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Security and Freedom

MANY VICTIMS wander unwittingly into socialism, gulled by assumptions they have not tested. One popular but misleading assumption is that security and freedom are mutually exclusive alternatives—that to choose one is to forgo the other.

In the United States during the past century more people achieved greater material security than their ancestors had ever known in any previous society. Large numbers of people in this country accumulated a comfortable nest egg, so that "come hell or high water"—depressions, old age, sickness, or whatever—they could rely on the saved fruits of their own labor to carry them through any storm or temporary setback. By reason of unprecedented freedom of choice, unparalleled opportunities, provident living, and the right to the fruits of their own labor—private property—they were able to meet the many exigencies which arise in the course of a lifetime.

We think of these enviable, personal achievements as *security.* But this type of security is not an alternative to freedom; rather, it is an outgrowth of freedom. This traditional security stems from freedom as the oak from an acorn. It is not a case of either/or; one without the other is impossible. Freedom sets the stage for all the security available in this uncertain world.

—*Leonard E. Read*

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John K. Williams

The Pied Piper and Our Children

ONE of the most delightful poems ever penned is Robert Browning's "The Pied Piper of Hamelin." Children delight in hearing it. The poem tells an exciting story and tells it well, Browning's choice of words and use of meter reflecting and reinforcing the events described.

Indeed, the poem has served me well. As a doting uncle not infrequently charged with the welcome task of minding my nephew and nieces, the poem has enabled me to lure Kristine, Elizabeth and Patrick away from the television set for what I fondly imagine is culturally a more edifying experience. More: while heaven forbid that I ever would abuse my role as trusted child-minder and become a propagandist for sound economics, I did on one occasion introduce the term and the concept of "opportunity cost" to the vocabulary and thinking of my charges by explaining that the "cost" of viewing "Diff'rent Strokes" was not hearing Uncle John reading "The Pied Piper of Hamelin." The success of this exercise was testified to by an agitated telephone call from my sister, who informed me that ten-year-old Patrick had reduced his class-teacher to despair by challenging the justice of a half-hour detention to which he and a fellow miscreant had been sentenced. He had informed his teacher that the opportunity cost of the detention for his partner-in-crime was not having to sweep the leaves off the front lawn of his home, whereas the opportunity cost for Patrick was not playing

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football with two cousins visiting that afternoon.

"The Pied Piper of Hamelin" is, however, more than a children's poem. It tells a story adults do well to consider. It describes a people who lost their children. Because of the irresponsibility of the adults of Hamelin, they lost their children. Their failure to keep a promise solemnly made resulted in a strange Piper leading their children away into a mountain the adults could not enter and from which the children could not leave.

Other Examples

If we think this mass loss of children is only the stuff of which fairy tales are made, we might be wise to think again. Think for a moment of the many pipers playing tunes to which young people, in this century, have responded. The children of Hamelin went laughing and skipping after their piper. The children of Nazi Germany, and of Marxist-Leninist regimes, marched stiffly in rigid ranks after very different pipers, entering a mountain not of delight but of despotism, decadence, and destruction.

We delude ourselves if we assert that pipers playing tunes composed by harbingers of hate either are not found, or are without influence, in nations founded on liberty, and born in the struggle of men and women who dreamed of freedom for themselves and their children's children. Documenting this claim is tragically easy.

I think, for example, of an ugly little volume which, in Australia, is set for study in many of our schools: *Social Sketches of Australia: 1888–1975*. This book has it that the history of my country is one of inhumanity and brutality, led by mean, cruel, small-minded people. According to the author, there is nothing in my nation's heritage worthy of admiration or deserving of praise. It would be an impertinence for a visitor to your country and the recipient of your hospitality to say too much about what he observes in your school system, but I am convinced that the text so distorting my nation's heritage might be matched by parallel texts similarly distorting your nation's heritage and studied by your children.

A Death-Wish

Joseph Schumpeter, I submit, is all too right. He argues that market capitalism in a classically liberal social order generates a set of men and women consumed by a pathological hatred of the socio-economic system of which they are the beneficiaries. Paranoid and careless, this set of people have as their power-base the so-called "knowledge industry." Their paranoia finds expression in the belief that they, uniquely representing the forces of goodness, are the persecuted victims of existing social structures which are the embodiment of evil and which conspire to destroy them. Their carelessness pervades their impassioned rejection of those values which, over long centuries, have proved vital for the emergence and sustaining of civilization and of liberty. They are incapable of understanding what Michael Oakeshott was asserting when, in his inaugural lecture at the London School of Economics, he suggested that "the greater part of what we have is not a burden to be carried or an incubus to be cast off, but an inheritance to be enjoyed."

It is not difficult to see this twisted mentality at work. It is seen in journalists and academics who determinedly keep the minds of their readers and their students fixed upon what is contemptible, thereby nurturing a sour sardonic attitude of rejection which, in the course of time, is extended to the most valuable realities the human heritage has to offer. Their task is not difficult, for in the mixed constitution of things it is easy to pick out what is bad, to ignore what is good, and to draw the black veil of hatred over a complex of light and shade, when it still offers considerable scope for kindness, sympathy, and improvement. Moreover, their task is facilitated by ideas and ideals which, at least superficially, conceal the dynamism of hate under a cloak of compassion. Some of these ideas and ideals I shall explore here.

The Rhetoric of Rights

On July 4, 1776, the then thirteen colonies on your eastern seaboard solemnly in Congress declared that all men "are endowed by their Creator with certain unalienable rights." In so declaring, a nation made its own an idea and an ideal for which men and women, over many long years, had fought, suffered, and died. The liberty of all people to dream their own dreams and to strive to make such dreams reality was, at long last, proclaimed to be a *right* possessed by all rather than a privilege conferred upon some by a caste or a class born to rule.

It may seem strange to observe that such a positive and enriching concept of unalienable rights equally possessed by all people enshrines an essentially *negative* term. Yet it does. A "right" all people enjoy by virtue of their humanity signifies the absence of an obligation to refrain from certain activities or to surrender certain goods. A right to free speech signifies the absence of an obligation not to voice certain opinions. A right to possess certain goods signifies the absence of an obligation to surrender those goods. The only obligation to the possessor of such a right generated in other people by that right is also negative: namely, the general obligation not to disregard or defy that right. The right of one person, X, to engage in some activity generates the correlative obligation in other people not coercively to prevent X engaging in that activity; the right of X to own something generates the correlative obligation in other people not coercively to make X surrender that something.

Let us suppose an individual claims the right to climb a mountain. He is claiming that he is not obliged to refrain from attempting to climb that mountain. He is further claiming that other people are obligated not to prevent him from making such an attempt. What is not being claimed, however, is that other people are obligated to provide him with the equipment or train him in the skills necessary successfully to climb the mountain. *Rights equally enjoyed by all do not generate positive obligations in other people.*

Why not? Simply because rights equally enjoyed by all are grounded in what human beings all share: a common humanity. If I were to claim that I have a right to own a wrist watch, and that men and women wealthier than I am are obligated to provide me with that wrist watch, I am grounding my alleged right in what I and those allegedly obligated to provide me with a wrist watch do *not* have in common, namely, wealth in excess of some arbitrary measure. Claimed rights for some generating positive obligations for other people presuppose two distinct classes of people: people enjoying a purported right to certain goods and services, and people burdened with an obligation to produce and provide those goods and services. Such a state of affairs is incompatible with the insistence that all people equally enjoy the same rights.

A Shared Determination

Again, it would be possible by a shared act of human will to ensure that the equal rights of all people are recognized and respected. Men and women could, by an act of will, refrain from actions involving violence, theft, and deception which, by their nature, ignore and defy the rights of their fellows. Such a shared determination to refrain from aggression against other people could not, however, produce food sufficient for all to eat or paid employment sufficient for all to enjoy. Indeed, the imagination fails when one attempts to describe what would be needed to produce the goods and services sufficient for all people everywhere to enjoy the right affirmed in the twenty-second article of the *Universal Declaration of Human Rights* promulgated by the United Nations, namely, the full development of their personalities in "economic, social, and cultural" spheres.

It is not denied that men and women exercising their shared rights can contract with one another and thereby incur contracted positive rights and correlative positive obligations. Nor is it denied that men and women may morally be obligated in positive ways to those people with whom their lives are entwined, even though those people enjoy no *right* to such compassionate and caring behavior.

The Good Samaritan

In the well-known Biblical parable of the Good Samaritan, it is asserted that the priest, the Levite, and the Samaritan traveler are obligated to assist the wounded victim of robbers; it is neither asserted nor implied that the victim has any *right* to these people's solicitude. The demands of charity have nothing whatsoever to do with any claimed rights. The demands of *clarity,* however, dictate that we use the term "right" to signify what Wesley Hohfeld, in his celebrated classification of rights, calls "liberties." *The right of a person to do A or to own B signifies simply the absence of any obligation to refrain from doing A or to surrender B, and the correlative obligation in other people not to force that person to refrain from doing A or to surrender B.*

In 1881, however, an influential English philosopher, Thomas Hill Green, gave eloquent expression to a seemingly plausible view. All civilized people agree, he suggested, that freedom "is the greatest of blessings." Yet freedom, "rightly understood," means not simply "freedom from restraint or compulsion." Rather, it signifies "a positive power or capacity of doing or enjoying" particular things. A person is thus not really free to climb a mountain unless he possesses the equipment and skills necessary so to do. Or so asserted Green, surreptitiously transforming the concept of freedom. Accompanying this metamorphosis was a corresponding transformation of the notion of a right. Some men and women allegedly *do* enjoy rights creating correlative positive obligations in other people.

Arbitrary Claims

The vision of rights equally enjoyed by all and grounded in the humanity of each and every person faded. In its place emerged a plethora of arbitrary claims and selfish desires pretentiously called "rights." President Roosevelt spoke of the rights of all to "freedom from want [and] freedom from enforced idleness or unemployment," albeit granting to privileged unionists the "right" coercively to prevent non-unionists laboring at wage rates below those arbitrarily decreed by unions, a "right" guaranteeing unemployment for the weak and the marginalized of a community.

Inexorably, a society of free men and women pursuing their diverse visions of the good life, yet bound together by the ties of interdependence and trust forged in the market place, gave way to a society of competing special interest groups, vying for favors and thrusting their snouts ever deeper into the government trough. Inexorably, the weakest and poorest went to the wall, the privileged assuaging their consciences by demanding that those they had forced out of work be paid unemployment benefits, and that those they had condemned to perpetual poverty be granted welfare payments. The politics of principle capitulated before the politics of expedience, parties competing with one another in the task of formulating policies which benefit groups of people who know what they are receiving, and disadvantaging those who do not know what they are paying.

How harmless the tune sounded when first played by the piper. How captivating the melody of positive rights proved to be when first heard. Yet how dark is the mountain into which that piper and that melody would lead us.

Equality

As the noble cry for rights enjoyed by all was transformed into the shrill demand for special privileges enjoyed by some, the dream of equality too became a nightmare. The document speaking of the unalienable rights of all insists that all men "are created equal," and the two assertions go together. All are equal in that all possess the same rights; the demand for equality is the demand for the recognition, in *all* people, of those rights human beings as human beings share. What is morally outrageous is the notion that the rights of different groups of people differ, and that this difference is grounded in one or more of the criteria defining these varied groups.

Springing from this revolutionary insight is the principle of equality before the law. Rule must be by known general principles of just conduct equally applicable to all in an unknown number of future instances. Any precept, even if it enjoys the approval of the majority, which places the interests of some before the interests of others, or prescribes one vision of the "good life" but proscribes alternative non-coercive visions, is thus anathema. Justice *does* wear a blindfold, treating all alike.

Dividing the Wealth

There are those, however, similarly speaking of "equality," who dream a different dream. Professor J.R. Lucas puts it thus: "The equality vouchsafed us by the equality before the law, although valuable and not vacuous, is still much less than the equality the egalitarian seeks." In truth Professor Lucas is too kind: the equality the egalitarian seeks is incompatible with equality before the law, and the equality of rights upon which the rule of law rests.

This other vision of equality today is the vision of many. Confining our attention merely to economists, one thinks of the late Arthur M. Okun, who asserts that "equality in the distribution of incomes . . . would be my ethical preference. Abstracting from the costs and the consequences, I would prefer more equality of income to less and would like complete equality best of all." Joining him is Charles E. Lindblom, who asserts that the closer societies move toward absolute equality of income and of wealth, the more they "approximate [to] the humanitarian vision." Certainly, no economic reasons for this ideal are proffered.

Perhaps the absence of any economic defense of egalitarianism is no accident. The late Henry C. Simons, in his celebrated study of progressive taxation, utterly demolished in his capacity as an economist all pseudo-economic defenses of such a policy and its egalitarian underpinnings, but concluded that "drastic progression in taxation" is an imperative because the distribution of wealth and income effected by market capitalism in a free society "reveals a degree (and/or kind) of inequality that is distinctly evil or *unlovely* [sic]." Such a strange appeal to an aesthetic consideration is echoed by Professor A.B. Atkinson who, in a volume detailing real and imagined inequalities obtaining in contemporary Britain, finds it unnecessary to devote more than a page to explaining what is wrong with these inequalities, and apparently regards as decisive an observation by another writer to the effect that "equality has a particularly powerful aesthetic appeal." Precisely how an aesthetic judgment can lead to a moral imperative and justify the degree of political coercion that imperative allegedly legitimates, is, sad to say, not explained.

Equality of Results

Let us get back to basics. The word "equality," and its cognate expressions "equal" and "equally," signify a relation. Two or more objects are "equal" in respect of a given quality or characteristic if they possess that quality or characteristic to the same degree. Two or more lengths of wood may be "equal" in *length*. Two or more material objects may be "equal" in *mass*. Absolute equality in *all* characteristics or qualities is impossible, for if two entities, A and B, are distinct, then each possesses at least one characteristic or quality the other lacks—minimally, spatio-temporal location. Used of human beings, the adjective "equal" is quite inappropriate, for it is utterly impossible to specify *any* characteristic or quality all people possess to the same degree. That is fortunate: it means that people are not interchangeable, for if A and B are equal in some respect they are, in that respect, interchangeable.

