics, but which portray the magnitude of Federal assistance to the island. As is well known, in order to purchase imports, any country must export goods or services to pay for the imports. Puerto Rico, however, during the past thirty years has consistently run a deficit in its balance of payments. Economists similarly decry the fact that there is no internal saving, but rather that Puerto Rico has become a "net dissaver" over this period of time.

The local government, following Tugwell's example, has continued its welfare orientation and consequently controls a large area of the economy. Government is by far the largest employer in the island—employing 20% of the labor force. The sugar corporation, the electric company, the shipping lines, the telephone company and other enterprises are owned by the government. Not unrelated to this, a Federal Power Commission study indicated that Puerto Rico's electricity rates were the highest in all of the United States. This undoubtedly places the island at a disadvantage in attracting capital for energy-intensive industries.

The government's impressive stature in the economy, however, has not followed a classic pattern. Many of the government's functions are performed by so-called public corporations which in turn are able to float bond issues. The Commonwealth government's debt, as a percentage of GNP was 15% in 1978. But if one adds the debt of all other governmental agencies and entities, the figure exceeds 70%. It is apparent that the government's future borrowing capacity is very limited.

Trade between Puerto Rico and the United States, which represents over four-fifths of the island's commerce, is governed by the Jones Act, a federal statute which requires that all trade between domestic ports be conducted in U.S.-flag ships. The effect of this statute has been to remove foreign competition from domestic shippers and to strengthen the grip of the maritime unions on this industry. Consequently, cargo rates of domestic shipping lines are among the highest in the world. This legislation has also served as an institutional roadblock impeding Puerto Rico's growth, since Puerto Rico's trade is so dependent on shipping.

The Welfare Mentality

Yet, the most serious of all of the obstacles facing Puerto Rico today is the inculcation of the collectivist and public welfare ideology which was started during the New Deal. This ideology views private enterprise negatively.

Conventional wisdom in Puerto Rico holds that the government, either Commonwealth or Federal, is the source of all wealth. This is not hard to understand in light of the fact that government is so omnipresent in the economy. The "share-the-wealth" philosophy has become so embedded that subsidies of all types abound for substantial portions of the population. It would be beyond the scope of this article to mention the different subsidies that exist in Puerto Rico today. However, historically the most important one was the expropriation on the part of the government of large tracts of land and their subsequent subdivision and transfer to thousands of people. The power of eminent domain in Puerto Rico is very strong and undoubtedly its effects have shaken the island's economy. The largest landholder at the moment is the government, which owns 130,000 acres of land.

Perhaps a reflection of the welfare mentality that is rampant in Puerto Rico is the flurry, over the past decade, of land squatters claiming their alleged right to hold property. After all, government had been expropriating land for so long that it seemed altogether natural to simply take over the land. It has been estimated that there are over 2,000 acres of land that have been squatted on during this period of time. Politicians have rushed to the scene in many cases to show their compassion for this, and it has not been unknown for the legislature to enact benefits that reward the efforts of the squatters.

The economic crisis which prevails in Puerto Rico today cannot continue for long without further adverse consequences such as an appalling crime rate and a continued increase in unemployment. The much-publicized tax cuts that were implemented recently, following the advice of Arthur B. Laffer, have been quietly interrupted. The last phase of the tax reduction has been rescinded for fear that it might create a deficit. The miraculous effects it was supposed to create were nonexistent because the government's role in the economy has continued to assume a greater importance.

Tourism, which represents an important industry for the island is nevertheless limited in what it may be able to achieve for it represents only 5% of GNP. Agriculture is similarly situated.

Prospects for the Future

As a result of receiving massive infusions of federal funds as well as experiencing the effects of migration into the continental United States, Puerto Rico's policymakers were able to attenuate the consequences of their economic policies. As the Commonwealth's government enacted more restrictive regulations, as it encroached more and more into the workings of the economy, the results of these decisions had to be malinvestments and unemployment. But precisely because migration served as a safety valve, and federal funds assumed a major importance in the economy, the policymakers became convinced that the interventionist legislation they favored could not adversely affect the economy. When the federal minimum wage became completely applicable to enterprises that operated in interstate commerce in Puerto Rico, for example, the government's position was that this could have no adverse effect on unemployment. The government obviously was wrong.

Many factors influence the workings of an economy, so that one governmental policy may partially offset the effects of another. This has been the case in Puerto Rico. As progress was taking place in the island during the decades of the 50s and 60s, people became convinced that the main reason behind such progress resided in the collectivistic policies enacted by the politicians who followed Tugwell's lead.

The Effects of Freedom

Yet, in analyzing all of the governmental efforts at promoting the local economy, one can fairly say that most of them achieved distortions and malinvestments in the economy. However, when private enterprise was granted a substantial tax holiday which offset many of the other costs implicit in starting an operation in Puerto Rico, growth spurted. Foreign visitors came to study the economic miracle that was taking place. Unfortunately, the costs of operating in Puerto Rico, in large part due to the local government's policies, have finally caught up with the tax exemption program, the result being that fewer industries are willing to locate in the island.

If there is anything to be learned from Puerto Rico's experience during the past four decades, it is that private enterprise has been the most efficient mechanism for increasing the productivity and the wealth of the people. Policymakers should recognize this and attempt to deregulate the economy in order to permit the private sector to bring its dynamism into the economy.

It is encouraging to observe that, in spite of the spending policies of the federal and local governments, the entrepreneurial spirit has not been completely quashed. Regardless of all the subsidies, privileges and controls that exist in the economy, people are willing to invest and take risks. The effects of these efforts would be magnified if the economy were freed of all the restraints that hold back its growth. The most significant change, however, is that the collectivist mentality which has been so successfully ingrained must be erased if individualism and liberty are to prevail.

—FOOTNOTES—

[1]Earl Parker Hanson, *Transformation: The Story of Modern Puerto Rico* (New York: Simon and Schuster, 1955), p. 31.

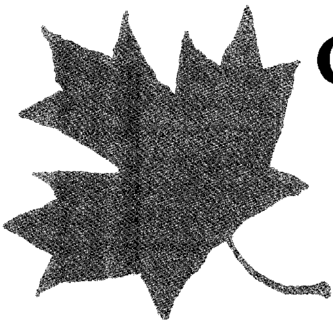
[2]Henry Wells, *The Modernization of Puerto Rico* (Cambridge: Harvard University Press, 1969), p. 148.

[3]Cayetano Coll Cuchí, "La Ruina de la Industria Azucarera," *El Mundo*, August 1938.

[4]United States Department of Commerce, *Economic Study of Puerto Rico*, 1979, p. 218. Statistics not otherwise footnoted were obtained from this U.S. Department of Commerce study.

[5]David F. Ross, *The Long Uphill Path: A Historical Study of Puerto Rico's Program of Economic Development* (San Juan: Talleres Gráficos Interamericanos, 1966), p. 79.

Kenneth McDonald



Canada Damaged by Faulty Theories

TRADITIONALLY, Canada's economic performance has trailed that of the United States. Markets and productivity suffer the consequences of a much smaller population spread thinly astride a narrow band that stretches 3,000 miles from Newfoundland to British Columbia.

In recent years, however, Canada's relative performance has slipped markedly. The Canadian dollar has fallen, inflation is much higher in Canada, and the budgetary deficit, in proportion to population, is much larger than that of the U.S.

Yet Canada's policy-makers, and the economic establishment that advises them, stick manfully to theories which are plainly at odds with the facts.

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For the layman, the contradictions appear the moment he asks himself some questions.

How can rising prices be attributed solely to their historic ingredients—cost of capital, materials and processing, cost of labor and profit—when the effect of taxes, which are rising faster than the rest, is ignored?

How can the provision of government services be continually expanded without a comparable rise in the cost of providing them?

How can that cost rise be paid for except through taxes?

How can wages ever "catch up" with the recipients' cost of living when no account is taken in those wages of the unseen government services from which the wage earner benefits?

So long as such services are unpriced, and assumed to be either free or supplied at someone else's cost, what is to stop society's pressure groups from demanding more of them?

How can the raising of interest rates bring prices down when the higher cost of borrowing pushes up not only prices but also the cost of the unpriced government services that prices include?

When elected representatives are regarded primarily as redistributors of income, how can they fail to support the structure which enables them to redistribute it?

In a democracy, changes in policy, and in establishment thinking that shapes policy, are presumed to come about as a result of arguments that persuade the policy-makers. But what if the establishment and the policy-makers refuse to listen?

Alternatives Ignored

There is ample evidence that answers to the layman's questions, and alternative policies that are suggested by the answers, have been presented to policy-makers. Explanations that fit the facts are available to the economic establishment in books and discussion papers. Of any sign that the alternative policies or the explanations have been given serious consideration, there is no evidence at all.

Let us call the innovators the new men, though they are not young, to distinguish them from the men of the establishment, many of whom are not old.

Prominent among the new men in Canada are Verne Atrill and William Krehm, who are businessmen and economists, and Arthur Bailey, who is a senior civil servant.

Running through their work is a common theme: nothing is free; everything must be paid for; obligations must be met.

That fundamental truth is obscured every day, but especially at election times, by politicians whose business it is to suggest the contrary. "The state," as Frederic Bastiat reminded us a century and a half ago, "is that great fiction by which everyone seeks to live at the expense of everyone else."

