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"I'm for the Achiever"

I HAVE just about reached the end of my tolerance for the way our society now seems to have sympathetic concern only for the misfit, the pervert, the drug addict, the drifter, the chronic criminal, the under-achiever. It seems to me we have lost touch with reality and become warped in our attachments.

I feel it is time for someone like me to stand up and say, in short, "I'm for the upperdog!"

I'm for the achiever—the one who sets out to do something and does it; the one who recognizes the problems and opportunities at hand, and endeavors to deal with them; the one who is successful at his immediate task because he is not worrying about someone else's failings; the one who doesn't consider it "square" to be constantly looking for more to do, who isn't always rationalizing why he shouldn't be doing what he is doing; the one, in short, who carries the work of his part of the world squarely on his shoulders.

It is important to recognize that the quality of any society is directly related to the quality of the individuals who make it up. Therefore, let us stop referring naively to creating a "great" society. It is enough at this stage of our development to aspire to create a *decent* society. And to do so, our first task is to help each individual be decent unto himself and in his relationship with other individuals.

We will never create a good society, much less a great one, until individual excellence and achievement are not only respected but encouraged. That is why I am for the upperdog—the achiever, the succeeder.

—Miller Upton

THE FOUNDATION FOR ECONOMIC EDUCATION, INC.
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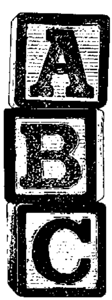
Henry Hazlitt

The ABC of a Market Economy



THERE are basically only two ways in which economic life can be organized. The first is by the voluntary choice of families and individuals and by voluntary cooperation. This arrangement has come to be known as the free market. The other is by the orders of a dictator. This is a command economy. In its more extreme form, when an organized state expropriates the means of production, it is called socialism or communism. Economic life must be primarily organized by one system or the other.

It can, of course, be a mixture, as it unfortunately is in most nations today. But the mixture tends to be unstable. If it is a mixture of a free and a coerced economy the coerced section tends constantly to increase.

One qualification needs to be emphasized. A "free" market does not mean and has never meant that everybody is free to do as he likes. Since time immemorial mankind has operated under a rule of law, written or unwritten. Under a market system as any other, people are forbidden to kill, molest, rob, libel or otherwise intentionally injure each other. Otherwise free choice and all other individual freedoms would be impossible. But an economic system must be dominantly either a free or a command system.

Ever since the introduction and spread of Marxism the great majority of people who publicly discuss economic issues have been confused.

Henry Hazlitt, a frequent contributor to *The Freeman,* has been a Trustee of The Foundation for Economic Education from its beginning in 1946. He is a noted economist, author, editor, reviewer and columnist. Best known of his numerous books is *Economics in One Lesson,* first published in 1946, with ten translations and with American sales of more than 700,000 copies, recently revised and available in inexpensive paperback. He celebrated his 90th birthday November 28, 1984. His working library is now housed at FEE.

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Recently a very eminent person was quoted as denouncing economic systems that respond "only to the forces of the market place," and are governed "by the profit motive of the few rather than the needs of the many." He warned that such a system could put "the world's food supply into even greater jeopardy."

The sincerity of these remarks is beyond question. But they show how phrases can betray us. We have come to think of "the profit-motive" as a narrowly selfish drive confined to a small group of the already-rich whose profit comes at the expense of everybody else. But in its widest sense the profit-motive is one that all of us share and must share. It is our universal motive to make conditions more satisfactory for ourselves and our families. It is the motive of self-preservation. It is the motive of the father who is not only trying to feed and house himself but his wife and his children, and to make the economic conditions of his whole family, if possible, constantly better. It is the dominant motive of all productive activity.

Voluntary Cooperation

This motive is often called "selfish." No doubt in part it is. But it is hard to see how mankind (or any animal species) could have survived without a minimum of selfishness. The individual must make sure he himself survives before the species can survive. And the so-called profit-motive itself is seldom solely selfish.

In a primitive society the "unit" is seldom the individual but the family, or even the clan. Division of labor begins within the family. The father hunts or plants and harvests crops; the mother cooks and bears and nurses children; the children collect firewood, and so forth. In the clan or the wider group there is even more minute subdivision and specialization of labor. There are farmers, carpenters, plumbers, architects, tailors, barbers, doctors, lawyers, clergymen, and so *ad infinitum.* They supply each other by exchanging their services. Because of this specialization, production increases more than proportionately to numbers; it becomes incredibly efficient and expert. There develops an immense system of voluntary productive cooperation and voluntary exchange.

Each of us is free (within certain limits) to choose the occupation in which he himself specializes. And in selecting this he is guided by the relative rewards in this occupation, by its relative ease or difficulty, pleasantness or unpleasantness, and the special gifts, skills, and training it requires. His rewards are decided by how highly other people value his services.

Free-Market Economy

This immense cooperative system is known as a free-market economy. It was not consciously planned by anybody. It evolved. It is not perfect, in the sense that it leads to the maximum possible balanced production, and/or distributes its rewards and penalties in exact proportion to the economic deserts of each of us. But this could not be expected of any economic "system." The fate of each of us is always affected by the accidents and catastrophes as well as the blessings of nature—by rainfall, earthquakes, tornadoes, hurricanes, or what not. A flood or a drought may wipe out half a crop, bringing disaster to those growers directly hit by it, and perhaps record-high prices and profits to the growers who were spared. And no system can overcome the shortcomings of the human beings that operate it—the relative ignorance, ineptitude, or sheer bad luck of some of us, the lack of perfect foresight or omniscience on the part of all of us.

No system can overcome the shortcomings of the human beings that operate it—the relative ignorance, ineptitude, or sheer bad luck of some of us, the lack of perfect foresight or omniscience on the part of all of us. But the ups and downs of the market economy tend to be self-correcting.

But the ups and downs of the market economy tend to be self-correcting. Over-production of automobiles or apartments will lead to fewer of them being produced the following year. A short crop of corn or wheat will cause more of that crop to be planted the following season. Even before there were government statistics, producers were guided by relative prices and profits. Production will tend to be constantly more efficient because the less efficient producers will tend to be weeded out and the more efficient will be encouraged to expand output.

The people who recognize the merits of this system call it the market economy or free enterprise. The people who want to abolish it have called it—since the publication of *The Communist Manifesto* in 1848—capitalism. The name was intended to discredit it—to imply that it was a system developed for and by the "capitalists"—by definition the disgustingly rich who used their capital to enslave and "exploit" the "workers."

The whole process was grossly distorted. The enterpriser was putting his accumulated savings at risk at what he hoped was an opportunity. He had no prior assurance of success. He had to offer the going wage or better to attract workers from their existing employments. Where the more successful enterprisers were, the higher wages also tended to be. Marx talked as if the success of every new business undertaking was a certainty, and not a sheer gamble. This resulted in his condemning the enterpriser for his very risk-taking and venturesomeness. Marx took profits for granted. He seemed to assume that wealth could never be honestly earned by successful risk-taking but had to be inherited. He ignored the record of constant business failures.

But the label "capitalism" did pay unintended tribute to one of the system's supreme merits. By providing rewards to some of the people who risked investing their capital, it kept putting into the hands of the workers more and constantly better tools to increase per capita production more and more. The system of private property and capitalism is the most productive system that has ever existed.

The label "capitalism" did pay unintended tribute to one of the system's supreme merits. By providing rewards to some of the people who risked investing their capital, it kept putting into the hands of the workers more and constantly better tools to increase per capita production more and more.

The Communist Manifesto was an appeal to "the masses" to envy and hate the rich. It told them that their only salvation was to "expropriate the expropriators," to destroy capitalism root and branch by violent revolution.

Marx attempted a rationalization of this course, built upon what he saw as inevitable deductions from a doctrine of Ricardo. That doctrine was in error; in Marx's hands the error became fateful. Ricardo concluded that all value was created by "labor" (which might almost be true if one counted labor from the beginning of time—all the labor of everybody that went into the production of houses, land clearing, grading, plowing, and the creation of factories, tools and machines. But Marx chose to use the term as applying only to *current* labor, and the labor only of hired employees. This completely ignored the contribution of capital tools, the foresight or luck of investors, the skill of management, and many other factors.

Economically, communism has proved a complete disaster. Not only has it failed to improve the welfare of the masses; it has appallingly depressed it. Before its revolution, the great annual problem of Russia was to find sufficient foreign markets for its crop surpluses. Today its problem is to import and pay for less than adequate foodstuffs.

The Errors of Marx

The theoretical errors of Marx have since been exposed by a score of brilliant writers. In fact, his preposterous conclusions could also have been proved wrong even at the time *Das Kapital* appeared by a patient examination of the available contemporary knowledge of incomes, payrolls and profits.

But the day of organized, abundant and even "official" statistics had not yet come. To cite only one of the figures we now know: In the ten years from 1969 to 1978, inclusive, American "nonfinancial" corporations were paying their employees an average of 90.2 per cent of the combined total available for division between the two groups, and only 9.8 per cent to their stockholders. The latter figure refers to profits after taxes. But only about half of this amount—4.1 per cent—was on the average of those ten years paid out in dividends. (These figures compared with public-opinion polls taken at the time which showed a consensus of most Americans that corporate employees got only 25 per cent of the total available for division and the stockholders 75 per cent.)

Yet the fierce diatribes of Marx and Engels led to the Russian Revolution of 1917, the slaughter of tens of thousands, the conquest and communization by Russia of some half-dozen neighboring countries, and the development and production of nuclear weapons that threaten the very survival of mankind.

Economically, communism has proved a complete disaster. Not only has it failed to improve the welfare of the masses; it has appallingly depressed it. Before its revolution, the great annual problem of Russia was to find sufficient foreign markets for its crop surpluses. Today its problem is to import and pay for less than adequate foodstuffs.

Yet *The Communist Manifesto* and the quantity of socialist propaganda which it inspired continue to exert immense influence. Even many of those who profess themselves, quite sincerely, to be violently "anticommunist," feel that the most effective way to combat communism is to make concessions to it. Some of them accept socialism itself—but "peaceful" socialism—as the only cure for the "evils" of capitalism. Others agree that socialism in a pure form is undesirable, but that the alleged "evils" of capitalism are real—that it lacks "compassion," that it does not provide a "safety net" for the poor and unfortunate; that it does not redistribute the wealth "justly"—in a word, that it fails to provide "social justice."

And all these criticisms take for granted that there is a class of people, our officeholders, or at least other politicians whom we could elect in their place, who could set this all right if they had the will to do so.

And most of our politicians have been promising to do exactly that for the last half century.

The trouble is that their attempted legislative remedies turn out to be systematically wrong.

It is complained that prices are too high. A law is passed forbidding them to go higher. The result is that fewer and fewer items are produced, or that black markets develop. The law is ignored, or finally repealed.

It is said that rents are too high. Rent ceilings are imposed. New apartments cease to be built, or at least fewer of them. Old apartment buildings stand vacant, and fall into decay. Higher rents are eventually legally allowed, but they are practically always set below what market rates would be. The result is that tenants, in whose supposed interest the rent controls were imposed, eventually suffer as a body even more than landlords, because there is a chronic shortage of housing.

Wages are supposed to be too low. Minimum wages are fixed. The result is that teen-agers, and especially black teen-agers, are thrown out of work and on the relief rolls. The law encourages strong unions, and compels employers to "bargain collectively" with them. The result is often excessive wage-rates, and a chronic amount of unemployed.

Unemployment relief and Social Security schemes are put into effect to provide "safety nets." This reduces the urgency for the unemployed to find new or better-paid work and reduces their incentive to look. Unemployment payments, Social Security and other such safety nets continue to grow. To pay for these, taxes are increased. But they do not raise the expected revenue, because the taxation itself, reducing profit incentives and increasing losses, reduces enterprise and production. The spending and safety nets are increased. Deficit spending appears and increases. Inflation appears, demoralizing production further.

Sad to relate, these consequences have appeared in country after country. It is hard to find a single country today that has not become a bankrupt Welfare State, its currency constantly depreciating. Nobody has the courage to suggest dismantling it or to propose reducing its handouts or safety nets to affordable levels. Instead the remedy proposed everywhere is to "tax-the-rich" (which turns out everywhere to include the middle-classes) still more, and to redistribute the wealth.

It is only when each of us has provided for more than his own needs that he can acquire a surplus to help meet the needs of others. Voluntary cooperation is the key.

Guided by Profit

Let us return to our point of beginning. The eminent person that I quoted then is mistaken when he tells us that we are governed by the profit-motive of the few rather than the needs of the many. The profit-motive is simply the name for the practically universal motive of all men and all families—the motive to survive and to improve one's condition. Some of us are more successful at this effort than others. But it is precisely the profit-motive of the many that must be our main reliance for supplying the needs of the many.

It is strange that so little recognition is given to the fact that a man cannot grow richer without making others richer, whether that is his intent or not. If he invests and starts a new and successful business, he must hire an increasing number of workers, and raise wages by his own increased demand. He is supplying his customers either with a better product than they had before, or as good a product at a cheaper price, in which case they have more money left to buy other things. Even if he uses his own receipts only to increase his own consumer demand, he helps provide more employment or higher pay; but if he reinvests his profits to increase the output of his business, he directly provides more employment, more production, more goods.

So let us be thankful for the successful profit-motive in others. Of course, none of us should respond "*only* to the forces of the marketplace." Fortunately few of us do. Americans are not only among the richest people in the world today but among the most generous. It is only when each of us has provided for more than his own needs that he can acquire a surplus to help meet the needs of others. Voluntary cooperation is the key.

Clarence B. Carson

CAPITALISM: YES and NO

SOME terms and phrases are well suited to lucid discourse and even debate. This is generally the case when they have a commonly accepted meaning, when they are generally used—or are capable of being used—with some precision, and when they are not overloaded with connotations. The fact that people differ as to the value or desirability of what the terms signify does not disqualify them. Otherwise, debaters would have to employ different terminology, depending on which side they were on. For example, it seems to me that "free market" meets the criteria of a phrase well suited to discourse and debate.