This truism leads to a familiar dilemma. If "equal" opportunities are extended to people of unequal abilities, unequal outcomes result. Yet if opportunities are so allocated that equal outcomes result, that allocation of opportunities must have been characterized by inequality. A policy defended on the grounds of equality can thus no less plausibly be attacked on the ground of inequality. Such was painfully evident in the controversies surrounding the much-publicized and debated Bakke case.

Prima facie, it seems impossible to formulate *any* public policy which generates equality along all of the important dimensions in which human beings have an interest. Empirically, it is far from obvious that the rectification of various social inequalities of outcome by manipulating the distribution of opportunities (by, for example, policies of positive discrimination) has proved particularly beneficial from the viewpoint of the "victims" of the alleged injustice being rectified.

Nor is it obvious that the "correction" of all inequalities affecting the well-being of human beings results in a morally "more desirable" state of affairs. The grotesque worlds of L.P. Hartley's *Facial Justice,* in which handsome men and beautiful women are "cured" by surgery remedying their envy-provoking excesses of sexual appeal, and of Kurt Vonnegut's *Harrison Bergeran,* in which people with abilities above the norm are "equalized" by the implantation of anti-pacesetters, are hardly morally desirable worlds. The examples, admittedly, are bizarre, but they usefully underscore the *directionless* nature of the imperative to eliminate inequalities.

Equal Abuse

Similarly, the *prescriptive* interpretation of "equality" is, considered in isolation, of little or no relevance to social ethics. People are treated equally if they are treated equally *badly;* they are treated with equal consideration or equal respect if they are treated with equally *little* consideration or equally *little* respect. The moral imperative to treat human beings with consideration or respect is *more* demanding than the imperative to treat them with *equal* consideration or *equal* respect. The demand for "equality" is not, in other words, a demand for quality. Nor does a commitment to equality somehow "add" to the value of morally contemptible behavior: the sadist who occasionally softens and spares an intended victim is not "morally worse" than the consistent sadist who tortures all of his victims with egalitarian efficiency.

Human history testifies to the terrible consequences of the attempt somehow to make human beings "equal." Even the seemingly benign attempt to establish equality of wealth or of income demands, as Robert Nozick has argued, a dictatorial State ruthlessly suppressing individual liberty. Nozick's point was eloquently stated some two centuries ago by David Hume, who noted that even if possessions are "rendered ever so equal," the exchanging of goods or the giving of gifts rapidly would "break" that equality. "The most rigorous inquisition is requisite" to check such behavior on its "first appearance," as is "the most severe jurisdiction to punish and redress it."

Once again, however, pipers playing a tune based on the theme of an "equality" quite other than equality of rights and equality before the law, are, today, familiar figures. The young follow them. The identity of these pipers is not difficult to determine. One thinks of such household names as Ralph Nader, Jane Fonda and Tom Hayden. One thinks of prominent journalists contributing to once respected newspapers. And if one is wise, one recalls the adults of Hamelin, who remembering their principles too late, lost their children.

Economic Growth

Finally, I draw your attention to the understanding of wealth and of conquest of poverty that captured the minds and the imaginations of those who, long ago, first dared a dream of a world in which destitution was no more.

How foolish their dream seemed to their contemporaries. Everyone knew that poverty, historically, was the norm. Everyone knew that life expectancy was, in the France of 1800, twenty-four years for males and twenty-seven years for females, and France was then the wealthiest nation in the world. Everyone knew that in 1780, over eighty per cent of French families spent ninety per cent of their income upon bread. Everyone in eighteenth-century Europe and European colonies knew that life, for the masses, was basically nasty, brutish, and invariably short. Everyone knew that the wealth of nations was something given and unchanging, and that one nation could improve its situation only by worsening the situation of other nations.

But a dream was born. Maybe wealth could be created. Maybe trade and exchange could benefit all. Maybe the material well-being of all could be increased. Maybe if the human spirit was unfettered and was released to experiment and to create, food sufficient for all to eat and clothing sufficient for all to wear and shelter sufficient for all to enjoy might become a reality.

And it happened. In one short century the working populace of Britain quadrupled. Real *per capita* income doubled between 1800 and 1850, and doubled again between 1850 and 1900. This sixteen-fold increase in wealth—this sixteen-fold increase in the goods and services available—did more in one hundred years to ameliorate poverty and exorcise the specter of destitution than had millennia of human history and eighteen centuries of preaching about the virtue of charity.

Discovering Uses for Previously Idle Resources

Men and women began to see that resources were not simply "there" to be enjoyed but were created when human creativity and hitherto useless products of nature came together. Human creativity took a black, viscous substance, known from Biblical days and once marginally useful for the making of ink and perfume, and gave it a new use. A new source of energy—oil—thus came into being. Human creativity took dead rocks—anthracite coal—and discovered how to ignite these rocks, and the steamship and the locomotive became realities. People actually began to think of progress; began to realize that the new and the unexpected could burst into being, displace what was the case and always had been the case, and better satisfy human needs and desires.

Yet, during the 1960s many men and women, like mediums conducting a seance, conjured up the dead. The old picture of wealth as something fixed and unchanging was resurrected. The old vision that depicted the gains of some as demanding corresponding losses by others rose from the ashes.

To take but one case, Paul Ehrlich in 1968 published a volume, *The Population Bomb,* proclaiming a dismal future for this fragile planet. I cite this volume because it asserted that 1984 would witness the fulfillment of the dire prophecies Paul Ehrlich made. I, as a visitor to this nation—if Ehrlich's most hopeful scenario for the future had become a reality—would be observing a country within which steak was but a memory. Between 1973 and 1983 the world would have witnessed one billion men, women, and children starving to death. The United States would have imposed strict food rationing. Riots would have torn this country apart when Congress during the mid-1970s passed the Family-size Regulation Act. Smog would be ubiquitous. The telephone system would be no more. Unemployment would be the lot of twenty-seven per cent of the potential workforce. Globally, disaster would reign. Since India's food production had reached its maximum potential in 1967–1968, that nation, and similar Third World nations, would be haunted by the dread horsemen of famine and of death. Or so Paul Ehrlich prophesied.

He was wrong. In the 1970s India, after three disastrous decades of socialist agricultural policies, largely deregulated agriculture. Price controls on food were lifted. Tax reforms were effected enabling farmers to retain more of the earnings from the produce they sold. Decisions as to what to plant were taken from central planners and restored to farmers themselves. In September 1977 U.S. grain exports to India began to wane, for India was almost self-sufficient in food. In 1983 India began to agonize over the new but welcome problem of how best to store surplus crops. Instead of rising, the birth rate in less developed countries has fallen from 2.2 per cent yearly in 1964–1965 to 1.75 per cent yearly in 1982–1983. Global food production, whether measured by grain prices, production per consumer, or the famine death rate, is vastly better today than ever before. The cost of such minerals as copper is falling, not rising, human ingenuity having made from sand a substance performing one of the uses to which copper once was put, and having launched space satellites substituting for the millions of tons of copper cable global communications once demanded. A higher percentage of the U.S. populace today engages in paid employment than ever before.

Paul Ehrlich and his fellow doomsayers are demonstrably wrong. Yet the pipers of cataclysmic disaster continue to play their dirge. Herbert I. London recently penned a volume entitled, *Why Are They Lying To Our Children?*, documenting the prolonged after-life of discredited dogmas about the limits of growth. Surveying sixty-eight school textbooks, London notes that the future therein depicted, based on demonstrably false statistical evidence, flawed methodological assumptions, and utter economic ignorance, is a future of depleted resources.

So in my own country. A set textbook for all students in my State desirous of sitting university entrance examinations is penned by a biologist, Professor Charles Birch, and it too depicts a desert-like future, withering any hope of a world in which destitution is no more. The very best strategy that Charles Birch, and his U.S. counterparts, can recommend is a world government coercively redistributing present wealth. What has failed in the U.S.S.R., failed in mainland China, failed in Tanzania, failed in Cuba, and failed wherever it has been tried is, apparently, to be implemented on a global basis.

Observed disaster is not, it would seem, sufficient to silence the dread piper playing the terrible tune that is "socialism." Play he still does, and the young—and sometimes the not-so-young—mindlessly follow.

Conclusion

Yet, I cling, and shall continue to cling, to the hem of hope. For there is another piper playing a very different tune.

He was heard during the fifth century B.C. in the city-state of Athens, and human beings began to dream of rule not by a tyrant's whim or a mob's caprice, but by law. He was heard by those men and women in medieval England, who made Magna Carta—the great *Constitutio Libertatis*—a reality, and forged a weapon before which all despots trembled, knowing their days were numbered. He was heard again in the eighteenth century by thinkers who challenged the world of guild and of caste and of privilege and of legally-fixed relations that was mercantilism. He was heard again by those who fled tyranny for a new and better world, and who penned the Virginia Bill of Rights, the Declaration of Independence, the Constitution of the United States, and the First Ten Amendments to that Constitution. And he still is heard by ordinary people who, suffering under today's tyrants, listen to their short-wave radios and, with tired and hurting fingers, transcribe the works of Solzhenitsyn and risk the concentration camp and the so-called psychiatric hospital in obedience to this other piper playing this other tune.

And what about us? We too have heard the piper who lures us by the song of liberty. We know we shall lose our children. After all, we know we never owned them in the first place. Yet to what pipers shall we lose them?

I spoke earlier of those sad and sorry men and women who betray the heritage of which they are the beneficiaries. I spoke earlier of their attempts to cheat our young people of that heritage. I thus remind you of the task the philosopher Alfred North Whitehead laid upon the shoulders of men and women such as we. What is that task? Simply to bring before the growing minds of our children "the habitual vision of greatness." When Matthew Arnold was installed as Professor of Poetry at Oxford, the great Benjamin Jowett pleaded with him to do one thing: "Teach us not to criticize, but to admire." Taken at face value, that plea was somewhat wholesale. There is that in my nation's history, and in your nation's history, which ought not to be admired. That is where criticism comes in. Yet the irony is that our shared heritage enshrines the very principles by which that meriting criticism is identified and that meriting condemnation stands condemned.

To insinuate a note of admiration in a generation reared in skepticism and cynicism is no easy task. Yet to no less a task are we called. You and I have caught a glimpse of the stars, and it is for us to say "No!" to those who would shield the eyes of our children from ever seeing those stars. In the final analysis, we cannot fail. For at the very heart of life—yes, at the very heart of God—lies freedom. Humankind, bearing the *imago Dei*—the Image of God—can never be content until freedom is a reality known to all and enjoyed by all. The tune the piper of liberty plays is the tune that pulsates and throbs through all that is, and which finds voice in that tiny part of the cosmos which has become aware of itself, the human spirit.

God grant that you, that I, that our children, keep our ears open to the piper who testifies to the reality of liberty built into the very fabric of our being. For it is only as we and our children follow that piper that we shall discover what Whitman sang of: "life immense in passion, pulse, and power"; and what the Jewish Rabbi of Nazareth meant when He spoke of "life, and life abundant."

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Dennis Bechara

Eminent Domain and The Rule of Law

ONE of the distinguishing features of a free society is its defense of the right of private property. As every individual has the right to his life, so has he the right to those things necessary to sustain life—among them, the private ownership of property and the ability to keep the fruits of his labor. Those rights not only assure that the individual enjoy the life and liberty promised him by a free society, but also assure continued freedom, independence, and security for all.

The institution of private property, however, is not without its critics. Socialists of all types decry private property as plunder and many parts of the world have instituted public ownership of the means of production. In this country, however, criticism about the validity of the institution of private property itself is very limited. Yet, in spite of the consensus regarding the legitimacy of private property, the concept itself has suffered a progressive erosion which is reaching potentially alarming proportions. As massive government intervention and forcible income redistribution has become the order of the day, real estate has come into play as an adequate means for the involuntary transfer of wealth.

In a sense, this development became inevitable once the proposition was accepted that some segments of the population had the right to be forcibly supported by the remainder of society. The redistributionist mentality has legitimatized the taking of one person's income and its transfer in favor of another. Yet, this process remained somewhat anonymous and detached, because the individual taxpayer has been at a loss to identify the particular beneficiaries who received his share of the taxes.

Since the costs of government programs are dispersed among all taxpayers, coupled with the general an-

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onymity of the specific beneficiaries, taxpayers have had little incentive to arrest the growth of the welfare state. Rather, the opposite has been the case. Groups have formed with the specific goal of receiving subsidies from the government, and the results of these organized special interest groups have been substantial.

Beneficiaries Identified

Recent judicial developments related to the power of eminent domain, however, have somewhat altered this reality. As owners of land become dispossessed as a result of the emergence of the exercise of eminent domain by local and state governments, the anonymity of the redistributive process has been shattered. The identity of the beneficiaries is known and in a sense this fact may pierce the cloak of altruism that has covered all the redistribution of wealth in which the government has been engaged.

The one case which highlights this expansion of government power, and which eloquently introduces its danger is *Hawaiian Housing Authority v. Midkiff,*[1] which was decided on May 30, 1984 by the United States Supreme Court.

The facts of the case are relatively simple. Hawaii, because of its Polynesian background, did not have a tradition of encouraging the private ownership of land. Land was held by certain island chiefs and subchiefs, and all who occupied it were tenants of the then governmental authorities. Over the years some settlers were able to purchase land but by the decade of the 1960s the government, both Federal and State, owned 49% of the land. In addition, 47% of the State's land was then owned by 72 landowners. One of the landowners, the Bishop Estate, owned 341,000 acres which belonged to Princess Bernice Pauahi Bishop, the last survivor of Kamehameha the Great, who unified the Hawaiian Islands in the eighteenth century.

Some of the landowners were discouraged from selling their land and leased it instead because of the adverse effect of the income tax laws. In addition, others, like the Bishop Estate, were charitable organizations which were exempt from taxes. Strict land use laws in effect in Hawaii have also interfered with the workings of the land market.