The purpose of this article is to bring the new men's work to the attention of a discriminating audience in the hope that its significance will come to be understood in time.

It is no exaggeration to say that there is not much time left. If the present policies are not changed, Canada's transformation into a collectivist state, consuming fatal quantities of what Atrill calls our precious economic energies, will have passed the point of no return.

The establishment, though it makes much play with the complexities of the economy it presumes to direct, is deaf to argument as it steers toward the simplest solution of all: the age-old institution of Hilaire Belloc's Servile State ("Socialism's essence consists in vesting in trust with the politicians what is now private property").[1]

Making Socialism Work

Unlike the men of the establishment, the new men recognize that combining man's creative instincts with his desire for individual freedom, and doing so within a society that still permits him a say in how he is governed, is a very complicated business.

In their books[2] they are concerned not with dismantling government, for there are many things that only government can do, but with making it work better than it does now.

Atrill explains how the solvency of entities is reflected in their debt structure ratios: the ratio between what is owed to, and owed by, the entity. All obligations are met, if only by the creditor. The wholesale transfer of economic energy from individual entities, which must retain solvency as a condition of existence, to governments which are increasingly insolvent, threatens the survival of individual enterprise.

Praising the money market as "man's noblest creation," Atrill shows how the private banking system has been subverted by central banks (Bank of England, Bank of Canada, Federal Reserve Board) whose prime function has become the maintenance of inflation so that the governments they serve can meet their obligations.

His Objective Economics demonstrates the relationship between economics and natural law which engaged the 18th-century physiocrats. Its essential difference from the establishment's subjective economics, which tries to insert decision-making man at the center of economic events, is that it shows how those events occur and proves the demonstration by extracting, over a seven-year period, the appropriate ratios from the balance sheets of the 300 companies in the Composite Index of the Toronto Stock Exchange.

Like Atrill, Krehm exposes the fallacies that dog the economic establishment. Both men show how the tool of mathematics, which the establishment has misused to determine equilibrium points that do not in fact exist, and which are then applied to the construction of equally fictitious econometric models, can be used properly to our advantage.

Both have reasoned their way from the establishment's obsession with Newtonian calculus, and with looking upon price as an invariant, to the realization that the right tool is tensor calculus as used by Einstein in his development of relativity theory. Atrill sees the "major mathematical problems posed by Objective Economics and the dimensionless science of observation of which it is a part" as forming the basis for an understanding between East and West. "I believe that neither Marxian catechism, nor the Leninist political eclecticism, nor the Stalinist brutality, nor the Maoist dogmatism will be able to stop some of the communist world's great intellects from involving themselves in those problems."

Krehm takes us through the development of physics and its application to economics. Showing how the efforts of central banks to "stabilize" prices are "a simple rewrite of Boyle's Law linking the volume, pressure and temperature of a perfect gas" he shows how, by ignoring new subsystems that intermesh with traditional components of price (supply and demand, materials, capital, wages), the establishment is in the same boat as pre-Einstein physicists.

"There is, for example, nothing more obvious to common sense than the invariance of time and space. Experiment, however, proved that the speed of light was the invariant; and to reconcile that with the known laws of physics Einstein showed that time and space were not invariant. The case of price is similar. . .

"Economic science should be seeking the real invariants of the new world that is evolving around us. But by setting up price as an absolute invariant, economists have made it impossible to carry on any serious investigation of our problems. . .

"Instead of dealing with the catch-all concept of 'inflation', we should have examined the very different factors that make for price rise. We should have studied the circuits through which these operate, and how they intermesh. Had we plotted these relationships, we could then have turned to the computer to help us ascertain how much each of them did in fact contribute to the price bulge. Such an effort, however, was ruled out by our faulty theory."

A Host of Contradictions

Faulty theory has led us into a host of contradictions. For example, civil service pensions are indexed to the cost of living while business profits are tied to the original rather than the replacement cost of fixed capital. Because government services are unpriced, the benefits in wages and salaries are unseen; their recipients try to keep up their take home pay while rejecting the tax increases that should pay for the benefits—taxes which are in everybody's cost and which, while unpaid, consume the society's capital.

Both Atrill and Krehm are drawn to physics for guidance out of the blind alleys into which faulty theory has led us. Just as the concept of space was changed by an understanding of the forces inherent in mass, matter and energy, so must the concept of an idealized market be changed to accommodate the non-market subsystems that distort it; new equations are needed.

How Arthur Bailey and Douglas Hull apply these concepts to the government sector is conveyed by their book's sub-title: "A More Revenue Dependent Public Sector and How It Might Revitalize the Process of Governing."

Their theme is the need to construct a new model of public financing that allows citizens some choice. Instead of the appropriations method, which accords to a small group the power to decide a broad range of social policies and consequently the appropriations which it then forces Parliament to approve, revenue dependency would link many of the government services to cost by pricing them.

Thus to the extent that enough citizens judged the benefits to be worth the price, and bought them, the services would be self-financing, as would the administrative overheads of the government departments concerned. (This would not preclude citizens who were in a state of dependency from being subsidized individually to secure the provision of common services.)

Political leaders and their permanent advisers would be relieved of the hopeless task of trying to plan the unplannable; government would be concerned with defining the limits and structures within which the citizens could go freely about their business. This meets Belloc's definition of a free society, "consisting in nothing else but the enforcement of free contracts."[3]

Revenue dependency would remove from many of government's activities their present advantage of monopoly. Required to pay their way in competition with private enterprises, the departments concerned would have to trim their costs accordingly; estimates would be based on true costs rather than on assumptions that merely added increments to those of the year before.

Trust to Competition

In the writers' view, substituting competitive for the present monopolistic delivery of services would yield dramatic gains in productivity. Real responsibility would devolve upon departmental managers. Instead of decisions being pushed up to the political level, many would be delegated to, and made by, the people responsible for the activities. Departmental managers would be under the same compulsion to economize as their competitors in the private sector.

The introduction of price and choice to government services would stifle the temptation upon politicians to promise more than they can deliver and to force upon the citizens "services" that are neither asked for nor needed: the test would not be one vote every four or five years, but millions of votes every day.

In a federal system, where much time and effort is wasted in jurisdictional disputes between three levels of government, the introduction of revenue dependency at all levels would show which was most efficient in the delivery of interlocking or competing services; many of the present redundancies would be eliminated. In the writers' words: "Under revenue dependency the most appropriate scale of operations would be settled more by public choice than by constitutional negotiations. Thus increased public choice could contribute to a more functional federalism."

The new men have advanced alternatives to theories that have proved faulty. The layman's hope is that policy-makers will examine the alternatives with open minds and have the courage to test them.

—FOOTNOTES—

[1]Hilaire Belloc, *The Servile State* (Indianapolis, Ind.: Liberty Classics, 1977).

[2]Verne Atrill, *How All Economies Work* and *The Freedom Manifesto* (Toronto: Dimensionless Science Publications, 1979 and 1981). A. R. Bailey/D. G. Hull, *The Way Out* (Montreal: The Institute for Research on Public Policy, 1980). William Krehm, *Price in a Mixed Economy, Babel's Tower,* and *How to Make Money in a Mismanaged Economy* (Toronto: Thornwood Publications, 1970, 1975 and 1977).

[3]Belloc, *op. cit.*

IDEAS ON LIBERTY

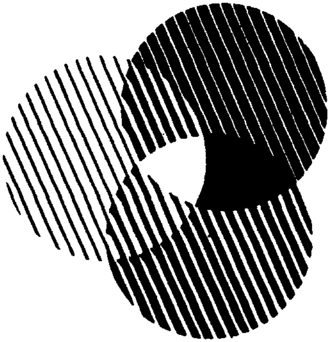
The Methods Are Unsuited

IN PRACTICE, therefore, a socialist society is one in which the vast majority of men are controlled by the tiny minority which has power to direct their economic activities. We might put the matter differently by saying that the socialist dream is based on the delusion that men's other freedoms will be enhanced if they are deprived of economic liberty. By eliminating economic liberty and replacing it with a planned economy socialists hope to usher in a brave new world.

It hasn't worked out that way in practice because the theory is all wrong. "Economic control is not merely control of a sector of human life which can be separated from the rest," writes F. A. Hayek, "it is control of the means for all our ends." Eliminate economic liberty in a society and you begin to institute a master-slave relationship.

EDMUND A. OPITZ, "Socialism—Substance and Label"

Ridgway K. Foley, Jr.



THE SOCIAL ROLE OF BUSINESS

THE current fashion is to pontificate, sometimes to excess, concerning the social role of modern business and the social responsibility of trade entities in late twentieth-century society. Given this tendency, the nature and appropriate role of business in any social setting deserves attention.

At the outset, let us propose a working definition of business: the methods of voluntary action utilized to conceive, produce, transport, and distribute scarce goods, services, and ideas from those who create such products to those who wish to trade some value they have created in exchange for those products. It is at once a structure, device or institution as well as a process. It serves those who wish to trade; it exists solely in a market; it does not partake of coercion; it exacts no penalty from those who prefer not to share their produce.