That is, "free market" has a commonly accepted meaning, can be used with precision, and is not overloaded with meaning so as to be value laden. A free market is a market open to all peaceful traders, one in which sellers are free to sell to the highest bidder and buyers are free to buy what they will from whatever seller they will. Or, to put it another way, it is a market in which buyers and sellers are free to contract without obstruction or interference from government.

Thus, when government intervenes in the market so as to restrict the number of sellers or buyers, to set prices, or to prescribe quality, it is not a free market. It is possible to oppose or favor such a market while agreeing as to what constitutes a free market. Nor do differences as to the extent of freedom entailed necessarily rule out the use of the phrase in discourse.

Dr. Carson specializes in American intellectual history. He has written a number of books, including *Organized Against Whom? The Labor Union in America*. His latest are volumes I and II of a series, *A Basic History of the United States*.

In a similar fashion "free enterprise" and "private property" generally meet the tests as terms of discourse. Enterprise is free when all who can and will may produce and dispose of their goods to willing buyers. The opposite of free enterprise would be government granted monopoly over any field of endeavor, or the restriction of it through franchises, licenses, or other devices which exclude some enterprisers. The phrase can be used both by those who favor and those who oppose it, though those who oppose it might prefer other language. Private property is simply property that is privately owned, and the owner is protected in his enjoyment of it by government. I have not, of course, exhausted the distinctions nor covered all the areas about which disagreement may exist, for any of these phrases, but it was my purpose only to make a prima facie case for them as terms of discourse.

Capitalism: A Value-Laden Word

The same does not go, however, for "capitalism." It does not have a commonly accepted meaning, proponents of it to the contrary notwithstanding. As matters stand, it cannot be used with precision in discourse. And, it is loaded with connotations which make it value laden. Indeed, it is most difficult for those who use it from whatever side not to use it simply as an "angel" or "devil" word, i. e., to signify something approved or disapproved. Meanwhile, what that something is goes largely unspecified because it is hidden beneath a blunderbuss word.

My considered opinion is that capitalism is not a descriptive word at all in general usage. Dictionary-like definitions may give it the appearance of being descriptive. One dictionary defines it as "a system under which the means of production, distribution, and exchange are in large measure privately owned and directed." On the face of it, the meaning may appear clear enough. We can come in sight of the difficulty, however, if we turn the whole thing around and look at what is supposed to be signified, shutting out of our minds for the moment the word used to signify it. Suppose, that is, that we have a set of arrangements in which the means of production, distribution, and exchange of goods "are in large measure privately owned and directed." I am acquainted with such arrangements, both from history and from some present day actualities.

But why should we call such arrangements "capitalism"? So far as I can make out, there is no compelling reason to do so. There is nothing indicated in such arrangements that suggests why capital among the elements of production should be singled out for emphasis. Why not land?

Why not labor? Or, indeed, why should any of the elements be singled out? Well, why not call it capitalism, it may be asked? A rose by any other name, Shakespeare had one of his characters say, would smell as sweet. That argument is hardly conclusive in this case, however, nor in others similar to it. Granted, that when a phenomenon is identified it may be assigned a name, and in the abstract one name will do as well as another, if the name be generally accepted. In the concrete, however, the name should either follow from the nature of the phenomenon or be a new word. Otherwise, it will bring confusion into the language.

Marxist Derivations

Capitalism, as a word, does not conform to these strictures. Its root is capital, an already well established word in economics, used to refer to one of the elements of production. Moreover, capital*ism* gave a form to the word that already had a more or less established significance. When an "ism" is added to a word it denotes a system of belief, and probably what has come to be called an ideology. It is highly unlikely, if not linguistically impossible, for such a formulation to serve as a neutrally descriptive word for the private ownership of the means of production, and so on.

But we are not restricted to theory in our efforts to discover whether capitalism is simply a neutrally descriptive word. It was given currency in the highly charged formulations of Karl Marx and other enemies of private property. Marx's fame hardly stemmed from any powers he may have had for neutral description. On the contrary, he is best known for his extensive efforts to reduce all of reality and all relationships to the point where they fitted within the ideological scheme of class struggle. He had the kind of mind that reduces everything to a place within a single dominant system. Thus, the private production of goods is a system, a system reduced in his scheme to capitalism.

In discussing the dictionary-like definition of capitalism, I dropped the word "system" used in the dictionary and substituted the word "arrangement" for it. I did so because it seemed to me that a society could have arrangements in which the production of goods would be privately owned without this constituting a system. Arrangements for distinguishing between claimants of property and protecting such claims are necessary in society. But, "system" is ominous when linked to capitalism on the one hand and the production, distribution, and exchange of goods.

Private ownership of the means of production does not dictate any particular mode of production. In point of fact, a great variety of modes of production do occur under private ownership. A man may own his own land and cultivating devices and produce what he will by his own efforts. Many have, and some do. Or, to take the other extreme, production may be organized in great factories by intricate division of labor and under extensive supervision and direction. Between these two extremes, there are in fact a great range of ways in which production and distribution have been and are carried on. Indeed, it is only where private property is the rule that this variety is possible.

In Marx's mental world this variety and diversity could not exist, or, if it did, it could not last. It must all be finally reduced to a single system—capitalism. And capitalism led to greater and greater concentrations of wealth until all was in a few hands. Then, of course, the apocalypse must come, the revolution, in which an impoverished proletariat would rise up in its wrath and seize the instruments of production, and so on and on through the whole Marxian scenario. The word "capitalism" still carries the overtones of this Marxian analysis. For example, the dictionary from which was drawn the earlier definition gives as further definitions of capitalism: "the concentration of capital in the hands of a few, or the resulting power or influence," and "a system favoring such concentration of wealth." Another dictionary says, "The state of owning or controlling capital, especially when tending to monopoly; the power so held."

The High Cost of Salvage

In sum, capitalism gained its currency from Marx and others as a blunderbuss word, misnames what it claims to identify, and carries with it connotations which unfit it for precise use in discourse. Even so, there has been a considerable effort to reclaim the word for discourse by some of those who are convinced of the superiority of privately owned capital in the production, distribution, and exchange of goods. It is a dubious undertaking. For one thing, Marx loaded the word, and when all that he put into it has been removed, only the shell remains. For another, linguistically, it does not stand for private property, free enterprise, and the free market. It is false labeling to make it appear to do so. Capitalism means either a system in which capital holds sway, which is largely what Marx apparently meant, or an ideology to justify such a system.

It is not my point, however, that it might not be possible to use capitalism as a label for private property, free enterprise, and the free market. Indeed, I think it has been done at what I call the bumper sticker level of discourse in the United States. Undoubtedly, if enough effort were put into it the name of roses could be changed to tomatoes. But I doubt that the game is worth the candle. Moreover, there is no real discourse, discursive reasoning, at the bumper sticker level. Bumper stickers assert; they do not reason or prove. So do titles of books, for examples. But labeling is an inferior art, and name calling is a form of propaganda. Thus, the problem of discourse with a word such as capitalism remains.

It is not my intention, however, to suggest that we should discard the word capitalism. Far from it. Rather, I see the need for the use of the word in its inherent sense in serious discourse. A word, certainly a word formed with an "ism" suffix, is governed by and takes its meaning from its root. Granted, words sometimes slip their moorings in the course of time and lose all connection with earlier meanings. This is apt to happen, I suspect, when the root word has fallen into disuse. That has by no means happened in the case of capital. Capital itself is as important today as ever, and the word is still in widespread use to describe it with considerable precision. Moreover, something that I would like to see correctly identified as capitalism is widespread, if not rampant, in the world.

Keeping in mind that capitalism, because of the "ism," is ideological in form, it means most basically an ingrained preference for capital over the other elements of production. That is, it means an imbedded preference for (or commitment to) capital over land and labor. Considered as a system, capitalism is the establishment of that preference by the exercise of government power. To put it into more precise economic terms, it is the forced transformation of some greater or lesser portion of the wealth of a people into capital. In political terms, it is the legalization and institutionalization of a preference for capital.

State Capitalism

Ironically, in view of Marx and socialist doctrine generally, capitalism is most rampant in Communist countries. It is there that the most extreme measures are taken to accumulate capital. The Soviet Union, for example, has long used slave labor to mine gold in forbidding climes. It has done the same for cutting timber in the arctic cold of Siberia and for reaching other hard to get natural resources. The basic aim of much of this is capital accumulation to foster industrialization. There is perhaps no better way to visualize the preference for capital over labor than political prisoners (slave labor) working in gold mines. But it does take other forms. There is confiscatory taxation, in which most of the wealth of all who produce is taken away for use by the state. The capital hunger in Third World countries is ravenous today, as they reach out to try to obtain it from countries in which there is more wealth. The thrust is for industrialization, and the industries are usually owned by the government.

Some writers who have noted this penchant of socialist and Communist countries for capital have called it state capitalism. While the phrase is not objectionable, it may well be redundant. If my analysis is correct, all capitalism is state imposed capitalism. Otherwise, it is most unlikely that there would be an established preference for capital over land and labor.

Granted, some people in their private affairs do evince a preference for capital over other sorts of expenditures. I have known men, for example, who were much more given to buying tools and various equipment than clothes. But then the same men often spend more on automobiles, not usually capital expenditures, than on either. Nor is it likely that businessmen, however enamored they may be with machinery or computers, will make so bold as to ignore the market for long in determining the mix of the elements of production. Only governments, because they spend what they have not earned, can afford to do that or have the power to require others to ignore the market. Capitalism is a will of the wisp unless it is established by the state.

A Red Herring

The notion that the conflict in the world is between capitalism and socialism is a Marxian red herring. Whether Marx deliberately conceived a perverse term to designate the conflict or not, it has had remarkable success in confusing the issue. In Marxian terms, capitalism is not simply the private control over the instruments of production. It is the effective ownership and control over the instruments of production by a few men with vast concentrated wealth at their disposal. In Marxian terms, again, this great wealth was obtained by the ruthless exploitation of workers. To argue the opposite position is to risk falling into a fairly well laid trap. At the most obvious level, it is to take on a variation of the old conundrum of whether or not you are *still* beating your wife.

Thus, the defender of "capitalism" begins by granting that, sure, 19th century capitalists were a hard lot. But that has all changed in the 20th century, he maintains; humane legislation and genteel businessmen have changed all that. To sustain this argument, he grants more and more of the Marxist, or at least the socialist, case, and justifies the increasing government control over private property. Those who argue in this wise have taken the socialist bait and rushed headlong into socialism with it.

But the heart of the difficulty is

that the word capitalism as it is employed is a semantic trap. On the one hand, it makes it difficult to keep the issues in focus, because it is used in a confusing and misleading way. On the other hand, it blocks from our view a mass of phenomena which we need to see clearly, and which capitalism used in its root sense would help to do. The issue is not between capitalism and socialism. There is an issue about private vs. public ownership of the means of production, but there is no logical connection between that and capital or capitalism.

Whatever Marx may have thought about capital, all too little apparently, there is no substantial difference among the leaders in the world today over the necessity for and desirability of capital to aid in both agricultural and industrial production. If anything, socialist countries are more determined to get their hands on accumulated capital and concentrate it than what remains of so-called capitalist countries.

Every device, ranging from the most sneaky to the most openly confiscatory, is employed in this quest. I nominate as the most sneaky the monetizing of debt, by which wealth in private hands is sopped up by a process of monetary debasement. There exists now a vast series of banking-like mechanisms by which this money is sopped up and transferred to countries around the world where governments more or less own and control the instruments of production. Capital is what much of this is about, and if we could call it by its proper name, it would be called capitalism. As matters stand, however, we are denied the use of the very word that could help to bring all this into focus.

Freedom vs. Tyranny

The issue, I repeat, is not between socialism and capitalism, in any meaningful sense of the words. In the broadest sense, it is between freedom and tyranny. As regards capital, it is between whether men shall be able to keep the fruits of their labor and dispose of accumulations of it as they think best, or have it confiscated and used for politically determined ends. It is between the free market and the hampered market. It is between free enterprise and state controlled activity under the direction of a vast bureaucracy. It is between dispersed wealth under individual control and concentrated wealth used to augment the power of the state. It is between the right to private property and the might of centralized government thrusting for total power. There are other dimensions, moral and social, to the contest, but the above are the major economic ones. Capitalism, as currently used, tends to act as a red herring to draw us off the scent and draw attention to largely extraneous issues.

So, I conclude, as regards the use of the word capitalism, *sic et non,* or, in English, yes and no. No, to take that part of the equation first, the word cannot be effectively used in discourse and debate in its Marxian or socialist sense. It cannot be used with precision because it is a loaded word, loaded with Marxian ideology. It has been severed from its root and made to connote what it does not clearly do. Nor does it have a commonly accepted meaning, or set of meanings, for Marxists and non-Marxists. Its use obfuscates the issues and conceals a major aspect of socialism (i. e., its capital hunger).

No, capitalism is not an apt word for the use of defenders of private ownership of the means of production. Linguistically, it does not mean private ownership, nor does the case for private property hinge upon its potential use as capital. The right to private property is grounded in the nature of life and labor on this earth, and it is, therefore, a gift of the Creator. Its use as capital is one of the possibilities of property. To defend private property from the perspective of the advantages of privately disposed capital is to approach the matter wrong end to. In any case, capitalism is still a misnomer for what the defenders are discussing; their flanks are exposed to the adversary because it is his chosen ground; and when the defenders have loaded the word with their own meanings it does not have a commonly accepted meaning for use in discourse.

Socialists Seize Capital to Achieve Industrialization

Yes, there is a place for the word capitalism in the language. There is an ideology and there are practices which cry out to have this word stand for and identify them. The ideology is the established preference for capital over the other elements of production. In practice, it thrusts to the use of government power to concentrate capital, to promote its accumulation, and to confiscate the wealth necessary to that end. Used in this way, the word capitalism helps to identify and bring into focus developments which are otherwise difficult to construe.

We can see clearly that capitalism is a disease of socialism, not the offspring of private property. It is not a system in which the instruments of production are privately owned, but one in which private property is taken to provide capital for publicly owned industries. Perhaps the most dramatic examples of it at the present time are the grants and loans to Third World and Communist nations by which wealth from the United States and European countries is being appropriated for their industrialization. That, by my understanding, is capitalism, and it should bear the name and onus.