Barriers to Market Transactions

Although the fact that the government owned such a substantial amount of land, coupled with the structural barriers to the land market, inevitably affected the real estate market in Hawaii, the State's legislators concentrated their attention on the 72 landowners and proceeded to enact the Land Reform Act of 1967.

Under the provisions of this statute, tenants who live in any developed residential tract of land of at least five acres in size may, if they so desire, petition the Hawaii Housing Authority and request the Authority to initiate condemnation proceedings so that the land may be forcibly transferred to them. In the event that the tenants do not have the financial resources to acquire the real estate, the State of Hawaii would lend them up to 90% of the purchase price. The statute provides for a hearing in which the landowner may introduce evidence as to the fair market price of the land, but otherwise the landowner may not object to the validity of the condemnation process.

The case arose because the Bishop Estate challenged the constitutionality of the statute, alleging that the Land Reform Act of 1967 violated the Fifth and Fourteenth Amendments of the Constitution. The thrust of their argument was that the taking of the land, as provided by the statute, was invalid because it was clearly not for public use, since the tenants were to acquire title to the land. The United States Supreme Court decided the case and it held that the statute was valid and not repugnant to the Constitution.

Following Precedent

The Court's approach in determining whether or not the intended use of the condemned land fulfilled the constitutional requirements that the land be publicly used was that since the state legislators had the power of eminent domain, it would be presumed that the use of the land by the tenants was constitutionally valid unless this was shown to be an impossibility. The Court cited a previous case, *Berman v. Parker*,[2] as the authority for reaching its decision. That case contained the following language:

> Subject to specific constitutional limitations, when the legislature has spoken, the public interest has been declared in terms well-nigh conclusive. In such cases the legislature, not the judiciary, is the main guardian of the public needs to be served by social legislation, whether it be Congress legislating concerning the District of Columbia . . . or the States legislating local affairs . . . . This principle admits of no exception merely because the power of eminent domain is involved.

Essentially, the Court's reasoning is that once it is determined that Congress or a state Legislature has the power to condemn land as a result of its power of eminent domain, then the Court will not invalidate the statute, in effect abdicating its responsibility of constitutionally evaluating the legislative scheme. The Supreme Court's position is that it will not substitute its judgment for that of the legislative branch, so long as the statute has a rational connection with the constitutional power enjoyed by the legislature. The implications of this case are very important, because state legislatures now have an additional power which they previously were not aware they had.

The power of eminent domain has existed for many centuries, but perhaps the clearest explanation of its purpose was proffered in 1625 by Grotius, when he said that:

> The property of subjects is under the eminent domain of the State, so that the State, or he who acts for it, may use or even alienate and destroy such property, not only in cases of extreme necessity, in which even private persons have a right over the property of others, but for ends of public utility, to which ends those who founded our society must be supposed to have intended that private ends should give way.[3]

This definition clearly sets forth the very limited function and role that eminent domain must play in society. One can envisage the prototypical example of extreme necessity—a fire in a city—which necessitates the destruction of houses which have not yet caught fire, precisely to avoid the spreading of the fire to the rest of the city. Similarly, whenever national defense is involved, it is reasonable that the government have the power of eminent domain in order to assure all of its citizens of the benefits of peace. The power of eminent domain, however, has expanded from the very limited role assigned to it by such legal scholars as Grotius, to the contemporary role of serving any broadly defined public purpose. In order to understand why the Supreme Court ruled the way it did in the *Hawaiian Housing Authority* case, it is instructive that we analyze the origins and developments of eminent domain in the United States.

British Policies

The right of eminent domain came to America via England, where it had been established for quite some time. In England, there were two varieties of eminent domain, one applicable to the Crown and the other to Parliament. The Crown was entitled to use privately used land in those areas where it was indisputable that the Crown had jurisdiction. For example, for such aspects as foreign defense or law enforcement, the Crown or its representatives were entitled to use any privately owned land so that the exercise of the Crown's powers would be more efficient. Parliament, on the other hand, could only take private property after payment of a fair compensation. The requirement that compensation be given to the owner was added after 1514.

In the colonies, the Crown faced the seemingly insurmountable problem that a vast unexplored continent needed public roads if it was to be developed. Therefore, the right of eminent domain was imported to

America as a road building tool. Prior compensation, however, was granted to the owner of improved land, but it was denied to the owner of unimproved land. The reason for this was that the owner of unimproved land actually benefited from the construction of a road through his property, so there was no need to compensate him for the land actually taken.

In Colonial Days

The understanding throughout colonial days was that a taking of private land would only be justified if it was for the public use. In fact, the Constitutions of Virginia and Pennsylvania, both of 1776, used the phrase "public use" when they both sanctioned the taking of private property. This requirement appears in the Fifth Amendment to the United States Constitution, which states in part that ". . . nor shall private property be taken for public use, without just compensation."

The power of eminent domain was also utilized, during this time, for the building of milldams. The reason the Mill Acts were enacted was that it was deemed a public necessity to facilitate the availability of mills to farmers. These statutes, which twenty-nine states had already enacted into law by 1884, provided a mechanism whereby mills were established without unnecessary restraints, the damages caused by the consequent flooding were compensated and the farmers had various mills from which to choose. It is entirely possible that had the Mill Acts not been enacted in the first place, many mills would have nevertheless been established on a voluntary basis as millers would have discovered that it was to their economic self-interest to reach agreement with the owner of the land they were to flood.

The right of eminent domain became an unimportant and uncontroversial footnote in the history and the development of the United States during the eighteenth and early part of the nineteenth century because of the vast territorial expanses of the country. However, with the development of the country there arose a need to improve transportation. Therefore, state legislatures began expanding the role of eminent domain to allow private companies to build private turnpikes, highways and canals. The public was served in the sense that more transportation alternatives were made available to them and they were guaranteed the use of these facilities. Thereafter, with the development of railroads, eminent domain was further utilized to grant some railroad companies the right to build their tracks in spite of the objections of the owners of the land taken by the railroads.

Recent research has demonstrated that although railroad companies were empowered to seize land that stood in the way of certain routes, the landlords who were about to be dispossessed were not without legal recourse. In his article, "Reassessing The Impact Of Eminent Domain In Early American Economic Development," Dr. Tony Freyer concluded the following:

> . . . local interests could get what they wanted from, or even obstruct the construction of, transportation facilities. Whatever benefit railroads and canals received from eminent domain law could be offset by localism; and working against such realities, the corporations either struck a bargain or looked elsewhere for a route. Either way, the operational impact of the assessment process was increased costs. Thus, while the right of eminent domain could potentially facilitate development, ironically, it also provided the means to impede development.[4]

Court Rulings

As the use of eminent domain became more prevalent, the landowners who were adversely affected by this development resorted to the courts in an effort to prevent the confiscation of their land. Since the purposes of eminent domain had so vastly expanded, the courts had to analyze whether or not the taking of the land was constitutional.

Essentially, courts were faced with the issue of whether or not these takings satisfied the public use requirement. Over time, courts began developing a distinction in the interpretation of the "public use" requirement of eminent domain statutes. Some courts felt that all that was required was that the general public receive some tangible benefit as a result of the taking. The danger with this interpretation was that it opened the doors to all types of takings, since it is logically conceivable that any type of enterprise will benefit society after it has taken some property. On the other hand, a narrow interpretation also began to take shape, as courts envisioned the possibility of abuse by powerful private interests as they associated themselves with the power of the state to plunder private citizens.

The law of eminent domain remained more or less settled during the latter part of the nineteenth century. In fact, the Federal Government did not exercise the power until 1875. Prior to that date, a state would condemn land and afterward transfer its title to the Federal Government.[5] However, it was rather settled that eminent domain could be exercised only in the limited cases where the public had a right to use the condemned property. That a taking may arguably benefit the public at large was deemed insufficient to justify the exercise of eminent domain. Yet, the United States Supreme Court was not altogether consistent in this point, and in the 1916 case of *Mt. Vernon-Woodberry Cotton Duck Co. v. Alabama Interstate*

Power Co.,[6] the Court embraced the public benefit analysis.

In that case an electric company attempted to condemn certain land and water rights in order to generate hydroelectric power. The company claimed that the taking was for public use because provision of electricity benefits society at large. Justice Holmes, writing for the Court, agreed, saying that if "... that purpose is not public we should be at a loss to say what is."[7]

New Deal

As the New Deal took hold of America, its effects were felt in the evolution of the law of eminent domain. The United States Housing Act of 1937 was the watershed. This statute created the United States Housing Authority, which in turn was enabled to grant loans to local housing agencies in order to eradicate slums and build public housing projects. Naturally, most states seized upon this opportunity for Federal funding and proceeded to condemn many areas that were described as blighted in order to build public housing projects. If the courts had maintained the narrow interpretation of the public use requirement, these condemnations could not have been effected. Instead, the prevailing interpretation became the broader view that the public benefit or receive some advantage, which permitted the taking of property for limited purposes. The Housing Act of 1949 further enlarged the states' right of eminent domain, as housing authorities were permitted not only to condemn slum areas but in fact were permitted to resell the land to private developers who in turn would follow a previously approved plan of land development.

A Radical Departure

Finally, the Supreme Court in 1954, in the previously mentioned case of *Berman v. Parker*, was faced with the issue of a landlord, whose department store was not "blighted" nor did it constitute a public nuisance. This person nevertheless had his property condemned because the area in which his store was located was classified as undesirable and the Federal Government had declared that it would serve the public interest if that area were sold to private entities who in turn would redevelop the land. Plaintiff lost his case, and the Supreme Court in effect granted Congress a blank check upon which to write its own brand of urban redevelopment. Therefore, the next logical step came in the *Hawaiian Housing Authority* case which upheld the right to condemn private property in order to transfer the land to smaller and fragmented private owners so as to take care of the "market failure" in land in Hawaii. The power of eminent domain is so prevalent and so powerful, that it is literally limited by our imagination.

Some of the governmentally subsidized projects that have been the object of eminent domain range from such projects as the Tennessee Valley Authority to the World Trade Center in New York City. But perhaps the case which demonstrates the most callous disregard for the rights of a community is a 1981 Michigan case, in which 3,468 people were displaced in order to allow General Motors to set up an assembly plant.

The Poletown Situation

The case arose when the cities of Detroit and Hamtramck decided that it was a desirable goal to acquire 465 acres which were located between them, at a cost of over $200 million. The cost included such other functions as relocating the residents, demolishing the existing structures and preparing the land so that in turn the corporation would be entitled to purchase it at the price of $8 million. GM would also be entitled to certain tax advantages which made it quite profitable to set up an assembly plant there. In return, GM would provide over 6,000 jobs with all the consequent benefits entailed by such job creation.

When the affected neighbors were apprised of what was in store for them, they filed suit, challenging the validity of this taking, because the use for which the property was ultimately intended was to be private and not public. The affected area, known as "Poletown" because of its predominantly Polish composition, was not a slum, nor was it considered an eyesore or a blighted spot in the city landscape. It just happened to be in the way of industrial development. The Michigan Court rejected plaintiffs' arguments, and considered that since the creation of jobs was in and of itself an action which benefited the general public, that the exercise of eminent domain was therefore valid in this instance even though a private entity would own the land and operate it for its own profit. In addition, the Court pointed out that the determination of what constitutes a public purpose belongs properly to the legislative branch, and that it would not question this finding without clear objections on constitutional grounds.

No More Dissent

The fact of the matter is that the court in the Poletown case[8] is not atypical of the rest of the courts in the country. The United States Supreme Court, in the *Hawaiian Housing Authority* case simply restated what are now well-settled principles of law. The fact that the Court decided this case with eight Justices in favor of the decision and none dissenting, should give us a clue as to how uncontroversial this interpretation of the law has become. Courts have in effect abdicated their responsibility of determining whether or not a taking is for public use. It is now sufficient that the legislature declare that a taking will be in the public interest if that taking has some rational connection with the evil that the legislature wants to eradicate.

Market Failures

One of the most popular evils that politicians are desirous of eradicating concerns "market failures." Yet if we were to analyze the root of these failures, whether they are unemployment, inflation, surpluses or shortages, a substantial cause of these failures is directly attributable to prior government intervention in the market. Therefore, in view of the fact that interventionism has taken such a firm hold of the economy, it is not difficult to visualize all the potential market "failures" that exist and that will appear to be ample justification for the exercise of eminent domain. Eminent domain has become yet another tool where special interest groups seek what they would otherwise not be able to obtain voluntarily in the market. The right of private property has in fact been eroded over the years as a result of this judicial development to the extreme that we hold our property at the pleasure of the government. If the government decides that someone else ought to have our land, whether it is for aesthetic reasons, or for job creation or for any other reason that conceivably benefits society, then we will almost inevitably have to succumb to the state's desire for our land.

A Hopeful Sign

Courts should limit the widening powers of eminent domain enjoyed by the government. They should undertake an analysis of whether or not a taking is truly for public use, and the conclusion of the legislature that a taking is in the public interest should not be blindly accepted. The victims of eminent domain have mobilized by filing appropriate lawsuits aimed at the prevention of the taking of their land. Although unsuccessful, the fact that people are actually opposing the arbitrary exercise of eminent domain is a hopeful sign. It is time that we should heed the comments of Justice Van Voorhis in his dissenting opinion in the case that paved the way for the construction of the World Trade Center in New York City:

> Disregard of the constitutional protection of private property and stigmatization of the small or not so small entrepreneur as standing in the way of progress has everywhere characterized the advance of collectivism. To hold a purpose to be public merely for the reason that it is invoked by a public body to serve its ideas of the public good, it seems to me, can be done only on the assump-

tion that we have passed the point of no return, that the trade, commerce and manufacture of our principal cities can be conducted by private enterprise only on a diminishing scale and that private capital should progressively be displaced by public capital which should increasingly take over. The economic and geographical advantages of the City of New York have withstood a great deal of attrition and can probably withstand more, but there is a limit beyond which socialization cannot be carried without destruction of the constitutional basis of private ownership and enterprise.[9]

—FOOTNOTES—

[1] 81 L. Ed. 2d 186 (1984).