All too often, observers tend to limit their thinking of business to modern corporate giants exemplified by Exxon, Standard Oil Company of California, or General Motors. While these entities do represent specific examples of one successful mode of business, such a myopic view distorts reality and conjures up the inaccurate premise that all business consists of large aggregations of people, machines and capital, mass-producing integrated or disparate goods for consumption.

In fact, business includes numerous corporations unlisted on the New York Stock Exchange and virtually

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unknown beyond the boundaries of a local or provincial area. It also encompasses myriad family enterprises, close corporations, general or limited partnerships, and individual proprietorships, all providing a host of desired goods, services and ideas. It further embodies such activities as farming which raises, transports and sells needed foodstuffs in the market yet which often receives undeserved discrete treatment in the political and economic realms. It envelops professional men and women who offer their services to others in exchange for value.

In the broad sense, business enfolds within its grasp anyone and everyone engaged in trading his ideas, his services, his goods, that which he creates and owns, with other individuals who possess goods, or services, or ideas which they consider expendable or less desirable than the exchange goods offered by others. Thus, every person who performs gainful employment in exchange for a wage, salary or other kind of remuneration really participates in business: he trades his time, energy and creative efforts to another for payment which, in turn, can be used to fulfill his needs and desires.

Economic Laws and Business

Man displays the curious communicative tendency to employ the identical term to convey quite disparate concepts. The word "law" offers a striking example.[1] Positive, or human, law generally refers to a system of rules and orders, emanating from a sovereign, directed to subject people, commanding or proscribing human action, and exacting a penalty or sanction for known noncompliance or disobedience. Natural law (of which economic law forms a part), on the other hand, refers to certain causal relationships which flow from human action. Like positive law, natural law enforces conduct and wrests a sanction for human action, but there the analogy terminates. Positive law emanates from mankind with its inherent fallibility; natural law reflects reality and neutrality rather than individual bias. Commoner and King both bleed when cut with a knife. Natural law makes no value judgments; it merely levies a cost related to universal truth by means of cause-and-effect consequences for human action.

The three fundamental economic laws concerning business form a part of the natural law rather than mankind-enacted and enforced normative rules.

The First Law of Economics: Scarcity

The first law of economics dictates that this science deals with the creation and distribution of *scarce* goods, services, and ideas. Where free goods exist, the study of economics disappears.

Imagine an island paradise, blessed with clean air, fresh water and an abundance of tropical fruit. Here business exists only in the most rudimentary form since little effort need be expended by the inhabitants to secure their daily foodstuffs and water. Yet, even that condition and the minimal effort reveals that business in some form may be necessary. A supply of fruit and water, while sufficient, is finite, not endless. Some method must be utilized to divide and distribute the existing or potential scarce goods to the islanders. Business represents a method, the best and fairest means of distribution, where each individual, acting voluntarily, offers to exchange that which he possesses for that which he desires.

Where wants exceed the free (not scarce) goods available, the exchange economy develops. An elementary specialization and division of labor arises, where, in place of each inhabitant carrying his or her own water, gathering fruit, and handling all needs, one member of society develops a skill in the production of grass skirts or handmade thongs which he or she exchanges for mangoes delivered to the door.

The law of scarcity introduces yet another salient economic concept: labor. Labor consists of the productive expenditure of human energy and provides the necessary base for business. Even on the tropical isle of our hypothesis, the rudiments of labor exist: picking breadfruit, carrying water, sewing clothing, and thatching a hut all require some effort.

Viewed broadly, all business rests upon labor, past or present. Present labor appears obvious: the physical and mental efforts of men and women engaged in the creation, production, transportation and distribution of scarce goods, services and ideas. Yet business enterprises also use past labor, stored-up and unconsumed labor, often termed capital. The productive results of labor may be consumed or saved; those efforts which are saved are invested in tools and machines to be used in future productive efforts. Capital renders present labor more productive and efficient. Past and present labor applied to existing resources creates new and desirable scarce goods for trade.

The Second Law of Economics: Insatiability

The second law of economics provides that man's needs, wants, and desires are insatiable, dynamic and never-ending. Man's acquisitive nature mandates that his individual and collective cravings always outstrip his production. In short, he is never satisfied with the current state of affairs.

Recur to the example of the isolated island. As man grows, he becomes more acquisitive; good food and plentiful drink, an adequate hut and basic clothing may not be enough. He will seek variety in his diet, distinguished and distinguishing feature in his living quarters and class or style in his clothes. He may hanker after a plow, a conveyance, a book or a whole host of other things. Faced with an array of scarce goods, services and ideas, his wants are insatiable.

The Third Law of Economics: Cost

The third law of economics follows from the roots of scarcity, labor, capital and insatiability: every thing possesses, and occasions, a cost. This immutable norm of natural law flows from the fundamental natural law rule of consequences, of cause-and-effect. Denial of the principle cannot destroy it.

Some state this premise in homely fashion, such as, "it's time to pay the fiddler" or "there ain't no such thing as a free lunch." The cost analysis of natural law provides that no one can secure scarce and desired goods, services or ideas without effort—even a taking by force or fraud requires risk of retribution, clever cunning action, and physical and mental effort. The effort constitutes the cost of the product, whether it represents effort by the producer in making the device, or effort by the trader in manufacturing trade goods, or effort by one (donor) on behalf of another, third party beneficiary.

In a free society, a business or market society, the cost of an exchange amounts to the intersection of that which someone who possesses the desired good, service or idea will demand from the buyer in trade, and that which the latter will voluntarily transfer to the producer in exchange. In simple economic terms, price represents the intersection of the supply and demand curves. But lines on a graph, being abstract, obliterate reality; the reality of price is cost, and cost stems from the natural law of the universe.

In a command society, the cost of an exchange will be disguised because of the avoidance of a market mechanism.[2] Nevertheless, each good, service, and idea will command a cost under the natural law as surely as men in power try to command their fellows. The cost required amounts to the effort expended—the past and present labor—in production, and the alternative courses of action avoided. Each human action (including economic or business activity) requires a choice and each choice produces moral consequences. The consequences constitute the cost of the actions.

In what manner do these three fundamental economic laws decree the need for business? Business—the structure and the process—deals with the rules of scarcity, insatiability and cost in a voluntary and efficient way. The allocation of scarce, desirable and valuable goods, services and ideas must be secured in some manner. Basically, two methods exist: coercion or voluntarism. Because men and women choose diffferent ways to satisfy their ever-expanding wants, property can be divided in two ways: (1) each person can bid for the goods and services sought against all competing uses (the nonaggressive method) or (2) some person or group can seize power and forcefully decide (choose) for others by allocating scarce goods, services and ideas to satisfy those insatiable wants (the coercive method). The coercive method allows some individual or group to use force to distribute these products in a forceful manner, according to their subjective value judgments. The voluntary method allows each individual to act without force to provide for his own ends and to pursue his own brand of happiness. The state represents the coercive method; business provides the voluntary method.

Property, the Creation of Value, and the Pursuit of Happiness

Business provides the structure and the process which creates and distributes property. Property constitutes the name given to those goods, services and ideas created by men and women, acting productively by themselves or in a group. One does a disservice if he limits property to land or "things," like furnaces and machine tools; property includes the corporeal and the incorporeal, the tangible and the intangible: legal and accounting services and management ideas as well as books and chairs.

In a broad sense, property may be described as the human creation of value. The world exists. Man can only create by taking existing things or elements and altering their character or transporting them so as to make those things or elements, or a combination of them, useful to him or to others, or by conjuring up ideas about existing things or documents useful to him or to others. Property sometimes connotes elements in a natural state: game or wilderness land or minerals. This presents too narrow a view: fauna or dirt or iron ore provide nothing of value—they just exist—until used by men to satisfy their needs and wants. In the more salient sense of the term, elements become property when they become useful to mankind, when men and women apply their value structure upon these existing matters.

How do human beings value items? The fundamental of business is that men and women value everything subjectively. Each person attaches worth to goods, services and ideas in accordance with his or her unique character and individual judgment. Mankind rates merit of various matters on individual and ever-shifting scales of preference, fueled by internal measurements, assessments, perceptions, desires and motivations which no one else can reproduce or appreciate. As a concomitant natural rule, one recognizes that objective value does not exist; no one can conceive of a universally defined and accepted "good chair" or "good city" or "good concept" which will rate equally with each person.

Value Is Subjective

If objective or inherent value existed, a single producer for each kind of product would suffice: everyone would prefer Borden's to General Foods and the latter would go out of business. Since men value everything subjectively, business develops to supply and service these insatiable and increasing wants related to scarce and costly items. As a result, several producers of similar goods will find their adherents in a market. Cost diminishes as competition between vendors keeps only the most efficient in the market. Profit appears, maintaining the sellers, as the buyers bid in competition with other potential users for wanted products.

Some who recognize that all value is subjective confuse value with reality and deny the existence of absolutes or truth. The two concepts do not war and are not coincident. Truth exists; it represents a facet of natural law which is no more than the face of reality. The concept of subjective value means that men—possessing the power of ultimate choice over their own destiny—may disregard truth and believe in, and value, fiction. The great lesson of liberty is that freedom implies the freedom to be wrong, to err. Because man is free to choose, he maintains the freedom to choose badly, to value fallacy over truth. Truth is not value, and value is not truth. Value represents an internal scale of preference while truth represents a natural law which applies a cost or consequence for choice freely made.