Hans F. Sennholz

The Demand for Labor

TO SPEAK of a *supply* of labor may refer to the productive exertions by all those individuals, whether self-employed or wage-earning, who do, or would like to do, any work for wage or profit. The potential supply in a given market depends on the size of population, the amount of time each individual spends working, and the skill and application which the workers bring to their jobs. The effective supply depends on the preferences and choices by the workers themselves.

The *demand* for labor springs from its usefulness in the satisfaction of human wants. The potential demand is as infinite as man's wants and desires. Some are necessary to sustain his life, others to please his fancy. When his desires are boundless, his labors are endless. They set a task he can never accomplish, and create work he can never finish.

The specific demand for labor depends on the preferences and choices by entrepreneurs in the labor market. Their bidding for labor in turn is dependent on their anticipation of the productivity of labor, which is the value consumers ascribe to labor services. It provides an excellent guide and sets a definite limit to employer bidding for labor.

Interdependence of demand and productivity does not imply a constant relationship. It does not follow that a rise or fall in productivity must result in proportional changes in the demand for labor. Modern economics rejects "quantitative analysis" because there are no constant relations that would permit quantitative measurement. Even if a statistician were to demonstrate that, at a given time and place, a ten percent

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rise in labor productivity brought forth a twenty percent rise in the demand for labor, no such relationship may exist at other times and in other places. Human behavior toward labor and every economic good is variable. Different individuals ascribe different values to labor and the products of labor. In fact, the same individual may change his valuations under changing conditions.

Production for the future must be ever mindful of the future and must anticipate future changes. Prices may change and affect the economic outlook. When wage rates are rising, employers must reflect on the possibility that the rates may soon revert to the old rates, that they may remain where they are at the present, or that they will rise still further in the future. Employers must give thought to the future prices of the product, which may rise, fall, or remain the same. In short, employer bidding for labor always hinges on the anticipation of future labor productivity.

The Productivity of Labor

Consumers, who are the ultimate directors of the production process, attach value to labor services. They judge labor like any other factor of production, by the improvement it adds to their well-being. Economists put it succinctly, labor is valued according to the anticipated improvement expected from the employment of an additional laborer. They call it "marginal productivity." In simple words, a worker's productivity is determined by the value consumers attach to his services and achievements. Employees, employers and capitalists, all are subject to the whims and wishes of consumers who want to be served at the lowest possible price. Employers, therefore, are eager to buy all the specific labor they need for production at the lowest price. But they must compete with other employers who are guided by similar considerations, offering wages high enough to attract the needed labor from their competitors. To remain in business they must outbid competing employers and pay the market rate, which is forever adjusting to the "marginal productivity" for each kind of labor.

If, for any reason, employers should offer wage rates that are lower than the productivity rates, a profit margin would appear. People eager to take advantage of the margin would bid for more labor and thereby push wage rates back to the height set by productivity. Surely, employers are interested in buying labor at the lowest possible price. But no one alone, or together with others, can actually lower his rate without creating a profit opportunity for competitors. Other employers and would-be employers seeing bargain labor would want to seize the opportunity and buy additional labor, which would lift wage rates back to the rates set by productivity.

Many economists have gone astray at this very point of labor market competition. From Adam Smith to Jean-Baptiste Say, John Stuart Mill, Alfred Marshall, and a host of disciples, they all lamented a conjectured failure of the competitive order; they all devised their specious doctrines of labor's disadvantage and exploitation. Their doctrines and theories in turn gave birth to the labor movement that commonly aims at replacing the competitive private-property order with a political command system. They induced governments the world over to embark upon radical government intervention in order to favor laborers at the expense of the owners of capital. In time they caused governments to restrict labor market competition and bestow legal privileges on workers' combinations and unions. Contemporary policies continue to reflect their notions and prejudices.

Guided by such spurious doctrines modern man is eager to use the force of law to raise his wage rates and improve his condition. Ever angry at his "disadvantages," he does not hesitate to use his political apparatus of coercion. His government may set minimum wage rates and mandate expensive benefits; disobedience is visited with fines and prison sentences. His labor association may engage in violent strikes in order to raise wage rates and reduce labor output. In every case he brings forth the specter of falling demand and rising unemployment, that is, people willing and able to work but unable to find employment at the coercive rate. Economists call it "institutional" unemployment. It must not be confused with "temporary" market-generated unemployment.

Directed by Consumers

Directed by consumer choices and preferences, employers buy definite performances at market rates. They do not knowingly buy labor at rates that can be expected to result in financial losses, nor do they for long retain labor that usurps income from investors and entrepreneurs. In fact, they discharge submarginal workers whenever they can, in order to preserve the production process and safeguard their own jobs as well as those of other workers.

Consumers acting on free markets may be responsible for fluctuations in wage rates. They may cause some to rise and others to fall and thereby reassign labor to various fields of production. Some rates may rise in reaction to rising consumer valuation and appreciation. Others may fall in response to declining consumer demand. But all such declines do not create mass unemployment unless wage rates are forcibly prevented from readjusting. Industries may shrink and vanish because of changing consumer aspirations and changing production technology. They may cut wage rates and reduce fringe benefits until laborers prefer to seek other employment. But such changes do not cause institutional unemployment. At the market rate of wages anyone willing to work can find employment and anyone looking for labor can find it.

A worker may be discharged because his employer is readjusting the production process in response to changing consumer demand. Or, having failed to adjust in time, the latter may face liquidation in bankruptcy, which releases all labor. Workers discharged may not immediately take another job; they may search for a better opportunity in other markets. They may want to relocate in another community or move to another climate. For any one of a thousand reasons they may choose to wait for a more propitious opportunity. Their unemployment, being the outcome of both market change and individual choice, is "temporary" and must not be confused with "institutional" unemployment, which is as persistent as the institutional force that is creating it.

Temporary Unemployment

Man is not free to choose permanent unemployment. He must labor in order to sustain his life and provide some comforts of living. In an exchange system he must adjust his labors to the demands of the market where his fellowmen manifest their wants and desires. Failure to adjust promptly to changing conditions may lead to unemployment.

There may be *technological unemployment,* which always attracts a great deal of popular interest. Technological progress may reduce the number of workers needed to perform certain operations. Computer production and management may result in simplifying and shortening the production processes, thereby reducing the number of workers required to perform them. Labor-replacing machinery and mechanical handling may result in a reduction of the number of workers needed to man a workshop.

The worker displaced by technological changes faces the risk of an extended period of unemployment unless he chooses to adjust quickly to the new situation. He may move to another industry that is expanding and bidding for more labor. Or he may choose to wait until his former employer recalls him. After all, the new process of production that displaced him usually results in lower goods prices and an increased demand for the goods. It may lead to an expansion of business and may necessitate the rehiring of dismissed workers and the addition of new workers.

New tools of production need to be

manufactured, installed, serviced, and operated, all of which require human labor. The new machines need designers, draftsmen, manufacturers, truck drivers, programmers, installers, operators, and repairmen. In most cases the laborer who is displaced by a machine may be qualified to work with it in some capacity. If, however, he makes no effort to learn and adjust, preferring to wait and see, the displaced worker may not get the job. Instead, it may go to a white-collar worker or a young school graduate who is eager to learn.

In recent decades manufacturing employment has been declining while certain service industries have expanded rapidly and required additional labor. Supported by massive government spending, the health-care industry, especially for the elderly, has grown significantly. It has absorbed some labor set free by manufacturing industries. In many instances, however, displaced factory workers refuse to make the move to another industry in another location; they had rather wait until they are called back or their unemployment benefits run out.

There may be *seasonal unemployment.* It is the composite effect of climatic and institutional forces that are felt regularly each year. Farm employment in the United States, for instance, rises from early spring until fall, then declines sharply as winter approaches. Many other activities are subject to similar fluctuations. Construction is affected directly by changing weather conditions. In the snow belt a cold winter may bring most outdoor construction to a halt. Intermingled with the climatic variations are the effects of institutional factors. Industries associated with education, for instance, are affected by the scheduling of the school year from September to June. Retailers are affected by the designation of tax dates by federal and state governments. Holidays have a wide range of economic effects. Christmas and Easter have major impacts on the volume of business; other holidays, such as July 4, Memorial Day, and Labor Day usually are of less effect. They all create an annual cycle that is recurrent and periodic.

Seasonal Fluctuations

The list of industries directly affected by seasonal factors is surprisingly large. Seasonal influence is clearly discernible not only in agriculture and construction, but also in iron and steel, automobiles, tires, cement, glass, shoes, appliances, confections, men's and women's clothing, and many others. Many businesses shut down or curtail operations during seasonal slumps.

Industries subject to seasonal fluctuations obviously need to compete for available labor with other industries that offer more regular employment. They can compete effectively only if their wage rates are high enough to induce a sufficient number of workers to prefer seasonal over regular employment. The structure of wage rates reflects the seasonal irregularity in demand.

Some workers prefer seasonal employment over year-round work; they may enjoy seasonal unemployment, which to them may be self-employment during the off-season. Most teachers love their seasonal unemployment; they call it vacation. Some may prefer to be fully employed throughout the year; they may teach during the school year and labor in commerce and industry, or seek self-employment during their vacations. Migrant farm hands may bend their effort in custom grain harvesting, starting in Oklahoma and following the season north until it ends in northern Saskatchewan. Fruit pickers may start in southern California and end up in British Columbia. During the winter they may retreat to their homesteads in Mississippi and Florida. In every case the wage and fringe benefit structure of the seasonal industry adjusts to the irregularity and thereby secures the needed number of workers.

There may be a great deal of *unemployment of older workers.* Many make little effort to adjust to a new situation, which makes employers reluctant to hire them. This well-known tendency is deeply rooted not only in custom and convention, but also in human nature itself. As he grows older, man may resist changes. When strength and energy wear away, his economic productivity tends to decline. But he may expect to be paid according to seniority, rather than productivity, which may make him more expensive than younger competitors. And even if he were to earn identical wage rates, his unit costs of production may rise as his productive efficiency declines.

Productivity and Income

Self-employed people are much more aware of the direct relationship between productivity and income than employees. They are prepared to face declining incomes when personal productivity declines in advancing age. The physician or dentist who attends to fewer patients readily accepts the fact that his income may decline. The businessman knows that his profit will shrink when his output decreases. But his aging employees tend to forget it; they may expect a stream of raises and improvements until they choose to retire. Their costs continue to rise while their productivity declines, which makes them primary targets for disemployment. In other words, there are no employment contracts calling for wage cuts after age 40, 50, or 60, but there is a great deal of unemployment. It also explains why self-employed people generally continue to labor in their professions long after employees have retired. Government usually compounds the trend by imposing laws and regulations that aim at benefiting elderly employees. But benefits exacted by force merely raise employment costs and thereby disadvantage the intended beneficiaries even more.

Physical strength and prowess may diminish early in life, but man may continue to grow in experience, knowledge and wisdom throughout his life. As long as he is growing, his economic productivity may be rising. There is no specter of unemployment, which appears only to submarginal workers. Unskilled laborers who have nothing to sell but their physical strength may become submarginal at an early age; they may become "old" in their thirties when youthful vigor is fading away. Factory hands who acquire their skills in a day or two become "old" early in life. Skilled workers who are masters of a difficult trade need not fear the competition of younger people; they may enjoy highest personal productivity in their middle years. Professional people who may be studying and learning all their lives may achieve their highest productivity in their fifties and sixties. The philosopher who inquires into the nature of things and synthesizes all learning may be at his best in his seventies and eighties. He has nothing to fear of the competition by his younger colleagues.

And yet, they all may fall prey to *cyclical unemployment,* which throughout recent history has been one of the great economic and social evils. Workers are laid off en masse when business is caught in the throes of depression. Millions are idled, and in time are impoverished, as economic wheels grind to a halt. Depression time is readjustment time. Economic production is readjusting to consumer demand, capital markets are correcting the mistakes made in the past, and labor markets are reassigning labor in response to changing demand.

Cyclical Unemployment

The public is poorly informed about cyclical unemployment. Under the influence of Mainstream Economics, most people are led to believe that depressions are the evil fruit of the competitive order. In reality, depression and unemployment are the inevitable outcome of government interference with money and credit. They are the consequences of boom-and-bust policies that lead to credit expansion, followed by credit contraction. The harm is wrought during the economic boom; it is corrected with much pain during the depression that follows.

Before the 1930s, when there was little government intervention, the depressions were relatively short and mild. There was little unemployment. After all, there was no institutional restraint on the labor market, no minimum wage legislation, no unemployment compensation. When economic production was forced to readjust, labor would readjust with equal speed and efficiency. It would freely move about the labor market and shop around for the best available position. Workers labored from dawn to dusk, especially during depressions. Chronic unemployment was utterly alien to them.

Institutional Unemployment

The specter of mass unemployment first made its appearance when government became a back-seat driver. In 1930, when there was some cyclical unemployment, the government urged business not to adjust, but to increase business spending. Municipalities and states were called upon to boost their spending for public works. The back-seat driver erected trade barriers, ran huge budgetary deficits, doubled income taxes and raised business taxes, and in many instances, seized control over the car while denouncing the driver. He set minimum wages, ordered fringe benefits, exacted and paid unemployment compensation, and introduced collective bargaining, all of which served to hamper the labor market. They gave rise to institutional unemployment.

Government is a necessary evil, like wheel-chairs and crutches. It protects the lives and property of its citizens from aggressors and wrongdoers. Our need of it reveals that there is evil in the world. The evil is multiplied if government itself becomes the instrument of evil. It may govern too much and thereby kill the self-help and energy of the governed. It may neglect to protect the property of the citizenry, or even prey on it for its own benefit or that of others. It may engage in massive transfer that seizes income and wealth from productive citizens and doles them out to its constituents. And in a moment of omnipotence it may interfere with economic production and enforce wage rates that cause mass unemployment.