[2] 348 U.S. 26 (1954).

[3] Grotius, 1 *De Jure Belli et Pacis,* Ch. 1.

[4] 1981 *Wisconsin Law Review* 1263, 1284.

[5] *Kohl v. U.S.* 91 U.S. 367 (1875). This case established the Federal Government's eminent domain power.

[6] 240 U.S. 30 (1916).

[7] *Ibid.*, at 32.

[8] *Poletown Neighborhood Council v. Detroit* 410 Mich. 616, 304 NW 2d 455 (1981).

[9] *Courtesy Sandwich Shop v. Port of New York Authority* 12 NY 2d 379, 399, 190 N.E. 2d 402, 411 (1963).

Property Condemned

IDEAS ON LIBERTY

THE VICTIMS, who in former years might have called upon the court or a policeman for protection, now find the court and the policeman on the side of the aggressor. We may not be able to measure the damaging effect on respect for law and order; but the damage is done, nevertheless.

Barbarism has its earmarks, and the acquisition of property through conquest or superior force is notably one of them. Civilization, too, has its earmarks, and the orderly disposition of property through the medium of deeds, leases, wills, and other contractual arrangements is not only an earmark of civilization but an absolute prerequisite. Leases, deeds, wills, and other contracts will all fall under the stroke of the proposed condemnation. With them will fall the personal security, the hopes, the plans, and—yes—the dreams of the many human beings who have placed their faith in their worth. Here, as always, the failure upon the part of large segments of any given society to understand and respect the rights of ownership can only result in the rise of innumerable pressure groups, all trying to suggest what should be done with other people's property.

EDWARD P. SCHARFENBERGER

Hans F. Sennholz

Some Evils of Inflation

TO BE IGNORANT of inflation is to suffer its evil effects. Most people define inflation as a period of generally rising prices and wages. They echo official pronouncements and news reports by the public media that interpret all price rises as inflationary. Quick to indict anyone who raises prices, they accusingly point to the lust and greed of other men, especially businessmen, as the root cause of inflation.

This popular interpretation of inflation contains all the futile means and remedies commonly used to fight inflation: the price constraints and controls designed to keep prices lower than they otherwise would be, the public condemnation of businessmen who raise prices and their prosecution for violating price control edicts, the imposition of income-tax surcharges, and so forth. It obscures economic reality, pointing at the visible effects of inflation and its victims; it does not call attention to the essence of inflation, the inflating of the money quantity.

The popular confusion about the meaning of inflation is more than just unfamiliarity with definition. It is a root cause of inflation itself without which it could not persist. It completely reverses cause-and-effect relationships and thereby indicts the victims for perpetrating the crime while it exculpates the monetary authorities who willfully and openly are creating ever more money.

Thought makes the word, and the word makes thought. Inflation breeds great evil, whether you define it as rising goods prices, as an increase in available currency and credit, or as an abnormal increase beyond available goods, resulting in a visible rise in prices. Of all injustice, inflation is one of the greatest as it devours the possessions of millions of hard-working people. And no

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matter who is perpetrating it, the courts of law actively collaborate with the perpetrators by upholding the evil and declaring it constitutional, equitable and fair. A dollar is a dollar, they proclaim, you shall accept a 10-cent dollar in payment of a 100-cent debt.

Political Injustice

It is easier to endure the losses that are suffered as a result of error and misjudgment than the damage sustained by injustice. Inflation ministers unbearable injustice, defrauding some people and enriching others. It impoverishes some social classes while it bestows comfort and wealth on others. There cannot be any doubt that inflation derives aid and comfort from its many beneficiaries.

Political injustice is committed from a great many motives and reasons and often makes use of legislation that goes under the name of legal tender, a perfectly innocent label for hideous wrongs. It appears to be harmless, indeed, when defined as "a currency which may be lawfully tendered and offered in payment of money debts and which may not be refused by creditors." In reality, legal tender is no offer at all, but a forced acceptance, no tender that may be freely refused, but a legal obligation to accept a currency no matter how much its purchasing power has fallen or is expected to fall. Legal tender actually denies the freedom of contract and the right to refuse acceptance of deteriorated means of payment.

Legal tender legislation grants government unlimited power over the monetary affairs of the people just as the coinage monopoly of the state did in antiquity and the feudalization of the coinage right during the Middle Ages. It creates this power in democratic societies as it does in the command societies under socialism and communism. Government, by way of legal tender legislation, forces people to accept its own currency, grants it monopolistic position, and prohibits its discount no matter how it may depreciate. In short, legal tender legislation outlaws monetary freedom and paves the way for great injustice.

It is difficult to fathom anything more unjust than legal tender legislation. It permits monetary authorities to inflate and depreciate their money and then force the people to accept it at face value and in full payment. It gives special privilege not only to the government but also to all debtors. They need not pay their debts in full but can discharge them by giving inferior money in exchange. Legal tender destroys the property rights of creditors. Under the pretense of creating order and stability, it turns every credit transaction into speculation on the future purchasing power of the medium of payment. It is immoral to the highest degree.

Legal tender legislation permits government to tax its people without having to seek their consent first. It enables government to issue any quantity of fiat money, declare it legal tender, and spend it for political ends. It is a tool of expropriation of property owners and creditors, including all sellers of goods, services and labor. It forces them to accept legal tender currency at face value no matter how much it has deteriorated and how low its purchasing power has fallen.

The legal tender evil has come to the U.S. through both legislation and jurisdiction. Under the plea of absolute necessity, the Continental Dollar was made legal tender in 1776 until its demise in March of 1781. During the Civil War, Union greenbacks were given legal tender force. In 1933 all Federal Reserve notes and U.S. Treasury currency were given coercive powers. In every case the courts sanctioned the action and ignored the evils. The U.S. Supreme Court confirmed the monetary powers of government in a number of conspicuous decisions. From John Marshall, Chief Justice for 35 years (1801–1835), to Charles Evans Hughes, Chief Justice during President Roosevelt's monetary machinations, most justices made the best of government control over the people's money. On June 5, 1933, a Joint Congressional Resolution voided the "gold clause" in all contracts and obligations. In 1935 the Supreme Court concurred. In the words of Chief Justice Hughes, "parties cannot remove their transactions from the reach of dominant constitutional power." (Henry Mark Holzer, *Government's Money Monopoly*, New York: Books in Focus, 1981, p. 185.)

Unearned Income and Loss

Inflation causes displacements in the distribution of income and property. As lenders and borrowers, most people do not take into account variations in the objective exchange value of money. If the monetary value should decline, the lenders are bound to suffer losses in purchasing power while the borrowers gain a corresponding amount. There are long-term contracts that do not have to be fulfilled until a later point in time. There are long-term employment contracts or contracts for the supply of materials, all of which involve money payments over time. They all face inflationary risks.

It is a popular, although erroneous, belief that inflation affects only wealthy individuals because they are said to be the money lenders. This may have been true during the Middle Ages when economic wealth was concentrated with a few wealthy noblemen and merchants, while the masses of people were struggling for mere survival. But ever since the nations of the West emerged from feudalism and mercantilism, and tried individual freedom and enterprise, an ever-growing number of people were able to save some part of their rising incomes, permitting most people to become lenders on net balance. There are millions of creditors of life insurance companies, pension funds, savings banks, and similar institutions. Millions of people own government savings bonds and other money assets. It is true, they may have charge accounts and other consumer debt. But in most cases savings probably exceed obligations, which suggests the conclusion that the American people are vitally interested in sound money.

The disastrous nature of inflation becomes apparent when we contemplate the magnitude of the losses which inflation is inflicting on millions of American creditors every year. Even at the modest rate of five per cent annual depreciation, the annual losses to creditors and gains to debtors amount to more than $100 billion a year. The economic and psychological impact of this silent transfer of wealth on millions of individuals surpasses all imagination.

Considering such staggering losses on the part of the thrifty and provident, the rising clamor for entitlement and transfer is not surprising. The losses strengthen the demand for social security, aged health care, and governmental controls over prices and rents. They foster Federal aid and subsidies and otherwise provide a chief argument for an extension of government power.

Long-Term Contracts

Long-term employment contracts permit inflation to inflict painful losses on millions of working people. Within a few years of employment they may lose a part of their purchasing-power income through monetary depreciation. Their relative economic and social position in society may decline when inflation ravishes them more than others. There cannot be any doubt that teachers, ministers, priests, and rabbis are primary victims of inflation. But they also are thought leaders who significantly affect the moral, political and economic trends of the future. Their losses in income and social position during the age of inflation may have contributed to the fact that many are more frustrated in political and economic outlook than other groups of society.

Monetary depreciation inflicts special losses also on industries that are controlled politically, in particular, public utilities. Being subject to commission control, their rates are fixed by decree in accordance with authoritative judgments of fairness and adequacy; but their costs keep on rising in reaction to inflationary pressures. American railroads and public utilities are eminent examples. In competition with other industries for capital, labor and supplies, their costs are rising; but their own rates are determined by government committees and commissions that are known to grant relief only after lengthy public hearings and long after inflation has raised production costs. Moreover, public authorities are tempted to "fight" inflation and "hold the line" by denying price adjustments. Squeezed by the vise of rising costs and rigid rates, the financial position of public utilities deteriorates considerably. In the end they stagnate and cease to function efficiently.

Booms and Busts

It is the course of every evil that it brings forth more evil. Unbeknown to most people, including most economists, inflation breeds business cycles with destructive booms and depressions. Indeed, what has been more damaging to individual freedom and the enterprise system than the recurrence of recessions and depressions! During the Great Depression government interventionism made its greatest strides. Each new recession gives new impetus to political power.

Inflation at first produces conditions that appear favorable to everyone. Businessmen earn extraordinary profits; there are few, if any, business failures. Employment conditions improve and wage rates rise, for which labor unions and allied politicians loudly claim credit. The general atmosphere is one of confidence and prosperity until the inflation-induced activity tends to raise business costs. In time costs soar until profits turn into losses and a recession takes the place of the boom.

Recession is a time for readjustment to the demands of the market. Loss-inflicting operations are abandoned, and business costs are reduced. Businessmen correct their mistakes made during the boom; the worst offenders are forced to sell out or face liquidation and bankruptcy. Even labor may need to readjust to market demands or face unemployment. In short, a recession or depression is a time of recovery from the excesses and blunders of the boom.

Business cycles have plagued this country from its beginning. In every cycle the U.S. government tried its hand in money and banking. Whether the debauchery of the Continental Dollar by the Continental Congress, the issue of U.S. Treasury obligations during the British-American War and the Civil War, the financial adventures of the First and Second Banks of the United States, the silver legislation, the World War I inflation—they all constituted preludes for the depressions that followed. Similarly, the Great Depression had its beginnings in the bursts of credit expansion by the

Federal Reserve System in 1924–25 and again in 1927–28. Without them there could have been no stock market boom and no crash of October 24, 1929. Since World War II, Federal Reserve credit expansion kindled seven booms and seven recessions.

Full employment through deficit spending and currency expansion is the official doctrine that guides the economic policies of Federal Administrations. Whether it is deficit financing or easy bank credit, the ultimate consequences are always the same. But each depression is bound to be deeper and more painful than the preceding one, and each boom more feverish than the preceding boom, because maladjustment, if not corrected, is cumulative. Recessions turn into depressions and booms into "crack-up booms" with panicky flights into gold and other real values. In the end, booms and depressions become "stagflations" that combine both evils: the destruction of currency and the depression with mass unemployment.

Rising Tax Exactions

The federal government is the greatest beneficiary of inflation; politicians, government officials and their proteges its greatest profiteers. When inflation raises money incomes it lifts taxpayers into progressively higher income tax brackets and thus allocates an increasing share of their incomes to government. It pushes them all toward the top rate. Similarly, it boosts government exactions through state and local income taxes, corporate income taxes, estate taxes, and other levies with progression features.

Business income and taxation are especially affected by monetary depreciation. When prices rise, a distortion in profits takes place. They are made to appear larger than they actually are. Inflation drives the cost of replacing plant and equipment above the original cost, but for tax purposes government recognizes only the original costs and thus forces business to overstate its actual earnings. It levies income taxes on imaginary profits which, in reality, are inflationary costs of maintenance.

The great popularity of inflation rests on its benefits to government. The federal government as a giant debtor reaps vast fortunes from monetary depreciation. On its nearly two-trillion-dollar debt it reaps gains of tens of billions of dollars every year. It may add new debt through budgetary deficits, and yet, the mountain of debt, in terms of purchasing power, may not rise at all because inflation may melt it away even faster.

In a modern transfer system government exists for the purpose of promoting the prosperity of those who run it—politicians and officials. Inflation permits them to spend vast amounts that directly and indirectly benefit them. Their remuneration usually exceeds the amount they can earn in productive employment. Their perks and fringes are much to be desired, their power over others to be feared. In order to secure their benefits and sustain their power, they need the votes of their constituents. Multi-billion-dollar expenditures for group entitlements may buy the votes. And the power to buy votes with entitlement legislation depends on their power to inflate. Without it, a Federal deficit of $200 billion annually would be inconceivable, as would be the myriad of transfer programs and the huge bureaucracy administering the programs. The transfer state builds on the power to tax and to inflate, the effects of which in turn give rise to ever more transfer demands.

The Dollar Standard

Inflation creates problems not only at home but also abroad. Until 1971, when gold was the international money and the U.S. dollar was payable in gold, inflation generally caused an outflow of gold from the country with the highest rate of inflation. Threatening inability to pay in gold tended to restrain the country from inflating any further, or force it to devalue its currency toward gold. But in 1971, the United States refused to honor its growing foreign obligations to redeem its currency in gold. Fearing more losses, President Nixon declared gold to be "unsuited for use as money," and vowed to remove gold from the monetary system of the world. When other major countries followed suit the transition from the traditional gold standard to irredeemable paper issues was completed.