Business does not engage in moral value judgments except to the extent that business decisions represent moral choices of the producers who must (like all men) live with their consequences. Business provides goods, services and ideas to those who wish to purchase or trade for them, without acting as a moral arbiter of the choices of the consumer. If a business distributes harmful automobiles or addictive drugs, the maker must bear the moral results of his part in the process, but unless his conduct partakes of force or fraud, the state should not step in and restrain a free transaction. The wisdom of the choice of the buyer cannot be measured by fallible men since (1) each element in the universe incorporates the potential for harm and (2) no person possesses the ability to supplant another actor's choice-making process. Hence, except as indicated regarding coercion or deceit, business remains morally neutral and the buyer must also bear the moral consequences of his choice.

Our Declaration of Independence did not promise eternal bliss and ethereal well-being; it recognized as supreme the *in*alienable human rights to "life, liberty and the *pursuit* of happiness."[3] It rests within each person to seek his own ends and to achieve happiness. No one, including the state, can promise another happiness; it cannot even define happiness for another. The proper role of the state is simply to leave man free to pursue his happiness in response to his subjective value system. Business merely exists as the most effective and efficient mechanism by which men can pursue happiness, compatible with natural law principles of inalienable rights.

The Multiple Roles of Individuals in a Business Society

Less perceptive observers tend to fragment society into sections like "business," "labor," "consumers" and "farmers." Actually, all members of a modern market society play many roles: most are shareholder-owners, worker-producers, and consumer-users and some are officer-managers of business. Fragmentation distorts reality and serves no useful purpose. Many people create value, directly or indirectly, and all consume. To the extent that they save some of what is produced, they become owners: every possessor of an insurance policy, bank account, pension plan, bond or stock is an owner of business in society.

The meaning of these roles may be both seen and unseen, obvious and obscure.

The visible meaning: class warfare destroys us because we are fighting ourselves. Anti-business legislation or litigation attacks all who own a share of that business. Moreover it destroys the structure and the process which fulfill our wants and desires as consumers most effectively.

The hidden meaning requires some thought. In which of these roles may members of society use the state to enforce their desires? Man merits no right to use force in any one of these roles except in two limited circumstances: he may band together to prevent and punish aggression, the initiation of force and fraud, and to secure common justice, the settlement of otherwise insoluble disputes. Beyond these limited roles, the state intervenes in business only at the peril to all who reside in society; each inhabitant, in one or several roles, derives exceptional benefit from the existence of business.

Consider two of the many aspects of this hidden or secondary truth.

First, mankind in a free society retains the absolute right to refuse to trade with those one wishes to avoid for whatever reason. If a party does not desire to drive a Ford, he need never buy one. If he does not believe that he has received proper recompense for his toil and his production of value, when his contract terminates he may go elsewhere and sell his services for whatever the market will pay. Business in a free society is noncoercive: has anyone, even in this euphemistically-labelled "mixed economy," ever forced another to buy a Chrysler instead of a Volvo, or to purchase Colgate-Palmolive products in place of a competitor's offering?

Second, the absence of business would render trade abominably slow, tedious, and uncertain. Imagine the difficulty you would encounter in this country of 225,000,000 souls if you attempted to satisfy your wants by trade without a business structure. Each of us would surely starve naked in the dark; as Leonard Read has so convincingly demonstrated, not one among us can construct—start to finish—an item as simple as a common pencil.[4] Business defines the means by which we voluntarily speed up and apply precision to the many transfers which make our lives productive and satisfying as we pursue happiness.

Three myths pervade the study of business: the myth of the windfall profit, the myth of the private monopoly, and the myth of the evil entrepreneur. Each fantasy accounts for much common misunderstanding of the role of business in society yet, in unmasking these chimeras, a nub of substance remains to be explored.

The Myth of the Windfall Profit

The consideration of the trading transactions of business introduces another term: profit. Profit represents the most misunderstood portion of business endeavors.

Profit describes the excess trade value transferred to a party in a transaction, beyond the value of the matter exchanged. Seller conveys a book to buyer for $5.00; the seller's profit is the excess of value received over the value of the book to him. Such a value may consist of tangible or intangible matters. For example, the book may be a fungible item, one of many almost exactly the same; in this case, the seller may trace his profit to the amount in excess of the cost of the book. After totalling the charges for typing, proofreading, printing and publishing the tome and adding on a figure for the labor involved in writing, the seller may conclude that his cost is $4.75 and his profit $0.25. In different circumstances, where the book could be classified as a collector's item or a first edition, other factors will enter into a determination of profit.

Often, analysts overlook the fact that all parties profit in all free transactions. The seller may receive a stated sum of money or goods of a value which represents his cost of goods sold plus an increment for the use of his time, capital and entrepreneurial abilities. He expresses willingness to trade his goods for their return; for any lesser amount, he would rather keep what he has produced. On the other hand, the buyer will trade a stated sum of money or goods of a value which represents the value the buyer places upon the seller's offer. If the seller's goods are worth less to the buyer, he will not make the trade and, instead, will keep his trade goods or money substitutes. If the trade takes place without coercion or fraud, both parties profit because each one receives something he values more from the other than that exchanged. This possibility takes place because of the doctrine of subjective value: individuals value things differently.

The Exchange Ratio

Price is not value. Price is an indicator of value at a particular time for particular individuals in a particular setting. But value shifts, so price merely marks the intersection of the supply and demand curves at that time.

Given this understanding, "excess" or "windfall" profits or prices can never exist unless a transaction possesses an element of coercion. Each party to a transaction freely and voluntarily entered receives the result he desires, and each profits in his subjective scheme of value. A windfall occurs when someone receives something undeserved or coerced; one cannot describe a gain as a windfall where both parties voluntarily agree and trade: in the absence of fraud, each receives that for which he bargained. "Excess" indicates a standard; if the standard of value is subjective, the gain cannot be excess in a voluntary situation.

Studies indicate that many individuals hold an unreal vision of business profits. Depending upon the poll, the sample and the source, people may believe that the average business receives up to 45 per cent of each sales dollar as profit. In fact, the average manufacturing concern receives something like $0.05 of each gross sales dollar as profit depending upon the measuring technique. Studies also indicate a misunderstanding about the amount of business cost related to labor and to government compliance. In addition, most profit figures contain the misleading assumption of measurement by a constant standard of value, whereas inflation causes a reduction of real value and an incorrect set of figures. Yet even if profit truly reached the imagined heights, one could not term them excess in a free society for the fact would merely betoken that the seller was supplying a needed service or good or concept desired so much by the purchaser that the latter was willing to trade a larger amount of goods or services or ideas in return. The greater the profit, the higher the need fulfilled.

The Myth of the Private Monopoly

A myth persists that, without governmental intervention in the business world "to assure competition," private monopolies would result.[5] This would leave society at the mercy of a few large enterprises free to raise prices at will and to impose their corporate desires upon unhappy consumers without recourse or restraint of any kind. Such purveyors of nonsense fail to understand basic economics, the free society or the concept of subjective value.

If everyone derived perfect satisfaction according to his or her subjective value structure from a single product, a single producer would dominate the field *for that item.* Yet this simplistic analysis ignores reality.

In the first place, subjective value varies among individual actors, leading to the need for many producers of a single type of product to offer a range of economic choices. Even where goods are fungible, such as steel, over 250 American enterprises appear as sellers, not to mention many foreign entities.

In the second place, if a producer satisfies a great number of consumers with a single product, his profits, far from being a windfall, merely demonstrate that he is assuaging a true demand.

In the third place, in a free society, without state-imposed barriers to market entry, subsidies, favoritism in distribution, and the like, high profits will tend to attract competing producers into the field, leading to innovation, improvement, and lower prices. Monopoly, even if possible, would constitute an ephemeral instance in the true private property order. New creators of value will hasten to share in a lucrative market, given the self-improvement and acquisitive nature of mankind.

In the fourth place, consumers vote in a dollar democracy among a great array of products and services.[6] Thus, not only do creators and traders compete in the market with manufacturers of like goods and services, but also each business must compete in the broader field among a wide variety of substitute, non-competing products; further, each enterprise must compete for the finite consumer dollar (stored-up labor or trade goods) which can be spent *or saved.* Remember: people tend to vote their own trade dollar more carefully and more in harmony with their true self-interest than they do in the polling place on election day, when many fall prey to the sins of greed, envy, covetousness and coercion. On the market, the consumer-voter trades *his or her* produce for that which he or she desires the most, based upon the trader's enlightened subjective value.

In the fifth place, the market provides an amazingly resilient and efficient apparatus for determining the employment of scarce and finite resources for the satisfaction of human wants at the lowest cost and on the most praiseworthy and efficacious basis. Business ought to produce what the user wants. Consumer desires rest on subjective value. Thus, the business which prospers best serves the greatest number of subjective value structures at a given time. Those enterprises which do not satisfy the needs of the buyers receive a command from the market: go and employ your scarce resources, your capital, your labor, your time, your inventiveness elsewhere. Thus endeth the Kaiser, the Fraser, the Tucker, the Edsel, and the Imperial, to name a few examples from the American automotive industry in the post-World War II years.