Government may set *minimum wages.* For any number of political reasons, it may issue minimum-rate mandates and call on courts and police to enforce them. To judge the economic effects of this intervention it is important to determine the relationship of the mandated rate to the market rate, that is, the minimum rate imposed by courts and police versus the going rate paid in the labor market. There are three conceivable possibilities with varying effects:

1. The police rate may be *lower* than the market rate; it may be $1 per hour, for instance, but everyone is earning more than the minimum.

No apparent ill effects may come from such intervention that actually does not intervene. It is potentially harmful, however, as the markets may change and cause some wage rates to fall below the minimum, in which case the minimum would now be higher than the market rate and give rise to unemployment. Moreover, it is conceivable that some youngster may not yet produce the minimum, which would cause him to fall into unemployment or, if he chooses to ignore the mandate, become a criminal in the eyes of the law.

2. The police rate may *coincide* with the market rate. Again, no apparent ill effect may come of the mandate. However, market changes may cause the police rate to be higher than the rate the market would set. In this case the minimum costs of some workers would exceed their productivity; they would become "submarginal" and face unemployment.

3. The police rate may be *higher* than the rate the unhampered market would set. This is the normal case of minimum wage legislation. After all, government means to lift the wage rates of poor people above the given rates in order to benefit them and earn their political support. It is unfortunate, however, that workers who produce less than the legal minimum tend to be unemployed. Every time government raises the minimum it boosts the unemployment rolls. It may want to raise the minimum from $5 an hour to $6 by mandating a higher hourly rate or adding fringe benefits. It may want to benefit millions of Americans who are earning less than $6 an hour, by lifting their incomes by order of court and police. The order is issued to all employers alike—*profitable* employers, *marginal* employers who manage to cover their costs and earn a going rate of return, and *submarginal* employers who are earning less.

Profitable employers earning returns higher than the going rates, may be able to cover the higher labor costs. The minimum mandate merely prevents them from forming more capital and expanding their businesses, and may discourage them from hiring new labor. The *marginal* enterprises will become submarginal as a result of the minimum wage boost. They will be earning less than they could earn in fields that require no minimum wage labor. In reaction, employer-entrepreneurs may choose to curtail their most expensive production. They may dismiss some labor, including minimum wage labor. *Submarginal* enterprises may do the same. The pressure of competition may force them even more than the others to curtail loss-inflicting output and discharge unneeded labor. The curtailment by both, the marginal and submarginal enterprises, reduces the supply of economic goods on the market, which in time may raise their prices.

Consumers are the ultimate bosses of the production process. They set prices and determine the payroll. It is a well-known fact that consumers usually buy fewer goods at higher prices, and therefore require less labor. How much less? No one can foresee the consumers' reaction, which may vary from product to product and may change over time. It is likely, however, that some are prepared to pay higher prices, which will permit employers to pay higher wages. As no one can know in advance how high prices will rise in reaction to the reduction in output and how many will pay the higher prices, no one can know in advance how many workers will find employment at $6 an hour. If 10 million people were to benefit from the wage mandate, 8 million, perhaps, may enjoy the boost and 2 million may be cast from the employment rolls. At other times and in other places 5 million workers may partake of the boost while 5 million may be condemned to long years of unemployment.

Benefit Mandates

Government intervention may take the form of *benefit mandates* for some or all workers. To be popular and "progressive" government may mandate new labor benefits. If wage rates are not reduced promptly to compensate for the boost in benefits, total labor cost may exceed the marginal productivity of some workers and, therefore, create unemployment. To reflect on employment and unemployment is to consider *total* cost, which usually comprises not only the workers' take-home pay and tax exaction, but also numerous employee benefits. Employers may be ordered to provide certain benefits or contribute to them. They may be directed to pay unemployment compensation, workman's compensation, paid vacations, healthcare benefits, and contribute to old-age and disability benefits and other labor causes.

To ponder over the demand for labor is to compare the productivity of labor with the cost of labor, that is, total cost. It is irrelevant to employers how the various shares of labor cost are to be distributed, as take-home pay or fringe benefit, as payroll tax or contractual contribution to Red Cross or the Little League. What matters is a comparison of total cost of labor with its productivity. If the former is made to exceed the latter, unemployment sets in.

Unemployment caused by benefit mandates may be temporary if other compensation is permitted to adjust. If a mandate raises labor cost by 10 percent and the unemployment in time depresses wage rates by 10 percent, they cancel each other. In the end, the mandate merely ordered benefits for workers and, by way of unemployment and wage rate adjustment, made them pay for the benefits. It is illusory to believe that government can for long force investors and entrepreneurs to grant benefits without receiving labor in return.

Some of the benefits accomplish the very opposite of what their political sponsors mean to accomplish. Unemployment compensation is designed to alleviate the pains of unemployment and facilitate the search for a job. But it is an unfortunate fact that every boost in unemployment taxation levied on employers raises the cost of labor and thus reduces the demand for labor. In deep recessions with heavy unemployment, state governments are quick to raise tax rates and bases, which invariably raises the unemployment. States with high rates of unemployment taxation suffer from high rates of unemployment.

Production Barriers Reduce Labor Efficiency

Government may erect production barriers that reduce the productivity of labor. It may raise business taxes, boost environmental costs, erect trade barriers, impose regulations and controls. It may engage in deficit spending and consume business capital, reducing labor productivity. If labor costs are not reduced simultaneously they may exceed the marginal productivity of some workers and thereby create unemployment.

To judge the import of production barriers it is important to distinguish between new and old barriers, between new and old government intervention. New barriers are those to which the price and production structures have not yet fully adjusted. The new business tax has not yet raised goods prices, business may still be in the throes of adjustment through reduction in output and disemployment of labor. The new trade barrier may not yet have had its full effect on output, prices and wages. The new budget deficit that is consuming business capital and reducing labor productivity, may not yet have run its course. Readjustment to new barriers takes time; it may take several years of painful readjustment until the apparatus of production has adjusted anew to consumer demand.

Old barriers are those to which the price and production structures have fully adjusted. The painful readjustment is over, wage rates are lower, goods prices are higher, and the unemployment that forced the labor adjustment lies in the past. Present unemployment cannot be placed on the doorsteps of old barriers erected during the 1960s and 70s. The apparatus of production has adjusted to them. Today's unemployment must be explained in terms of new barriers to which the labor market has not yet fully adjusted, and in terms of insurmountable barriers to which no legal adjustment is feasible. Price and cost adjustment cannot easily overcome the minimum wage barrier that prevents the employment of much unskilled labor, nor can it readily compensate for the generous subsidies granted to the unemployed. For many workers their choice of job or joblessness may depend on the difference between labor income and unemployment compensation. For them, the utility of labor tends to shrink and that of leisure may rise whenever leisure is subsidized.

Unemployment compensation constitutes a production barrier in the sense that it may induce some workers temporarily to withdraw from production. It reduces the supply of labor, which in turn raises the marginal productivity and wage rates of the remaining labor. The boost tends to be temporary unless the compensation succeeds in creating a standing army of unemployed. In that case, it must not be overlooked that the increase is accomplished at the price of mass unemployment and grievous suffering of the unemployed. It is financed by unemployment taxes exacted from the income of the employed, and is borne by all members of society who are made poorer by the idleness of some of its members. Unemployment compensation is a rather ineffective method of raising wage rates and improving the economic lot of working people.

Interference with Prices

Government may interfere with the pricing process and thereby lower the productivity of labor. If labor costs are not adjusted simultaneously some labor may become submarginal. As government is most keenly interested in "essential" products and services, e.g., fuel, utilities, steel, and the like, it may forcibly hold their prices below market rates, thereby depressing labor productivity.

Throughout the 1970s the Federal Government kept oil and gas prices far below world market prices. The price controls, together with a fuel allocation program, struck hard at economic production and employment. It brought Sunday closings of filling stations, created long lines on other days, lowered home and office thermostats, and reduced commercial air service. It brought energy brown-outs, and energy-related industrial layoffs. Once self-sufficient in energy, the U.S. was forced by price controls to supplement gas and oil supplies with overseas purchases. By 1980 no fewer than 69 government agencies and a dozen Congressional Committees were exercising authority on energy questions. Unemployment rose from some 4.1 million Americans at the beginning of the decade to nearly 6 million at the end.

This is not to imply that the energy chaos was solely responsible for soaring unemployment. There were many other policies that contributed to the evil. There cannot be any doubt that the comprehensive price and wage controls imposed in 1971 were largely responsible for the severe recession that was to descend on all markets in 1974 and 1975. Average unemployment in 1975 was estimated at 7.8 million Americans. If it had not been for the rampant inflation that was to follow, the unemployment undoubtedly would have grown worse.

Inflation and Unemployment

Under the sway of Keynesian doctrines and recipes, governments the world over are practicing deficit spending and credit expansion in order to alleviate unemployment. They are convinced that such policies constitute an efficient method for gradually lowering labor costs. Lower real wages raise the demand for labor and actually reduce unemployment. But the success of Keynesian policies depends entirely on the ability to deceive the workers and their unions or, if this should fail, to persuade them to suffer losses in real income.

Inflation and credit expansion as an employment policy cease to be effective when the workers resist the obvious reduction in real income. They are foiling the Keynesian plan when they demand wage boosts that compensate for the rise in goods prices. In fact, they may create new unemployment pressures when their contract demands anticipate future purchasing power losses. This is why moderate dosages of inflation no longer cause real wages to decline and the demand for labor to rise.

Application of ever larger doses of inflation must, in the end, lead to a complete breakdown of the monetary system and to mass unemployment. Double-digit inflation causes businessmen to hedge for survival. They invest their working capital in inventory and capital equipment, or other durable goods that are likely to escape the monetary depreciation. Investors buy real estate, precious metals, and collectors' items. Economic output, especially for consumers, tends to decline, which causes goods prices to rise and unemployment to soar.

The ultimate folly of the Keynesian recipe is a combination of inflation and price control. Both together instantly paralyze all markets, hamper economic production, encourage consumption, and create goods shortages. They cause the exchange system with its magnificent division of labor to disintegrate and give way to a primitive command system. Disintegration causes mass unemployment.

Labor Unions

Long before there was a Keynesian recipe governments began to rely on labor combinations for improving labor conditions. Guided by popular notions of labor's disadvantage they bestowed legal immunities and privileges on labor unions so that they would raise wage rates above those the unhampered market would set. Unfortunately, simple economics reveals that disemployment sets in wherever labor costs are forcibly lifted above market rates.

It does not matter whether government or union is imposing the coercive rates. The effects are the same: institutional unemployment. The rates may differ according to the measure of coercion. Government edicts usually are more comprehensive and, therefore, more restrictive than union rules. Minimum wage legislation may affect millions of workers. Union coercion may be limited to a few companies in a few industries, which obviously limits their restrictive powers. As long as unionism is a limited phenomenon, the disemployment it imposes may bring forth an adjustment in non-unionized employment. The labor market may absorb the labor set free by unions and thus prevent mass unemployment.

Disemployed union labor reduces the marginal productivity of unorganized labor and depresses its wage rates. It creates a visible difference between union rates and market rates, which is both boon and bane to unionism. The difference obviously helps to promote the union ideology according to which unions do raise wage rates and improve the economic conditions of all working people. It is a bane because it gives rise to much suffering. It creates unemployment among union members and depresses the wage rates of all others. When union rates amount to double or triple the market rates, the industry usually falls on hard times. With the demand for its products and services declining, it tends to contract, releasing labor, until it ceases to function as a viable industry. Foreign producers may ultimately fill the gap torn by union restriction and industry contraction.

The decline of a unionized industry is bound to accelerate when the quantity and quality of labor may decline as a result of diminishing effort and application by the workers themselves. They may choose to loaf and goof off, dally and tarry, or do shoddy and shabby work. They may steal from their employer, damage their tools and equipment, and otherwise sabotage the production process. Union labor usually is angry labor pressing its grievances. When labor productivity declines for any reason, wage rates must be reduced simultaneously. Failure to adjust labor cost to declining labor productivity leads to unemployment.

An Invitation to Labor

Human life is a constant want and a standing invitation to labor. In dictatorships, the invitation becomes a command that is enforced by court and police. In free societies, it takes the form of business demand for workers. Employers are bidding for labor in order to serve consumers who are the directors of the production process.

Consumers judge the efforts of every worker and determine his income. They decide upon employment and unemployment. Being weighed on their sensitive scales of productivity and cost, some labor is found wanting. In free labor markets it is free to readjust. In markets constrained by onerous rules and regulations it is condemned to chronic unemployment.

IDEAS ON LIBERTY

Unemployment

REAL wage rates can rise only to the extent that, other things being equal, capital becomes more plentiful. If the government or the unions succeed in enforcing wage rates which are higher than those the unhampered market would have determined, the supply of labor exceeds the demand for labor. Institutional unemployment emerges.

Firmly committed to the principles of interventionism, governments try to check this undesired result of their interference by resorting to those measures which are nowadays called full-employment policy: unemployment doles, arbitration of labor disputes, public works by means of lavish public spending, inflation and credit expansion. All these remedies are worse than the evil they are designed to remove.

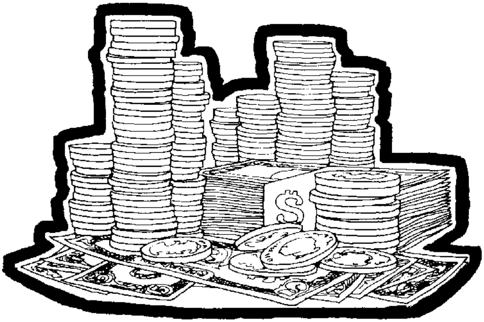
Assistance granted to the unemployed does not dispose of unemployment. It makes it easier for the unemployed to remain idle. The nearer the allowance comes to the height at which the unhampered market would have fixed the wage rate, the less incentive it offers to the beneficiary to look for a new job. It is a means of making unemployment last rather than of making it disappear. The disastrous financial implications of unemployment benefits are manifest.

On the unhampered market there is always for each type of labor a rate at which all those eager to work can get a job. The final wage rate is that rate at which all job-seekers get jobs and all employers [get] as many workers as they want to hire. Its height is determined by the marginal productivity of each type of work.