The U.S. dollar emerged as the primary international currency serving trade and commerce the world over. It already had acquired a leading position under the Bretton Woods system that had made the U.S. dollar the international reserve money payable in gold at a price of $35 per ounce. When, in August 1971, President Nixon repudiated the agreement the world continued to use the U.S. dollar without its redeemability. After all, the world's merchants and bankers had grown accustomed to it. It afforded access to the markets of the most productive country in the world, and its record of relative stability was one of the best in recent monetary history despite its devaluations in 1934 and 1971. But above all, the official repudiation of gold created a void which no other fiat currency could possibly fill. It left the U.S. dollar in the most prominent position for becoming the world medium of exchange and reserve asset.

The world desperately needs a common money that facilitates foreign trade and international transactions. For hundreds of years gold served as the universal money uniting the world in peaceful cooperation and trade. Today the U.S. dollar is called upon to assume the very functions of gold. But in contrast to the gold standard, which was rather independent of any one government, the dollar standard depends completely upon the wisdom and discretion of the U.S. government. That is, the world monetary standard now rests solely on the political forces that shape the monetary policies of a single country—the United States.

We can think of no greater responsibility for any country than that of the United States to the world. Every day assumes a fearful responsibility when we view the fate of the free world that rests on the U.S. But unfortunately, the dollar standard is a political standard in which the purest motives are mixed with the most sordid interests and fiercest passions of the electorate. The dollar standard itself is the outgrowth of an ideology that placed government in charge of the national monetary order. It is the handiwork of governments and their apparatus of politics. To expect much of such a creation is to invite bitter disappointment.

The world fiat standard leads to temptations which no contemporary government can be expected to resist. The world demand for a reserve currency constitutes an extraordinary demand that tends to support and strengthen its purchasing power. It affords the country of issue a rare opportunity to inflate its currency and export its inflation without immediately suffering the dire consequences of currency debasement. In particular, it presents an opportunity to the administration in power to indulge in massive deficit spending, which hopefully bolsters its popularity with the electorate, while its inflation is exported to all corners of the world. The country that provides the world reserve asset can, for a while, live comfortably beyond its means, enjoy massive imports from abroad while it is exporting its newly created money in payment of such imports. In short, it can raise its level of living at the expense of the rest of the world.

Government as Beneficiary

For more than a decade the U.S. government has been the beneficiary of this ominous situation. It engages in massive deficit spending and currency expansion with minimal inflationary effects as the dollar inflation is exported to foreign countries. For several years the foreign dollar holders even financed most of the budgetary deficits which the U.S. government was incurring. Inevitably they suffered staggering losses on their dollar holdings which they had earned in exchange for real wealth. And yet, they are coming back again and again because their own currencies are worse than the U.S. dollar.

The greatest factor of dollar strength is the chronic weakness of other currencies. Leading European currencies do poorly in foreign exchange markets because their banks of issue are pursuing policies of easy money and credit. European central banks are undermining confidence in European currencies and thereby generating an extraordinary demand for U.S. dollars.

The exchange rate between various currencies is determined by their purchasing power. It is explained by the purchasing-power parity theory, according to which the rate of exchange between currencies tends to adjust to their purchasing powers. If the exchange rate were to deviate from parity and a discrepancy were to appear, it would become profitable to buy one and sell the other until the discrepancy would disappear. If the exchange rate of the U.S. dollar versus the Swiss franc were to favor the U.S. dollar it would be profitable to sell the dollar and buy the franc until the disparity would disappear.

Foreign-exchange rate changes anticipate relative changes in goods prices. But it is safe to assume that a rise in foreign exchange rates is unlikely to signal an anticipated rise in purchasing power. After all, in this age of inflation every currency is losing purchasing power most of the time. "Strength" in foreign exchange rates merely means relative strength in terms of other currencies that are losing purchasing power even faster. The U.S. dollar may be the strongest currency around although it, too, is losing purchasing power. It may rise to spectacular heights versus other currencies although it is sinking to new lows in purchasing power.

Exporting Inflation

Foreign inflation is giving the dollar a boost; every foreign attempt at prosperity through credit expansion is giving it new strength. On the other hand, every U.S. government effort at expansion is sapping the dollar strength, every new attempt at financial stimulation through Federal Reserve credit expansion is weakening the dollar vis-a-vis all other currencies.

U.S. monetary authorities now are orchestrating the international flow of funds. During the 1970s they generated the greatest credit boom the world has ever seen. There had been some credit expansion before August 15, 1971, when President Nixon unilaterally abolished the last vestiges of the gold standard. But it accelerated dramatically thereafter when the U.S. government showered the world with U.S. dollars. Central bank reserves consisting primarily of paper dollars expanded from $92 billion in 1970 to more than $800 billion in 1983. The Eurodollar market, which recycles the flood of petrodollar deposits to debtors all over the globe, grew from some $100 billion in 1970 to nearly $2 trillion today. All these credits fueled an inflation the likes of which the world has never seen before.

The 1979 Crisis

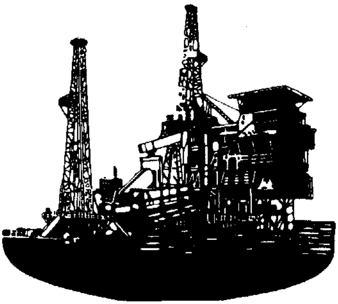
In October 1979 an international flight from the dollar visibly shook the world dollar standard and cast serious doubt on its future. It forced President Carter to raise $30 billion in harder currencies in order to stem the panic. When the discount rate was raised to 13 per cent the crisis subsided. Federal Reserve authorities subsequently reduced the expansion rate and in some months even abstained from any further credit expansion, which soon triggered the beginning of painful readjustment. The 1981–1982 recession was the inevitable effect of this new self-restraint. It precipitated a worldwide scramble for liquidity and gave rise to a "crisis-demand" for U.S. dollars. The demand gave new strength to dollar exchange rates and new support to its purchasing power.

The recession put a heavy strain on the world's banking system. A number of large debtor countries were unable to meet their obligations. Poland, which owed large debts to financial institutions in the West, fell victim to its own socialistic policies. Argentina, mismanaged by a military junta, sought a rescheduling of its considerable debt. Mexico, in a similar situation, gave rise to the fear that her failure could lead to a chain reaction bringing about a collapse of several large financial institutions and eventually the world banking system. Throughout the fears, strains, and volatile changes in foreign exchange markets, the U.S. dollar was gaining in strength.

The crisis demand for dollars was bolstered further by the fears of political and financial instability abroad, making the U.S. dollar a "refuge currency." In many countries suffering from sustained currency depreciations the U.S. dollar is the key currency. It can be found in the cashholdings of people everywhere who use it as their unit of calculation and medium of exchange. They are bidding for U.S. dollars by offering their goods and services in exchange for more dollars.

As long as individuals the world over are willing to hold dollars and keep on adding dollars, the dollar is bound to remain strong. But if they should lose faith in U.S. policies and reduce their holdings, the dollar would turn weak again, perhaps weaker than ever before. It could tumble in an abrupt and disorderly fashion, and the dollar standard disintegrate in confusion and disarray.

Bill Anderson



Industrial Policy

DURING the 1984 election season, Industrial Policy became a catchphrase as candidates outlined their economic positions. Since the elections have now passed (at least for two quiet years), the phrase is not bounced around in the news columns as before, but advocates of Industrial Policy are as anxious as ever to see their ideas come to fruition. Thus, their ideas bear watching and those who see this particular policy initiative as potentially disastrous to our economy should try to obtain whatever intellectual and political ammunition is available to see that Industrial Policy remains only an idea.

Throughout this paper I shall be critiquing the so-called Industrial Policy ideas, but before I criticize I shall give the readers a general description of what these ideas are and how they would be implemented.

First, it should be noted that Industrial Policy advocates such as Harvard University's Robert Reich, Barry Bluestone of Boston College, Senator Gary Hart and business executive Lee Iacocca see American industry in decline: our basic industries such as automobiles, steel, rubber and textiles are falling prey to subsidized or outright government-owned foreign competition. The loss of such jobs, they contend, means the end of the American middle class as we have known it, and further erosion of the job base will relegate us to low-paying service jobs such as keyboard punching and hamburger flipping. America the once-powerful and wealthy will become America the exploited colony.

Second, advocates see Industrial Policy as fitting into a broader picture of "quality of life," which emphasizes things like health care, support services, paid vacations, environmental purity, welfare compensation and other such amenities that

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"protect" us from the often harsh realities of life. Government planning and intervention, they argue, can help raise the standard of living for most, if not all, of us by providing more quality of life services.

Specific Industrial Policy implementations would include the following:

(1) Increased government spending in health care, unemployment compensation, worker retraining, housing and relocation for displaced workers.

(2) "Domestic Content" legislation for automobiles as well as increased "protection" for other domestic producers that must compete with foreign firms both in the U.S. market and abroad (included in this package would be a broad range of subsidies both for exporters and firms that sell mostly in this country).

(3) Increased (or targeted) regulation of U.S. firms, especially those in the transportation industry to insure "stability" in the marketplace.

(4) Reinstitution of the Hoover-era Reconstruction Finance Corporation that would make low-interest loans available to "threatened" U.S. firms.

(5) Restrictions on plant closings to keep firms from shutting down unprofitable plans or enterprises in one area of the country and moving them to a more suitable business climate either in this country or in a foreign land.

(6) Expanding labor union power, giving "participatory rights" to workers in the decision-making of the firms where they are employed as well as providing workers' groups with low-cost liquid capital to enable them to buy plants that are closed or are being closed.

(7) Targeting of potentially profitable new firms (such as high-tech companies) by giving them "protection" as well as low-cost capital.

Interventionism

Of course, any observer of government intervention into our economy can readily see that government has, at one time or another, followed the above scenario. Government expenditures for health care and unemployment benefits have steadily increased since the 1960s. Protectionism has been a part of Federal policy since the founding of our republic. The regulatory monster has expanded its reach for nearly a century, and government support of unions has guaranteed organized labor a far larger share of the workforce than it would have if unions were forced to compete in the marketplace the way firms compete for workers.

But the advocates of Industrial Policy recognize this fact as well. They, too, admit that government already intervenes in the ways specified previously and further admit that intervention can even be harmful at times. The choice, they say, is not between intervention or non-intervention; rather, we must choose between "smart" policy and "stupid" policy.[1] Stupid industrial policies, the advocates say, disintegrate into a chaotic mixture of zero-sum clashes between competing sectors of the economy.[2] Smart policy, they say, brings the different sectors together in a coordinated effort. The key, of course, is to know the difference between that which is "stupid" and that which is "smart," then have the political conviction and courage to see that Congress implements these policies. As Reich has noted:

> America has a choice: it can adapt itself to the new economic realities by altering its organization, or it can fail to adapt and continue its present decline. Adaptation will be difficult. . . . A new consensus is difficult to achieve when each person seeks to preserve his standard of living but finds that he can only do so at the expense of someone else. But failure to adapt will rend the social fabric irreparably. Adaptation is America's challenge. It is America's next frontier.[3]

Examples given by industrial policy advocates include the so-called success of the Japanese Trade Ministry, or MITI, and (if one can believe it) American farm policy. Both cases, the advocates write, show that by coordinating private businessmen and government officials, an entire economy can benefit from new success and productivity. Most important, they say, is that the new efforts at Industrial Policy are not a case of the private sector versus the public sector, as is the case of socialism. Rather, they note, the key word is "coordination," or, perhaps, a "public and private partnership."

Partnership?

To those who have become weary of the false battles of "public interest" against the "private interest," such a proposed partnership might bring some relief. The truth is, however, this so-called "partnership" is every bit the assault on the private economy that has come with decades of socialist planning. At best, Industrial Policy is a naive idea that will be rendered harmless by public indifference and its greatest sin will be that of wasting a valuable commodity called paper. But at worst, Industrial Policy will bring about large distortions and misallocation of capital in the economy while, at the same time, increasing the already intolerable mass grab for funds from the Federal treasury and pushing productive entrepreneurship underground.

Distorting the American economy is the last thing on the minds of the Industrial Policy promoters. After all, they say, the idea is to *help*, not *hurt* our economic prospects. One might ask, "How can anything so destructive come out of something meant to do so much good?"

To refute the promoters' claims, then, we must show the ways in which such policy implementation will cause damage to the economy, as well as demonstrate the difficulty of putting such legislation in force. Before dealing with those subjects, however, we will first examine the two examples of success cited by policy proponents.

Learning from Japan

When viewed with a critical eye, the so-called magic of MITI fades into political and economic reality. This is not to say that MITI has not had some success, but most likely those Japanese success stories would have occurred even if the bureaucrats in the trade ministry had not "targeted" the semiconductor industry, among others.[4] What is more important, however, is what MITI failed to accomplish—to the relief of the Japanese. In the early to mid-1970s, MITI attempted to persuade Japanese investors to target the steel and petrochemical industries rather than the automobile industry, which MITI declared could never be competitive with U.S. auto manufacturers on an international basis. As we know today, Japanese steel stays alive mainly because of government support while the Japanese automobile industry has become the envy of the industrialized world.[5]

No wonder, then, that Economist Katsuro Sakoh said that the recent economic success of Japan is "based not on how much it [the Japanese government] did for the economy, but on how much it restrained itself from doing."[6]

As seen by the recent wave of farm foreclosures—coming at a time when record supports are being paid to farmers—one is hard-pressed to comprehend the excitement Industrial Policy proponents have for farm programs. Yet, Economist Lester Thurow, an ardent supporter of interventionism, has written, "In agriculture what started as a desperate effort to prop up a very large, sick industry in the 1930s ended as an industry that is the world's most efficient. There is no reason that feat cannot be duplicated elsewhere."[7]

In answering Thurow's glowing endorsement of farm policy, Richard McKenzie, an economist from Clemson University, comes directly to the point:

> What such advocates fail to report is that we have an agricultural policy that props up the price of food for the rich and poor alike, that adds to the impoverishment of the lower-income groups in this and other countries, that contributes to the destruction of the soil base, and wastes a monumental amount of food—all in the interests of appeasing a very powerful political interest group.[8]

McKenzie touches on the point of interest groups made by Reich, but unlike Reich, he understands the nature of interest groups and is fully aware that appeasing such groups is not costless. For even if one ignores (and we will not do so in this paper) the economic illiteracy shown by Industrial Policy advocates, it is impossible to bypass their political naïveté. Their fallacy is simply the fallacy of composition; that is, they forgot that what may be good for one special interest group is not necessarily good for the public at large. Farmers who receive supports from the federal government no doubt personally benefit, but the benefit is not shared by the public. Rather, the public must pay for this transfer of wealth through higher taxes and higher food prices. To give such support to every sector of the American economy simultaneously is virtually impossible, since there would be no sector left to plunder. Instead, such universal support would be an act of self-plunder, of everyone attempting to prosper at the expense of everyone else.