Signals from the Market

If no one, or too few persons, buy a product even at a low price, that fact indicates to the seller that his merchandise does not accord with the subjective value system of the public at the present; in a word, there exists no demand for the stock. A hypothesized private monopolist occupies the other end of the continuum: by presupposition and definition, he serves a real need and best accommodates the fancies of the public in that arena. However, as indicated heretofore, if the market provides a return for such a good, service or idea, the monopolist will not remain the lonely producer for long; he will find plenty of company as new entrants into the field try to outdo him for the reward of profit. If these newcomers succeed, the price drops by virtue of increased competition; if they fail, the market signals that the former supplier still slakes the customer's thirst best of all.

In the sixth place, while price does not constitute the sole determinant to trade, it does represent a register of value so that the producer—even an averred monopolist—who generates great numbers of goods and holds them for a too-high price (beyond what the subjectively-valuing public wishes to pay) will find himself burdened with a useless inventory. Since the management at General Motors cannot eat Pontiacs or use Skylarks for shelter without inconvenience, we witness a reduction in price by means of lower finance charges (encouraging payment over time in fewer real dollars, given the inflationary sweep of the economy), rebates (price reductions by another name) and similar actions. Even these price diminutions have proved of remarkably minor assistance to Chrysler, which has reported losses in recent quarters in significant amounts and which would probably have left the field of automobile manufacture and sales without the existence of a governmental subsidy.

Thus monopoly represents a chimera in the real world in the absence of state intervention in the economy. The only true monopoly: the government monopoly of force.

The Myth of the Evil Entrepreneur

Television, radio, newspapers, magazines, books and plays all portray the American businessman and woman as evil, cunning, treacherous, crooked, greedy, immoral and, sometimes, downright murderous. Think back to the last time one of these media pictured a person in business as wise, decent, helpful, and virtuous. Few can recall such a display. This unfortunate characterization has embedded the populist notion of the evil entrepreneur deep into the fabric of our society, to the extent that it far overshadows reality and truth and does a gross injustice to many millions of upstanding individuals.

In fact, in a free society, people in business are neither better nor worse than their counterparts in education, labor, agriculture, the professions, or the social services. Business people partake of the same flaws which afflict all of us and demonstrate the identical virtues which render us little lower than the angels. Indeed, those who engage in business may often exceed some of their fellows in virtue because the entrepreneur, seeking profit from the satisfaction of wants by the deployment of scarce resources, helps his fellowman pursue the latter's subjective vision of happiness.

Again, the traducers of business focus on the seen and ignore the unseen. They tend to overlook not only the role of business but also the multiple roles each of us plays in the real economic world: as worker, employer, owner, user, investor, in short, as businessmen and women. By chastising the business community, the unreflective writer or politician demeans us all—yet curiously, they invoke their little statist schemes as a prescribed nostrum for society's real or feigned ills, artifices which assume perfectibility of the very mankind they disparage.

The Grain of Truth Behind the Myths

A nubbin of truth reposes in these three myths of business: since the business person is no better nor worse than the mill run of people generally, he like his peers may seek an edge, an advantage conveyed by government to one but not to others. It is the entry of the state into the affairs of business and the free flow of the market which leads to unfair profits, monopoly and wicked advantage. Business is designed to function best in a free society; the state represents the viperish interloper in the market Garden of Eden, corrupting what it touches when it exceeds the bounds of providing a fair field to all and special privileges for none.

How does the government disrupt the political economy? The ways and means are too numerous to count. However, the use of the law for favoritism generally takes one of two broad forms: limitations upon any entry into the marketplace or benefits for some entrepreneurs at the expense or to the exclusion of others. In the first category reside license fees, public utility franchise laws, rules favoring cartels and "natural" monopolies, norms restricting the admission and practice of specified professions, and the like. In the second category one finds subsidies, tariffs, government contracting and purchasing requirements, beneficial tax treatment and rules, and a whole host of curtailments stemming from the shibboleth "self-regulation" where certain members of an industry cloaked with the mantle of law under the guise of a quasi-public entity receive jural authority to make rules and issue orders which govern the conduct of others in that discipline. The variations on these themes are constrained only by the ingenuity of the minds of men propelled by greed and envy.

Finding a Scapegoat

The populist who rails at "big business" often fails to discriminate between business operating in a free society and business maneuvering in a command society. No one will attain complete satisfaction and happiness in any economy, free or slave, for that is not the lot of mankind. Nevertheless, the purveyors of business myths often decry business practice as a supposed cause for their own shortcomings, failures, or losses. It is quite one thing to challenge a private economic enterprise which receives subsidies, land grants, favorable tax treatment, and a restrictive franchise from the state or federal government. It is quite another matter to preach hatred for a business which becomes successful and highly profitable not by virtue of special favors but by dint of meeting customer needs and subjective desires.

The acorn of truth from the oak tree of myth merely advises the thoughtful that the mandate state may taint the people who partake in the business process and structure. Thus, profit is not excessive where a freely acting seller and buyer reach a mutually-acceptable price without coercion; profit becomes an unfair transfer payment where the government limits the number of sellers or artificially enhances the price by means of law. Thus, monopoly ought not be feared nor even exist in a free society where the state merely acts as an impartial arbiter and policeman; the monopoly to be feared is the monopoly of power possessed by the government and utilized to favor one producer over others. Thus, the entrepreneur perceived as evil deserves no such incantation when he merely serves his purchaser without a forced exchange, for Adam Smith correctly saw that myriad persons, each following their own self-interest, are guided by an Invisible Hand to achieve the desired public result; the businessman merits opprobrium only when he seeks and gains an advantage by use of force or fraud, either individually or with the aid of a compliant state.

The Social Role of Business

We arrive at the seminal inquiry: what represents the social role of business in our community? Since "social" and "society" stem from the same root, the proper answer compels an understanding of two discrete concepts, the state and society.[7]

Society constitutes a voluntary, sharing, exchanging fraternity among consenting human beings. By nature, society is free and open-textured, permitting growth or termination at will as dictated by the mores, consciences and values of the participants. Simply put, one may enter or leave society at any time for any reason without penalty.

On the other hand, the state represents a coercive territorial body issuing commands which must be obeyed by all subjects. It rests on power, not contract. It is closed; one cannot debark without sanction, sometimes quite severe penalties. The state's existence derives from the nature of mankind and a Rule of Necessity: flawed and finite people possess destructive tendencies which must be curbed, ere freedom is lost for all.

Society and state co-exist and complement each other, each reflecting one of the dual aspects of human nature. Society fosters mankind's creative desires; the state obstructs the human disposition to coerce and destroy.

Open Competition

In the true sense, business only involves voluntary, nonaggressive human action. Thus, it provides the *means* for carrying out the *concept* of society. The state's role: provide a fair field and no favor. When the state takes a hand in business, it taints the process and the structure beyond recognition. Instead of retarding force and fraud, the interventionist state uses its power to tilt the field and afford special privileges to the few.

Business harmonizes with the open texture which delineates society. One may dissolve a business relationship without sanction, subject only to self-imposed contractual restraints and the reasonable promissory expectations of the parties. A consumer may cease using a manufacturer's product; a worker may stop laboring for a concern; a shareholder may sell his stock; all without reason or for any reason at all. Society fosters the creative inclination by providing harmonious surroundings and stimulating circumstances within which to live, work and exchange ideas, goods and services and to develop friendship, harmony and warmth. Business provides the mechanism by which such goods, services and ideas are created, transported and distributed under the voluntary exchange system which distinguishes society.

In the societal sense, then, the social role of business is simply business, to produce the best possible goods, services and ideas at the lowest possible cost and at the greatest possible profit for the entrepreneur. When business fulfills this role, it acts in harmony with society and its own nature by carrying out the function for which it is well and solely suited. In a word, society favors harmonious interchange of scarce economic goods to satisfy the most pressing subjective wants of mankind at the natural law cost; business provides the process to facilitate that interchange.

How Business Serves Society

Because business performs voluntary, creative and productive accomplishments by its very nature, it necessarily acts in the highest social role when it does what it is supposed to do. On the other hand, business is poorly equipped to achieve or carry out some sort of egalitarian social justice (which is not justice at all) or to redistribute income or wealth by means of transfer payments or to penalize less than virtuous conduct on the part of some individuals in society. Those who assign the foregoing aspects as business' social role fail to comprehend the nature of business: imposition of "social policy" normally embodies the dictation of A's value structure upon an unwilling B, a function best left to the state (the monopoly of coercive force) if to be performed at all. Creative entities and processes, like business, cannot easily expedite the destructive functions associated with the state.

All of this does not portend that business is not, and should not be a good neighbor. Most persons engaged in business normally act harmoniously with the universe and kindly toward their compatriots. They must obey the same moral laws as the rest of us do or suffer the identical moral consequences. However, the businessman ought not be forced to act as the moral arbiter of society: such a task would remain a blatant impossibility since no two persons maintain synonymous value standards at any time. If business misbehaves remedies exist: the consumer who disagrees possesses the perfect retort by nonviolently withholding commerce, and the state restrains the use of force and fraud by any predatory endeavor. By impressing these restrictions and no others upon the world of trade, we avoid the stultifying effects of prior restraint[8] which stifles creative enterprise and we accord business the freedom to serve the subjective needs of the populace.