LUDWIG VON MISES

Donald R. Wells
L. S. Scruggs

The Free Banking Alternative



ON MARCH 31, 1980, a major piece of legislation was passed by Congress to deregulate commercial banks and other deposit-type financial institutions. This deregulation took the form of phasing out interest rate ceilings on various types of time deposits and of extending the type of assets thrift institutions were authorized to hold. However, this act took three steps in the opposite direction: it required all banks, member and non-member, and all thrift institutions offering checkable deposits to hold the same percentage of these checkable deposits as non-interest reserves, either in vault cash or on deposit with the Federal Reserve; it increased federal deposit insurance to $100,000 per account; and it allowed all these institutions to borrow from the Federal Reserve.

It is apparent that Congress did not intend to unleash the forces of competition on the financial system. If this had been Congress' intention, it would have phased out, rather than increased, deposit insurance and would have left the amount and location of reserve holding to the individual institutions.

The purpose of this paper is to explain how a completely free banking system would operate. Under free banking, all financial institutions are subject only to the general laws of incorporation and against fraud. They would not be restrained by the rules of a central bank and not be audited by any government agency, nor be protected by any government deposit guarantee. The first part of this paper hypothesizes how individ-

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ual banks would thrive in this competitive environment, while the second part shows how the most serious problem this economy faces—inflation—can be controlled without any government agency doing the controlling.

The Individual Financial Institution in a Free Banking Environment

In a free banking system, any firm can enter the banking business by acquiring funds in any non-fraudulent manner and can put those funds to any legal use it wants. A bank may attract funds by offering banknotes (currency) or deposits convertible on demand to specie (gold or silver coin). The bank's success would depend upon its gaining public confidence for holding its banknotes and other bank liabilities, and on the probability that it can use its funds profitably. No bank would have any special privileges, like those currently enjoyed by central banks, such as a monopoly of the note issue or the protection of a legal tender law, giving its notes forced currency. There would be no government agency or central bank on which the bank could rely as a lender of last resort; it would have to borrow in the private market at a rate consistent with the risk involved.

Under free banking, both notes and deposits would be promises to pay on demand some generally accepted medium, such as gold or silver.[1] The particular combination of notes and deposits issued in lending by each bank would be determined solely by public preference. The bank would be indifferent between the two, but the total amount of sight liabilities would by limited by its reserves of specie. No government regulation would specify that a bank had to hold certain assets, such as low-yielding government bonds, as backing for its banknotes, as was the case under the National Bank Act.

Not only free entry, but freedom of exit is a necessary condition of free banking. Banks unable to redeem their demand obligations, and unable to obtain private credit, would be forced to liquidate. This market pressure, along with the knowledge that there is no central bank acting as a lender of last resort, would force banks to act prudently.

Without a central bank, the check clearing process would be privately operated at its true cost, to the mutual benefit of banks and the public. Any cost reductions resulting from innovations would, by force of competition, be passed along to the public. Banks would have total freedom to branch anywhere. They would extend their operations nationwide, as have banks in Canada, England and other countries.

The unit bank system was not a natural development but a result of restrictive legislation. The unit bank system led to correspondent banking, not only for holding reserves, but also for performance of services which small unit banks found too expensive to undertake individually. In the United States, these reserves tended to accumulate in financial centers, where they were subject to the fluctuations of speculative markets. But with a branch banking system, even if a remote bank's reserves did find their way to financial centers, they would be held at a branch of the remote bank, which would retain total control over the funds. Each bank's own liability structure would determine how these funds were invested and in what maturities, in order to maintain adequate liquidity. With no need for a correspondent relationship, non-bank corporations could have a single banking connection nationwide as in Canada.

Branch Banking

Evidence from the depression clearly shows that branch banking was safer than unit banking, but that safety increased with the widening of the geographical area over which a bank could branch. Without branching, few banks could grow to a size large enough to handle the more desirable accounts. One study showed that 80 percent of the bank closings were in unit bank states,[2] and furthermore, that two-thirds of the branch banks that did fail were those that were restricted to a city.[3] Canadian branch banks gained millions of dollars of American deposits, especially in border cities like Windsor, Ontario.

Another study on California banking in the depression demonstrated that the diversity of California's economy, accompanied by statewide branching, enabled that state to achieve one of the lowest bank failure rates in the country. Again, the two small branch bank systems that failed in that state were those that restricted branches to one city.[4] This study also pointed out that the strong branch banking system in California also strengthened that state's unit banks by competitive example.[5]

Under a free banking system, it might be possible for a well-run unit bank to prosper, but it would have to do so without the currently available privilege of issuing government-guaranteed liabilities. The FDIC coverage is probably responsible for making the deposits of many small banks acceptable at par whereas they might not be so acceptable in a free market.

The specialized financial institution would be unlikely to exist for very long under free banking. Investment banking was part of commercial banking until forcibly separated by the Banking Act of 1933. Many activities of one-bank holding companies are merely tactics for circumventing laws which restrict banks to a narrow line of business. Thrifts, such as savings and loans, mutual savings banks, and credit unions, may have developed because banks were not interested in some particular lines of lending at first, but whenever those activities became profitable, it would have been the natural course of events for thrifts and banks to have merged.

The public would be much better served by a more diversified financial institution than by a single-purpose lender. A legally imposed distinction between deposit-type institutions does not serve the public well, because it leads to further government assistance to these single-purpose lenders, such as Regulation Q, the Federal Home Loan Banks, the FSLIC and the NCUA. None of this intervention is costless: funds are channeled into areas that otherwise would not receive them except at higher interest rates, while other erstwhile borrowers are crowded out of the capital market.

Under free banking, some of the strongest competition for existing banks may be provided by large retailers, brokerage firms and credit-card companies. Sears and Roebuck, Merrill-Lynch, and American Express already have in place nationwide offices from which to conduct a banking business. Automatic teller machines could give a depositor instant cash anywhere in the country. The one-bank holding company has already been responsible for combining banking with other financial services, so free banking would only remove the artificial restraints.

The Market Decides

The market would eventually decide which of the many new services offered by banks would be profitable, but the chief beneficiary would be the consumer. Not only actual competition but potential competition from new entrants would work more to the consumer's advantage than most of the "performance" laws that were specifically designed for consumer protection. Under free banking, there would be no legal requirements for "truth in lending," "equal credit opportunity," or "community reinvestment," and no restrictions on debt collection practices. These performance standards add substantial reporting and regulatory costs, which are at least partially passed on to the consumer.[6]

Compared to a single governmentally issued currency, private banknotes might present a greater temptation to counterfeit. Counterfeiting was prevalent before the Civil War when there were so many different banknotes being used. However, a single government currency does not guarantee a counterfeit-free economy either: today's overdrafts and forged checks are analogous to the antebellum counterfeiting of state banknotes. Furthermore, modern communication technology would strongly discourage counterfeiting. At any rate, insurance companies can underwrite any losses the public may suffer, as they do now for stolen or forged credit cards.

With different banknotes being used, some company or group of retailers might sell fractional coins to be used for small purchases and plastic tokens with electronic markings to be used in vending machines.[7]

How Free Banking Would Prevent Inflation

Deregulation of bank money alone will not give us an environment free of inflation unless there is some way to stop the unlimited creation of the money base by the central bank. When gold or silver is the base into which all banknotes and deposits are convertible, there is a limit on the money supply, because this base cannot be created at will as fiat money can be issued by a central bank.[8] Central banks, being politically sensitive, use their monopoly of the money base to help organized sectors at the expense of the general public, often under the guise of lowering interest rates. It was recognized long ago that free banking restricted credit expansion, whereas central banks were tools for creating an easy-money environment.[9]

The imposition of a money-growth rule on a central bank is not the cure for inflation. Congress has never shown any inclination to impose a fiat-money growth rule as monetarists have advocated, and the Fed could not be trusted to follow it, judging from experience with gold reserve requirements. In 1913, the Fed was ordered to hold gold equal to 40 percent of its note liabilities and to 35 percent of member bank reserve deposits. Every time the limit was reached, these requirements were either suspended (1933), reduced (1945), or abolished (1965 & 1968). Emergency currencies without gold backing were issued in the depression and in World War II.

Prudent Practices Encouraged

By contrast, commercial banks in a free banking system could never go off gold as could a privileged central bank with legal-tender banknotes. A private bank would be forced into liquidation if it could not convert its sight liabilities into specie. However, there is another limit to overexpansion in a free banking system besides exhaustion of gold reserves, and that is the reflux of banknotes. Each bank would only pay out its own notes over the counter, because unlike the notes in the National Banking System, these notes would be distinctive. Therefore, a bank that expanded its lending beyond prudent limits would have its notes and deposits presented for payment faster than those of its rivals. If a bank wanted to protect its "brand-name capital," it would have to curtail its lending or face the possibility of its notes circulating at a discount. The marginal cost of *printing* banknotes may be zero, but the marginal cost of *keeping them in circulation* clearly is not zero.

Central banks could try and compete with private banknotes, but the public would only hold the central bank's notes if they retained their value relative to the private notes. However, the central bank could not monetize government deficits at will, nor bail out any bank or industry in trouble, because an oversupply of notes would result in depreciation. One might envision the Fed and private banks competing through advertising the way the U.S. Postal Service and private package carriers do now.

—FOOTNOTES—

[1]Vera C. Smith, *The Rationale of Central Banking* (London: P. S. King & Son, 1936), p. 149.

[2]Gaines T. Cartinhour, "Branch Banks versus Unit Banks," *Annals of the American Academy of Political and Social Science* 171 (January 1934): 36.

[3]*Ibid.*, p. 37.

[4]John P. Wernette, "Branch Banking in California and Bank Failures," *Quarterly Journal of Economics* 46 (February 1932): 371.

[5]*Ibid.*

[6]Catherine England, *The Case for Bank Deregulation*, (Washington: The Heritage Foundation, 1982), p. 24.

[7]F. A. Hayek, *Denationalization of Money—The Argument Refined*, 2nd ed. (London: The Institute of Economic Affairs, 1978), p. 48n.

[8]Lawrence H. White, "Competitive Money, Inside and Out," *Cato Journal* 3 (Spring 1983): 296.

[9]Ludwig von Mises, *Human Action: A Treatise on Economics* (New Haven: Yale University Press, 1949), pp. 443–44.

The Source of Money

IDEAS ON LIBERTY

UNLESS the creation and issue of money is withdrawn from the State and restored to the private banking system, I believe that parliamentary government and democracy will become impossible to maintain.

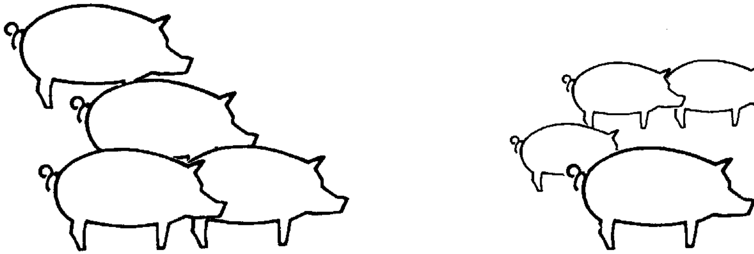
John Maynard Keynes, in *Essays in Persuasion,* referring to the famous statement of Lenin as to the best way to destroy the capitalist system, wrote: "Lenin was certainly right. There is no subtler, no surer means of overturning the existing basis of society than to debauch its currency. This process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one in a million is able to diagnose."

The strange thing is that it appears never to have occurred to Lord Keynes that, under a free economy, it is impossible to debauch the currency.

GEORGE WINDER, 1958

Ernest G. Ross

The Deficit Connection



FROM the man-in-the-street, to economists, to politicians, to academics, nearly everyone seems worried about federal deficits.

During Presidential campaigning, Walter Mondale called deficits "a travesty"; in more reserved tones, Ronald Reagan called deficits "a problem."

Distinguished professors write grave tracts warning of deficit repercussions "in the out years" (i.e., in the longer run). In an informal television tabulation of my own, in a single week over 100 interviewees and speakers from different walks of life were quoted making disparaging comments about deficits.

That deficits seem destined to be with this nation for awhile is hardly disputed. Even the more optimistic forecasts project several hundred billion dollars in deficits added to the national debt before the end of the decade. Some estimates push a trillion dollars.

While most people regard deficits as bad, there is considerable controversy over whether deficits are connected—that is, whether they must lead—to higher prices, to what current political jargon terms "an inflationary environment."

Many analysts, such as economist Fred D. Kalkstein, warn or imply that deficits *are* ultimately connected to higher prices via interest rates. Accelerated borrowing to pay for the deficits pushes up interest rates, and the borrowing tends to temporarily dampen or "hide" the

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effects of extraordinary levels of monetary growth.

(M1 money supply—primarily currency in circulation and checking-type accounts—averaged over 10 percent annual growth from mid-1982 to mid-1984, the highest sustained two-year rate since World War II; M2 and M3, much broader money measures, also showed abnormally rapid growth.)

"The longer the combination of disinflation [meaning less rapidly rising prices] and high interest rates persists . . . [a]t some juncture," wrote Kalkstein, "the money will begin to flow from our shores . . . the dollar will fall . . . and the inflation inherent in the Fed's monetary stimulation will come home to roost." (*The Wall Street Journal*, 31 July, 1984.)

Other economists remain sanguine about deficits.

For instance, in an August 31st *Wall Street Journal* letter Hoover Institution Senior Research Fellow, Milton Friedman, said, "I do not regard the deficit as a major issue or cause for concern." Coming from the man who has been one of the nation's more popular and vociferous—although less than consistent—modern opponents of inflation, this was quite a statement. While Friedman has many times contended that higher money growth and higher taxes lead to price increases, he apparently found no worrisome connection between deficits and higher prices.

Purported gold standard advocate, Congressman Jack Kemp, is another leader of the camp which takes a relatively benign view of deficits.

Kemp even went so far as to say that the way to handle deficits is through much *more* rapid monetary growth; he thus proposed to "fight" deficits by inflation—although, as can only be true in the bizzare world of political double-think, Kemp steadfastly stated that this actually amounts to a policy of *combatting* inflation.