Industrial Policy proponents totally misread the true nature of government. In the view of those who believe government is the best tool to correct so-called "market failures," according to economists Robert E. McCormick and Robert D. Tollison, "the state is a productive entity that produces public goods, internalizes social costs and benefits, regulates decreasing cost industries (monopolies) effectively, redistributes income Pareto optimally (giving to some without hurting others), and so forth."[9]

A Flawed Theory

But McCormick and Tollison, through their studies of government, find that such an approach "is not a very *believable* theory of government action and, moreover, that it is flawed by the unwarranted assumption that government can be called upon to correct imperfect markets in a perfect and costless manner. That the state is not a perfect instrument for correcting market failures hardly needs demonstration. . . . Indeed, although imperfections in the economy may be lamentable, lamenting is the best that can be done if the consequence of government action is to decrease rather than improve economic welfare."[10]

As stated earlier, Reich acknowledges the impact of interest group behavior (called "rent seeking" in economic jargon), but then declares that Americans must "adapt" to "new economic realities," as though a few exhortations to unselfishness by (self-interested) politicians can change things. But the truth is, people who have their hand firmly placed in the Federal cookie jar, along with those trying to jam their own hands into the chaos, will not suddenly turn altruistic because a few intellectuals write books. It must be remembered that the fallacy of composition works both ways. Most handouts to special interest groups constitute a small part of the Federal budget—that is, by themselves. Particular groups asking for more Federal money, protection, or the like usually preface their requests with an acknowledgement that whatever portion comes to them will be only a minute part of the budget and that cutting out that giveaway will have almost no effect on efforts to balance the Federal budget. And, most importantly, such groups are firmly aware of the old adage that governments grow "because the benefits are concentrated and the costs are diffused." They argue, "See the good this program will do for us, yet the cost to the taxpayer is very minimal."

Behavior at the Margin

If the case is seen as being isolated from the rest of the budget, then the argument makes sense. But economics and the study of political and economic behavior does not simply concentrate on total spending or total outlays. Rather, studies emphasize behavior *at the margin.* That is, when we look at the total budget picture, we view it as the sum of every little program (plus the gargantuan ones as well) that Congress slips into law. Any one of those programs by itself constitutes only a small fraction of total spending; added together, however, the programs become part of a budget out of control.

Can such rent-seeking behavior be changed through exhortations by politicians and intellectuals? Hardly. If one views the present budget picture as the political norm, the prospects for ending the interest-group giveaways are not bright. For one, neither intellectuals nor politicians are free of rent-seeking qualities. In the case of the politician, he or she is part of a barter system that trades favors for votes. Politicians are fond of asking for budget restraint—in someone else's district; they like to seek tax increases—far away from their constituents. Intellectuals, on the other hand, are not free of government largess themselves. Universities are perennial grant recipients, as are particular professors who receive Federal monies for their own pet studies. And, finally, there is the issue of power. One can readily surmise that if the federal government were ever to implement the version of Industrial Policy advocated by the proponents, those in charge of overseeing the resulting programs would be the very intellectuals who are interested in seeing the programs come to fruition.

Thus, one can be sure that the initiation of a so-called comprehensive plan of Industrial Policy would not end the destructive rent seeking that presently characterizes our budgetary process. Instead, it would give government intervention a new respectability at a time when the realities of intervention are proving just how harmful intervention and regulation has become. And as the political process would steadily worm its way into the decision-making of the Industrial Policy czars, the facade of economic impartiality would crumble until nothing remained but rent seeking and interventionism.

Economic Fallacies

Plans of Industrial Policy can be criticized as in conflict with political reality. But those plans contain a multitude of economic sins as well, a mountain of errors which will be discussed next.

The first challenge to the so-called need for Industrial Policy deals with the very claims that America is in the throes of deindustrialization. This challenge is vital because it attacks what proponents see as the basic reason for implementing Industrial Policy in the first place.

While it is true that many of America's factories have shut down in recent years, many on permanent shutdown since the 1981–82 recession, one must keep those facts in perspective. For one, much of the unemployment in this country is concentrated in *heavily unionized industries*, including manufacturing and mining. (The construction industry—much of which is unionized—also suffers from high rates of unemployment, but high unemployment rates in that industry are common, due to a large number of economic factors.) Because of the nature of unionism, such high unemployment rates are predictable, especially given the militancy of union leadership in this country. The higher-than-average wage of the union worker helps bring about unemployment in two ways. First, as economic theory predicts, the high price of unionized workers forces the company to hire fewer employees than it ordinarily would have hired had market rates, rather than coerced wage rates, prevailed. Second, the high wages make it attractive for other workers to seek union work, as well as making it attractive for laid-off union workers to remain unemployed until being recalled. Thus, the high rates of unemployment in unionized sectors.

But unionization has other negative effects on industry as well. Most of the recently closed plants were shut down because they lacked the needed capital to operate profitably. Unions have long been known to resist recapitalization in plants because such retooling often leads to a smaller workforce in those particular factories, which equates to less membership in unions. Therefore, plant owners and managers have often had to limp along in a high-technology age with yesterday's capital. While the economy was booming, such problems could be masked; when the latest recession hit, however, the party was over and old, obsolete plants closed by the hundreds.

No Mass Migration

This is a grim picture, but does it translate into the claim by Industrial Policy advocates that there is at present a mass transfer of jobs from the Northeast (snowbelt) to the South (sunbelt)? No doubt, some firms are relocating facilities from the Midwest and Northeast into the South. But the so-called massive transfer claimed by the Industrial Policy proponents just is not happening. Richard McKenzie points out that New England's manufacturing employment rate in the latter 1970s grew at a compound annual rate of 3.46 per cent, which was 50 per cent more than that of the South Atlantic region. This was no simple wealth transfer; rather, it reflected the growing high-tech boom and the ability of the New England states to provide such firms with a labor force that could match the job requirements.

In fact, according to U.S. Department of Labor Statistics, projections show the distribution of manufacturing jobs in this country to remain relatively static through the rest of this decade.[11] While it is true that certain changes, some pleasant and some not, are occurring on the micro level of our economy, the broad picture is that the U.S. economy is strong. True, there is a small but significant growth rate in the service economy, but this growth is a sign that we are becoming wealthier, not poorer as Industrial Policy proponents tell us.

This is because the growth of services tells us that we need not employ huge numbers and proportions of our population in basic manufacturing jobs as was required in years past. The growth of fast food restaurants, for example, is not a threat to our well-being, but rather reflects the fact that Americans are eating out more, a sign of greater disposable income. The same can be said of numerous other service industries as well. Because our manufacturing base is efficient, and because low-cost foreign firms see this country as a strong market for selling their products, we are able to buy basic items at far less cost (in percentages of personal income) than could our forebears. This means that we have money left over to eat out or purchase services becoming more and more available to us. And as the potential for service industries continues to grow, the opportunities for new kinds of employment grow as well.

Those who declare that the increase in imports and the growth of service employment threaten our well-being forget that foreign firms will sell here as long as they believe they can receive something in return. Japanese auto manufacturers, for example, are not philanthropists; they do not sell us high-quality, inexpensive automobiles out of altruism. Rather, they seek goods and services in return and if the day comes that we have no manufactures or if all of us are turning over hamburgers at the local fast-food place, the Japanese or any other foreign producer will look elsewhere for new markets (or the Japanese will undergo massive changes in their dietary habits—highly unlikely).

The actual implementation of Industrial Policy, judging from what has been described about the rent-seeking aspects of the political process, would be nearly impossible. But, for the sake of argument, if it were actually put into law, could it succeed? That is, are opponents actually afraid that such an initiative could be more effective than free markets, thus discrediting a whole body of economic literature and its authors?

If the writings of Nobel Laureate Friedrich A. Hayek are to be believed—and economic history has yet to discredit Hayek's work—the answer is a flat no. First, and most important, Hayek has shown time and again that centralized planning cannot replace the efficiency of the marketplace, and his writings have been proven by the unqualified market failures of socialist economies.

The Role of Knowledge

A recurring theme in Hayek's work is the role of knowledge in economic processes, a theme recently emphasized by economists Israel Kirzner and Thomas Sowell.[12] Hayek points out that while economic knowledge can be centralized in a few areas, it cannot be centralized when dealing with the entire workings of an economy. As McKenzie notes:

> The mental capacity of our leaders is limited. They are capable of digesting only so much information intelligently. Central control of the economy will ultimately be restricted by the mental limitations of our elected and appointed leaders, even though they may be the "best and the brightest" among us. Growing complexity in products and productive processes, which is forecast by industrial policy proponents, will necessarily make us more, not less, dependent upon decentralized decision-making. This is because the growing complexity of production means that our leaders will be less capable of knowing and handling the entirety of the complex information that is known by others.[13]

No doubt the Industrial Policy experts are bright, intelligent persons. Few persons would deny that fact. However, the U.S. economy will not function better just because intelligent, highly-educated men and women are trying to centralize economic decisions. Rather, these decisions are better left to those who, while lacking high-powered college degrees, are far more capable at understanding their own economic surroundings than someone in Washington, D.C. As Sowell has noted, we need the skills of all persons in the economy, not just the skills of a chosen few.[14] Centralized knowledge simply cannot replace decentralized knowledge.

Another serious flaw in the economic reasoning of Industrial Policy advocates is their failure to understand the problems of economic malinvestment, a problem that has been analyzed by Austrian economists since the beginning of this century. The outline of Industrial Policy calls for "targeting" growing or promising sectors of the economy with protection from foreign (and some domestic) competition as well as making cheap capital available. It is this portion of the plan that makes malinvestment a virtual certainty.

First, there is an inherent contradiction in the advocates' analysis. For a new industry to have promise, it must perform well in the marketplace, for the market is the only true bellwether for any product. If people do not see a use for a new product or service, if they believe that the new item cannot meet their present or future needs, then that item has no future in the marketplace. Because the market reflects the needs and wishes of large numbers of people, it is by far the best way to measure the promise of a product or service. No other method is comparable. Even if a government official declares an unpopular item to be a new member of the marketplace, there is no guarantee that the item will ever be used in large quantities if at all.

Therefore, the best that economic planners can do in determining the potential for a new product or service is to make their determination *after the fact.* Their decision cannot precede the market's verdict; it can only follow. With that in mind, it is important to realize that the market, and only the market, can truly pick winners and losers. For government to do so can have disastrous results. Farm price supports, for example, have made farming an attractive business for some investors because they were already guaranteed a price for their product—provided they could produce it. The lure of guaranteed prices has brought so many producers into the market that even government policies have not been able to keep prices at profitable levels. The result has been a 1930s-style liquidation of the Farm Belt (made vividly clear by recent news reports).

The same scenario would repeat itself anywhere the government tried to "target" what it perceives to be promising producers. The lure of easy capital and protection would entice new entrants into the market, and the resulting glut of production would bid input prices up and drag profits down. To put it bluntly, if the U.S. government were to give the same kind of support to the semiconductor industry as it presently gives to farmers, that industry would be flat on its back within a short time. The policies of easy money and protection would bring about massive malinvestment of capital, a malinvestment that would sooner or later have to be liquidated when the market would correct itself.

Of course, malinvestment and liquidation are impersonal terms. A human translation of them would include words like unemployment, joblessness, depression, and the like. For the price of malinvested capital must ultimately be paid by human beings, and it is the poor who suffer most.

On a large scale, as both Hayek and Ludwig von Mises have pointed out, malinvestment of capital has led to every one of our recessions in this century, and the central culprit in each period of capital malinvestment has been government policy, both fiscal and monetary. The new Industrial Policy promises to be a repeat of former mistakes and a guarantee of more recessions.

Thus, Industrial Policy is not a new promise of prosperity and a new age of American industry. Instead, it is simply, as McKenzie puts it, a hoax. Granted, the deception is not deliberate, but it is deadly all the same. Government planning cannot substitute for the market at any time, even when one perceives problems of "market failure." The market will ultimately speak; it is up to us to be sure that the words it uses include prosperity and wealth instead of depression and unemployment.

—FOOTNOTES—

[1]Lester Thurow in Industrial Policy debate with Dr. William H. Peterson in Chattanooga, Tennessee, March 19, 1984.

[2]These ideas are put forth by Lester C. Thurow in his book *The Zero-Sum Society*, in which he sees government being pulled apart by competing special interest groups.

[3]Robert Reich, *The Next American Frontier* (New York: Times Books, 1983), p. 21.

[4]Richard McKenzie, "The Great National Industrial Policy Hoax," lecture given at Notre Dame University November 17, 1983, pp. 11-12.

[5]*Ibid.*, p. 12.

[6]Katsuro Sakoh, "Industrial Policy; The Super Myth of Japan's Super Success," *Asian Studies Center Backgrounder*, No. 3 (July 13, 1982).

[7]Thurow, "Farms: A Policy Success," *Newsweek*,, May 16, 1983.

[8]McKenzie, p. 15.

[9]Robert E. McCormick and Robert D. Tollison, *Politicians, Legislation, and the Economy* (Boston: Martinus Nijhoff Publishing, 1981), p. 3.

[10]*Ibid.*, pp. 3-4.

[11]McKenzie, pp. 9-13.

[12]Both authors have made extensive use of Hayek's analysis on knowledge, Kirzner in *Perception, Opportunity and Profit*, and Sowell in *Knowledge and Decisions*.

[13]McKenzie, p. 15.