—FOOTNOTES—

[1]By reason of the limitations of this paper, I confine my analysis of positive law and natural law to its most rudimentary form, reserving for separate treatment this most interesting and absorbing subject.

[2]This is the great teaching of Dr. Ludwig von Mises in his work on *Socialism,* which proves that a socialist society must import a market concept in order to price, plan and distribute economic goods. See Mises, Ludwig von, *Socialism* (Liberty Classics, Indianapolis [1936], [1951], [1969], 1981).

[3]Declaration of Independence of the United States of America.

[4]See Read, Leonard E., "I, Pencil" (The Foundation for Economic Education, Inc., Irvington-on-Hudson, New York).

[5]Several significant thinkers much more gifted than I have debunked the monopoly charade. See, e.g., Sennholz, Hans, "The Phantom Called 'Monopoly' ", VII *Essays of Liberty* 295–317 (1960) and D. T. Armentano, *The Myths of Anti-Trust* (Arlington House, New Rochelle, N.Y., 1972).

[6]Interestingly, the greatest diversity in products and widest range of choice exists not in the socialist economy allegedly designed for consumer protection but in the market economy characterized by freedom.

[7]See my detailed exposition of the nature and interrelationship of these two concepts in Foley, Ridgway K., Jr. "The Texture of Society", 27 *Freeman* 495–504 (August 1977).

[8]See Foley, Ridgway, K., Jr. "Prior Restraint", 31 *Freeman* 609–614 (October 1981).

Capital Formation

IDEAS ON LIBERTY

IT has often been found that profuse expenditures, heavy taxation, absurd commercial restrictions, corrupt tribunals, disastrous wars, seditions, persecutions, conflagrations, inundations, have not been able to destroy capital so fast as the exertions of private citizens have been able to create it.

THOMAS BABINGTON MACAULAY

Ralph Bradford

The American Idea

THE really significant American Revolution was not the military revolt that led to political independence from England, but the philosophical about-face which freed the developing American economy from the deadly shackles of bureaucratic control, and by liberating the creative energies of the people, made possible the miracle of American production.

That was the real American Idea—the idea of the Free Market. To some people that phrase had, and still has, only a commercial connotation; but in reality it had, and still has, a much broader significance. It refers not only to the free trading of goods in the market place, but to the untrammeled exchange of ideas, and to the fullest possible development of the human mind and spirit. It refers to such added aspects of liberty as freedom of speech and of the press. It means also freedom to write, and to create a literature. That was the true essence and spirit of the American Revolution.

Such concepts, it must be noted, were not new in the world. Here and there they had blossomed, and men had grown in spirit, and had prospered materially. We know this because, wherever and whenever this occurred, men were free in the large sense to follow the creative urge that resides deep in the human heart. They made pictures, they carved images, and, sooner or later, *they wrote!*

Ralph Bradford, noted poet, writer, speaker and business organization consultant, is now retired in Ocala, Florida.

On the skins of animals, on papyrus, on rock walls, on stone steles, on clay tablets—they wrote! Using pictures, or crude cursive script, or ideograms, or hieroglyphics, or cuneiform indentations—they wrote! What the chief said, what the king decreed, what the priests pronounced, what the artisan created, whether the harvest was good or bad, what the laws were—they wrote! They set it down. And thus in signs and symbols we have history far beyond any literature or language of the present century, or in the historic age of man.

Flashes of Freedom

Yes, *freedom,* which is a timeless torch, glowed brightly here and there through the centuries—obscured and destroyed now and then in one black era after another, to reappear and relive elsewhere as the fortunes of man, the developing animal, rose and fell with the ages.

But it had never been so carefully expressed, or as extensively implemented, as it was in America. It had even gained a foothold in parts of Europe for a time; but it was snuffed out there in the dark medieval centuries, and as a consequence the scale of human production, comfort and well-being had sunk to the level of general impoverishment and privation.

By the same token, the literary output of those times is practically non-existent. Only the troubadours survived the general intellectual impoverishment; and their songs, while sometimes poetically beautiful, are concerned mainly with the ephemeral splendors of court life, and with the evanescent beauties and languors of romantic love, usually of an illicit and clandestine character.

Getting back to America, it should be noted that the recent departures from the original American Idea—namely, the so-called "modern" notions about the need for governmental management and supervision of all our economic processes, *are not modern at all.*

Incidentally, they are not "liberal," either, though they are so termed by their supporters. The classical liberal concept was that of a government of sharply limited powers. The true liberal, from Thomas Jefferson to Woodrow Wilson, was afraid of big government. Jefferson, indeed, was afraid of *any* government. "The best governed," he once declared, "are the least governed." And as for Wilson, he wrote: "The history of liberty is a history of limitations of governmental power, not the increase of it."

And as to the "managed economy"—the idea of substituting the decisions of bureaucrats for the operation of the free market—all this is not new, or modern, or original, but very old. Examples are not hard to find, both in the literature *of* the

Romans and in that *about* the Romans. In the latter category, Gibbons' *Decline and Fall* is perhaps the most voluminous—and ponderous. Much easier to handle and digest is a book called *The History of the World in 300 Pages,* translated from the French of Rene Sedilot. In one section he describes the situation in ancient Rome. It sums up thus:

Under the Emperor *Alexander Severus* laws were decreed to control all businesses that were operated on accumulated capital, and loans were made by the government to people in certain categories for use in buying land. Under *Domitian,* in order to prevent over-production of wine the State ordered a portion of the grape vines to be uprooted. Under *Vespasian,* on the theory of spreading employment, a ban was laid on mechanization. Under *Diocletian,* in an effort to keep down the cost of living, both wages and prices were fixed by a state official.

Needless to say, all this created a vast and expensive bureaucracy. It also resulted in debt, inflation, and monetary devaluation. The *denarius* had its silver content progressively reduced. The weight of gold coins was scaled down by 50 per cent. Rome's balance of payments (due partly to her extensive foreign operations) showed a mounting deficit; and her gold and silver reserves melted away.

Need I go on? It all sounds very "modern," doesn't it? Yet it happened many years ago! And of course it had all occurred in similar fashion long before that—as in the state socialism of Egypt, with its "ever normal granary" operation; or as in the pre-Babylonian culture of the Sumerians, around 3000 B.C. It was also repeated later, with many repressive variations, in the guild systems of Europe's Middle Ages.

That Sumerian culture, by the way, has been substantially reconstructed by enterprising archeologists. They not only unearthed the capital city of Lagash, but found and deciphered the records of the Sumerian people. And it is in those records that we find some of the first expressions of what I consider to be the essence of what became the American Idea.

Free from Oppression, Free to Achieve

I said at the outset that that Idea was freedom, but we need to be explicit as to what we mean by that term. We associate freedom with the abstractions of political liberty—very properly so. However, that is not the entire meaning and content of freedom. To be free is not just to escape oppression. The true free man is free *from* something, of course—from tyranny, from abuse, from over-taxation; but he is also free *for* something—free for the purpose of self-development, of fulfillment, of self-expression. He is free to think, to question, to doubt, to believe, to speak, to write.

But the word "freedom" was not written down by some scribe for the inspiration and guidance of our colonial ancestors. It didn't have to be! They knew it, as it were, by instinct. It was born with them by reason of what they and their ancestors had suffered in its denial.

I have no wish to over-idealize those colonial days. Some of them were very dark days, indeed. There was privation, and hardship, and danger; there were cruelties and treacheries—for our ancestors were not all great and noble. Some came here to enjoy religious liberty, only to deny it to others who desired to live among them. But if I am realistic about the seamy side, I am also not disposed to discount the importance of those days in making possible the miraculous decades that followed.

Self-Responsible Individuals

The secret was that in the development of most of North America *men were on their own*. This was not true farther south. The Spaniards and Portuguese were nearly all sent out by the state, and that meant a curtailment of freedom at the very outset. When Columbus set out on his voyage, Queen Isabella furnished the ships and paid the crews. Columbus was to get a cut and receive certain honors; but he didn't defray the cost. In contrast, Queen Elizabeth didn't outfit Sir Walter Raleigh when he headed for what was to become Virginia. He had to "find" his outfit.

The same thing was true with respect to the other colonies in the North. They were "chartered" by the King or Queen, of course, but the state didn't finance the enterprise. That was done privately. Companies were formed. Shares were sold. Those who put their money into such enterprises were known as "adventurers"—not because they were personally going off to settle the wilderness, but because as investors they had "adventured" their money. If the trip paid off, if the Colony was successful, well and good. They would get their money back with interest and maybe with a profit. But they had no guarantee. The thing was not underwritten by the State. If it failed they took the loss.

And it was similarly so with the colonists themselves. Nobody guaranteed them against failure. They were face to face with wilderness reality. It was sink or swim. It was root hog or die. It was a rough, tough school; and of course it would be utterly repugnant to a certain type of politician and intellectual today—people who want the State to be a kind of universal Sugar Daddy. But it taught a great lesson. It was the essential conditioning for what followed—namely, the formalization and institutionalization of the American Idea in a structure of government. This was the mechanism for realizing the American Heritage.