Anti-Deficit Magic

There are many who share Kemp's view that with enough economic growth, deficits will eventually "take care of themselves." If this sounds strangely similar to the old (but apparently not yet worn out) notion that monetary stimulus (i.e., inflation) is a good play for prosperity, read on . . .

On its own terms, how would this "modern" notion work its anti-deficit magic?

To use a sports analogy, perhaps as a skilled slalom skier averts obstacles, growth will bypass all the impediments of (ever-increasing) government interferences in the economy and skim along joyously unabated for the next several years. But in order to make a continuous *uphill* run possible, our growth-skier will be endowed with a jetpack containing a clever mixture of "supply-side" and Keynesian doctrines. So powerful, yet controllable, will this mixture be, that the skier will not only effortlessly avert obstacles and speed ever higher, he will be able to tow a bobsled full of happy, taxable workers and producers behind him.

In short, through this enormous economic ingenuity, growth will permit continued expansion resulting in the U.S. Treasury's ultimately taking more revenue from more freshly employed workers and profitable companies. Under this view, the new revenue would supposedly be used to pay for what are now deficits.

Naturally, if somehow this wonderful theory did *not* produce quite enough growth-generated taxation—if growth proved a little too sluggish—it might be "necessary" to raise taxes outright.

Sound economics says higher taxes would inhibit growth, but—perish the thought. Economic history suggests the accelerated money supply portion of the jetpack's fuel would be unstable and likely explode into higher prices, but—perish the thought.

In "answer" to these "dangerous" thoughts, the public is treated to an interesting argument: 1. It will not be necessary to raise taxes *if* the Federal Reserve "cooperates" and doesn't, as Kemp put it, "flirt with deflation," i.e., if the Fed keeps pumping up the money supply. 2. The money supply will *not* be volatile if there's enough growth to "absorb" the new money. Hence, one point conveniently supports the other: More money is needed for growth, which will then justify the money supply increases. This argument deserves an economic "Circular Reasoning Award."

Actually, most economists now accept the view that monetization of debt eventually leads to higher prices. But this does not get to the core of the matter at hand. For what if deficits were entirely financed by borrowing or taxation—i.e., without monetization?

Political Factors

This question forces us to refocus on a broader context, to include in our economic view at least some of the major machinations of modern *politics.* Politics is inextricably intertwined with any economy and the nature of political favor-brokering is inextricably intertwined with a full understanding of the connection between deficits and higher prices.

Without getting into the "I'm honestly coercive" arguments from the morally smug advocates of "openly" higher taxes, let's move on to those advocates who believe that if deficits are financed out of *existing* supplies of money, inflation (by which they mean rising prices) cannot rear its ugly head to strike at America's pocketbook. In other words, if the Fed does not add greater quantities of money to the economy and the government *only* borrows or taxes to meet its overspending, there is no "inflationary impact."

How would this work?

The borrowing portion of the argument holds that those who lend to the government would have lent the money to *someone* anyway; whoever gets the borrowed money will in some fashion spend it.

For example: if a savings and loan is lent money, the firm relends the money to a homebuyer, who then spends the money in the housing market; if a car manufacturer is lent the money—perhaps by sale to the public of corporate bonds—the company uses the money to purchase what it needs to make automobiles.

So, what's the difference if the government is lent the money—through sale of Treasury bills, notes, or bonds? Doesn't the government then turn around and spend the money just as the savings and loan or car company would? Isn't this just a "macro-economic" reshuffling of the cards?

No, it is not. But the argument rests on an interesting premise—out of the same epistemological grab bag that so reliably gives us levitation, clairvoyance, and mental spoon bending. The premise is that government can, in theory, reliably spend money for purposes which are productive, for instance, delivery of mail, road maintenance, dam construction, courts of law, police, and so on.

Marking the Deck in Favor of Government

But despite the theory, often motivated by desperate binges of Rooseveltian political nostalgia (i.e., of how Roosevelt "pulled us out of the Depression," which he did not), most government money *in fact* goes into nonproductive—or at best, far less productive fields—than does money which is left in the private economy. And this is an important clue to discovering the deficit connection to higher prices. This is where we begin to get involved in political machinations. *Increased lending to government is not a question of reshuffling the economic deck, but of marking the deck in favor of government growth.*

(Incidentally, Roosevelt knew of the unproductiveness of government spending, but he was the "Great Communicator" of the emerging Keynesian liberals and successfully exploited a combination of public ignorance about economics and disguised appeals to something for nothing in order to shift blame from government to the bleeding and battered remnants of 1930's business, thus terribly *prolonging*, rather than relieving, the Great Depression.)

The reason most government-directed money tends to end up in unproductive ventures is precisely because it is *politicized* money, money governed mainly by the whims of politicians rather than by the judgments of markets. In most of today's studious tomes of economic analysis, this fact is at best given token treatment. (To his great credit, Milton Friedman gave the subject prominent, if incomplete, treatment in *Tyranny of the Status Quo*.)

Not only does government lack the foresight and standards by which to rationally prejudge what is or is not productive (the most fundamental practical reason for having free markets), but no matter how it acquires its money, government does not really have to suffer failure in the marketplace.

Witness the Postal Service, which has historically been a money-losing operation, and yet grows larger and continues to require government subsidies or abnormal price hikes for its services year after year. As of this writing, the postal primates are engaging in a new round of typical government monkey business, demanding a 23-cent first-class stamp as well as steeper rate hikes for some other classes of mail. If the Postal Service were truly private, investors and users would long ago have relegated it to the marketplace junkyard.

Even worse, look at the various "entitlement" programs. The agencies which disburse money for all manner of purposes, ranging from medical care to food stamps, have conspicuously limited connections to the marketplace. For instance, as economist Alan Greenspan noted in a column (*WSJ*, 4 September, 1984), Medicare and Medicaid operate under *hundreds* of price controls—controls which virtually divorce consumers of medical services from true medical costs.

The Ticket to Success

Modern political history shows that regardless of the money it squanders, if an agency is popular with politicians, it will survive—and grow. The prevailing, though seldom admitted, standard of what is good becomes what is approved; what is good becomes what those in power *say* is good; a pat on the head from a politician becomes more precious than profits, more prized than prices; politics, not markets, become the agency's "ticket to success."

When one discounts expenses for the legitimate government functions of defense and courts of law, all the rest, a majority, amounts to redistributing purely politicized money, coercively gathered from millions of individuals, to special interests selected by the favoritism of those in power.

Despite decades of glorious campaign rhetoric from both major parties to the contrary, government continues to grow and now comprises about one-quarter of the total economy (GNP), up from about one-fifth just four years ago.

As men ranging from Bastiat to Smith to Mises to Hazlitt have illustrated, it is a political rule of thumb that regardless of *how* it gets it, the more government gets to spend *the more it becomes accustomed to spending.*

I admit it is hardly an attractive analogy, but government's appetite is much the same as that of a growing pig; the more you feed it, the bigger it grows and the more food it demands. And remember that *it doesn't matter at all* to the pig's metabolism how you went about getting the food; the animal will grow just as well on borrowed food as it will on food gathered by "legitimate" means.

Just as increased taxes lead to increased inflation and expand the government's appetite, so does a borrowing-financed deficit. Each year of deficit spending accustoms politicians to a new, higher level of spending—spending to redistribute to powerful supporters, whom the politicians hope will constitute a grateful voting majority.

Given the outlandish modern political appetite, taxes, inflation, and borrowing *reinforce* each other. When one becomes insufficient, politicians switch to another.

This is precisely why we see so many demands for "standby" (higher) taxes and why Ronald Reagan—with ample Congressional "encouragement"—signed several tax *increase* measures in the three years after signing into law near the beginning of his administration a personal income tax reduction.

As sad and disgusting as it may be, in good times or bad times for the citizenry as a whole, politicians want only good times for themselves. This is why no matter how badly the economy is doing, the politicians refuse to cut *overall* government spending. They make cuts in some programs, but others increase; they accept a *change* of diet, but squeal in protest at a *reduction* of diet.

The Inflation Tax

When the economy slips into recession, and people are not able to lend the government enough to take care of deficit spending, the government resorts to increased taxation or inflation.

Of course, higher taxes are extremely unpopular during recessions, so inflation commonly becomes the answer to deficit financing. But because the effects of inflation are usually not seriously felt for about two years after it begins, higher prices are put off to times of prosperity. During such times, because people are at least temporarily better off, they are more generous—including toward government; therefore, it is during economic recoveries that taxes are normally raised *and* fresh borrowing is begun, firing up government's share of economic activity to an accelerated, higher level.

Eventually, exploding prices and an updraft of taxation create a mushroom cloud of malinvestment and the deadly economic fallout begins to mutate and kill healthy growth—and recession returns. This gloomy scenario always comes about when government takes more money from the private sector.

Perversely, as we had during the early 1980s, the new round of recession usually occurs as prices are still rising. Price *increases* may slow, but in a fiat-money economy, even during recession, prices seldom actually decrease. In modern vernacular, we get "disinflation" but not general "deflation."

Almost *any* form of financing government's deficit-growth provides more incentive for government to expand—and that expansion leads to inflation. Deficit-borrowing thus becomes just one of several forms of government financing leading to inflation.

In sum then, always it is into the process of steadily increased *political* confiscation of wealth that the question of borrowing-financed deficits must be figured. Financing deficits through borrowing is *not* a contextless phenomenon. To return to my earlier analogy, borrowing to finance deficits *is* a time-tested way of making Government-the-Porker fatter and increasing its appetite.

How to regain control and put the porker on a diet is really another subject—outside the scope of this essay. But until our profligate politicians awaken to the dangers of deficits—no matter how financed—a provocative bumper sticker might be: IF YOU LOVE DEFICITS—OINK!

Dean Russell

An Ancient Chinese Story

IN this particular satire or parable, Bastiat illustrates the ever-present and always-popular concept that government can create jobs and prosperity by means of useless (even destructive) make-work schemes, e. g., digging post holes and then filling them in, as was frequently done by our government in the 1930s to get the economy going again. This story is based on the same idea.

There were in ancient China two large cities, Tchin and Tchan. They were connected by a magnificent canal that had been built to encourage more trade at less transportation cost between the cities.

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This is one of a series of articles examining current interventions of the welfare state in the light of warnings from the French economist and statesman, Frederic Bastiat (1801–1850).

But during a depression in that section of China, the Emperor decided to create jobs and prosperity by ordering large blocks of stone thrown into the canal, thus making it useless.

The Emperor's Prime Mandarin, when ordered to carry out this plan, said to him, "Son of Heaven, this is a mistake!"

The Emperor replied, "Kouang, you talk nonsense!" ("I am here giving you only the substance of their conversation," said Bastiat.) At any rate, the quarrying, transporting, and throwing of those blocks of stone into the canal did clearly provide jobs for many Chinese. And that isn't all.

At the end of three months, the Emperor summoned his Prime Mandarin and said, "Kouang, look across the old canal."

Kouang looked and saw a multitude of men at work. On the other side of the old canal, workers were busily excavating, filling, leveling, and paving. They were building a new highway between the two cities to facilitate trade!

When another three months had elapsed, the Emperor again sent for his Prime Mandarin and said, "Kouang, look."

And Kouang looked. He saw the road completed. Crowds of carts were carrying goods from one city to the other. And a multitude of Chinese porters were carrying on their tired backs enormous burdens from Tchin to Tchan, and from Tchan to Tchin. He also noticed that builders were busily constructing inns for travelers along the new highway. Kouang was beginning to be convinced that his Emperor's scheme to create prosperity by filling in the canal was a brilliant and practical idea. But there is still more.

Another three months passed, and the Emperor sent again for Kouang and said, "Look."

Kouang looked. In addition to all the activity he had seen before, there was now a great deal more. The hostelries were now completed and full of travelers. And to supply their needs, there were butcher shops, bakers' stalls, shops for the sale of edible birds' nests, and so on. There were also tailors, shoemakers, sellers of parasols and fans, and many more. And as those service-people also needed houses, there was a plentiful supply of masons, carpenters, and roofers. Then, of course, there were policemen, judges, and other necessary officials. There was even an increase in the number of persons who employed themselves as smugglers and robbers.

Finally Kouang was fully convinced that his Emperor was indeed the most brilliant genius who had ever lived. The Son of Heaven had proved conclusively that prosperity . . . [and] jobs can be created by obstructing trade.

As usual, Bastiat followed his satire by applying the principle to some current law or governmental scheme designed to create prosperity by obstructing the free market economy. In this particular case, he featured the concepts that, as a result of the make-work scheme, "The people as a whole in Tchin and Tchan were now working harder and producing less; that prices had gone up and real wages had gone down because of the increased transportation and labor costs of moving goods between the two cities."

Less Production, Higher Wages, and Lower Prices

These governmental interventions in the market place (including make-work and other legal-plunder schemes) are producing precisely the same results in the United States today. If I'm right, that idea certainly deserves a closer look. So let's briefly develop the results predicted by Bastiat, i. e., less production, higher prices, and lower wages—all caused by substituting a more expensive factor of production (labor) for a less expensive one ("machinery"). Since all those ideas are inextricably mixed, I'll just include them as they come up.

My students at the University of Wisconsin were usually baffled when I argued that we American people are indeed working hard but, as the government increasingly moves into the economy, we're producing less and less. They found that concept hard to grasp; it seemed contrary to what they could actually see around them.

As near as I can figure, the reason was this: The students were looking at the Gross National Product, i. e., the amount of products and services produced and sold, whatever the type or quality or cost. That's not too surprising since, in their courses in macro-economics, that's precisely how they were taught to look at it. And true enough, by that measurement, the yearly increase in goods and services is usually impressive; and, of course, we can buy only what's available to be bought.

By that GNP measurement, however, our government can (literally) increase national production and national income by paying people to destroy what they've already produced, e. g., plow the crops under, or kill the little pigs, or build a new and expensive canal alongside an existing and under-used and lower-cost railroad (one part of our famous TVA project). Thousands of projects of that nature most definitely did create jobs and increase the GNP during the 1930s, and we're still following that same policy today.