[14]Thomas Sowell, *Pink and Brown People and other Controversial Essays*, (Stanford: Hoover Institute, 1980).

John L. Chapman

CAPITALISM & SOCIALISM

MY PURPOSE here is to extol the virtues of a social system based on the precepts of private enterprise, limited government, and maximum individual liberty. This system, known as "capitalism," will first be defined, and its major features will then be highlighted. Additionally, the primary competing social system, known as "socialism" or "interventionism," will be defined, and compared or contrasted where appropriate. Finally, key features of current public policy debates will be addressed where they relate to points under general discussion.

One of the most intriguing of all intellectual debates concerns the most optimal method of organization of human society. More specifically, from the time of Aristotle onward a great debate has raged concerning the proper form, scope, and role of government in society, in order to effectuate the "good life."

Most people would agree that two polar-opposite kinds of society have evolved through the ages, and the aforementioned debate centers around which society is superior. Using the analogy of a continuum or spectrum, at one pole we have what is commonly referred to as "capitalism," and at the opposite pole is the system known as "socialism." All nations reside along this continuum,

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and none is at either absolute extreme. Closest to the theoretical pure capitalism is the United States; closest to pure socialism is the U.S.S.R. All other nation-states lie in between. A definition of each social system and a look at some of the major fundamentals of each will help us determine why capitalism is clearly the superior form of social organization.

Market Allocation

Capitalism is a system of social organization whereby capital is allocated and distributed via market-based channels. More simply capitalism is a system where private individuals or organizations determine the production, distribution, and ownership of all goods and services in an economy. "Capital" may be defined as any entity used in the production of goods and services. Examples of capital would include raw materials, equipment, buildings, money, and machines. In a capitalistic society, all the above-mentioned examples are owned and utilized by private individuals or organizations for the attainment of the owner's ends.

Socialism is a system whereby capital is owned, allocated, distributed, and utilized by the collective society as a whole, rather than by private people or groups. The concept of private property and use of capital for private ends is replaced instead by public ownership and collective employment of capital. Government bureaus, acting in the name of "the public" as a whole, replace private organizations as the main actors in an economy. For example, in socialist Great Britain, the steel industry has been nationalized, and there is one government-run computer company as well. Both enterprises thus avoid the rigors of marketplace competition facing such United States firms as U.S. Steel and IBM in these respective industries.

A final level-setting point of importance concerning capital is the undisputed fact that the only way a country is able to increase its wealth is to experience an increase in capital per worker. The only method of increasing "output per worker"—meaning either (a) more work in the same amount of time, or (b) the same amount of work accomplished in less time—which is commonly referred to as productivity, is to increase the amount of capital invested in that worker. For example, factories with automated machinery today produce thousands more articles of everything, from widgets to automobiles, than in previous times.

Another example of capital invested in a worker to increase his productivity—and thus his wealth—is the pocket calculator. A student utilizing a calculator to do his math homework will finish earlier than the student computing the same problems in his head or with pencil on paper; the resultant time savings may either be used as leisure time—an economic good—or to increase income, with either choice representing a net increase in wealth. Therefore, any economy, socialistic, capitalistic, or mixed, has to invest in capital in order to increase output and thus wealth, and thereby improve living standards.

Government or Market?

The key question all concerned human beings must answer is this: which institution, the "government" or the "market" (an intangible consisting of freely acting individuals or groups), is better equipped to solve the problems confronting society today? All rational men and women, whatever their political and philosophical leanings, would like to see a world at peace, fully employed, with equality of opportunity for all, and the eradication of poverty. Which kind of society, the command economy or the market economy, will generate the capital wealth necessary to eliminate social ills?

The answer, it would seem, is self-evident. Yet the debate rages on, because the illiteracy and lack of knowledge of the general populace with regard to economics is rampant in our world. Lacking the intellectual tools to correctly analyze problems or interpret relevant data, most people, whether they be commoners of the street or members of the United States Senate, misinterpret the causes of a problem, and subsequently then advocate solutions *which usually will tend to make the problem worse!* Let us then analyze briefly the workings of capitalism, and expose the shortcomings of government interventionism, whether total (as in socialism) or partial (as in a mixed economy, such as the United States today).

Capitalistic institutions had their latent beginnings in the periods of Greece and Rome, disappeared during the Dark Ages, and reappeared during the Reformation. During most of this time, from primitive tribal cavemen through to the rise of civilizations in the Middle East, the Far East, and then Greater Europe, societies were authoritarian in nature. A ruler-king or ruling class devised several rationales for their subjection of others ("divine right," position of birth, wealth, or ancestry, for example), but the end result was the same.

It is obvious but important to note that throughout the thousands of years of human history, up to the present day, the fundamental economic problem of "scarcity" has persisted; that is to say, man's wants (for scarce goods and resources) have not been, and never will be, satiated. It is of further fundamental importance to note that through the ages, up until just a few hundred years ago, man's material condition, or standard of living, was relatively constant. It rose briefly with the advent of Greek and Roman civilization, but receded as those societies died. Authoritarian structures may have resulted in pyramids or great cathedrals, but life continued mostly to be "nasty, brutish, and short."[1]

Only with the advent of free enterprise capitalism was the standard of living for all to suddenly realize a dramatic improvement. This is important only because of the widespread but fallacious notion that material progress is merely a function of the progression of time (i.e., the quality of life in the 1980s is an improvement from the 1880s, but not as good as it will be in the 2080s). In fact, the standard of living is a function of the prevailing social and economic institutions of any given society.[2] Indeed, only when such capitalistic institutions as private property, limited government, and liberal trade were developed, did the quality of human life show marked improvement from the relative stagnation of the preceding centuries.

Social Contract

As Locke, Hobbes, and others have observed, individuals form a "social contract" (or government) to protect individual life, liberty, and property. Capitalism developed as individuals began to withdraw from the yoke of authoritarianism, and instead desired individual liberty to order their lives. The "social contract," or government, entailed a delegation of fundamental rights of individuals to protect themselves. Thus, early government was an "umpire" rather than an active participant in day-to-day affairs, and as such treated each individual neutrally (or equally). This was an important development because the private property order and individual liberty allowed for the first time a "long-run view" of life, rather than a preoccupation with immediate concerns. In economic terms, the individual could now save and accumulate goods for future use (i.e., "investment"), because of societal guarantees of life and property.

The resultant saving and capital accumulation led directly toward increased specialization and a productive division of labor, and the "Industrial Revolution" quickly ensued. Most Marxian analysis of this period focuses on the horrors and exploitation, but the facts were otherwise. People flocked to the urban centers of Europe and then America as capital investment steadily increased worker productivity and thus raised the living standards of the masses.[3] More recently, South Africa has experienced a tremendous influx of immigrants seeking improved opportunities.

The functioning of this emerging

market society was brilliant to behold. As Adam Smith first so eloquently described, a market-based economy was driven by an "Invisible Hand" which promoted order out of seeming chaos. Each individual laborer in a capitalist society seeks to acquire a marketable skill in order to trade with others. Thus, increased specialization (with all its attendant productive efficiencies) is promoted. As literally thousands of specialties are developed, relative prices (which are nothing more than the collective monetary votes of the masses of consumers) point the use of scarce economic resources toward their most highly-valued ends.

Consumers in Charge

The Invisible Hand of the market directs capital to wherever consumers desire. For example, in recent years the demand for improved decision support and analysis tools (leading to improved professional productivity in business) has led to an explosive growth in low-cost personal computers and software that is easy to use. Market signals prompted data processing companies in this direction, and market competition has resulted in steadily lower prices and improved quality. Conversely, the market signaled to Ford Motor Company several years ago that its production of the Edsel was a waste of scarce resources (because Ford was not realizing a profit on this auto), and consequently Ford ceased Edsel production.

A few significant points should be noted here. First, the Invisible Hand, when allowed to operate unhampered by government, serves individual consumers by catering to the satisfaction of their wants. This is a *monumental* development; throughout most of human history, the masses toiled for the king, the pharaoh, or the oligarchical elite. Under capitalism the reverse is true; the captains of industry seek to serve the consuming masses.

Secondly, resources are most efficiently allocated, and production most effectively coordinated under capitalism. The free movement of prices signals capital and labor (the two main ingredients of production) to migrate to their highest-valued marginal uses. The production of the most desired goods and services ensues, and this obviously promotes social welfare in the best possible way, by satisfying the most urgent wants.

Thirdly, the private property order engenders a spirit of peaceful, harmonious coexistence and cooperation among individuals and groups. Permitting and protecting the natural right to property encourages saving and capital accumulation (and of course as capital invested per worker increases, standard of living and quality of life increase), fosters a climate of production by encouraging labor, and encourages individual self-reliance and responsibility (through the growth of personal assets).

Of course, what is true for individuals can scarce be folly for nations as a whole.[4] International specialization and division of labor lead to increased production of goods and services worldwide. Increased production, enhanced by full and efficient employment of labor, capital, and land, leads to generally lower goods prices, and market competition improves quality. Where active trade across borders occurs, the living standard is improved and war will never occur; Canada and the United States have no need for armies and border guards. In fact, there has never been an armed conflict between two capitalistic societies, because the bonds of free trade and peaceful noncoercive coexistence are too strong.

Economic Progress

Under capitalism, then, the engines of production turn at full speed. Individuals are free to pursue their own interests, and the consumer is king. Any individual who seeks employment finds it, because wages are not distorted by any intervention and compensation is based on marginal contribution to needed production (labor is always in demand, as wants are insatiable). It is talent and merit, and not birth or wealth, that propel the individual up the economic ladder. And of course, it is absurd to deride those individuals who amass great wealth; no one is any poorer because of them, and they attained such rewards by serving the rest of us!

Peace and prosperity prevail among individuals and nations, and poverty is eradicated through full employment. Additionally, and most importantly, the individual leads a free, uncoerced life and has complete sovereignty over his own existence, as long as his actions are peaceful and create no negative externalities for others. As long as the spirit and responsible attitudes engendered by capitalistic institutions are promulgated, the happy state of affairs such liberty fosters will never break down.

In the short span of a *few hundred* years, capitalism has delivered an improvement in the general quality of life unparalleled in the *previous thousands* of years of human history under the *ancien regime* of authoritarianism. It would thus seem self-evident that capitalism is the most superior form of social organization (even more so if one travels to and observes the two Berlins, or the two Koreas, or the two Chinas). A brief look at the underpinnings of socialism shows, however, why it is still so prevalent, just as its functional workings expose its false glamour.

Most socialists (and I use the term here to apply to any individual favoring an active, interventionist government) claim to be altruistic, compassionate people professing concern for and a desire to help others. They view the market economy as an impersonal, cold institution promoting crass material gain, and chastise its instability and always-changing chaos, brought about by the "animal spirits of investors."[5] They seek to bring order and security to society by instituting a certain amount of control over economic activity, through fiscal, monetary, and even social policy. Through legalized intervention ("legalized" in the sense of a law being passed) government seeks to ameliorate social conditions.

Alleged Examples of the Failure of Competitive Enterprise

Adherents of interventionism see various failings of the market economy. Among those heard most often are the charges that capitalism causes a rather widespread distribution of income, and that unequal income distribution consigns some to a permanent "underclass." Further, most members of this underclass are from minority groups, and since such groups historically have been the victims of racial discrimination, collective government action is required to right earlier wrongs and raise these groups' living standards, argue the socialists. This argument, incidentally, is merely a variant of the old Marxian critique of the bourgeois exploitation of proletarian labor.

Another failure of the marketplace pointed to by collectivists is the "misallocation" of resources. How can funds be properly sourced, say these social well-wishers, when professional athletes, for example, command astronomical salaries when compared with public school teachers? After all, education is a far more noble and socially useful profession than basketball or football. Additionally, defense contracts, say, are a terrible waste, when such money should really be spent to feed the poor.

More examples could be cited, but the key point to understand is that policies of social welfare seek to redress inequities and social ills allegedly caused by an unhampered market economy. Conscious collective efforts are made to redistribute resources toward women, minorities, and other institutions and special interests. Again, to paraphrase Marxian analysis, the "problem of production" has been solved—*distribution* is now the focal point for interventionists.

The policies of socialism are so alluring (especially to the idealists often found in graduate schools, universities, the arts, and the media) precisely because of the appeal to altruism, and the exhortation to exhibit concern and compassion for others. Government interventionism (all of society supposedly working together for the common good) may be used to achieve a better society for all, and to root out the incessant competition, change, and chaotic insecurity of the market society, replacing these with the tranquil, orderly security of the collective command society.[6]

Sadly, the appealing rhetoric that always lies behind the well-meaning policies of active government interventionism does not shield the false premises on which such actions are based, or the unfortunate consequences that ensue. A brief look at the background and general structure of a few of these programs and their consequences will suffice to point to socialism's broader failings.

The Transfer Society

Policy-makers in government possessing a socialistic orientation seek to redress market failings, as previously stated. In the United States, this process began in earnest with the advent of Roosevelt's New Deal. Social Security was set up to aid the aged. Agriculture and various small businesses then received subsidies. Later, benefits were drawn up for veterans (and then other groups) for housing, education, and vocational training. By the administration of Lyndon Johnson, vast health care, public works, and anti-poverty schemes had come into being. The result of all this is the existence today of a plethora of public laws showing favor to select groups, industries, or institutions, and of course organized lobbies representing hundreds of special-interest pressure groups.

This sytem of interwoven welfare programs constitutes what Hans Sennholz and others have aptly named "the transfer society." In the transfer society that the United States is fast becoming, there are classes of beneficiaries receiving government largess in the form of entitlements, subsidies, grants, or generous pensions flowing from the just-mentioned social programs and hundreds of others as well. Less visible to the public, however, are the classes of victims that are paying the bills for such largess. The very progressive and high marginal taxes (not to mention chronic inflation) levied on the victims to pay for the subsidies and benefits flowing to the targeted beneficiaries has had a highly negative effect on the level of production and output (and a concomitant rise in taxpayer cynicism and disgust, as their work efforts grow increasingly futile).