In part, to be sure, that heritage consisted of a vast new continent, enormously rich in natural resources. But the same thing could be said of other lands—of South America, of Africa, of India. What made the difference? *Freedom!* Not just freedom from colonialism, not just political liberty, but freedom for growth, for development; freedom for the individual life to develop its capacities. How? *Through freedom from too much government!*

The Founders Hesitated to Put Their Trust in Government

Now to a generation that has grown up under an almost ceaseless propaganda for more and more government, it comes as a profound shock when I assert that the Architects of the American State had a deep distrust of government itself. But so it was; and the quotations I have cited above from Jefferson and Wilson were fairly representative of the attitude of most of the Founders.

It was in their bones, from the talk of fathers and grandfathers, who told vividly of State usurpations in the older countries. The Founders themselves had lived their lives under the relatively petty but persistent and cumulative tyrannies of the British Crown. They were determined that the new State they were creating should be limited in its powers, responsible to the people, and never allowed to dominate and control the lives of its citizens.

So what happened? It is no form of jingoism but a simple statement of historic fact to say that in less than 200 years the people of this country achieved a greater efficiency in production, and a more abundant distribution of the necessities, comforts and luxuries of life than had been attained anywhere, at any time, in all the centuries of history taken together.

The explanation of this paradox includes a number of factors; but the over-riding element is the simple fact that we have been free to make a better use of our energies and resources than most other peoples. And that freedom came from the circumstance that in all the period of our great growth and expansion as a nation, our government, by the deliberate design of its founders, gave us the protection of law—*and left us free to achieve.*

That was the American Idea in principle and that was the American Idea in practice.

Shall we keep it that way—or shall we trade it for the imagined comforts and benefits of the welfare state?

Back to Basics

It has been called the Reagan Revolution. But the movement that Burton Yale Pines describes and analyzes in his *Back to Basics* (New York: William Morrow, 349 pp., $13.50) goes much deeper than politics. It is a cultural movement that is invoking a return to tradition in religion and ethics and educational methods; and its support of free market economics has more to do with its belief in the moral value of free choice than with any purely economic concern with efficiency.

Mr. Pines once wrote cover stories for *Time* magazine, which presumably brought him into prolonged contact with Eastern Establishment ways of looking at things. But somewhere along the line he began to have sympathy for the large groups in society that had a feeling the so-called counterculture was pushing them to the brink. A first-rate reporter, he persuaded the American Enterprise Institute in Washington to support him in an eighteen-month job of measuring the depth of the traditionalist resurgence.

As luck would have it, he caught innumerable people at the very moment when they were moving from thinking into action. Ideas, said the late Richard Weaver, have consequences. And Mr. Pines began combing the country at a time of consequences, when businessmen were beginning to fight back against excessive regulation, when taxpayers were organizing to put a cap on both taxing and government spending, when parents were objecting to sloppy methods of teaching and aggressive anti-religious secularism in the schools, and when the New Right in Washington began to make its first fruitful contact with the Moral Majority at the grassroots.

Nomenclature bothers Mr. Pines a bit. The New Right and the Moral Majority are "rightist" in a political sense, but Mr. Pines properly observes that there is nothing political about the return to basics in education, or the quest for spirituality in religion, or the pro-family movement. "Conservative," Pines says, fits the movement better than "rightist," but there is nothing peculiarly conservative about a concern for national defense. Many liberals share a distaste for abortion with conservatives.

The Old-Fashioned Liberalism and The Traditionalist Movement

Looking for an umbrella word, Pines settles for "traditionalist." He notes that tradition, in America, includes a faith in conquering frontiers and building better societies, in political democracy and free market capitalism, in a federal system that protects the separate states, and in a "public ritual" that celebrates patriotism. In his discussion of names, Pines shows he has no quarrel with the old-fashioned liberalism of the nineteenth century. But to be useful today it has to be labeled "traditional liberalism," which makes out a tacit case for "traditionalist" as against such obfuscating descriptions as "neo-conservative."

Mr. Pines doesn't do much with the intellectual pioneers of the traditionalist movement beyond noting that George Nash has profiled many of them in his 1976 book, *The Conservative Intellectual Movement in America*. Of the pioneers he says, "prolific though they were, conservative intellectuals generally had but limited impact on the public policy process." This may seem a bit ungenerous of Mr. Pines, for, as the history of Britain shows, a Fabian Society must come before there can be any Fabian success at the polls. But Mr. Pines' decision to take for his starting line the emergence of such conservative or traditionalist institutes as the Heritage Foundation, the Hoover Institution and the American Enterprise Institute was correct for his purpose. What he is giving us is contemporary reportage, which is not yet history.

Pines' account of the epic fight of the Illinois Power Company against the Columbia Broadcasting System over an alleged mispresentation is battlefield reporting at its best. Business is only now beginning to break out of its silences, and Mr. Pines is an engaged man in his efforts to keep the momentum going. The battle of the W. R. Grace Company's Peter Grace for a change in the capital gains tax had an enormous impact: when 106 papers had published stories about Grace's embroilment with President Jimmy Carter, Congress cut the maximum rate from 49 per cent to 28 per cent. With businessmen turning to activism, students are also getting into the fight. There are 6,000 members of the new Students In Free Enterprise at 150 colleges, which is a big switch from the campus scene of the Nineteen Sixties and early Nineteen Seventies.

Keynes Losing Ground

Mr. Pines' front-line reporting took him to the University of Minnesota, whose economics department has been identified with Walter Heller, described by Pines as "America's best-known, most visible Keynesian." Well, Walter Heller is still at Minnesota. But he is "out of step with most of the exciting work now going on in the department." Pines notes that the new "glittering lights" at Minnesota now—Edward Prescott, Thomas Sargent, Christopher Sims, Neil Wallace—have all turned their backs on Keynes.

Pines quotes Tom Sargent, an enthusiastic advocate of the new "rational expectations" school of economics. "When I started teaching," said Sargent, "I gave my students the standard Keynesian stuff." But the "moment of truth" came for Sargent while he was working with Neil Wallace on a project at the Federal Reserve Bank in Minneapolis. A study that began as the "apotheosis of Keynesianism" started to crumble after eighteen months of work. "It was a tragic realization," so Sargent recalls. What Sargent and Wallace discovered was a fundamental flaw in the Keynesian analytical method itself. Sargent concluded that Keynesian "economic models do not work well; they give bad predictions."

Looking back to the days when he was teaching courses based on Keynesian analysis, Sargent says: "It makes me sick to my stomach." "I looked up to them," he says of the Keynesian "giants." "I would not have believed that these men could have been so wrong. It's been like discovering that your parents are wrong."

Mr. Pines wrote about the Equal Rights Amendment before it had encountered its doomsdate on June 30 of this year. But he accurately notes that in fighting to keep ERA out of the Constitution, Phyllis Schlafly, Lottie Beth Hobbs, Jo Ann Gasper and other supporters of the "traditionalist" family proved that women could exercise their rights of free speech just as effectively as men even without a new amendment. Since the Constitution already guarantees the "equality" of all citizens without reference to sex, the ERA would have been redundant. Its proponents said it was needed as a "symbol." But the fight against it by Mrs. Schlafly in favor of the "traditional" family was symbolic, too. And traditionalism, says Pines, will go on winning.

THE DOMINION COVENANT: GENESIS
by Gary North
(The Institute for Christian Economics, P.O. Box 8000, Tyler, Texas 75711) 1982
496 pages ■ $14.95 cloth

Reviewed by Edmund A. Opitz

GARY NORTH's name is well known to readers of *The Freeman* as the author of a score of articles, lucidly written and well argued. His fortnightly newsletter, *Remnant Review,* contains brilliant analyses of current economic and political trends, and offers sound advice for those who are struggling to hold body and soul together during this trying period in the world's history. His Institute for Christian Economics issues four publications, one monthly, three bimonthly. It also publishes books, tapes and home study courses. A Divinity School is on the drawing board.

Dr. North seems to get more things done than any two ordinary people, and all is done well. But central to his life's purpose is the writing of a multi-volume *economic* commentary on the Bible. Of ordinary exegetical works there is a profusion, but no one, to my knowledge, has ever gone through the Bible book after book to see what the whole Bible has to say about the way our economic activities should be organized. Dr. North has dedicated himself to this task, and the formidable book before us is volume I.

Gary North's doctoral thesis explored the economic thought of the New England Puritans. His theological convictions lie in this area, that is, within the orthodoxy laid down by John Calvin. Calvinism strikes some as a legalistic and cheerless creed. But that Calvin's was a powerful mind no one can deny, and it is equally true that Calvinism has attracted minds of the highest caliber from its early days to the present time. Basing their theology on an infallible Book, Calvinist thinkers put modernity to the test and find it wanting; it is man-centered not God-centered and this causes everything to be more or less skewed.

Gary North starts at the beginning, with Genesis 1:1, and by the time he reaches Genesis 50:20 he has written a book of 496 pages and displayed a sure-footed understanding of Biblical theology, science, sociology, free market economics, Darwinism, Marxism, and sundry other issues. There is heavy stuff here, but the writing is lively and heavy does not mean dull. There will be readers who will find something to disagree with on every other page, but even the most sceptical—if they can think at all—will find much to ponder.