To my way of thinking, the net result of those uneconomic projects (and most other similar governmental schemes) to increase work and jobs is a constantly decreasing rate of growth of goods and services we can use for the improvement of our material welfare. Unfortunately, we have no reliable figure for the amount of wanted goods *not* produced because our money is spent by government on something our congressmen quite openly refer to as "pork barrel" projects, i. e., uneconomic projects designed primarily to create jobs in their congressional districts. Sometimes they even joke about it.

The Auto Industry

Restrictions against trade are, of course, imposed by government for this same purpose of creating jobs. The automobile industry offers an excellent example.

We're all familiar with quotas and tariffs against foreign cars. And as advertised, that policy most definitely does create more jobs in the automobile industry in the United States, as well as more "tariff jobs" in government. Surely all of us are also familiar with the fact that the constantly-rising prices we must pay for our cars (both foreign and domestic) is due directly to that make-work scheme. But just in case there's one person somewhere who hasn't made that connection, I'll here develop it briefly.

We'll never know precisely how much more we must pay for our cars because of this governmental scheme to increase jobs and production in the

United States. We can't know it because the only accurate measuring device (i. e., you and I buying cars in a free economy) has been abolished by government in this particular area. Even so, we can look at historical prices and compare the pertinent relationships when there *was* a free market. And we can compare prices in existing protected and nonprotected industries in general. By those measurements, we can estimate with reasonable accuracy that almost all of the $3,500 (average) price increase (since 1981) you paid for your new car was the direct result of our government's policy to bring prosperity to our country by restricting trade.

We're talking many billions-of-dollars that you and I and all the rest of us would have spent for goods and services we want but can't buy because we must pay several thousands of dollars more for our car than would be the case if the market were free. It's doubtful, of course, that prices on *all* protected products have increased by more than one-third (the automobile rate) because of these governmental "prosperity schemes." But surely a figure of 15 percent is realistic. By any economic measurement, however, we're in the range of hundreds-of-billions-of-dollars of lost production of wanted goods and services that'll never be produced because our government is protecting us from competition. That's why I'm convinced that the production of wanted goods and services in the United States is going down, not up.

Backed by Force

Most people obviously disagree (sometimes almost violently) with my reasoning. They're the ones who have such sublime faith in our government officials. I'm impressed with their sincerity, and a couple of times I've been tempted to give some credence to their arguments for interventions by government. But then I remember where I last saw a large number of them; they were leading the parade to cut our defense budget by at least $100 billion.

At that point, I get the strange feeling they've stolen my arguments. They count in great detail all the *real* (i. e., consumer-productive) jobs that would be created if that $100 billion of "useless spending" were cut from the defense budget. They sometimes even refer to armament production as a vast make-work scheme to make the rich even richer!

I'm not about to get involved in the "defense controversy," but I'm always astounded when I hear the opponents of that "wasteful military budget" actually using Bastiat's argument of the "broken window fallacy," i. e., recounting what can't be seen because what *is* seen blocked it out. I do wish, however, they'd suggest the "saved money" be returned to you and me. Instead, however, they just want it transferred to the various "social service departments." At that point, they re-find their faith in the omniscience of the officials of government—and, of course, they immediately adopt arguments directly opposed to the ones they were just using against the defense budget.

I wonder if they'll accept this fact: The government officials in any department are no more (or less) efficient or omniscient than the officials in any other department. They're just you and me—with their decisions backed by the police force. Personally, I'm *always* distrustful of people who want to have that power over you and me. If that sounds a bit harsh, I'll happily apologize to the offended officials of government, but I doubt I'll change the sentiment. I'm convinced that Lord Acton was correct when he spoke of the corrupting influence of power, and said that "absolute power corrupts absolutely."

When it comes to administering "justice," I'm aware we must give power to our officials. But let's keep it restricted, slow, and inefficient, with all sorts of checks and balances. I'm quite willing to pay the high cost of that vital but non-economic service on behalf of "justice." But when it comes to economic goods and services, I'm after the lowest possible price for the best possible product in the shortest possible period of time. The last mechanism I look to for that performance is our cumbersome form of government with its frequent and disruptive elections that remind me of a particularly vicious proxy-fight to take over a company.

Costly Intervention

I'm aware of the contrary arguments. And I'm especially aware that many people argue quite sincerely that, "Man, I'm an American. I was born here. And I'm entitled to a job that pays a living wage. If that means more governmental intervention in the economy and higher prices for you, so be it."

While I won't endorse that popular argument, at least I can understand why poor and sometimes-ignorant people frequently use it, i. e., legal plunder is acceptable if it's for needy and deserving people. But when our highly educated politicians and industrialists try to hide their own greed and lust for power behind fallacious economic arguments—or behind a plea for plunder "to help others" or even behind patriotism itself—I become unhappy. The automobile industry offers an excellent example of this trend.

Three or so years ago a leading automobile company executive was pleading with Congress for "temporary breathing room" to get his company going again. The "law factory" in Washington produced what he ordered. Today, he's dropped the "breathing room" simile for the even more poetic one of laws to insure "a level playing field," i. e., permanent restrictions against competition, so that the less-talented players can compete on equal terms with the better players, a sort of golfer's handicap arrangement in the production of goods and services. Or to phrase it brutally: To bring the highly-automated and more efficient Japanese automobile industry down to the level of the comparatively labor-intensive and less efficient American automobile industry—at your and my expense.

The result of that first grant of "legal plunder" was (and is) easily predictable. Since Congress awarded it in 1981, the prices for automobiles to you and me have gone up by more than one-third, more than $3,000 per car. And if he and his fellow-executives who've joined him are successful in the current campaign to make that "breathing room" permanent, the prices for automobiles in the United States are likely to go up again by another $3,000 or so per car.

Now for a brief look at the primary reason American cars cost more to build and buy than do Japanese cars. You may recall that "the emperor-son of heaven" in Bastiat's story began his job-creating scheme by first hiring men to destroy the canal with its cheap transportation costs. Then he created still more jobs by building a new road from Tchan to Tchin. This, in turn, created a vast number of additional jobs for men to pull loaded carts from one city to the other or (the traditional method of transportation before those canal-barges came along) to carry the goods on their backs. He replaced a cheaper factor of production (a waterway and wind-power) with a more expensive factor of production (human labor). In short, he hit on the ancient (but ever-present and always-popular) idea of creating jobs by destroying machines.

And that's precisely the reason the cost of American-made cars is at least one-third higher than the cost of Japanese-made cars. The Japanese use as little as possible of the most expensive factor of production (labor) and as much as possible of the cheapest factor of production (capital).

Capital Creates Jobs

As you doubtless know, the result of this low-cost method of production is *not* fewer jobs. Actually, more jobs are thereby created; they're better jobs but found in other areas that support the cheap machines and the highly paid people who produce and run them. There're far more jobs today in highly-mechanized Japan than ever before, and those jobs pay as much as ten times the pre-World War II wage rate. The result of massive capital formation in a free market economy is more jobs, shorter hours, higher pay, and better products at lower prices—in *any* country that follows the principles of free trade, domestic and foreign.

Try to tell that to the president of the United Automobile Workers union—or to the president of any American automobile company. Save your breath. The answer will invariably be that those sneaky Japanese are just "dumping" their cars in the United States by selling them cheaply—"probably below the cost of producing them." (There's that old joke: "If they sell below their costs, how do they make a profit?" The answer: "Mass production; they sell so many of them.")

There's just no way that our industrial and labor leaders are going to admit that the Japanese are better managers than we are, or that the Japanese understand the realities of production-costs and market-pricing better than do the American managers, or even that low-cost machine production provides more and better jobs for people in general.

I suspect you'd even put your physical safety at risk if you made those comments in any UAW meeting, especially if you concluded with the flat statement that the reason our cars are more expensive to build than the Japanese cars (and also probably inferior mechanically as well) is that we use too much of the most expensive factor of production (labor) and too little of the less expensive factor (machines).

Now for a summary of those specific predictions Bastiat made in his "Ancient Chinese Story," i. e., less production, higher prices, and lower wages.

1. Well, obviously we're producing fewer goods and services we ourselves would select if the inefficient and protected and subsidized companies were compelled to meet market demands instead of merely government requirements that permit them to continue to receive the legal plunder.

Our laws are surely protecting millions of jobs that would soon disappear if you and I could decide in the market by voluntarily spending our own money. That automatically includes all jobs in any company that must have tariff protection to continue to exist. Without it, they would all fail or be radically reorganized. I have no count of just how many companies are being kept alive by those non-economic subsidy and tariff laws; it could quite easily run into more than one hundred thousand. We'll never find out as long as we permit them to hide from reality.

2. In 1980, prices were rising at the yearly rate of as much as 20 per cent. The new administration initiated unpopular measures to bring the yearly rate of increase down to

less than five per cent, but it's still a situation of steadily rising prices—and there seems little doubt but that the increase will accelerate again.

3. While jobs are indeed increasing, there are millions of Americans whose current pay won't buy as much as their pay did a few years ago, i. e., there has been a decrease in *real* wages for a large percentage of the American people.

Free to Try

In short, our rejection of a free, open, and competitive economy has cost us dearly, and will cost us even more as time goes on. It's not that we're bad people; we most definitely aren't. In fact, there's good evidence to support the belief that the primary reason we favor these "make work" measures is a misguided effort to help people who need help. But if we continue to confuse charity and economics, I wonder if we'll continue to produce enough to go around.

Perhaps the following short story of two young Americans who set out to "make their fortunes" more than three-quarters of a century ago will demonstrate what made America great, and how far we've now degenerated.

My Uncle Elliot was an excellent harness and saddle maker. In 1908, he went into business for himself in Burlington, North Carolina—The Russell Harness Shop—with $5,000 capital, a whale of a lot of money at that time and place. By chance, another skilled artisan (a wagon maker) also went into business for himself that same year—Frederick J. Fisher, in Detroit; The Fisher Body Company.

Both those young men—each a hardworking and skilled artisan with an eighth-grade education—had an equal chance to "make their fortunes." And that's what they set out to do. The founder of the Fisher Body Company realized his dream. The founder of the Russell Harness Shop didn't. After several years as a fairly successful businessman with four employees, he went broke; his biggest account, the Burlington Fire Department, changed from horses to trucks. And when Uncle Elliot died, we had to "pass the hat" to get enough money to bury him.

It would've been nice if my uncle had been the one who bet on the car instead of the horse. But it's not important. The vital element at stake is this: Both were free to try. Nothing else is of any great consequence. It doesn't really make much difference how it comes out—just so long as everyone is free to try.

And that's the vital mainspring (freedom to try) that's being eroded in America today. And of all things, it's being destroyed in the name of giving everyone an equal chance!

There's just no way everyone can be equal (we aren't) or have an equal chance; for there's no possible arrangement whereby unequal people can have equal chances. And there's nothing our government can do about it.

But we can quite easily arrange for everyone to be free to try. All we need do is repeal all subsidies, tariffs, and similar interferences by government in the market economy. Then anyone can try who wishes. How he goes about it is his problem and privilege.

If he "bets on the car instead of the horse" and produces a product or service you and I want at a price we're willing to pay, he'll get rich—and provide good jobs for the many people who throw in their lots with him. If he fails to provide you and me with what we want, however, he'll fail, as he should. And, of course, all those who bet on his success will suffer the consequences of their poor judgment.

I simply can't imagine a better arrangement to encourage maximum production at minimum prices for the largest number of people—just pass no law that prevents anyone from trying.

Russell Shannon

Trade Barriers

WHEN he wrote *Wealth of Nations* in 1776, Adam Smith referred to "a certain propensity in human nature . . . to truck, barter, and exchange one thing for another."[1] Even children are known to be prone to swap such items as stamps, bubblegum cards, marbles, and other items of mutual desire. But enjoyable and beneficial though trade may be, there is also a propensity to stifle it. Even the Reagan Administration, with a strong and outspoken penchant for free markets, has succumbed to pressures to curb imports of cars, steel, textiles, motorcycles, and other products from foreign lands.

About 50 years after Adam Smith wrote, John Stuart Mill in 1829 clearly explained and soundly denounced such restrictive policies in an admirable essay entitled "Of the Laws of Interchange Between Nations." Mill was following in the footsteps of Smith, who openly opposed the mercantilistic policies whereby European nations had interfered with trade. As the basis for his arguments, Mill expounded the ideas of his more recent predecessor, David Ricardo, who had demonstrated that there is mutual benefit for countries which specialize and trade on the basis of "comparative advantage."

This simple and fundamental principle can be readily illustrated by the examples of the businessman who hires a secretary, the doctor who employs an accountant, or the working mother who turns her child over to a baby sitter. The businessman may be a better typist, the doctor may have superior calculating abilities,

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and the mother may excel in providing affection and entertainment for her child. But by directing their time and energy to their professional duties, these three people will earn more than enough to pay their employees. The businessman and doctor will have even more time for leisure, and the working mother will be better able to provide her child with needed food and clothing.

Yet, what we all implicitly accept and practice in our daily lives, we are pathetically apt to forget when we read or hear news about how some American industry is "hurt" by foreign competition. Nonetheless, the same principle applies. If the Japanese can produce cars and motorcycles more efficiently relative to other products such as beef, then we should buy our cars from them in exchange for our beef. If the Chinese can produce textiles by giving up less of other products than we must forgo here, then we should buy from them. Not only will we enable our consumers—especially the poorer ones—to improve their living standards; we will also provide jobs for our producers of wheat and soybeans, items in which we have a comparative advantage. If some people criticize the Chinese for "underselling" our producers, they should take note of Mill's words: "the world at large, buyers and sellers taken together, is always a gainer by underselling."[2]

Yet, despite the common sense of the free-trade argument, we continue to erect barriers to impede trade. Just as Ricardo and Mill advocated free trade, they reviled restrictions. In 1817, Ricardo had written that "the sole effect of high duties on the importation either of manufactures or corn . . . is to divert a portion of capital to an employment which it would not naturally seek."[3] Mill similarly deplored barriers which have "the effect of encouraging some particular branch of domestic industry," for, he said, they are "purely mischievous."[4]

We Hurt Ourselves

Sometimes it is argued that since foreign governments impose barriers and provide subsidies of their own, they have rendered laissez faire unfair. Certainly, such policies abound and they surely hurt our exporters. Shouldn't we engage in "tit for tat"? If we do, we are sure to suffer for it; as Mill put it, trade barriers are "chiefly injurious to the countries imposing them."[5]

The loss to American consumers when our government restricts imports outweighs the gain to the protected industry. Trade barriers such as quotas and tariffs raise the price on *all* the protected products, whether their origin is domestic or foreign. That is the clear impact, for example, in the case of the agreement by Japan to limit the export of cars to the U.S. Both American and

Japanese producers can hike their prices; both Chrysler and Toyota gain. The costs to our consumers exceed our producers' benefits.