Since approximately 1960, defense spending as a proportion of the Federal budget has dramatically decreased, from 53 per cent of total spending to less than one-fourth. At the same time, "social spending" has exploded. One would hope, at the very least, that this would have resulted in less poverty, better job opportunities and lower unemployment for the poor, rebuilt cities and highways, and improved international conditions. Unfortunately, the general living standard for minorities and underclasses has in relative terms not seen improvement.[7] The inner cities are as decayed as ever, and foreign aid and agricultural and technological subsidies have not aided the Third World—Africa, a net *exporter* of food in the 1950s, is today the site of massive famine. Benevolent socialism has failed.

Rational Behavior

The transfer society, as are all forms of socialism, was destined for failure for a few key reasons (which, I would argue, one could have determined *a priori*, without ever bothering to gather comparative statistics).[8] First and foremost, man is a praxeological being. That is to say, man behaves purposively, utilizing various means to arrive at chosen ends. As such, he responds in a generally predictable manner to changing incentives; as the incentive structure in the economy has changed, so has the behavior of economic agents. This again is a seemingly self-evident tautology, but it is mentioned because the proponents of Big Government constantly ignore the inexorable laws of human action through policies which carry perverse incentives. Incentives to produce are replaced by incentives to receive statist handouts.

> Government is not capable, by nature, of being productive or constructive. In its capacity as government, it acts to restrain and restrict. When it uses these powers against those who would disturb the peace in one way or another it enables peaceful men to produce and construct. When it uses them to restrain peaceful men, it inhibits the constructive. Thus it is that limited government is the requirement for releasing the energies of men.
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> CLARENCE B. CARSON

The economic distortions these handout programs cause is truly massive. What kind of sense, for example, does it make to *pay farmers not to produce food*? Agricultural price supports are a related absurdity. By setting maximum prices (ostensibly to help the poor) government artificially pumps up demand for a product at the same time it *curtails the incentive* of the producer to supply the commodity. Increased shortages result.

Minimum wage laws and union wage floors, again designed to aid certain targeted groups, have the same effect. The employer's demand for labor is reduced (labor, like everything else, is a cost phenomenon) at the very time the higher wages guarantee an increase of job applicants; the end result is a certain amount of *unemployment.* Those lucky enough to obtain the artificially high-wage jobs benefit at the expense of the unemployed; this is the collectivist's idea of "compassion" (of course, in a free market, all who wished work and the opportunity to acquire skills and advance would have a job at market wage rates). It is unnatural to be unemployed, and anywhere and everywhere this condition occurs, it is a sign of market interference of some sort.[9]

Benefits of Deregulation

All government interventions in the domestic economy, and international protectionism as well, have a common denominator: restricted supply and higher end-prices to the consuming public. Where government backs off, immediate positive effects are realized. Airline and trucking deregulation has led to a flourishing of new carriers offering better services at lower prices to the consuming public. Of course, the Teamsters Union and executives at Eastern Airlines may be less than happy, but the *masses benefit.*

Confiscatory tax rates and inflation are perhaps the most insidious interventions of all, however, for they lead literally to the destruction of civilized society (as Lenin once observed). Taxes are a direct disincentive to produce, and the phenomenon of "capital flight" is a direct result of high progressive rates. Is there any doubt as to why Bjorn Borg left his native Sweden for Monaco? Trying to grab ever more income, the Swedish government lost it all. This is but one example of a widespread phenomenon—tax avoidance and outright evasion are dramatically increasing, as luxury goods boom and the "underground economy" grows perhaps beyond 15 per cent of Gross National Product.

Inflation is a surreptitious tax caused directly by government mismanagement of the money supply. By continually inflating the money stock, the FED adds high uncertainty into longterm contracts, stifling business investment. Why would any creditor loan to a debtor when the payback will result in cheapened dollars? As money loses its unit of account and store of value functions, this relationship is ruined, and further impedes vital trade. Fixed-income pensioners are devastated by real wealth transfers away from them, yet "compassionate" government officials scoff at attempts at monetary reform.

The worst aspect of inflation, however, is undoubtedly that it is a key ingredient of boom-and-bust business cycles. By falsifying interest rates, flows of investments into capital goods industries are stopped as inevitably project costs rise, and resources flow into consumer and service sectors only later. Malinvestment and misallocation of scarce resources, with attendant hardship and disruption for human beings, is always the end result.[10] This is best exemplified by the current situation in the United States, where certain sectors and geographic areas have enjoyed a sparkling recovery, while other sectors, such as agriculture and certain import-export businesses, are lagging. Inflation and intervention always combine harmfully, with grave human costs.

The Unseen Effects

In addition to the foregoing distortions, socialism's toll must be viewed in terms of opportunity cost. What would have been built, produced, and delivered in lieu of the inefficient profligacy of government? What would each individual and group have done with their extra income? We of course will never know. Certain individuals or groups benefit from subsidies or direct transfers *in the short run*, and these positive effects are seen by all (a public housing project is of course highly visible, for example). The aggregate costs which burden the rest of society will in the longer term far outweigh the short run visible benefits, however. These costs are currently widespread and diffuse, but they are growing rapidly, and will come due.

In addition to economic distortion and curtailed production, interventionism leads to expanding powerful bureaucracies. Groups no longer motivated to produce and serve the consuming public instead lobby for a larger portion of government handouts (colloquially, grab a larger portion of a redistributed pie rather than grow the whole pie). Senators and Congressmen, looking only toward winning the next election, set up large bureaus to visibly transfer resources to privileged groups. Such an environment, geared toward redistribution rather than production of wealth, is highly conducive to the waste, fraud, and corruption so often found.

This is another predictable consequence of interventionism, because government bureaus are not subject to the rigor and discipline of the free market; where there are no pricing signals or competition, there will be tremendous inefficiency and waste. Does anyone really know the purpose of the Department of Energy? Has it produced any oil? Has the Department of Transportation produced any autos, or run transit systems effectively? What do the Labor, Commerce, and Education Departments really do? Would the free market have granted thousands of dollars to study insect sex lives, or the effect of pornographic literature on children?

Obviously there is tremendous waste in a system where groups are encouraged to spend productive time trying to obtain grants from government bureaus. The masses who are not beneficiaries are big losers. Innovation will always be stifled under such a system. Can anyone see a self-serving Federal Department of Railroads, under heavy pressure from railroad industry lobbyists, granting a government permit to the Wright Brothers to test their airplane? How fortunate socialism was not well developed in the United States in 1903.

Legal Plunder

Perhaps the worst effect of socialism, however, is that the transfer society is tantamount to legal plunder.[11] Leaving aside the obvious disincentives, what is "fair" about taking differing percentages of income from different laborers? The United States once had the highest taxpayer compliance in the world, but the increasing perversity of the transfer society has caused millions to enter the underground economy. People fight the government's unfairness by becoming corrupted thieves and tax-cheats.

Additionally, the transfer society promotes true Marxian "class warfare," as several special interests compete for government handouts. Beneficiaries and victims, agriculture and small business, black and white, and young and old are but a few of the many groups fighting each other for privilege. In fact, the conflict has many levels; within the agricultural lobby, for example, tobacco interests are surely in contention with dairy farmers for agricultural price supports. *Socialism breeds violence and warfare,* as competing entities vie for what is "fairly" theirs.

In summary, then, the command economy has proved to be a failure because it is based on a false theory of human nature. To understand this one need only observe masses of people seeking freedom and opportunity, "voting with their feet" worldwide (Southeast Asia and Cuba are recent examples of a popular flight from socialism), or talk briefly with the likes of Lech Walesa to know why: government programs take away the incentive to work and produce.

Seeds of Conflict

Capital formation, the necessary prerequisite to an increased standard of living and improved quality of life, is stifled as government bureaucrats and politicians wield power which rightfully should fall to consumers. Strife and conflict replace the peaceful coordination and exchange of goods and services that capitalism provides. Once this is discerned, it is easy to see why the billions spent on "social programs" in the last 20 years *have done nothing* to end poverty in the aggregate.

It is no coincidence that socialism's most ardent supporters are relatively wealthy, and are often found in academia or the media. Coming from a controlled and comfortable environment, these people seek only to lift the living standards of the poor. Their aims and concerns are commendable, but their intellectual arrogance is unseemly. They wish to order society after their own fashion, and impose their own designs and standards on the rest of us, thinking they know best. Having no knowledge of economics, they pursue policies which in the end cause misery to the unemployed, condemn millions to poverty, stifle innovation and production, and in the long run lower us all. In their ignorance, they disparage the very system that has brought them several amenities of life and the time to deride capitalism, and they vote for politicians and policies which will come to hurt them, ironically. The road to hell is, after all, paved with good intentions.

However, ideas rule the world, and the human spirit burns to be free of all man-made fetters. Those who understand the free market must undertake to explain the adverse consequences of interventionist policies to the well-meaning but misguided proponents of collectivism, and return again to freedom, prosperity, opportunity, and peace for all individuals. The alternative is too sad to contemplate.

—FOOTNOTES—

[1]See Thomas Hobbes.

[2]See Ludwig von Mises, *The Anti-Capitalistic Mentality.*

[3]Mises makes reference to the blatant fallacies of Marxist interpretation on this point several times in his various works.

[4]See Adam Smith, *The Wealth of Nations.*

[5]Keynes, of course, felt government could ingeniously temper these animal spirits, and his *General Theory* prescribes the formula.

[6]Clarence B. Carson gives an excellent rendition of socialism's soothing rhetoric and appeal in *The World in the Grip of an Idea* (New Rochelle, NY, Arlington House Publishers, 1978).

[7]A growing body of literature, exemplified by George Gilder in *Wealth & Poverty* and more recently by Charles Murray in *Losing Ground*, points to the harmful social effects of bad economics. For example, the number of single-parent black families and illegitimacies has risen steadily over the last twenty years.

[8]This is the traditional analysis of the Austrian school of thought, which makes use of the tenets of praxeology and methodological individualism to arrive at valid conclusions.

[9]Hans Sennholz, "The 'Natural' Rate of Unemployment" (*The Freeman,* November 1984, pp. 644–650).

[10]Only Austrian business-cycle theory adequately explains concurrent inflation and recession. The reader should look to authors such as Mises, Hayek, Rothbard, Sennholz, and others.

[11]Dean Russell, "The Source of Rights" (*The Freeman,* November 1984, pp. 661–668).

Pattern for Failure

In *A Pattern for Failure: Socialist Economies in Crisis* (New York: Harcourt Brace Jovanovich, 175 pp., $22.95), Sven Rydenfelt, a Swedish economist, offers a general proposition endorsed by Milton Friedman in a thoughtful introduction. The general proposition is that wherever there is detailed central economic planning the ordinary man suffers. The reason, says Rydenfelt, is ecological: people are dependent on their economic and social environments, and when individual entrepreneurs are discouraged by oppressive government-imposed constraints the creativity that feeds everybody languishes.

There is some elaboration of Rydenfelt's general thesis in an opening section devoted to the importance of the entrepreneurial environment. Like George Gilder in America, Rydenfelt thinks the supply of entrepreneurial incentive is more important than the supply of capital. If a man has a good idea, and there are no regulations to prevent him from pushing it, he will get the capital he needs somehow.

Once having established the outlines of his theory of the general importance of the entrepreneurial climate, however, Sven Rydenfelt rapidly shifts the emphasis of his book. What he is really interested in doing is to show how socialist governments mess up their agricultural policies, bringing starvation by their treatment of the peasants.

Formula for Famine

Communist and socialist governments, no matter how they come to power, are impelled by Marxist theory to favor the industrial proletariat. Partly this is due to Marx's own contempt for what he considered the stupidity of country life. Depending on the city workers to keep them in power, socialist governments fix the price they are willing to pay the peasants at a point that is low enough to guarantee cheap food to the urban masses. It doesn't matter whether the peasant keeps nominal title to his acres or not—the failure to let farmers sell their crops as they please reduces the incentive to produce. Peasants will normally work hard enough to keep their own families fed, but without market freedom there will be nothing extra to forestall possible famines.

Sven Rydenfelt's evidence, which is elaborately displayed, is that the famines always come. The pattern was set in Soviet Russia, when there was drought in the Ukraine in the years after the Bolshevik takeover. There wouldn't have been serious trouble if there had been a stored reserve. But the civil war had emptied the grain bins. Lenin used the weather as an excuse. But he was realistic enough to postpone agricultural collectivism.

Telling the peasants to enrich themselves—i.e., to become kulaks—he proclaimed the so-called NEP, or New Economic Policy. The theory was too successful to please Stalin, who, in the early Thirties, decided to break the power of the kulaks and establish big state farms. The result was a forced famine that killed some three million skilled agriculturalists.

Stalin in Charge

Stalin claimed successes for the new collectives, but when Khrushchev decided to expose the excesses of Stalinism, one of the first figures he revealed was that in 1953 Russia had fewer livestock than it had in 1913, when there were 60 million fewer people to feed.

In the long run Khrushchev proved to be no improvement on Stalin as a farm manager. His attempt to bring new acres under cultivation in semi-arid areas worked out badly. Rydenfelt says there were crop failures in Russia in nine out of twenty years between 1963 and 1983. The excuse was always that the weather had been bad. The Communist high command solved the problem of the recurrent shortages by importing grain from the capitalist West.

Sven Rydenfelt follows his section on the failures of Soviet agricultural planning with chapters on what has happened to farming in Poland, Romania, Czechoslovakia, Yugoslavia, Hungary, Portugal, China, India, Vietnam, Sri Lanka, Ghana, Tanzania, Cuba and Argentina.

In all cases save that of Hungary the courses followed by communist or "planning" governments have resulted in general impoverishment. The Hungarians have saved themselves by letting their peasants sell their produce in the open market. There is a repetitive quality to Sven Rydenfelt's story, but this is bone and marrow of the central point that he is determined to drive home.

Rydenfelt's examples do not include Ethiopia, Angola, Mozambique, Chad and the general sub-Saharan region in Africa. But we know from the news stories that there are no exceptions to Rydenfelt's rule that, where socialism prevails, starvation is just around the corner.