Readers who want a basic course in Austrian economics will find it here, supplied with Biblical reinforcement of key points. If it is light on the Creation vs. Evolution controversy, there is a 77-page appendix with 203 footnotes. There are strong opinions on almost every page, and a twenty-page index enables the reader to find his way around in the book.

Twentieth-century socialism has made deep inroad among the more liberal church bodies, and it has recently gained a foothold among Evangelicals. Which makes it appropriate to note here the appearance of a second edition of David Chilton's fine polemic (*Productive Christians in an Age of Guilt-Manipulators,* I.C.E., Box 8000, Tyler, Texas 75711). The New Preface is by Dr. North.

MARKETS AND MINORITIES

by Thomas Sowell
(Basic Books, Inc., 10 East 53rd Street, New York, N.Y. 10022) 1981
141 pages ■ $12.95 cloth, $5.95 paperback

Reviewed by Tommy W. Rogers

THOMAS SOWELL demonstrates that many of the things we "know" about ethnicity and economic status are not so. Variables commonly thought of as decisive, skin color, for example, prove on examination to be far from determinative. Orientals and black West Indians are more economically successful than are some white groups. Commonly overlooked variables, such as fertility, socialization, and attitudinal and behavioral disposition, have a significant impact on incomes and occupations.

Sowell presents some revealing facts: The incomes of ethnic minorities differ so widely within the group as to call into question the meaningfulness of comparisons based on national averages; discrimination cannot account for the incomes of minorities who earn more than the national average; the lower earnings of some groups are not necessarily explainable by discrimination since other factors may be determinative.

With respect to the application of this analytical process, Dr. Sowell outlines his methodology:

> In applying the general logic of decision-making to particular social processes, we will examine the peculiarities of those processes but will treat human beings as similar, whether they are in politics or business or the schools . . . We will also avoid making "the market" an automatic producer of certain results, but will instead consider what kinds of markets are being analyzed, and what incentives and constraints exist in such markets. The whole emphasis will be on the specific characteristics of particular decision-making processes—not on a vague figure of speech called "society."

Sowell examines the operation of incentives and constraints as influenced, for example, by intergroup differences, job markets, consumer markets, and government regulation. Groups with strong family and community ties—such as Chinese, Japanese, and Jews—have been prominent as entrepreneurs, setting up businesses drawn from resources within the ethnic community. Jews often started as pushcart peddlers, Chinese as operators of laundries. Blacks, Sowell observes, have seldom set up independent businesses, but the subsets of Blacks who have (Black West Indians, Black Muslims, and followers of Father Divine's religious sect) contrast sharply with the massive failures in the prosperous 1960s and 1970s of Black businesses financed by the federal government in programs created by "experts" and often receiving preferential treatment by banks and private and governmental purchasers.

Dr. Sowell calls attention to the fact that some of the most dramatic rises from poverty to affluence in the United States have taken place among groups who did *not* follow the political route to economic advancement, i.e., the Chinese, Japanese, and generally, the Jews. The most politically successful American ethnic group—the Irish—were the slowest rising of the nineteenth-century European immigrant groups.

Dr. Sowell also calls attention to the important role of the values people cherish; the *behavior pattern* of group is a crucial variable in both racial and non-racial contexts. He quotes the rueful conclusion of reformer Jacob Riis that some people "carry their slums with them wherever they go." Dr. Sowell believes there is no compelling reason to believe that government activity has benefited ethnic minorities on net balance, even when that has been its purpose. Furthermore, the fickleness of government policy suggests that determining its purpose over some meaningful span of time is not easy, since "whatever the merits or demerits of government policies (relating to minorities), nothing seems surer from history than that those policies will change."

Contrasting the results of voluntary economic transactions ("the market") with governmental intervention which forces, penalizes, or subsidizes decisions different from those which the transactors would have preferred, he finds numerous instances where even well-intentioned interventions have thwarted the efforts of ethnic groups to advance. As Dr. Sowell points out, economic analysis does not make human beings better or more moral, but it does offer insight into the way different economic institutions affect the well-being of human beings as they are.

Dr. Sowell is without question one of the leading economists in the

United States. When he writes or speaks he is worth heeding. Milton Friedman describes *Markets and Minorities* as a breath of fresh air on a topic which is often prejudiced by unreasoning emotion. Sowell's book deserves to become a classic in the literature on the economic and social problems of minorities. If it does not so become, it will not be due to any deficiency of analysis or presentation.

THE PURSUIT OF VIRTUE AND OTHER TORY NOTIONS

by George F. Will

(Simon and Schuster, Inc., 1230 Avenue of the Americas, New York, N.Y. 10020)

397 pages ■ $16.50 cloth

Reviewed by Joseph S. Fulda

WHETHER one follows his twice-weekly columns, reads his bi-weekly essays, or enjoys his lively comments as a television panelist, one cannot fail to be impressed with George Will's expressive erudition. No other contemporary columnist has quite his way with words or quite his ability to extract, in a thousand words or so, that which is " 'inside' public matters: not what is secret, but what is latent, the kernel of principle and other significance that exists, recognized or not, 'inside' events, policies and manners." Will's latest collection of essays and columns is truly a restorative for those with Tory sensibilities and "the understanding that education consists primarily of arguing from, not with (one's) patrimony."

In more than six score finely fashioned, tightly reasoned pieces, two distinctly different Tory sensibilities emerge. The first is the conscience of the cultural conservative lamenting "the decline of almost everything since 1914" of "stained glass minds" which, not altogether jokingly, "mourn the passing of the thirteenth century: feudal codes, heraldic banners, serried ranks of bishops . . ." This is Will at his best, Will the social critic, conveying his urgent concern that Americans not lose what he terms "social sympathy": "the ability to comprehend, however dimly, how other people (must) live."

This is the Will educated at Oxford ("Like civilization, it is cumulative, complicated, old and densely packed.") who reminds us that education "presupposes students who acknowledge their incompleteness and teachers who believe that the purpose of education is to put something into students rather than to let something—'self-expression'—out."

But there is a second Tory voice which makes itself heard in Will's pages, and it is political. This is the argument that since "social and cultural anxieties find their way onto a society's political agenda" it is well to use government as "an instrument of conservative values, tempering and directing social dynamism." Will believes, indeed, with much of the New Right, that the "nation's moral makeup is, today, soft wax on which national leadership can leave a long-lasting impress." Needless to say, this is not the classical liberal's view of the rightful role of the state, and George Will does not present it as such. "The overriding aim of liberalism, properly understood, is the expansion of liberty . . . Conservatism, properly understood, rejects the idea of a single overriding aim. Real conservatism is about balancing many competing values . . ." Well, life *is* about balancing competing values, but the classical liberal does not want such decisions made in the political realm. Not all of us have the same values, similarly ranked, and it is thus that liberty is not only itself a value but also the sine qua non for all personal value choices: it is not the role of government to undertake the balancing of competing values.

To Will, ". . . libertarianism is a recipe for the dissolution of public authority, social and religious traditions, and other restraints needed to prevent license . . ." To call oneself a "libertarian conservative," he asserts, is a label as contradictory as "promiscuous celibate." But few libertarians are nihilists, and those who are never redeem themselves with the nobel label "conservative." The truth is that confusion is being promoted here at a rather elementary level: the doctrine that morality ought not to be imposed is philosophically distinct from the doctrine that there is no morality.

If Will sees liberty in general as the antithesis of sustained virtue rather than as the crucible out of which virtue is formed, his attitude towards capitalism is even less satisfying. It is not animus, by any means, but rather what George Gilder aptly labelled "the dirge of triumph."

The 1980 Republican platform, Will argues, is woven from two incompatible strands. "One is cultural conservatism. The other is capitalist dynamism. The latter dissolves the former." This, says Will, is perhaps the only point Marx got right. Capitalism, he continues, is a "relentless engine of change, a revolutionary inflamer of appetites, enlarger of expectations, and diminisher of patience." "Republicans," he warns, "see no connection between the cultural phenomena they deplore and the capitalist culture they promise to intensify." For Will this tension between the bourgeois ethic and conserving social values presents an "especially vexing" dilemma—that of "deciding what is to be conserved, and how."

Mainstream conservatives can, however, and for the most part do, accept the position of Frank S. Meyer and Friedrich A. Hayek, that the alleged tension between social conservatism and economic freedom is largely given the lie by history. The first century of our nationhood saw both morality and piety, on the one hand, and freedom and the private property order, on the other. Rather than working against each other, freedom and tradition reinforce each other as Hayek so beautifully exposited in *The Constitution of Liberty.* Will writes that "Capitalism means the liberation and incessant flaming of appetites," the "predictable consequence" of which is "social disintegration." But, as Will should know, that is not the way things worked out. Social disintegration was brought on by slavery, not liberty, and later by intervention, not economic freedom.

But these are subordinate matters, among philosophical soulmates, for on almost any specific policy issue, Will's instincts are not with the statists. In essays such as "Government and the 'Cheerleader Problem'," "The FTC as Federal Nanny," and "Sexism in the Car Pool: DOT Rides to the Rescue," Will proves himself as witty an antistatist as ever was. But perhaps his finest writings are his legal analyses, which give one "the joy, than which there is nothing purer, of an argument firmly made, like a nail straightly driven, its head flush to the plank."