Moreover, by setting up trade barriers, we abdicate the opportunity for setting a good example. As Mill wrote in his essay, "A country cannot be expected to renounce the power of taxing foreigners unless foreigners will in return practice towards itself the same forbearance."[6] We should expect foreign countries to do as we do, not as we say. Until we renounce our own protectionist sins, how can we justify throwing stones?

Before yielding further to the temptation to plunge deeper into the web of trade restraints, it helps to remember that basic fact of all economics: our resources are scarce. We simply cannot produce all the goods and services people want and need. Thus we must bend all our efforts toward employing our resources to their utmost efficiency. Mill said it well: it is "the common interest of all nations that each of them should abstain from every measure by which the aggregate wealth of the commercial world would be diminished."[7] On these grounds we should oppose all laws requiring our cars to be manufactured on the basis of "local content" and others forcing us to "buy American." Suggesting that they simply emulate the practice of others is to argue that two wrongs make a right.

Of course, it may be sadly true that if the Reagan Administration had not acted, Congress would "beat it to the punch" with even more punitive legislation. In that sense, the Administration's policies may well be a lesser evil. But there is another option. The Administration could, instead, devote some time and effort to explaining to the American public the folly of such policies. Then, just like the businessman, the doctor, and the working mother mentioned before, President Reagan and his staff would be making the best use of their resources. And if they need any assistance articulating their ideas, they will find ample help in an essay more than 150 years old written by John Stuart Mill.

—FOOTNOTES—

[1]Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (New York: Modern Library, 1937), p. 13.

[2]John Stuart Mill, *Essays on Some Unsettled Questions of Political Economy* (2nd ed., 1874; New York: Augustus M. Kelley, 1968), p. 36n.

[3]David Ricardo, *The Principles of Political Economy and Taxation* (first published in 1817; New York: E. P. Dutton, 1911), p. 210.

[4]Mill, p. 28.

[5]Mill, p. 38.

[6]Mill, p. 29.

[7]Mill, p. 31.

JOHN CHAMBERLAIN

The Liberal Crack-Up

NOT so long ago R. Emmett Tyrrell, Jr., the editor of *The American Spectator*, wrote a very funny book called *Public Nuisances*. Its humor was Menckenian, which is to say that it relied on hilarious burlesque. Whereupon his editor, Midge Decter, began chivvying him to deal in more systematic terms with the ideas behind the proliferation of the nuisances. Tyrrell, an accommodating soul, capitulated at once.

Surprisingly, in his review of origins, Tyrrell found little fault with such liberal pragmatists as Franklin D. Roosevelt, Harry Truman and John F. Kennedy. It was a good thing in his estimation that Roosevelt had stood up to Hitler and that Truman had moved to "contain" the Soviets. As for welfare, there was reason behind FDR's desire to get apple sellers off the streets.

No ideologue, Tyrrell is actually a believer in the idea of the "vital center," which once allowed for reasonable compromises with doctrines coming from the extremes. The Americans for Democratic Action could have been his brothers-in-arms. He could have broken bread with the Arthur Schlesinger, Jr. of 1950. But, alas, the New Day liberalism that developed in the Sixties couldn't stay on the common sense level. It went off the track by indulging all manner of enthusiasms that actually perverted the aims of the Roosevelt-Truman-JFK past.

Tyrrell's concessionary offering to Midge Decter, *The Liberal Crack-Up* (New York: Simon and Schuster, 256 pp., $16.95), is the story of how the enthusiasms of "post-JFK times" combined to make up a crazy set of blotches of ideas that Tyrrell thinks were noble in their first manifestations. Number One is the blotch the New Age liberals made of civil rights. Number Two is their perversion of welfare. Number Three is the mess they made out of Southeast Asia, where we had a just cause in our desire to save the South Vietnamese and the Cambodians from a Red-inflicted genocide that has outdone anything decreed by Adolf Hitler himself.

Civil Rights to Special Rights

The civil rights movement went off the rails because the New Age liberals turned it into a movement for the promotion of special rights. "Reverse discrimination" fostered a new racialism by its insistence on ethnic quotas. Where the New Dealers had tried to save capitalism by Keynesian means that, unfortunately, had devastating monetary consequences, the New Day liberals were secretly enamored of a more fundamental socialism. They hid their basic animosity for the "system" by devious stratagems. Their undiscriminating environmentalism went the Barry Commoner route of blaming pollution on the big corporations. Their anti-nuke enthusiasm was a derivative of their larger preoccupation with the notion that wicked profit takers were bent on killing off their own purchasing clientele. The feminists—"women of the fevered brow," as Tyrrell calls them—were as chauvinistic as any gang of macho males. The peacemongers agitating for a nuclear weapons "freeze" without considering the record of the Soviets for systematic violation of previous agreements put the whole West in jeopardy by leaving it vulnerable to blackmail.

Legacy of Fabianism

The Liberal Crack-Up is such hilarious fun to read that it leaves one with no desire to criticize its basic acceptance of the idea that special laws were necessary to save us way back in the Nineteen Thirties. Nevertheless, as a more doctrinaire libertarian than Tyrrell, I feel duty-bound to point out that the liberal crack-up was an inevitable legacy of the older Rooseveltian and Kennedyesque Fabianism. There was a whole group of libertarians in the Britain of the Eighteen Eighties who accurately predicted what would happen if the voters were to accept the State welfarist philosophy that was being promulgated by Bernard Shaw, H. G. Wells and Sidney and Beatrice Webb. The idea that socialism would founder because it would fail to solve the problem of calculation without a free market system (including private property) was known in the Eighties. This was some thirty years before Ludwig von Mises had worked it out in detail.

So let not readers of *The Liberal Crack-Up* be deluded into thinking that there is any safety in returning to a New Dealism that predates John Fitzgerald Kennedy.

Privatization

Must we be ready then to say farewell to compassion? Actually there is nothing the State can do for us in terms of offering welfare that couldn't be done much better by privatization. Unlike public welfare, private welfare does not involve what William Rickenbacker has called the death of the dollar. It became ridiculous for Geraldine Ferraro to complain of the lack of "compassion" among the Republican rich when she, as a Democrat, had three houses to live in and a few million dollars at her disposal. She and like-minded friends could have set up private foundations to help the poor without seizing other people's money to do it. Teddy Kennedy might have helped her. As for Social Security, it ought to be floated off in some sort of private insurance that would leave large blocks of capital available to the economic system that supports us all. It was a liberalism that predated Tyrrell's "crack-up" by many years that gave us a social security scheme that is headed for bankruptcy as the elderly live longer and the young are subjected to taxation and inflation that drastically limit the jobs that are available to them.

The liberalism that is so wonderfully spoofed by Bob Tyrrell was a botch from the very start. To begin with, it stole its name of liberalism from the much sounder anti-State liberalism of the Adam Smith followers in England and the Austrian economists of the European continent.

The liberal crack-up as it has manifested itself in the colleges is the substance of another delicious book, *Poisoned Ivy*, by Benjamin Hart, foreword by William F. Buckley Jr., (New York: Stein and Day, 254 pp., $16.95). Hart, the son of *National Review* editor Jeffrey Hart, loves Dartmouth as F. Scott Fitzgerald loved Princeton. But, as a founding editor of the dissenting *Dartmouth Review* (a paper that the college administration sought to kill), Hart was scandalized by the way the "ethos" of the American university would allow for only one opinion when it came to discussing "race, feminism, pacifism, homosexuality, the Third World, U.S. oppression, reverse discrimination—the whole McGovern menu."

What Ben Hart does not tell us is that the "ethos" is already crumbling on the American campus insofar as faculties are concerned. Burton Pines, in his *Back to Basics*, has discovered that Keynesianism is no longer the rage in the economics departments. If the news hasn't reached Dartmouth already, it won't be long before it does.

MANAGING
by Harold Geneen with Alvin Moscow
(Doubleday & Company, Inc., 501 Franklin Avenue, Garden City, NY 11530) 1984
297 pages ■ $17.95 cloth

Reviewed by Melvin D. Barger

FEW business leaders can ever hope to match the dazzling record established by Harold S. Geneen in his 17 years as chief executive officer of ITT. Although some of his corporate decisions were reversed by successors after he stepped down in 1977, none will dispute that ITT's spectacular growth and quickened vitality of the 1960s and early 1970s were entirely the results of Geneen's brilliant leadership. He was so highly regarded as a managerial wizard that some feared ITT would self-destruct without him.

In the 1970s, however, Geneen became tagged as "controversial" by an often hostile press. Critics gleefully pounced on the company's political contributions and alleged involvement in the overthrow of Chile's Allende government to discredit both Geneen and ITT. In this tumultuous period, Geneen was usually too busy running his company to explain himself to the public.

But in retirement, Harold Geneen with his collaborator Alvin Moscow has produced an excellent book that goes far in revealing Geneen's view of himself and his world of business. Unlike the picture of cunning manipulator and power broker presented by his enemies, the Geneen who emerges in *Managing* is a man of simple beliefs whose driving force is an almost religious devotion to the principles and practice of good management. Geneen found his greatest self-expression and enjoyment in his work, which completely absorbed his life and most of his waking hours. The book carries little mention of family and friends, and even his recreational interests had a business tie-in. Some would consider his life austere and narrow, despite his great business success, but it's obvious that Geneen found his business career immensely satisfying and reveled in its problems and challenges.

Although Geneen is a modern manager, he has little patience with management fads such as the currently popular "Theory Z" on the art of Japanese management. "The secret of how to succeed in business or life is that there is no secret," he asserts. "No secret at all. No formula. No theory."

But then his own secret starts to come through in a number of highly interesting chapters, and it becomes clear that hard work, efficient planning, close attention to certain details and unwavering pursuit of specific business goals were the elements of his great success. There was no way that Geneen himself could have fully grasped the products and operations of the 250 profit centers in the ITT tent, but he managed to control this empire by demanding careful planning from his managers and holding them accountable for hitting growth and profit targets. The cardinal sin for an ITT manager was to be surprised by events such as strikes and shortages which he had not anticipated in his previous planning.

Geneen, a financial executive in his earlier years, devotes a complete chapter to the importance of "The Numbers" in managing a business. Geneen believes that "the numbers" have a language of their own and can reveal the facts about a business if a person studies them enough. In fact, however, such "numbers" are best understood by executives like Geneen himself, who was really a born manager and drove himself to understand and use the tools of management.

Managing also carries a brief account of Geneen's own early life and business career. There is a bit of the Horatio Alger, Jr., success story in Geneen's dogged trek to the heights. Although he appeared in his ITT years as the completely self-confident leader who could not possibly fail, Geneen actually had a lonely childhood and years of painful struggle before he was able to seize the brass ring at ITT. Geneen even had to earn his college degree by attending night classes over an eight-year period. But his experience at a public accounting firm and several major companies finally brought him, as if led by an invisible hand, to the opportunity at ITT. Under Geneen's leadership, ITT became a major world corporation, and it's not hard to believe that Geneen's early struggles to perfect his talents were needed to prepare him for this remarkable task.

Beyond explaining how ITT succeeded in the tortuous and confusing world of conglomeration, *Managing* also reveals Harold Geneen as a man of high character and decency who wanted only to be left alone to run his company in the most efficient way. Geneen is the sort of person whom the public often misunderstands, and yet needs if we are to maintain and strengthen our business heritage. Geneen takes it for granted that running successful, profitable business operations is a form of high service to the community, and he sees little need to argue this point.

Like Thomas Edison or General George S. Patton, Jr., Geneen is something of an eccentric who has, nonetheless, amazing gifts in his own special field of interest. We don't have to understand these gifted eccentrics completely in order to benefit from their services. The late Benjamin Rogge used to argue that we would all be better off if we would simply let the superior business manager do his own thing. Maybe Geneen's *Managing* will help get that message across, along with offering splendid advice on how to run a business.

YOUR WEALTH IN GOD'S WORLD
by John Jefferson Davis
(Presbyterian and Reformed Publishing Co., Box 817, Phillipsburg, N.J. 08865)
1984
134 pages ■ $4.95 paperback

Reviewed by Buddy Matthews

THEOLOGIAN John Jefferson Davis' new book is a call to look at the free-market from a Christian and biblical perspective. Though he does not see the Bible as a text book on economics, he does see some economic principles involved. "The Bible makes it clear that spirituality and economic life are related. God controls both and uses economic events to teach His people spiritual truths." His major premise is that the free enterprise system is itself patterned after the Christian life. "[The] biblical pattern of humble service and subsequent reward lies at the heart of the free enterprise system at its best."

As a rebuke to Christians, Davis feels that much of what we know as the welfare state today has come about because Christians have failed to follow Jesus in His concern for the lowly. "The early church cared for its poor. Widows who had no other means of support were to be cared for by the church. Families were to take care of their own, and children were to help their elderly parents. If the Christian church were to consistently apply the provisions today, much of the taxation for social welfare programs would be unnecessary."

Davis views the major cause of poverty as ultimately ethical, noting that the family has lost its role in teaching moral values in Western societies. It is instructive here to see how several Asian countries, because of their close family ties and character building efforts, have begun to prosper. "One of the ironies of the modern world is that the 'Protestant work ethic' seems best exemplified by non-Christian states such as Japan, Singapore, South Korea, Taiwan, and Hong-Kong. Insofar as these new industrial giants of Asia have applied virtues commended by the Bible, they have enjoyed remarkable economic prosperity."

Economic prosperity reflects the efficiency of the free market, as nearly everyone agrees. But beyond efficiency, Dr. Davis argues, the free market embodies high ethical values, and thus should recommend itself to churchmen.